

International Trade Alert

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After Nearly Ten Years Under Review, CBP Revises Its Policy to Allow Post-Import Pricing Adjustments for Related Party Goods

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Companies that import goods from related foreign parties may soon be eligible to more easily implement post-import pricing adjustments required under transfer pricing policies and advanced pricing agreements. In a modification of its long-standing approach, U.S. Customs and Border Protection (CBP) issued a ruling on May 30, 2012 setting forth the agency's new policy toward the treatment of post-import pricing adjustments for related party transactions. Under the new policy, which comes into effect on July 30, 2012, CBP will allow related parties to use the transaction value (i.e., the price actually paid or payable for the goods) in the appraisal of imported merchandise, even where post-import pricing adjustments apply, provided that: (1) the companies' transfer pricing policy constitutes an objective formula, as determined by an analysis of enumerated criteria; and (2) the parties demonstrate that the relationship did not influence the price. The ruling was in response to a Request for Internal Advice that had been under review by CBP for nearly ten years.

A large percentage of imports into the United States involve trade between related parties. In fact, related-party trade accounted for over 40% (\$1,295 billion) of the total goods imported into the United States during 2010. For tax purposes, U.S. companies typically implement formal intercompany transfer pricing policies to ensure that the relationship of the parties does not impact the price of intercompany sales. To replicate the price of an arm's-length transaction, these transfer policies often provide for various post-import adjustments to the transfer price.

Prior to the recent ruling, CBP held that transaction value appraisal was inappropriate for such related-party imports subject to post-import adjustments. In HRL 547654, CBP determined that the post-import adjustments required under the transfer pricing policies were calculated based on factors within the control of the buyer and/or seller, and were not fixed or determined prior to importation by an objective formula. Accordingly, CBP reasoned that such transfer pricing policies did not fall within the objective formula exception to the fixed price rule. Therefore, CBP prohibited the use of the transaction value method of appraisal for calculating post-entry adjustments.

In the case at hand, CBP reflected a significant change in its policy by proposing a broader interpretation of whether a transfer pricing policy constitutes an "objective formula" for purposes of the exception to the fixed price rule. In that decision, the parties had used the reconciliation program for valuation and were able to satisfy CBP that the post-importation adjustments adequately reflected the intercompany pricing formula. Based upon this decision, CBP will now permit importers to use the transaction value to make both upward and downward price adjustments to the sales prices as required under a company's formal transfer pricing policy, provided that the transfer pricing policy constitutes an "objective formula," as determined by satisfying the following criteria:

- . A written "Intercompany Transfer Pricing Determination Policy" is in place prior to importation and the policy is prepared consistent with IRS Code Section 482;
- . The U.S. taxpayer uses its transfer pricing policy in filing its income tax return, and any adjustments resulting from the transfer pricing policy are reported or used by the taxpayer in filing its income tax return;
- . The company's transfer pricing policy specifies how the transfer price and any adjustments are determined with respect to all products covered by the transfer pricing policy for which the value is to be adjusted;
- . The company maintains and provides accounting details from its books and/or financial statements to support the claimed adjustments in the United States; and
- . No other conditions exist that may affect the acceptance of the transfer price by CBP.

In addition to meeting these five factors, importers must also comply with a second step in the

analysis. That is, the parties must demonstrate that their relationship did not influence the price. Per CBP's ruling, the second step is distinguishable from factor (5) of the "objective formula" test, as it goes to the validity of the prices declared to CBP.

How Can Your Company Benefit From the Policy Change?

- **Identify Cost Savings From Post-Import Adjustments:** In light of the recent ruling, importers that frequently purchase items from foreign related parties should evaluate whether taking advantage of valid post-importation adjustments could result in duty savings.
- **Review Transfer Pricing Policy and Customs Valuation Methodology:** Importers who wish to benefit from transaction value appraisement for their related-party goods should familiarize themselves with the five factors enumerated by CBP and assess their transfer pricing policies accordingly. If a pricing policy fails to comply with any one of the enumerated criteria, the respective imports will not qualify for transaction value appraisement. More sophisticated transaction pricing policies may require the assistance of outside auditors and counsel to ensure compliance with CBP's customs valuation policies.
- **Participate in CBP's Reconciliation Prototype Program:** CBP strongly encourages importers to participate in its Reconciliation Prototype Program for reporting post-import pricing adjustments. Reconciliation allows importers the flexibility to file entry summaries with CBP using the best available information, with the mutual understanding that certain elements, such as the declared value, remain outstanding. While enrollment in the program is not mandatory, importers claiming an adjustment without using the program must demonstrate at the time of entry that the price is arm's length. By contrast, the program allows importers twenty-one months to file a reconciliation entry, and provide the final value information to CBP.

For additional details on how CBP's new policy may impact your international business activities, please contact any attorneys in our [International Trade and Customs Group](#) for assistance.