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Can Your Transfer-Pricing Documentation Help at Customs?

By Andrey Shpak

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Andrey Shpak
Partner, Tax
Goltsblat BLP

This year marks a cornerstone for both tax and customs legislation in Russia: Both the long-awaited new transfer-pricing rules came into effect, and WTO accession was finally made a reality. With the introduction of these new frameworks, taxpayers will be subject to an increased tax compliance burden, requiring a significant amount of additional documentation. On the other hand, a new set of defenses has also become available to taxpayers. This article explains how transfer-pricing documentation can help to support the value of goods at customs.

It has generally been a common trend for the two government price control regulations for tax purposes and customs purposes to work parallel to each other without much intersection. Although both have a similar objective — identifying what the arm's length price of a deal should be — and use similar methodologies to determine such a price, the unwillingness of the controllers to converge is perfectly understandable. Fiscal bias requires customs to seek a higher price of goods at customs, while tax authorities generally are not interested in inflating the cost of goods sold and other expenses that are deducted from the profits tax base.

Anna Zelenskaya
Associate, Tax
Goltsblat BLP

To be fair, customs valuation and transfer pricing have a significant number of differences that make an easy consolidation of the rules practically impossible. Transfer-pricing rules analyze income depending on particular comparable commercial circumstances, rather than the price of a specific article. There are critical differences in the factor of time, the sources of information and the level of aggregation accepted.

Nevertheless, considering that most multinational businesses are facing a need to support their prices for both customs and tax purposes, there is certainly room for optimizing the intra-group documentation processes.

With the accession to the WTO, Russian taxpayers are eligible to use "circumstances of the sale" tests based on internal comparables. The Agreement on the Implementation of Article VII of the GATT 1994 and Interpretative Notes to it allow the importer to apply the transaction value method for customs valuation where the circumstances surrounding the sale show that the relationship between the parties did not influence the price. The circumstances of the sale test may be met where the price had been settled in a manner consistent with (i) the normal pricing practices of the industry in question, or (ii) the way the seller settles prices for unrelated buyers, or (iii) where the price is adequate to ensure recovery of all seller's costs plus a profit in selling goods of the same class over a representative period of time.

Considering that a multinational's global TP policy surely addresses the profit levels earned by the related seller, it can be used as a proof of circumstances of the sale, provided it is properly tailored to satisfy the customs authorities. Assuming further that there are internal comparables available to support the arm's length pricing for the seller, drafting TP documentation with a view to show it at customs becomes even more important. Furthermore, in its recent commentary, WCO Technical Committee on Customs Valuation expressly stated that a transfer-pricing study can serve as one of the sources of information for examining the circumstances of the sale.

To summarize, the need to invest time and effort in setting up two sets of supporting documentation for both transfer pricing and customs valuation cannot be fully obviated, but it can be optimized; a properly tailored TP policy covering both the importer and the related seller's operations might be useful evidence for customs purposes. Thus, for those who think globally, the two worlds can in fact converge.

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