

China Customs Valuation and Transfer Pricing: The Hidden Conflict

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Unofficial English translation prepared for reference only. The official Chinese text prevails.

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If your WFOE imports goods from a related party overseas—a parent company, a sister subsidiary, or a contract manufacturer—customs valuation isn't just about the invoice price. It's about whether that price is arm's length.

Customs and Tax: Two Different Perspectives

Here's the trap: customs wants your import price to be high, so they collect more duty and VAT. The tax bureau wants your import price to be low, so your costs are lower and your taxable profit is higher. Two government agencies, opposite incentives, and your related-party transaction sits in the middle.

A foreign manufacturer we worked with set their intercompany transfer price at a level they thought was reasonable. Customs reviewed it and decided the declared value was too low—they issued a reassessment demanding back duty plus a penalty. The company then had to negotiate with both customs and the tax bureau simultaneously, each pulling in opposite directions.

How Customs Values Related-Party Imports

Chinese customs applies the WTO Valuation Agreement methodology. The primary method is transaction value—the price actually paid. But if customs suspects the relationship influenced the price, they can reject transaction value and apply alternative methods: the transaction value of identical or similar goods, the deductive method (working backwards from the domestic resale price), or the computed value method (cost of production plus profit).

Customs will specifically ask: does your transfer pricing documentation support the declared customs value? If your transfer pricing report says the arm's length margin is 5% but your customs declaration implies a margin of 2%, that's a red flag.

Transfer Pricing Studies and Customs

Many multinationals prepare transfer pricing documentation for tax purposes but never think about customs. That's a mistake. Your transfer pricing study can be your best defense in a customs audit—or your worst enemy if it contradicts your declared values.

The solution: coordinate your transfer pricing policy and your customs valuation. Before setting intercompany prices, consider the customs implications. If your parent company charges a markup that makes your China import price artificially low, customs may challenge it regardless of what your transfer pricing study says about profitability.

The Audit Trigger

Customs audits related-party transactions more aggressively than arm's length ones. If your WFOE's import prices are consistently lower than industry benchmarks, you're at risk. If prices fluctuate significantly without a clear commercial reason, you're at risk. If your declared values don't match what competitors declare for similar goods, you're at risk.

A customs valuation audit can go back three years. The liability isn't just the duty and VAT shortfall—it's also late payment surcharges that compound daily.

Practical Steps

Document your transfer pricing methodology and keep it consistent with your customs declarations. If there's a legitimate reason your intercompany prices differ from market prices—say your parent provides proprietary technology that reduces production costs—document it. If customs comes asking, you need to show your work.