German Federal Fiscal Court on customs valuation: Retroactive transfer price adjustments not to be taken into account (*Hamamatsu* decision)

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In its May 17, 2022 ruling, the German Federal Fiscal Court (*Bundesfinanzhof*, ***BFH***) confirmed that it is irrelevant to determine the customs value for imported goods if the transaction value is adjusted subsequently (Case No. VII R 2/19). The ruling marks the end of the *Hamamatsu* case, in which the European Court of Justice (***ECJ***) already had taken a position (Judgment of 20 December 2017, C-529/16). The core of the proceedings hinges on whether transfer pricing adjustments in cross-border transactions between affiliated companies are to be taken into account retrospectively when determining the customs value.

Background

The *Hamamatsu* dispute, spanning several years, stemmed from an unsuccessful application filed by the plaintiff in 2012 for reimbursement of customs duties which the plaintiff believed that he had overpaid. When declaring imports, the plaintiff had stated the actual price charged for the goods in question. The price was based on an advance pricing agreement between the plaintiff and its Japanese parent company. According to this agreement, certain transfer prices were initially set and invoiced for the goods supplied. After the end of the fiscal year, these prices were reviewed and then corrected under the residual profit distribution method. Because this method resulted in a reduction of the transfer price, the plaintiff claimed that, as a consequence, the customs value of the goods should also be reduced by the respective adjustment amount as a lump sum.

According to Art. 236 (1) of the Customs Code (***CC***), which is applicable to the period at issue, such reimbursement of customs duties paid is possible if the amount paid was not actually due at the time of payment, i.e. the import duty in question was not incurred in the amount paid. The import duty is determined, among other things, by the customs value of the goods concerned. This is to be determined primarily by the "transaction value method" on the basis of the price actually paid or payable for the goods concerned (Art. 29 CC). If the customs value cannot be determined in this way, the transaction value of identical or similar goods must be used. Alternatively, the customs value can be determined deductively or according to a computed value (Art. 30 CC). If none of the

above-mentioned methods is usable in individual cases, the customs value can be determined on the basis of the data available in the EU by other appropriate methods according to the residual method (Art. 31 CC).

If a subsequent correction of the customs value were taken into account, this could in principle lead to a refund of the part of the customs duties that the plaintiff had overpaid on the basis of the original customs value. The Munich Fiscal Court, which was dealing with the action against the negative decision of the authorities, referred this question to the ECJ. The latter refused to take into account subsequent adjustments to the transaction value. After the tax court subsequently rejected the claim, the plaintiff appealed to the BFH.

Decision of the BFH

The BFH rejected the appeal and confirmed the decision of the Fiscal Court. There was no entitlement to a refund, as the customs value could not be adjusted downwards retrospectively. Only the time of acceptance of the customs declarations was, according to the BFH, decisive for determining the customs value within the framework of the transaction value method pursuant to Art. 29 CC, since the import duty was incurred at this time (cf. Art. 214 (1) CC). The determination of the customs value was therefore "a goods-related and effective date-related valuation" (para. 40 of the BFH's judgment). On this reference date, however, it was not certain for the goods imported in the dispute whether an adjustment would be made after the end of the fiscal year and, if so, whether this would be upward or downward. The price adjustments in question could therefore not be considered.

Beyond the statements already found in the ECJ ruling, the BFH also held that this principle applies "in the context of all customs valuation methods," including the residual method under Art. 31 CC (para. 59 of the ruling). This method was, as the BFH noted, equally goods- and date-specific. Art. 31 (1) CC further referred to the Agreement on the Implementation of Art. VII of the General Agreement on Tariffs and Trade of 1994 (***Implementing Agreement***). According to Art. 8 (3) of that Agreement, additions to the price for determining the customs value may only be based on objective and quantifiable data. The BFH held that this rule also applies in the case of deductions (para. 48 of the judgment). At the time of the customs declaration, however, any subsequent price adjustment was precisely not quantifiable and therefore not to be taken into account in the result.

Outlook

Given the ECJ's ruling, the BFH's decision was to be expected with regard to downwardly corrected price adjustments. However, it is also likely to have a considerable impact beyond this constellation. In our opinion, the following three points support this assessment:

- First, the BFH did not differentiate between downward and upward price adjustments. That is, the BFH's main finding – namely that a subsequent price adjustment, which cannot be quantified at the time of acceptance of the customs declaration, is not to be taken into account – applies in case of both downward and upward adjustments. This is also supported by the analogy made by the BFH to Art. 8 (3) of the Implementing Agreement, which, according to its wording, only permits additions to the price on the basis of quantifiable data. This does not seem to be (easily) compatible with a subsequent charge on imports due to initially understated transaction values.

- Secondly, the case decided by the BFH concerned the assertion of a lump-sum price adjustment. In our opinion, the basic considerations of the ruling could also apply if the adjustment is broken down to individual goods. In case the respective correction was not foreseeable at the time of the acceptance of the customs declaration, it should not be relevant for the customs value either.

- Finally, the BFH's decision likely influences the contemporary legal situation under the Union Customs Code (*UCC*). This is because the rules on customs valuation according to Art. 69 et seq. UCC essentially parallel to those of the CC.

Against the backdrop of the BFH ruling, we recommend that any subsequent charge of import duties be reviewed in a timely manner. Companies should check whether it is necessary to adjust the customs process - even using a simplified customs procedure - in order to reduce financial risks. It may also be advisable to file an objection to the levying of duties at the same time as the customs declaration.

However, the last word has probably not yet been spoken in this context. This is particularly true that the World Customs Organization has so far considered the subsequent adjustment of the customs value on the basis of advance pricing agreements to be permissible (see World Customs Organization, Guide to Customs Valuation and Transfer Pricing, 2018, pp. 68 et seq.). Current administrative practice in Germany appears to permit a retroactive adjustment of the customs value only under three conditions:

- First, the price adjustment must have been agreed in principle at the time of acceptance of the customs declaration;

- second, the respective adjustment must be determined in relation to individual goods or groups of goods and not on a lump sum basis; and

- third, the adjustment must be calculated exclusively according to a previously agreed calculation method.

BLOMSTEIN will closely follow further developments in case law and administrative practice. If you have any questions, please do not hesitate to contact Roland M. Stein, Leonard von Rummel and Tobias Ackermann.