Brooklyn Journal of International Law

Volume 25 | Issue 3 Article 12

1-1-1999

The Effect of Customs Reconciliation on Taxable Income

Suzanne I. Offerman

THE EFFECT OF CUSTOMS RECONCILIATION ON TAXABLE INCOME

I. INTRODUCTION

A multinational corporation may have to forego a reduction to its taxable income when it files a reconciliation[1] pursuant to the Customs Modernization Act[2] (Mod Act) to comply with Section 1059A of the Internal Revenue Code.[3] The problem arises when a multinational corporation: (i) files a reconciliation with the United States Customs Service (Customs) that increases the customs value of imported merchandise transferred from a related party;[4] (ii) based its inventory cost of the merchandise for tax purposes on the customs value of the merchandise prior to the reconciliation; and (iii) is forbidden from increasing its inventory costs to reflect the higher price paid because the increase is made after the customs value becomes final.[5]

This Note proposes that both customs and tax statutes, as well as their respective legislative histories, suggest that a multinational corporation should be permitted to upwardly adjust its inventory cost of merchandise for tax purposes to the customs value of the merchandise after the Customs reconciliation is filed. Part II discusses some of the tax law considerations facing a multinational corporation, including transfer pricing, Section 482 of the Internal Revenue Code[6] and Advanced Pricing Agreements.[7] Part III examines some of the customs law considerations encountered by a multinational corporation, including the Customs Valuation Statute,[8] and

---

1. *See* 19 U.S.C. § 1484(b)(2) (1994). See *infra* Part II.C, for a discussion of reconciliation.

2. North American Free Trade Agreement Implementation Act, Pub. L. No. 103-182, §§ 501-06, 107 Stat. 2057, 2149-52 (1993) (codified as amended in scattered sections of 19 U.S.C.) [hereinafter Mod Act].

3. I.R.C. § 1059A (1994). See *infra* Part IV.B, for a discussion of section 1059A.

4. *See* 19 U.S.C. § 1484(b)(2).

5. *See* I.R.C. § 1059A.

6. I.R.C. § 482 (1994). See *infra* Part II.A-B, for a discussion of section 482.

7. *See* Rev. Proc. 96-53, 1996-2 C.B. 375 [hereinafter Rev. Proc. 96-53]. See *infra* Part II.C, for a discussion of Advance Pricing Agreements.

8. 19 U.S.C. § 1401(a) (1994). See *infra* Part III.A, for a discussion of the

the Reconciliation Prototype.[9] Part IV investigates the tension between customs law and tax law. Specifically, it probes the problem that arises when a multinational corporation files a reconciliation with Customs and then wishes to increase inventory costs for tax purposes to reflect the higher price actually paid. Finally, Part V demonstrates that a multinational corporation should not have to forego the tax reduction when it files a reconciliation, and proposes a program, modeled on the APA program, called a Reconciliation Agreement, to help alleviate the problem.

II. TAX LAW CONSIDERATIONS

A. *Transfer Pricing*

Transfer pricing is a term of art that refers to the process that controls how an international corporation[10] prices merchandise when it transfers property[11] between a parent company and its subsidiary.[12] In general, whenever a corporation conducts an international transaction with a related party,[13] it must determine an intercompany transfer price that accu-

---

Customs Valuation Statute.

9. *See* Announcement of National Customs Automation Program Test Regarding Reconciliation, 62 Fed. Reg. 5673 (1997); Revised National Customs Automation Program Test Regarding Reconciliation, 63 Fed. Reg. 6257 (1998); Modification of National Customs Automation Program Testing Regarding Reconciliation, 63 Fed. Reg. 44,303 (1998). See *infra* Part III.C, for a discussion of the Reconciliation Prototype.

10. For purposes of this Note, international corporation, multinational corporation, related parties and controlled parties are used interchangeably.

11. *See* Roland Ryan Davis, *The New Transfer Pricing Tax Regulations: Now That They're Here What Should You Do?*, 10 SANTA CLARA COMPUTER & HIGH TECH. L.J. 195, 196 n.2 (1994). Tangible property includes inventory and goods that are transferred between related companies for the manufacturing or the sale of a product. *Id.* Intangible property includes intellectual property rights and "[o]ther similar items . . . if it derives its value not from its physical attributes but from its intellectual content or other intangible properties." 26 C.F.R. § 1.482-4(b)(6) (1999).

12. *See* William W. Chip, *Tax Officials Will Target Intercompany Transfers: Multinationals Must Defend The Prices They Set, But The Method Of Calculation May Be Disputed*, NAT'L L.J., May 4, 1998, at C9; Karl William Viehe & Donald T. Williamson, *Tax Issues in Planning Transnational Transactions: The U.S. Perspective*, 2 TRANSNAT'L LAW. 93, 110 (1989).

13. Related parties are companies that are controlled directly or indirectly by the same interests. For example, if Widget Company, USA, and Widget Company, Canada, are subsidiaries of Widget Parent Company, Japan, then all three companies are related parties under section 482.

rately allocates income between the related parties.[14] It is difficult to establish an acceptable intercompany transfer price as "[i]nternational firms must consider many variables in establishing the appropriate transfer price."[15] Tax consequences and Customs duty rates are among those factors.[16]

Although the transfer price set between related parties is largely an economic decision "serving to allocate profits between exporting and importing firms,"[17] it has developed into a legal decision as well. Primarily because "[t]ransfer prices divide taxable income among countries in which a multinational operates,"[18] an international corporation must ensure that it complies with domestic and foreign tax laws as well as international tax treaties.[19] In general, tax officials use transfer prices to allocate the income of one corporation, i.e., a parent corporation, to the income of another corporation, i.e., a subsidiary corporation.[20] More specifically, the Internal Revenue

---

14. *See* Michael Avramovich, *Intercompany Transfer Pricing Regulations Under Internal Revenue Code Section 482: The Noose Tightens on Multinational Corporations*, 28 J. MARSHALL L. REV. 915, 922-29 (1995); Kevin K. Leung, *Taxing Global Trading: An Appropriate Testing Ground For Formula Apportionment?*, 1 MINN. J. GLOBAL TRADE 201, 203, 209 (1992). Income allocation is important as it determines whether a parent corporation or a subsidiary corporation is liable for the tax on that income.

15. Avramovich, *supra* note 14, at 929 n.70.

16. See R. Tang, *Transfer Pricing in the 1990s*, 73 MGMT. ACCT. 22, 22-26 (1992), *reprinted in* TRANSNATIONAL CORPORATIONS & MANAGEMENT DIVISION, UNITED NATIONS, 14 TRANSNATIONAL CORPORATIONS: TRANSFER PRICING AND TAXATION 314-15 (Sylvain Plasschaert & John H. Dunning eds., 1993), for a 1990 survey of the 10 most important "environmental variables of international transfer pricing" for Fortune 500 companies. *See also Multinationals' top tax issue: transfer pricing*, J. COMM., Nov. 12, 1999, at 4 (reporting that according to an Ernst & Young survey, transfer pricing is the most important tax issue for multinational corporations).

17. L. Eden, *The Micro-economics of Transfer Pricing*, *in* MULTINATIONALS AND TRANSFER PRICING 13-46 (A.M. Rugman & L. Eden eds., 1985), *reprinted in* TRANSNATIONAL CORPORATIONS & MANAGEMENT DIVISION, UNITED NATIONS, 14 TRANSNATIONAL CORPORATIONS: TRANSFER PRICING AND TAXATION 151 (Sylvain Plasschaert ed., 1994).

18. Chip, *supra* note 12, at C9.

19. *See* Sylvain Plasschaert, *Introduction: Transfer Pricing and Taxation*, *in* TRANSNATIONAL CORPORATIONS & MANAGEMENT DIVISION, UNITED NATIONS, 14 TRANSNATIONAL CORPORATIONS: TRANSFER PRICING AND TAXATION 1, 181 (Sylvain Plasschaert & John H. Dunning eds., 1993). "[T]he pervasiveness and the legal technicalities of the tax variables in the realm of transnational business focus special attention on them." *Id.*

20. *See* Congressional Research Service Report for Congress, *Transfer Pricing and Taxes: Background and Issues*, 94-823e (Oct. 19, 1994) *available in* 1994 WL

Service (IRS) utilizes transfer prices to determine what income of an international corporation is taxable, deferred, exempt or credited based on where the income of a parent corporation and its subsidiary corporations is derived.[21]

From an IRS perspective, international corporations tend to fall into two categories: (i) U.S. corporations with foreign subsidiaries;[22] and (ii) foreign corporations with U.S. subsidiaries.[23] First, when a U.S. corporation establishes a subsidiary operating overseas, income derived from the U.S. parent is taxed differently from income earned by the foreign subsidiary even though they are related parties.[24] The U.S. parent corporation is subject to U.S. federal income tax regardless of where its income is earned and so, "its foreign income is subject to U.S. taxation as it is earned."[25] However, if the U.S. parent corporation's non-U.S. income falls within the foreign government's tax jurisdiction, then the amount collected by the foreign government may be credited against the amount owed to the United States.[26] On the other hand, the income of the foreign subsidiary corporation is tax deferred until it becomes part of the U.S. parent's income.[27] Thus, when the IRS examines the activity between a U.S. parent corporation and its foreign subsidiary, the IRS uses the international corporation's transfer prices to determine what income is covered by the "deferral principle" and what income is not.[28]

Second, when a foreign corporation establishes a U.S. subsidiary, there are two tax possibilities for the parent corporation depending on whether the U.S. subsidiary is chartered in the United States or abroad. If the subsidiary is incorporated in the United States, as opposed to the parent corporation

797728, at *3 (maintained by the Library of Congress) [hereinafter C.R.S. Report]. Although it appears as if the role of transfer pricing is to distinguish the origin of a corporation's income, it is actually the Internal Revenue Code's "source rules" that determine domestic from foreign income for a single corporation. *Id.*

21. *See id.*

22. *See id.*

23. *See id.*

24. *See id.*

25. *Id.*

26. *See* C.R.S. Report, *supra* note 20, at 3. The U.S. government credits the amount of foreign taxes in order to prevent double taxation on the same income. *See id.*

27. *See id.*

28. *See id.*

establishing a U.S. branch incorporated abroad, then the entire income of the U.S. subsidiary corporation is subject to U.S. federal income tax.[29] However, if the U.S. company is "a branch of a foreign-chartered parent corporation, only the part of the parent's income that is from U.S. sources is subject to U.S. taxes."[30] When it is taxable, the IRS uses the international corporation's transfer price to determine what income is outside the U.S. tax jurisdiction and consequently, exempt from tax and what income is subject to U.S. tax.[31]

Whether the international corporation is a U.S. corporation with foreign subsidiaries or a foreign corporation with U.S. subsidiaries, transfer prices directly influence the amount owed in federal income taxes to the U.S. government.[32] Therefore, because transfer prices distinguish taxable income from non-taxable income, both the IRS and the international corporation operating in the United States have an interest in the manner in which the transfer price is calculated.[33]

29. *See id.*

30. *Id.*

31. *See id.*

32. *See* C.R.S. Report, *supra* note 20, at 3. Transfer pricing "can . . . reduce the net, overall tax bill [in the United States], as the loss of after-tax profits, suffered by the more heavily-taxed affiliate, would be more than offset by the lower tax paid in the country with the comparatively lower tax burden." Plasschaert, *supra* note 19, at 1.

33. *See* C.R.S. Report, *supra* note 20, at 3; C.R.S. Report for Congress, *International Tax Provisions of the 1993 Budget Act*, (Oct. 6, 1993) 1993 WL 739669, *2-3.

B. *I.R.C. § 482*[34] *and Income Allocation*

Section 482 of the Internal Revenue Code grants the Secretary of the Treasury Department the authority to make adjustments to the way an international corporation allocates its income between a parent corporation and its subsidiary.[35] It was enacted specifically to place related corporations on par with unrelated corporations by ensuring that related party transactions generate the same taxable income as though the transaction was not controlled.[36] Thus, it prevents the loss of federal revenue that may occur if a related corporation sets a transfer price not at arm's length, thereby reducing U.S. taxable income.[37] The IRS determines whether the transfer price in a related party transaction realizes "the true taxable income" of the parties.[38] If it does not, the IRS adjusts the income allocated to the "wrong" party to the "correct" party, assuring that the appropriate party is responsible for paying its taxable U.S. income.[39] For example,[40] Subsidiary Corporation, S, sells widgets to its Parent Corporation, P, at $10 per widget and to an unrelated corporation, U, at $4 per widget.

---

34. Section 482 of the Internal Revenue Code, entitled "Allocation of income and deductions among taxpayers" reads:

> In any case of two or more organizations, trades, or businesses (whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests, the Secretary may distribute, apportion, or allocate gross income, deductions, credits, or allowances between or among such organizations, trades, or businesses, if he determines that such distribution, apportionment, or allocation is necessary in order to prevent evasion of taxes or clearly to reflect the income of any of such organizations, trades, or businesses. In the case of any transfer (or license) of intangible property (within the meaning of section 936(h)(3)(B)), the income with respect to such transfer or license shall be commensurate with the income attributable to the intangible.

I.R.C. § 482 (1994).

35. *See id.*

36. *See* 26 C.F.R. § 1.482-1(a)(1) (1999).

37. *See id.*

38. *Id.* For the purposes of section 482, true taxable income is defined as "the taxable income that would have resulted had it dealt with the other member or members of the group at arm's length. It does not mean the taxable income resulting to the controlled taxpayer by reason of the particular . . . transaction . . . the controlled taxpayer chose to make (even though such . . . transaction . . . is legally binding upon the parties thereto)." *Id.* § 1.482-1(i)(9).

39. *See id.* § 1.482-1(a)(1).

40. Although this example does not reflect the complexities involved in income allocation, it was included simply to make a difficult concept clearer.

Because P paid $6 more than U, P's inventory cost basis for the widgets is higher than U's, and as such, P's U.S. taxable income is lower than U's. However, since there is a presumption that unrelated party transactions are at arm's length, (S wishes to sell the widgets at the highest price the market will bear, while U wishes to buy the widgets at the lowest price it can), the transfer price between P and S is not at arm's length (it is $6 higher). Therefore, the IRS may upwardly adjust P's income by $6, which is the amount P's income would have been if P and S were unrelated.

The federal regulations written for Section 482 explain how the IRS and the taxpayer ensure that the related parties allocate their taxable incomes correctly.[41] An international corporation's taxable income is accurate when it is based on a transfer price that fosters an arm's length result.[42] A related party transaction satisfies the arm's length standard when the income derived from a controlled transaction is the same as though it was derived from an uncontrolled transaction.[43] The regulations provide an array of methods that the taxpayer may use to show that its related party transaction was an arm's length transaction. Although there is no preferred method,[44] the regulations dictate that "[t]he arm's length result of a controlled transaction must be determined under the method that, under the facts and circumstances, provides the most reliable measure of an arm's length result."[45] This is known as the "best method" rule.[46] To discover the best transfer pricing method, a taxpayer applies the comparability factors[47] set forth in the regulations to determine taxable income derived from a transfer of tangible or intangible property between related parties.[48]

41. *See* 26 C.F.R. § 1.482-1(a)(2)-(a)(3).
42. *See id.* § 1.482-1(b)(1).
43. *See id.*
44. *See id.* §§ 1.482-1(b)(2)(ii), (c)(1).
45. *Id.* § 1.482-1(c)(2).
46. *See id.*
47. *See id.* § 1.482-1(d)(i)-(v). Among the comparability factors "that could affect prices or profits in arm's length dealings," and thus, should be evaluated are functions, contractual terms, risks, economic conditions and property or services. *Id.* § 1.482-1(d)(1).
48. *See id.* § 1.482-1(c)(2)(i).

C. Advance Pricing Agreements

Aware of the difficulty that related corporations face in complying with Section 482 and the potential for weighty penalties,[49] the IRS issued a revenue procedure explaining how related party taxpayers may obtain an advance pricing agreement (APA)[50] "covering the prospective determination and application of transfer pricing methodologies (TPM) for international transactions."[51] An APA is a binding agreement[52] between a related corporation and the IRS that results in the determination of "the TPM to be applied to any . . . allocation of income" between related parties.[53] A related party that enters into an APA gains assurance from the IRS that it has complied with the best method rule of transfer pricing[54] and has satisfied the arm's length standard of the regulations.[55]

A related party taxpayer that wishes to obtain an APA may request a pre-filing conference with the APA department of the IRS.[56] The pre-filing conference enables the taxpayer to decide if an APA is a worthwhile endeavor by preliminarily suggesting its applicability to the taxpayer's situation.[57] The taxpayer, who may remain anonymous,[58] submits background materials,[59] relevant tax data,[60] pertinent financial statistics,[61] TPM information[62] and summaries of the applicable laws, treaties or regulations.[63] The taxpayer submits these "[s]pecific factual items . . . to establish the arm's length basis

49. *See* I.R.C. § 6621(c) (1994).
50. *See* Rev. Proc. 96-53, *supra* note 7, at 375.
51. *Id.* at 375, § 1.
52. *See id.* at 383, § 10.
53. *Id.* at 375, § 1.
54. See *supra* Part II.B, for a discussion of the best method rule of section 482.
55. *See* Rev. Proc. 96-53, *supra* note 7, at 383, § 10.
56. *See id.* at 376, § 4.01.
57. *See id.*
58. *See id.* at 376, § 5. Not only may a taxpayer remain anonymous, but all information remains confidential under section 6103. *See* Cym H. Lowell & Jack P. Governale, *A Guide to APA Program Procedures From Prefiling Conference to Administering the Agreement*, 9 J. INT'L TAX'N 24 (1998).
59. *See* Rev. Proc. 96-53, *supra* note 7, at 377, § 5.03.
60. *See id.*
61. *See id.*
62. *See id.* at 376, § 5.
63. *See id.* at 377, § 5.03.

of the proposed TPM under, [Section] 482"[64] and any "critical assumptions" made in determining the proposed TPM.[65] Although determinations made during a pre-filing conference are not binding, they suggest what information will be relevant for an APA, indicate if the proposed TPM complies with the various tax provisions, advise the taxpayer about the possibility of a bilateral APA and schedule future meetings.[66]

Upon request for an APA and after all the information is submitted, an APA team is formed[67] "to negotiate and recommend an agreement, and [when a bilateral APA is desired], to recommend in consultation with the taxpayer a competent authority negotiating position, to the Associate Chief Counsel (International)."[68] After the APA is formed, it meets with the taxpayer to choose a "Case Plan and Schedule"[69] that sets forth the parameters on the information necessary to settle an APA and the deadlines for "case milestones."[70] Although the taxpayer and the APA team should attempt to comply with the time frames set up during the initial meeting,[71] either may bring the APA process to a halt.[72] The IRS may also request

---

64. *Id.* at 377, § 5.04.

65. *See id.* at 378, § 5.07. "A critical assumption is any fact . . . related to the taxpayer, a third party, an industry, or business and economic conditions, the continued existence of which is material to the taxpayer's proposed TPM [e.g.,] . . . a particular mode of conducting business operations." *Id.* Because critical assumptions are fact based, they have a direct effect on the chosen transfer price and so must be accounted for in the APA. *See* Lowell & Governale, *supra* note 58, at 29.

66. *See* Rev. Proc. 96-53, *supra* note 7, at 376, § 4.01.

67. *See id.* at 380; § 6.02. The team comprises of representatives of the Office of Associate Chief Counsel (International), the District Counsel, and at times, the Appeals authority. The U.S. competent authority is part of the team when the taxpayer requests a bilateral APA. *See id.* at 380-81, § 6.04.

68. *Id.* at 381, § 6.05(6).

69. *Id.* at 381, § 6.05(1).

70. *Id.* Case milestones are:

> (a) submission of any necessary additional information by the taxpayer; (b) evaluation of the information by the government; (c) negotiation of a recommended agreement or competent authority negotiating position; and (d) presentation of the recommended agreement or competent authority negotiating position in writing to the Associate Chief Counsel (International).

Id.

71. *See* Rev. Proc. 96-53, *supra* note 7, at 381, § 6.05(4).

72. *See id.* at 381, § 6.06-07. A taxpayer may only withdraw the request before the APA is executed. The IRS may decline to execute an APA, even after the APA request was accepted. *Id.*

that the taxpayer provide an independent expert to evaluate the proposed TPM and give his or her non-binding opinion.[73] During the negotiations of the APA, the taxpayer may make a "rollback request"[74] to use the TPM in the APA "to resolve transfer pricing issues for years prior to the earliest year covered by the APA."[75]

Not only are APAs used to ensure compliance with U.S. tax laws, but also to prevent double taxation of related party transactions.[76] Double taxation occurs when a corporation is taxed on the same income in different taxing jurisdictions.[77] Thus, when a related party is "entitled to seek relief under the mutual agreement provision of a tax treaty between a foreign country and the United States, . . . the competent authorities may enter into agreements concerning the APA,"[78] creating a bilateral APA.[79] Bilateral APAs are usually favored over unilateral APAs as they are more efficient, "minimiz[ing] taxpayer and governmental uncertainty and administrative cost."[80] A multinational corporation avoids double taxation via a bilateral APA because the taxpayer, the IRS and the foreign tax authority agree how a multinational's income should be allocated and what part of its income is subject to U.S. taxes and what part of its income is subject to foreign taxes.[81]

When a taxpayer wishes to enter into a bilateral agreement, it should simultaneously apply for an APA with the foreign tax authority and the IRS so that the foreign tax au-

73. *See id.* at 383, §§ 9.01, 9.04. Although the taxpayer pays for the expert, both the taxpayer and the IRS must agree on the expert retained for the negotiation.

74. *Id.* at 382, § 8.

75. *Id.* at 382, § 8.01.

76. *See id.* at 381, § 7.02.

77. *See* BLACK'S LAW DICTIONARY 491 (6th ed. 1990).

78. Rev. Proc. 96-53, *supra* note 7, at 381, § 7.01.

> '[C]ompetent authority' includes the U.S. and foreign competent authorities under income tax treaties to which the U.S. is a party, and also includes the Assistant Commissioner (International) acting with respect to a possession tax agency described in Rev. Proc. 89-8, as well as a designated possession tax official within the meaning of that revenue procedure.

Id. at § 5.10.

79. When the APA is among the taxpayer, the IRS and two or more foreign tax authorities, it is called a multilateral APA. When the APA is between the taxpayer and the IRS, it is called a unilateral APA.

80. Rev. Proc. 96-53, *supra* note 7, at 382, § 7.07.

81. *See id.* at, 381-82, § 7.

thority is included in the APA negotiation process as early as possible.[82] The IRS endeavors to get the foreign tax authority to keep the taxpayer's data confidential and to "agree to a mutual exchange of information."[83] These goals are set "[i]n order to provide timely clarification of factual issues, minimize the potential for miscommunication, and assist in development of a multiple party agreement on a timely basis."[84] However, as there are no guarantees that an agreement will be reached among the parties, the taxpayer may withdraw the request for an APA or negotiate a unilateral APA with the IRS.[85]

Whether a taxpayer is a party to a unilateral or a bilateral APA, it must file an annual report for each year covered by the APA to show that it complied with the terms of the APA.[86] The annual report should reflect the "taxpayer's actual operations for the year . . . requests to renew, modify or cancel the APA, and must describe any compensating adjustments made."[87] In some instances, the IRS requires documentation from the taxpayer, establishing that the "critical assumptions" upon which the APA was based remain accurate.[88] In all cases, the taxpayer is responsible for keeping records so that the IRS may examine them if necessary.[89]

There are a few situations when the taxpayer and the IRS may revise the APA. First, when a TPM agreed to in an APA results in taxable income that is not within the anticipated range of operating results, the APA is revisable.[90] In accordance with the flexible APA negotiation process, the APA allows "the parties to make a compensating adjustment to bring the results to an agreed upon point within the described range."[91] Second, when a critical assumption reflected in the APA proves to be inaccurate, the APA can be changed upon the consent of the IRS and the taxpayer.[92] Third, when there is a

---

82. *See id.* at 381, § 7.01. When applicable, the IRS will try to get the foreign tax authority to attend the pre-filing conference.

83. *Id.* at 382, § 7.05.

84. *Id.* at 381, § 7.01.

85. *See id.* at 381, § 7.02.

86. *See id.* at 383, § 11.01(1).

87. *Id.*

88. *Id.* See Rev. Proc. 96-53, *supra* note 65, for a definition of a critical assumption.

89. *See* Rev. Proc. 96-53, *supra* note 7, at 384, § 11.04.

90. *See* Lowell & Governale, *supra* note 58, at 47.

91. Rev. Proc. 96-53, *supra* note 7, at 383-84, § 11.02(1).

92. *See id.* at 385, § 11.07(1). When an underlying critical assumption is not

change in law or treaty "that changes the Federal income tax treatment of any matter covered by the APA, . . . [t]he parties may revise the APA . . . to reconcile it with the new law or treaty provision."[93]

III. CUSTOMS LAW CONSIDERATIONS

A. *The Customs Valuation Statute*[94]

The Customs Valuation Statute sets forth the manner in which Customs arrives at the dutiable value of imported merchandise.[95] The U.S. Customs Valuation Statute conforms with international standards of appraisement[96] under the GATT Valuation Agreement.[97] Generally, the value of imported goods must result from an arm's length transaction between the buyer and the seller.[98] Specifically, the statute provides different methods, in order of preference, for valuing imported merchandise.[99]

Transaction value is the preferred and most common method of appraisement of imported merchandise for Customs purposes.[100] According to Section 1401, "[t]he transaction value of imported merchandise is the price actually paid or payable for the merchandise when sold for exportation to the United States, plus"[101] statutory additions[102] and less statutory deductions.[103] Statutory additions are added only if they are not already included in the selling price.[104] Similarly,

---

realized in a bilateral APA, the foreign tax authority must also consent to the changes. If the foreign tax authority does not agree to the revised APA, then the taxpayer may either use the original APA, revise the APA again, or cancel the APA. *See id.* at 385, § 11.07(4)

93. *Id.* at 385-86, § 11.09.

94. 19 U.S.C. § 1401(a) (1994).

95. *Id.*

96. The Trade Agreements Act of 1979, 93 Stat. 194, Title II.

97. Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade, April 12, 1979 *in* URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS: GENERAL AGREEMENT ON TARIFFS AND TRADE 171 (1994).

98. *See id.* at General Introductory Commentary, 171.

99. *See* 19 U.S.C. § 1401(a)(1)(A)-(F).

100. *See* Committee on Ways and Means, 105th Cong., 1st Sess., OVERVIEW AND COMPLICATION OF U.S. TRADE STATUTES—THE TRADE GREEN BOOK (Comm. Print 1997) [hereinafter OVERVIEW].

101. 19 U.S.C. §1401(b)(1).

102. *Id.* § 1401(b)(1)(A)-(E).

103. *Id.* § 1401(b)(3)(A)-(4)(B).

104. *See id.* § 1401(b)(1)(E)

statutory deductions are deducted only if they are not already excluded from the selling price.[105]

First, the statutory additions to the transaction value are "packing costs incurred by the buyer;"[106] "selling commissions incurred by the buyer;"[107] "the value . . . of any assist;"[108] "royalty or license fee[s] . . . that the buyer is required to pay . . . to the seller;"[109] and "the proceeds of any subsequent resale, disposal, or use of the imported merchandise that accrue . . . to the seller."[110] For example, when the buyer or importer provides certain items for free or at a reduced price to the seller "for use in connection with the production or the sale . . . of the merchandise," the buyer or importer has provided an assist.[111] Assists include items that the seller would have had to provide at the seller's own cost if the buyer did not supply them.[112] There are two ways to value an assist depending upon whether the assist was purchased from an unrelated seller or was produced by the buyer or a party related to

---

105. *See id.*

106. *Id.* § 1401(b)(1)(A).

107. *Id.* § 1401(b)(1)(B). Selling commissions are payments made by the buyer to the seller's agent who is a related party to the seller or who works for the seller. See Rosenthal-Netter, Inc. v. U.S., 679 F. Supp. 21 (Ct. Int'l Trade 1988), for a discussion of the difference between selling commissions and buying commissions.

108. 19 U.S.C. § 1401(b)(1)(C). Assists are "(i) [m]aterials, components, parts, and similar items incorporated in the imported merchandise; (ii) [t]ools, dies, molds, and similar items used in the production of the imported merchandise; (iii) [m]erchandise consumed in the production of the imported merchandise; (iv) [e]ngineering, development, artwork, design work, and plans and sketches that are undertaken . . . [outside] the United States and are necessary for the production of the imported merchandise" unless they are performed by an agent of the buyer who is domiciled within the United States and are "incidental to other engineering, development, artwork, design work, or plans or sketches . . . undertaken within the United States." *Id.* § 1401(h)(1)(A)-(B).

109. *Id.* § 1401(b)(1)(D).

110. *Id.* § 1401(b)(1)(E).

111. *Id.* § 1401(h)(1)(A).

112. The U.S. Customs Service provides the following as an example:

> A U.S. buyer supplied molds free of charge to the foreign seller. The molds were necessary to manufacture merchandise for the U.S. importer. The U.S. importer had some of the molds manufactured by a U.S. company and other manufactured in a third country . . . [The mold] is an addition required to be made to transaction value.

U.S. Customs Service, *What Every Member of the Trade Community Should Know About: Customs Value: Customs Value* (U.S. Customs Service) May 1998, at 7 (visited Nov. 9, 1999) <http:\\www.customs.treas.gov\imp-expl\comply\value96.htm>

the buyer.[113] If the assist was purchased from an unrelated seller, then the value of the assist is equal to the cost of purchase.[114] If the assist was produced by the buyer or a party related to the buyer, then the value of the assist is equal to the cost of production.[115]

Second, the statutory deductions from the transaction value are "cost[s] . . . incurred for . . . the construction, erection, assembly, or maintenance of, or the technical assistant provided[116] [for] . . . or the transportation of the merchandise after [its] importation [into the United States];"[117] international transportation and insurance costs[118] and any customs duties or federal taxes paid.[119] For example, the price of U.S. inland freight would be excluded from the transaction value.

B. *Customs Value and Related Party Transactions*

Although transaction value is the favored appraisement method and related parties are not automatically disqualified from establishing an acceptable transaction value, the statute limits when transaction value may be used in related party transactions.[120] The limitation allows Customs to evaluate the related party transaction to ensure that the transfer price meets commercial standards and accurately reflects the value of the imported merchandise.[121]

The statute provides that "[t]he transaction value between a related buyer and seller is acceptable [if the transaction value meets either] the circumstances of the sale"[122] test or one of the test values. The tests validate the transaction value of merchandise imported to a related party, ensuring the transfer price was derived from an arm's length transaction. A transfer price meets the circumstances of the sale test when the selling price: (i) would be the same to an unrelated buyer;

113. *See* 19 U.S.C. §1401(h)(1)(C).
114. *See id.* § 1401(h)(1)(C)(i).
115. *See id.* § 1401(h)(1)(C)(ii).
116. *Id.* § 1401(b)(3)(A)(i).
117. *Id.* § 1401(b)(3)(A)(ii).
118. *See id.* § 1401(b)(4)(A).
119. *See id.* § 1401(b)(3)(B).
120. *See id.* § 1401(b)(2)(B)-(B)(ii).
121. *See* Transfer Pricing: Related Party Transaction, 58 Fed. Reg. 5446-47 (1993).
122. 19 U.S.C. § 1401(b)(2)(B).

(ii) is within industry standards; (iii) covers all costs and procures a profit reflective of the corporation's overall profit.[123]

Alternatively, a test value may also ensure that the transaction value of merchandise in a related party transaction is accurate. A test value may be used to evaluate a related party transfer price when the comparison merchandise is exported at approximately the same time as the related party merchandise[124] and the test value chosen served as an accepted appraised value in a prior transaction.[125] In order of preference, the test values are the transaction value of the imported merchandise, identical merchandise from the same country sold to an unrelated buyer,[126] the transaction value of similar merchandise from the same country sold to an unrelated buyer,[127] deductive value or computed value of the same merchandise[128] and deductive value or computed value of similar merchandise.[129]

If the appraised value of the merchandise transferred in a related party transaction "closely approximates" the appraised value of the same or similar merchandise sold in an unrelated party transaction, then the price was made at arm's length and consequently, will be accepted as the transaction value.[130] The deductive value method determines valuation by starting with the selling price in the United States and making statutory deductions.[131] The computed value method determines

---

123. *See id.* These examples demonstrate that the price has not been influenced by the relationship, however, they are not exclusive. LESLIE A. GLICK, GUIDE TO UNITED STATES CUSTOMS AND TRADE LAWS AFTER THE CUSTOMS MODERNIZATION ACT 41 (2nd ed. 1997). Other factors that help Customs determine the circumstances of the sale are whether "invoices are regularly sent and paid within commercially accepted time periods by check . . . [and whether] the importer or manufacturer maintains its books and records in accordance with generally accepted accounting principles." *Id.* at 41-42.

124. *See* 19 U.S.C. § 1401(b)(2)(B).

125. *See* Transfer Pricing, *supra* note 121, at 5446.

126. *See* 19 U.S.C. §1401(b)(2)(B)(i); Transfer Pricing, *supra* note 121, at 5446.

127. *See* Transfer Pricing, *supra* note 121, at 5446.

128. *See* 19 U.S.C. §1401(b)(2)(B)(ii); Transfer Pricing, *supra* note 121, at 5446. An importer may chose to use computed value in place of deductive value. Deductive value cannot be used if the transaction involves an assist. *See* 19 U.S.C. §1401(d)(3)(D)-(E).

129. *See* Transfer Pricing, *supra* note 121, at 5446; 19 U.S.C. § 1401(d)(3)(D)-(E).

130. *See* 19 U.S.C. § 1401(c)(1).

131. *See id.* § 1401(d)(3)(A)(i)-(v). The statutory deductions include "commission[s] . . . or [usual] . . . general expenses;" "costs of transportation and insur-

valuation by adding the processing costs, including: labor and materials; an industry accepted profit and general expenses; assists; and packing costs.[132] Adjustments to the price are necessary when there is a difference between the comparison merchandise and the related party merchandise in "commercial levels,"[133] "quantity levels,"[134] statutory additions to the price actually paid or payable,[135] or any difference in costs incurred by the unrelated buyer that was not paid by the related buyer.[136] Finally, if none of the specified methods are feasible, then the imported merchandise requires "a value that is derived from the methods" previously described.[137]

C. *Reconciliation*[138] *and the Customs Modernization Act*[139]

Valuation is an integral part of the entry process of merchandise imported into the United States as Customs will not liquidate entries[140] without the proper appraised value.[141] However, there are times when an importer may not have all the information available pertaining to the value of the merchandise until after entry. For example, Domestic Corporation (D) contracts to buy widgets from Foreign Corporation (F). The invoice value is based on standard costs and consequently, D does not know what final cost will result.[142] Reconciliation

---

ance incurred with respect to international shipments;" "customs duties and other Federal taxes;" and "the value added by the processing of the merchandise after importation." *Id.*

132. *See id.* § 1401(e)(1)(A)-(D).

133. *Id.* § 1401(b)(2)(C)(i)-(iv).

134. *Id.*

135. *See id.*

136. *See id.*

137. *Id.* § 1401(f). This value has been referred to as the "surprise value" because it is difficult to predict. Robert J. Leo, *Impact of the Asian Crisis on Transnational Legal Practice: A Primer on Pricing Issues for Counsel to Importers and Exporters,* 12 INT'L L. PRACTICUM 105, 106 (1999).

138. *See* 19 U.S.C. § 1484(b)(2).

139. Mod Act, *supra* note 2, §§ 501-06.

140. *See* U.S. CUSTOMS SERVICE, IMPORTING INTO THE UNITED STATES: A GUIDE FOR COMMERCIAL IMPORTERS 46 (1998). Liquidation is the point at which Customs decides the final rate and amount of duty for merchandise entering the United States and posts a notice of liquidation on the Customs bulletin board. *Id.*

141. *See* OVERVIEW, *supra* note 100, at 30. Valuation is necessary to assess the Customs duty as most duty is *ad valorem.*

142. *See* U.S. CUSTOMS SERVICE RECONCILIATION TEAM, U.S. CUSTOMS SERVICE, ACS RECONCILIATION PROTOTYPE OPERATIONS HANDBOOK: A GUIDE TO COMPLIANCE, VERSION 1.0F 4 (1998).

allows D to enter the widgets into the United States, despite the unknown final cost of the widgets, on the condition that D provides the information on the final cost of the widgets when it is known. Thus, a reconciliation permits an importer to "file[] their entry summaries with the best available information . . . with the mutual understanding"[143] that certain elements remain outstanding but will be reconciled at a later date.[144] A reconciliation allows Customs to "[m]ake progress under this key component of the Mod Act, [e]stablish uniformity in an area which has traditionally operated under a variety of procedures, [p]rovide financial safeguards, and [i]nstitute a legal mechanism for reconciling entries."[145]

On October 1, 1998, Customs implemented the Automated Commercial System Reconciliation Prototype[146] (Prototype) as the sole way to reconcile entry summaries. Scheduled to run approximately two years, the Prototype limits reconciliation to subsequent changes in value,[147] HTS 9802 Value,[148] certain classification situations[149] and NAFTA eligibility.[150] The Prototype sets forth two ways to notify Customs of the need for a reconciliation and two methods an importer may use to file a reconciliation.[151]

First, an importer notifies Customs "electronically via ABI [Automated Broker Interface] [which] inputs an indicator on all entries which are subject to reconciliation."[152] An importer may choose between electronically flagging[153] the entry sum-

143. U.S. CUSTOMS SERVICE, *supra* note 140, at 4.

144. *See* 19 U.S.C. § 1484(b)(1) (1994).

145. U.S. CUSTOMS SERVICE, *supra* note 140, at 3.

146. *See* U.S. CUSTOMS SERVICE RECONCILIATION TEAM, *supra* note 142.

147. See discussion *supra* Part II.A, for a discussion on Customs valuation.

148. U.S. CUSTOMS SERVICE, ACS RECONCILIATION PROTOTYPE OPERATIONS HANDBOOK: A GUIDE TO COMPLIANCE, VERSION 1.0F 11 (1998)

149. Classification is the first step in determining the tariff rate of imports. Details on classification are beyond the scope of this article. See GLICK, *supra* note 123, for a brief overview on classification. For a more detailed explanation, see OVERVIEW, *supra* note 100.

150. *See* Mod Act, *supra* note 2, §§ 501-06. Entries reconciled pursuant to NAFTA are allowed 12 months instead of 15 months to file a reconciliation. *See* 19 U.S.C. § 1484(b)(1) (1994).

151. Customs refers to this as the "*menu approach* to Reconciliation." *See* Revised National Customs Automation Program Test Regarding Reconciliation, *supra* note 9, at 6259.

152. Modification of National Customs Automation Program Testing Regarding Reconciliation, *supra* note 9, at 44,304.

153. Flagging refers to the importer's notice of intent to file a Reconciliation.

maries individually, i.e., entry by entry, or by blanket application, i.e., all entries for a specified period.[154] Second, the information unknown at the time of entry must be filed on a reconciliation within 15 months of the earliest entry summary date.[155] At that time, the importer files a reconciliation to the importer's assigned Customs port[156] via the entry-by-entry method or the aggregate method.

The entry-by-entry method is a "reconciliation in which the revenue adjustment is specifically provided for each affected entry summary."[157] When an importer uses the entry-by-entry method, the importer calculates the new duty amount for each flagged entry separately and in detail when the final cost of the imported merchandise is known.[158] Because the importer provides details, the entry-by-entry method is appropriate when there is an increase, decrease or no change in the duty on the imported merchandise.[159]

On the other hand, the aggregate method is a "reconciliation filed with summarized data showing reconciled adjustments at an aggregate level."[160] When an importer uses the aggregate method,[161] the importer calculates the new duty amount for all flagged entries together instead of for each entry summary individually.[162] Like the entry-by-entry method, the aggregate method is applicable when there is an increase, decrease or no change in the duty on the imported merchandise. However, if an importer uses the aggregate method to report a decrease in duty owed, the importer must waive its right to claim a refund of those duties later.[163]

See Revised National Customs Automation Program Test Regarding Reconciliation, *supra* note 9, at 6259.

154. *See* sources cited *supra* note 9.

155. *See* Revised National Customs Automation Program Test Regarding Reconciliation, *supra* note 9, at 6257.

156. *See* Modification of National Customs Automation Program Testing Regarding Reconciliation, *supra* note 9, at 44304. Although the entry summaries for imported merchandise may be filed at any port, the reconciliation may only be filed at specific ports. *Id.*

157. Revised National Customs Automation Program Test Regarding Reconciliation, *supra* note 9, at 6258.

158. *See id.*

159. *See id.* at 6259.

160. *Id.* at 6258.

161. *See* sources cited *supra* note 9.

162. *See* Revised National Customs Automation Program Test Regarding Reconciliation, *supra* note 9, at 6260.

163. *See* Modification of National Customs Automation Program Test Regarding

Finally, when an importer files a reconciliation, it must comply with the "reasonable care" standard set forth in the Mod Act,[164] "shifting more of the legal burden to the importing community."[165] Thus, when an importer declares value at entry, the importer estimates the declared value to the best of the importer's ability, rather than use estimated and inaccurate information[166] because "reconciliation cannot be used to defer (or serve as a substitute for) compliance obligations."[167]

IV. THE TENSION BETWEEN CUSTOMS LAW AND TAX LAW

A. *High Value for Taxes and Low Value for Customs*

When a multinational corporation imports goods for sale in the United States, it is subject to Customs duty on the value of the goods imported[168] and federal income tax on the profits from the sale of those goods.[169] Because duty is primarily *ad valorem*, an importer seeks a low value for the merchandise for Customs purposes. For example, an importer pays less duty for a widget appraised at $5 each than for $10 each. On the other hand, because federal income tax is based on income, a taxpayer saves if its income is lower. Thus, if a U.S. corporation shows that its cost for each widget is $10 instead of $5, its costs for inventory of the widgets increases as its income decreases because the corporation must spend $5 more per widget.

Aware of the inherent conflict between valuation of imported merchandise for Customs and the IRS, some multinational corporations whipsawed[170] the U.S. government, "on

Reconciliation, 64 Fed. Reg. 39,187, 39,188 (1999).

164. Mod Act, *supra* note 2, §§ 501-06.

165. GLICK, *supra* note 123, at 2.

166. *See* U.S. Customs Service, *Reconciliation Information Page: What is Reconciliation?*, (visited Nov. 10, 1999) <http:\\www.customs.ustreas.gov\imp-exp2\comm-imp\recon\what.htm>. For a more detailed explanation of the requirements of the reasonable care standard, see H.R. 103-361(1) (1995). *See also* U.S. CUSTOMS SERVICE, *supra* note 140, at 18-20.

167. Donald Fischer, *Reconciling data for US Customs*, J. COM., July 28, 1999, at 12.

168. See *supra* Part III, for a discussion on Customs valuation.

169. See *supra* Part II, for a discussion on transfer pricing and income allocation by the IRS.

170. Whipsawing is the process by which a taxpayer uses "different valuations for customs and tax purposes . . . [in an attempt] to minimize the overall amount

property acquired from a related party, . . . [by] claim[ing] a low valuation for customs purposes and a higher valuation for tax purposes,"[171] thereby decreasing amounts owed in both Customs duty and federal income taxes. Consequently, the U.S. government potentially loses revenue during transfer pricing between a foreign parent corporation and its U.S. subsidiary. A loss of federal revenue results if the multinational corporation upwardly adjusts the cost of the imported merchandise, shifting profits and taxable income oversees.[172] For example, a Swiss based multinational corporation reported to the IRS that it imported tweezers to its U.S. subsidiary for $218 each.[173] A British parent corporation reported that it imported television antennas to its U.S. subsidiary for $1738 each.[174] First, these transfer prices guarantee that neither U.S. subsidiary will sell the merchandise at a profitable price because a consumer will not spend hundreds of dollars for a tweezer nor thousands of dollars for an antenna.[175] Second, because neither U.S. subsidiary will show an income from the sales, neither will pay federal income tax on those sales.[176] Consequently, the United States loses tax dollars. In an attempt to stop related corporations from manipulating transfer prices, like in the examples above, Congress passed Section 1059A of the Internal Revenue Code, which places a ceiling on a "taxpayer's basis or inventory cost in property imported from related persons."[177]

---

owed to the government." J. Com. Staff, *Transfer Pricing Problem Moves to the Forefront: U.S. Multinationals: It's a "Lose-Lose" Situation*, J. COM., Nov. 14, 1997, at 3A.

171. International Taxation: IRS' Administration of Tax-Customs Valuation Rules in Tax Code Section 1059A, 3/1/94 Gen. Acct. Off. Rep. & Testimony, Vol. 199, No. 03.

172. *See* 105 CONG. REC. S4203 (1998), Internal Revenue Service Restructuring and Reform Act of 1998 (1998).

173. *See* 144 CONG. REC. S4203, 1210 (1992).

174. *See id.*

175. *See id.*

176. *See id.* at S4203-04.

177. I.R.C. § 1059A (1994).

B. *Section 1059A*[178] *Limits a Taxpayer's Inventory Cost*

Section 1059A limits related corporations from assigning higher costs to merchandise imported from a related party for income tax purposes once its appraised value becomes final.[179] Accordingly, the general rule is that absent a protest filed by the importer, a related corporation may not upwardly adjust its costs, thereby decreasing its income, 90 days after the notice of liquidation.[180] However, exceptions to the rule exist and thus, circumstances where a taxpayer may upwardly adjust its costs and still comply with Section 1059A.

The regulations for Section 1059A specifically designate circumstances where upward adjustments to the inventory cost are permitted.[181] First, Section 1059A applies only to merchandise imported from a related party.[182] Second, when merchandise is imported from a related party through a middleman working on behalf of one or both of the related parties, inventory costs may reflect the middleman's markup or commission, even if it is not included in the customs value, provided that: (i) there is no other reason to prevent it from being included; (ii) the markup or commission was actually paid; and (iii) the middleman was used for "a substantial business reason."[183] Third, merchandise that is not subject to duty is not

---

178. I.R.C. § 1059A states:

> (a)In general.—If any property is imported into the United States in a transaction . . . between related persons (within the meaning of section 482), the amount of any costs–
>
> (1) which are taken into account in computing the basis or inventory cost of such property by the purchaser, and
>
> (2) which are also taken into account in computing the customs value of such property, shall not, for purposes of computing such basis or inventory cost . . . be greater than the amount of such costs taken into account in computing such customs value.
>
> (b) Customs value; import.—For purposes of this section–
>
> (1) Customs value.—The term "customs value" means the value taken into account for purposes of determining the amount of any customs duties or any other duties which may be imposed on the importation of any property.
>
> (2) Import.—Except as provided in regulations, the term "import" means that entering, or withdrawal from warehouse, for consumption.

Id.

179. *See* 26 C.F.R. § 1.1059A-1(a) (1998).

180. *See id.* § 1.1059A-1(d).

181. *See id.* § 1.1059A-1(c)(2).

182. *See* I.R.C. § 1059A(a); 26 C.F.R. § 1.1059A-1(a).

183. *Id.* § 1.1059A-1(b)(2). For an explanation of Section 1059A's application to

subject to Section 1059A.[184]

Finally, the regulations indicate allowable adjustments for charges that are supposed to be included in determining value of merchandise for tax purposes, but are not meant to be included in determining value of merchandise for Customs purposes.[185] They are charges for freight,[186] insurance,[187] "construction, erection, assembly, or technical assistance provided . . . after [the property's] importation into the United States"[188] and other similar charges "which are not properly includible in customs value, and which are appropriately included in the cost basis or inventory cost for income tax purposes."[189] For example, U.S. parent corporation, P, pays its foreign subsidiary, S, a price of $12 per widget, including ocean freight of $2 per widget. The Customs appraised value per widget would be $10 because freight is not included in the transaction value.[190] However, since the $2 freight charge is properly included in the cost of the widgets when determining value for taxable income, P may increase its cost by $2 (the charge for the ocean freight) and remain in compliance with Section 1059A.[191]

Not only do the regulations specify permissible increases to the inventory cost of imported merchandise, but they also indicate when those adjustments must be offset by "reductions in the price actually incurred"[192] in the related transaction. For example, if U.S. subsidiary, S, purchases widgets from its foreign parent corporation, P, for a price that includes insurance charges, the cost of the insurance may be properly added to the inventory cost of the imported property. However, if

---

three tiered transactions involving related parties and a middleman, see Priv. Ltr. Rul. 95-43-048 (Aug. 1, 1995) and *U.S. Sub's Basis in Imported Property Not Limited by Section 1059A*, 7 J. INT'L TAX'N 80, 80 (1996).

184. 26 C.F.R. § 1059A-1(c)(1). "Thus, for example, the portion of an item that is an American good returned" is not subject to Section 1059A because it is "not subject to duty." *Id.*

185. *See id.* at § 1059A-1(c)(2).

186. *See id.* at § 1059A-1(c)(2)(i).

187. *See id.* § 1059A-1(c)(2)(ii).

188. *Id.* § 1059A-1(c)(2)(iii).

189. *Id.* § 1059A (c)(2)(iv).

190. See *supra* Part III.A, for a discussion on statutory inclusions to transaction value.

191. *See* 26 C.F.R. § 1059A-1(c)(8). The example is derived from illustration (1) presented in the regulations.

192. *Id* § 1059A-1(c)(3).

after entry, P grants to S a rebate off the purchase price, S "is required to reduce the amount of the customs value by the lesser of the amount of the rebate or the amount of any positive adjustments to the original customs value"[193] to comply with Section 1059A.[194]

A related taxpayer may also comply with Section 1059A via the comparison method.[195] When the same costs are used in determining both IRS inventory costs and Customs value, a related taxpayer may compare the two costs to demonstrate compliance, i.e., that the costs are equal or that the inventory costs are lower.[196] When a related party taxpayer shows compliance with Section 1059A through the comparison method, it does not need to calculate adjustments and offsets to adjustments.[197]

Regardless of whether a related taxpayer shows compliance with Section 1059A by calculating adjustments and offsets to adjustments, or by comparing costs, Section 482[198] remains applicable in related party transactions.[199] The IRS still has "the authority . . . to increase or decrease the claimed basis or inventory cost"[200] as Section 1059A serves only as a limit to taxpayers and not the IRS.[201] Moreover, a taxpayer is forbidden from increasing the cost of imported merchandise simply because it is lower than its customs value.[202] However, as discussed earlier, if a related taxpayer enters into an APA with the IRS, the taxpayer avoids exposure to the limit imposed by Section 1059A and an income allocation adjustment by the IRS pursuant to Section 482.[203]

---

193. *Id.* § 1059A(c)(8).
194. *See id.* This example is derived from illustration (2) presented in the regulations.
195. *See id.* § 1059A-1(c)(6).
196. *See id.*
197. *See id.*
198. See *supra* Part II.B, for a discussion of Section 482.
199. *See* 26 C.F.R. § 1059A-1(c)(7).
200. *Id.*
201. *Id.*
202. *See id.*
203. See *supra* Part II.C, for a discussion on Advance Pricing Agreements.

C. Multinationals Encounter a New Dilemma: Reconciliation and Section 1059A

A multinational corporation may have to forego a reduction to taxable income when it files a reconciliation with Customs to comply with Section 1059A of the Internal Revenue Code.[204] The problem arises when a multinational corporation: (i) files a reconciliation within fifteen months from the first flagged entry summary that increases the customs value of the merchandise transferred from a related party;[205] (ii) previously established its inventory cost of the merchandise for tax purposes based on the customs value at entry; and (iii) pursuant to Section 1059A, is forbidden from upwardly adjusting its inventory costs to compensate for the reconciled customs value because the increase was made after ninety days from the date of liquidation of the merchandise.[206]

For example, U.S. Parent Corporation, P, contracts to buy widgets from Foreign Subsidiary Corporation, S, for $10 per widget. P supplies equipment that is necessary for producing the widgets at no charge to S. The equipment is an assist and as such, its value must be added to the price of the widget for customs value. When S transfers the widgets to P, P, as the importer, enters the widgets into the United States. Upon entry, P notifies Customs that it wishes to reconcile the value of the equipment at a later date because its value is currently unknown. P flags the entry of the widgets and agrees to supply Customs with the declared value of the assist within fifteen months of the date of the first entry of the widgets.[207] Ninety days after liquidation, the value of the widgets becomes final as per Section 1059A.[208] Therefore, if P does not file its reconciliation before ninety days, P may not increase its cost of the widgets unless the increase is permitted pursuant to the Regulations for Section 1059A.[209] An upward adjustment pursuant

204. See *supra* Part IV.B, for a discussion of Section 1059A.

205. *See* 19 U.S.C. § 1484(b)(2) (1994). See Part III.C, *supra*, for a discussion of Reconciliation.

206. Customs Value becomes final under Section 1059A 90 days from liquidation. *See* I.R.C. § 1059A.

207. *See generally* U.S. CUSTOMS SERVICE RECONCILIATION TEAM, *supra* note 142 (explaining the reconciliation process).

208. *See* I.R.C. § 1059A.

209. *See id.*

to a reconciliation is not one of the allowable increases.[210] P files the reconciliation for the equipment eight months after the first entry of the widgets. The Customs value of the equipment is $2 per widget, increasing the final customs value to $12 per widget. P pays Customs duties on the final customs value, $12.

Although P should be able to claim a $12 inventory cost per widget, for tax purposes,[211] it is not allowed to increase its inventory cost by the $2 reconciled value of the equipment because a reconciled value is not specified in Section 1059A's regulations as an allowable upward adjustment. Therefore, P must claim $10 as its inventory cost of the widgets or risk penalties for noncompliance with Section 482 and Section 1059A even though the transfer price was derived from an arm's length transaction. Because P is unable to increase its inventory cost to reflect the true value of the widgets, P is exposed to both higher duty and higher taxes. However, P's income should be lowered as the reconciliation reflects that P paid $12 per widget instead of $10 per widget to S. As S's income rises, (S receives $12 instead of $10 per widget), P's income decreases, (P is required to pay $2 more per widget). Thus, P's federal income taxes for the related party transaction should be lowered to reflect its lower income. Presently, this is not the case.

V. THE EFFECT OF CUSTOMS RECONCILIATION ON TAXABLE INCOME

A multinational corporation should be permitted to increase its inventory cost to the customs value of imported merchandise after a reconciliation is filed. An examination of the Customs Valuation Statute,[212] the Reconciliation Program of the Customs Mod Act[213] and Section 1059A of the Internal Revenue Code,[214] as well as the legislative history behind the

210. *See id.*

211. See *supra* Part II.A, for a discussion on transfer pricing and Section 482.

212. *See* 19 U.S.C. § 1401(a) (1994). See *supra* Part III.A, III.B, for a discussion of Customs valuation principles.

213. *See* 19 U.S.C. § 1484(b)(2). See *supra* Part III.C, for a discussion of the Reconciliation Program of the Customs Modernization Act.

214. *See* I.R.C. § 1059A. See *supra* Part IV.B, for a discussion of Section 1059A.

statutes, demonstrate that a related party should be able to reduce its taxable income when the increase in inventory cost is due to a Customs reconciliation.[215] Not only do the pertinent statutes and their respective legislative histories indicate that it is legally permissible and desirable for a related corporation to increase its inventory cost to the customs value after reconciliation, but past agency action supports it.[216] Finally, it would be legally workable to design a program where the multinational corporation, Customs and the IRS jointly agree to a transfer price for the imported merchandise after the reconciliation is filed so that the multinational corporation is protected from a change to its income allocation pursuant to Section 482.[217]

First, an increase to a related corporation's customs value due to a reconciliation will not automatically render the transaction value method untenable. In 1995, a proposal was made to test the use of reconciliation for adjustments made to the price of imported merchandise in related party transactions.[218] Although the test was never implemented,[219] Customs planned to "consider the fact that the related party importer has reason to believe that an upward adjustment may be made to the price [due to a reconciliation] as evidence that the relationship may have affected the price actually paid or payable for the imported merchandise . . . [and] [t]herefore, transaction value may not be acceptable."[220] Instead of allowing related parties to use transaction value, Customs dictated that related party importers who filed a reconciliation would need to appraise its merchandise via Subsection F of the Customs Valuation Statute.[221] However, the legislative history of

215. *See* S. Rep. No. 99-313, title IX (1986); H.R. 103-361(1), *supra* note 166, at 136.

216. *See* Priv. Ltr. Rul. 95-43-048, *supra* note 183.

217. *See* I.R.C. § 482. Section 482 delegates authority to the IRS to make adjustments to an international corporation's allocated income to ensure that it accurately reflects the taxable income of the related parties. *Id.* See *supra* Part II.A, for a discussion of transfer pricing and Section 482.

218. *See* Notice to Test the Use of Reconciliation for Adjustments Made to the Price of Imported Merchandise by Related Party Companies Under 26 U.S.C. § 482, 60 Fed. Reg. 35,105 (1995) [hereinafter Notice to Test].

219. The Reconciliation Prototype was never implemented because there were no applicants. E-mail from Shari McCann, U.S. Customs Service (Jan. 25, 1999) (on file with author).

220. Notice to Test, *supra* note 218, at 35,106.

221. 19 U.S.C. § 1401(f) says in part:

the Reconciliation program in the Mod Act indicates that reconciliation was a procedure implemented to help Customs and importers enter merchandise "in a more business-like way, reducing paperwork and many of the administrative costs."[222] Nothing in its legislative history suggests that a reconciliation should change the manner in which a transaction value is calculated. In fact, to the contrary, the legislative history of the Reconciliation program indicates that Congress wished to keep all Customs entry procedures the same, but simply add the option to reconcile certain unknown value issues when they become available.[223] Congress wrote, "[a] reconciliation will permit importers to submit information not available at the time of entry that is necessary . . . to determine the correct amount of duty on a shipment,"[224] and yet, the method remains the same for: (i) determining transaction value for the underlying merchandise; (ii) liquidating merchandise at the time of entry; and (iii) protesting Customs determinations.[225]

Given that valuation methods remain unchanged by the reconciliation program, entries flagged for reconciliation can be tested for an arm's length transaction price as any related party transaction is examined.[226] A related party transaction is at arm's length when the price is uninfluenced by the relationship between the parties.[227] More specifically, the selling price: (i) is the same to an unrelated buyer; (ii) is within industry standards; or (iii) procures a profit similar to the corporation's overall profit.[228] If the circumstances of the sale reveal a price that is not at arm's length, then the parties'

> (1) If the value of imported merchandise cannot be determined . . . the merchandise shall be appraised . . . on the basis of a value that is derived from the methods set forth in . . . [the] subsections, with such methods being reasonably adjusted to the extent necessary to arrive at a value.

Id. The methods from which the value is derived are: (i) transaction value of imported merchandise; (ii) transaction value of identical merchandise and similar merchandise; (iii) deductive value; or (iv) computed value. *See id.* § 1401(b)-(e).

222. H.R. 103-361(1), *supra* note 166, at 136.

223. *See id.*

224. *Id.*

225. *See id.*

226. See *supra* Part III.B, for a discussion on Customs valuation for related party importers.

227. *See id.*

228. *See* Transfer Pricing: Related Party Transactions, *supra* note 121, at 5446. *See also* discussion *supra* Part III.B.

relationship affected the transaction value regardless of the importer's need to reconcile an unknown cost at a later date. Although there may be circumstances when the price of an assist is influenced by the relationship of the parties, the relationship is not necessarily the reason a reconciliation is needed, but rather there are times when, "[f]or example . . . the importer supplies 'assists' which can only be captured on an annual basis."[229]

Moreover, an importer may file a reconciliation for entries imported from an unrelated party or a related party. The assumption that the relationship between the parties affected the price any time an importer flags for reconciliation an entry imported from a related party prevents a related party from ever using a reconciliation. It forces the importer to use a derived value[230] when it imports goods from a related party and files a reconciliation. This virtually incapacitates a related party from using a reconciliation since both importers and Customs dislike the unpredictability of a derived Customs value.[231] To discriminate against related parties is both unfair and unsupported in the legislative history of the Customs Valuation Statute and Reconciliation Program of the Mod Act, as a reconciliation is the sole manner by which an importer may liquidate entries and yet still hold open an unknown value.[232] It follows that provided the circumstances of the sale show that the appraised value of the merchandise was not influenced by the relationship between the parties, there is no reason to treat entries that are flagged for reconciliation differently from an entry that is not.

Furthermore, as the test values satisfy the arm's length standard by comparing the related party transaction to the unrelated party transaction, nothing in the Customs Valuation Statute[233] or the Mod Act[234] or their respective legislative histories suggests that an importer is barred from comparing its transaction to an unrelated party transaction solely because the merchandise's final cost is unknown at the time of entry. A

229. H.R. 103-361(1), *supra* note 166, at 135.
230. *See* 19 U.S.C. § 1484(2) (1994).
231. *See* Leo, *supra* note 137.
232. *See* U.S. CUSTOMS SERVICE RECONCILIATION TEAM, *supra* note 142, at 6.
233. 19 U.S.C. § 1401(a).
234. Mod Act, *supra* note 2, §§ 501-06.

comparison value could be adjusted to include or exclude certain factors, as necessary.[235] For example, Parent Corporation, P, imports widgets from its Subsidiary Corporation, S, and flags its entry summary of the widgets for reconciliation. The invoice value is based on standard costs and thus P does not know the final cost at date of entry. If the importer uses one of the test values to show that its transaction value is at arm's length, then the cost corresponding to the unknown cost in the transaction could be deducted from the comparison transaction to ensure a fair comparison. As "the reconciliation will be treated as an entry,"[236] the importer can show that the transaction value of the reconciliation is at arm's length the way it would establish an arm's length transaction of any entry of merchandise imported from a related party. Thus, for example, if an importer files a reconciliation for an unknown price of an assist, the importer may use either the circumstances of the sale test or a test value where the importer would compare the value of its assist to a similar assist used in an unrelated transaction, confirming that the reconciled value of the assist is accurate.

Second, the legislative history of Section 1059A suggests that an upward adjustment to a related taxpayer's inventory cost is permissible when the difference between the two costs is a reconciled value of a cost unknown at the time of entry of the imported merchandise.[237] According to its legislative history, the statute was enacted specifically in response to a case[238] where an importer claimed "a transfer price for income tax purposes that . . . [was] too high to be consistent with the transfer price claimed for customs purposes."[239] Congress feared that importers who purchased merchandise from a related party would manipulate its transfer prices solely to less-

235. *See* 19 U.S.C. § 1401(a). Adjustments are permitted when they will produce a more accurate comparison between the related party transaction and an unrelated party transaction. *Id. See also* discussion *supra* Part III.B.

236. H.R. 103-361(1), *supra* note 166, at 135.

237. *See* Notice to Test, *supra* note 218, at 35,105.

238. *See* Brittingham v. Commissioner, 66 T.C. 373 (1976), *aff'd*, 598 F.2d 1375 (5th Cir. 1979) (holding that "the Commissioner acted unreasonably in determining that the customs value constituted an arm's length" transfer price between related corporations for the sale of tile).

239. *See* S. Rep. No. 99-313, *supra* note 215.

en its taxes and Customs duties in an improper manner.[240] However, nothing in the statute or legislative history intimates that the transfer price claimed for tax purposes could never be higher than the transfer price claimed for Customs purposes and yet still remain at arm's length. To the contrary, the legislative history suggests that a multinational corporation could not claim a different transfer price for tax purposes than claimed for customs purposes specifically to whipsaw the U.S. government out of tax dollars. An increase to the inventory cost of merchandise is not an attempt by a multinational corporation to cheat the U.S. government from revenue, but rather reflects a corporation's actual increased cost of the merchandise as indicated on the reconciliation filed with Customs. Consequently, the inventory cost to merchandise imported from a related party should not be limited to the Customs value before the reconciliation is filed.

Moreover, the legislative history of Section 1059A acknowledges that occasions arise where "[a]ppropriate adjustments may be made in applying the rule in cases where customs pricing rules differ from appropriate tax rules."[241] In fact, the IRS has relied on the "appropriate adjustment" of inventory costs to permit the transfer price used for tax purposes to be higher than the transfer price used for customs purposes.[242] In a Revenue Letter written about a three tiered transaction involving related parties, the IRS did not limit the related party's inventory cost to the Customs value.[243] Rather, the IRS permitted the corporation to use the full purchase price charged by the middleman to the importer for tax purposes even though the corporation used the lower transfer price charged by the manufacturer to the middleman for Customs purposes.[244] The IRS issued the ruling in response to the first-sale rule set forth in *Nissho Iwai American Corp. v. Unit-*

240. *See id.*
241. *Id.*
242. *See id.*
243. Priv. Ltr. Rul. 95-43-048, *supra* note 183. A three tiered transaction is one that involves an importer, a middleman and a manufacturer, two or more of which are related parties. Generally, the importer places an order with the middleman who then hires a manufacturer to make the merchandise. Thus, the price between the importer and the middleman is higher than the price between the manufacturer and the middleman as the former price includes the middleman's markup.
244. *See id.*

ed States,[245] where the court opined that the lower price paid by the middleman to the manufacturer was an acceptable transaction value.[246] The IRS excused this situation from the ceiling price set by Section 1059A "[b]ecause the essence of customs planning under Nissho Iwai is to permit the importer to tender lower duty on the lower first sale, even though it has paid a higher price for the imported goods, [and] the importing taxpayer always has a price disparity."[247] Similarly, the IRS should allow a related party taxpayer to upwardly adjust its inventory cost to reflect the higher price paid which is known to the importer only after it files a reconciliation.

Finally, as "Congress expected that the Secretary . . . [would] provide rules for coordinating customs and tax valuation principles,"[248] I propose that it would be legally workable to implement a procedure that permits a related party taxpayer to file a reconciliation with Customs, increase its inventory cost to the higher price actually paid (known after the importer files a reconciliation), without violating Section 1059A or risking changes to its income allocation pursuant to Section 482. Similarly to the manner in which the IRS negotiates a bilateral APA with foreign tax authorities,[249] the IRS negotiates a mutually agreeable transfer price with the related party corporation and Customs after the corporation files a reconciliation with Customs. Because the agreement is made after the reconciliation is filed, all inventory costs are known to the corporation. Therefore, it knows the price actually paid for the imported merchandise and possesses all the information necessary for the IRS to accurately determine if the taxpayer should be allowed to increase its inventory cost to the Customs value in-

---

245. 982 F.2d 505 (Fed. Cir. 1992). Nissho Iwai's first sale rule can be implemented when there is: (i) a sale; (ii) for exportation to the United States; and (iii) the transfer price is a valid transaction value, i.e., made at arm's length. *Id.* at 509.

246. *See id.* at 509.

247. Mark K. Neville, Jr., *'First-Sale-For-Export' Rule Represents a Major Victory For Importers*, 7 J. INT'L TAX'N 72, 77 (1996).

248. General Explanation of the Tax Reform Act of 1986 (Bluebook) BLBK86 T. XII, E 8 (May 4, 1987).

249. Bilateral APAs are binding advance pricing agreements made between the taxpayer, IRS and foreign tax authorities that distribute the corporation's taxable income between the countries to accurately reflect what is owed to each and to avoid burdening the taxpayer with double taxation. *See* Rev. Proc. 96-53, *supra* note 7, at 381-82, § 7. See also *supra* Part II.C, for a discussion of APAs.

cluding the reconciliation. I propose the following as the steps to a procedure, called a Reconciliation Agreement where the multinational corporation, Customs and the IRS negotiate a transfer price so that the multinational may upwardly adjust its inventory cost to accurately reflect the reconciled value without violating Section 1059A and risking an income allocation adjustment under Section 482:

1. Pursuant to the reconciliation procedures, the related party importer flags the entry summary so that Customs knows it wishes to reconcile an unknown, e.g., the value of an assist, at a later date.[250]

2. Upon notifying Customs of the reconciliation, the related party importer notifies the IRS that it wants to enter into a reconciliation agreemnt. The request to enter into a reconciliation agreement lets the IRS know that a portion of the related party's inventory cost is unknown and will not be known until it files a reconciliation with Customs. In return for the taxpayer's promise to determine the inventory cost of the imported merchandise when the necessary information becomes available (and within the 15 month Customs reconciliation deadline),[251] the IRS will not limit the allowable inventory cost to the pre-reconciliation custom's value. Instead, the IRS will use the reconciled customs value as the ceiling.[252]

3. After the related party notifies both agencies and files an entry by entry reconciliation, Customs examines the Reconciliation package[253] and determines whether the related party's custom value is correct based on the information provided by the importer. After Customs makes its determinations, it forwards the Reconciliation

250. *See* Modification of National Customs Automation Program Testing Regarding Reconciliation, *supra* note 9, at 44,304. *See also* 19 U.S.C. § 1484(b)(2) (1994). See *supra* Part III.C, for a discussion of Reconciliation.

251. *See* U.S. CUSTOMS SERVICE RECONCILIATION TEAM, *supra* note 142, at 9. See *supra* Part III.C, for a discussion of Reconciliation.

252. *See* I.R.C. § 1059A (1994). See *supra* Part IV.B, for a discussion of section 1059A.

253. The Reconciliation package is comprised of the Reconciliation Header Record, the association file and a summarized data spreadsheet. *See* U.S. CUSTOMS SERVICE RECONCILIATION TEAM, *supra* note 142, at 23-24.

package to the IRS where a reconciliation agreement team[254] evaluates whether the customs value accurately reflects an arm's length transaction between the related parties.

4. If the IRS decides that corrections are needed, it adjusts the value accordingly and submits its changes to Customs. Customs examines the changes made by the IRS and if it doesn't agree, then the agencies negotiate until an agreement is reached.

5. The related party importer/taxpayer will be notified of any changes made to its reconciliation, whether it was made by Customs or the IRS. Additionally, the related party importer/taxpayer will remain available in case either agency questions the reconciliation or requires documentation to support its conclusions.[255]

6. Once the reconciled value is decided, the related party, Customs and the IRS enter into a reconciliation agreement, a binding document which provides assurance for the taxpayer that it complied with Section 1059A and therefore, will not be subject to penalties for increasing its inventory cost of merchandise to a price higher than the customs value before the reconciliation was filed. It also ensures that the IRS will not adjust its income allocation based on the upward adjustment.

Not only should a related corporation be permitted to increase its inventory cost to the Customs value that includes the reconciliation, and thus, lower its taxable income because it is legally permissible, but the reconciliation agreement provides a manner that is legally desirable to the multinational corporation and legally workable to the U.S. government.

A reconciliation agreement is legally desirable to the mul-

254. The reconciliation agreement team is similar to an APA team in that it includes representatives from the interested parties. For example, the reconciliation agreement team would include a representative from the corporation, Customs and the IRS.

255. This is similar to the way the taxpayer must remain available when the IRS negotiates with foreign tax authorities for a bilateral APA. *See* Rev. Proc. 96-53, *supra* note 7, at 37, § 7. See *supra* Part II.C, for a discussion of APAs.

tinational corporation because as a binding document, it provides a way for the corporation to decrease its tax burden without the risk of penalties for violating Section 1059A[256] or changes to its income allocation under Section 482.[257] For those times where the parties cannot reach an agreement after the reconciliation is filed, the corporation does not incur any new risks. As the taxpayer does not know the final cost of an import at the time of entry, the corporation already faces the risk of a dispute over the reconciled value by Customs. Moreover, the corporation already faces the potential for a change to its income allocation by the IRS, via Section 482, and a dispute over how it arrived at its transfer price.[258] Consequently, the related party corporation risks little in entering into a reconciliation agreement with Customs and the IRS, but to the contrary, has the opportunity to decrease its tax bill.

Additionally, a reconciliation agreement is desirable for the multinational corporation because the corporation is not required to maintain additional information or extra paperwork specifically to enter into a reconciliation agreement. Because the related party corporation is subject to penalties for noncompliance to the various statutes and regulations directed at related party corporations, these corporations must already keep paperwork to prove compliance. Furthermore, as multinational corporations have recently become a target for both Customs and IRS audits,[259] "[t]he guidelines call for multinational companies to maintain documentation that will enable taxing authorities to accurately assess a company's transfer pricing policies."[260] The documentation maintained by the corporation for those purposes is sufficient for entering into a reconciliation agreement because "[g]reat care has been taken to avoid imposing an additional layer of documentation upon existing documentation/accounting practices."[261]

256. I.R.C. § 1059A.
257. I.R.C. § 482.
258. *See id.*
259. *See* Chip, *supra* note 12; Pamela L. Kayfetz & Leo B. Helzel, *Achieving Fair National Taxation of International Transactions*, 3 ANN. SURV. INT'L & COMP. L. 193, 198 (1996).
260. Milton Zall, *Getting Price Right IRS Settles Transfer Pricing Disputes Involving US Multinational Firms*, J. COM., Dec. 16, 1998, at 3A.
261. *Id.*

A reconciliation agreement is legally workable to the U.S. government because as both Customs and IRS are in the Treasury Department, they share the same goals.[262] Both agencies are responsible for collecting revenue for the United States as well as for ensuring compliance to regulations implemented by the agencies.[263] More specifically, Customs confirms that the transaction value claimed on merchandise imported from a related party is at arm's length.[264] Similarly, the IRS is authorized to allocate income between commonly controlled entities as necessary to prevent evasion of taxes or clearly to reflect income.[265] From a practical perspective, if the IRS negotiates with foreign tax authorities, whose interests may be adverse to its own,[266] and yet still participates in bilateral APAs, it certainly should be able to negotiate with an agency in the same Treasury Department that adheres to a similar agenda and promotes similar goals.

Finally, a reconciliation agreement is legally workable to the United States because it will not affect U.S. obligations to its trading partners. The United States will stay in compliance with its international agreements on Customs valuation as transaction value will remain the primary basis for appraising imported merchandise and neither the Customs Valuation Statute nor the Mod Act will change. In addition, a reconciliation agreement will not interfere with international tax treaties to which the United States is a party. Thus, the reconciliation agreement is legally beneficial to all parties involved.

VI. CONCLUSION

Although a multinational corporation must currently forego a decrease to its taxable income when it files a reconciliation pursuant to the Customs Modernization Act in order to comply with Section 1059A of the Internal Revenue Code, it should not be the case. Sections 482 and 1059A of the Internal Revenue Code, the Customs Valuation Statute, agency regula-

262. *See* BLACK'S LAW DICTIONARY 386, 816 (6th ed. 1990).

263. *See id.*

264. *See* C.F.R. § 1.482-1(b) (1994).

265. *See* I.R.C. § 482 (1994). The Secretary is given this authority pursuant to section 482.

266. The foreign tax authorities' goal is to collect revenue for its own country, while the IRS' goal is to collect revenue for the United States.

tions, statutory history and common sense dictate that a multinational corporation should be permitted to reconcile an unknown cost at a later date for Customs purposes and reflect that increased cost for tax purposes without risk of noncompliance.

Suzanne I. Offerman