The convergence of transfer pricing and customs in the GCC

Content

01 Introduction 04

02 How do customs and transfer pricing interact in related-party imports? 05

03 The role of transfer pricing year-end adjustments 06

04 Compliance considerations: What to look out for 07

05 Customs valuation: How transfer pricing adjustments affect import and export valuations 08

06 Other factors affecting customs value 10

07 Practical steps for businesses 11

08 Navigating complexity with confidence 22

01

Introduction

In today's interconnected global economy, multinational enterprises (MNEs) face a complex web of regulations, especially when it comes to tax compliance. In the Gulf Cooperation Council (GCC), the convergence of transfer pricing (TP) and customs rules has created new challenges and opportunities for companies that extend well beyond tax into commercial operations. From pricing strategies and supply chain management to profitability and cash flow, the ripple effects of these rules can be significant to many areas of the business.

In recent years, TP regulations have become a key focus for businesses in the GCC, as countries like Saudi Arabia and the UAE align more closely with global tax standards. The Kingdom of Saudi Arabia (KSA) introduced its TP regulations in 2018, adopting the OECD's guidelines, and extended these rules to Zakat payers from January 2024. The United Arab Emirates (UAE), with its new Corporate Income Tax (CIT) regime effective from June 2023, has also implemented TP rules that emphasise the 'arm's length' principle and require detailed documentation.

As an inevitable outcome of the changing tax landscape, there is bound to be a co-relation between various taxes, and the tax authorities are also cognisant of the need to keep pace with the changing tax landscape. As a result, we have seen the consolidation of the former General Authority of Zakat and Tax (GAZT) to the present-day Zakat, Tax and Customs Authority (ZATCA) in Saudi Arabia.

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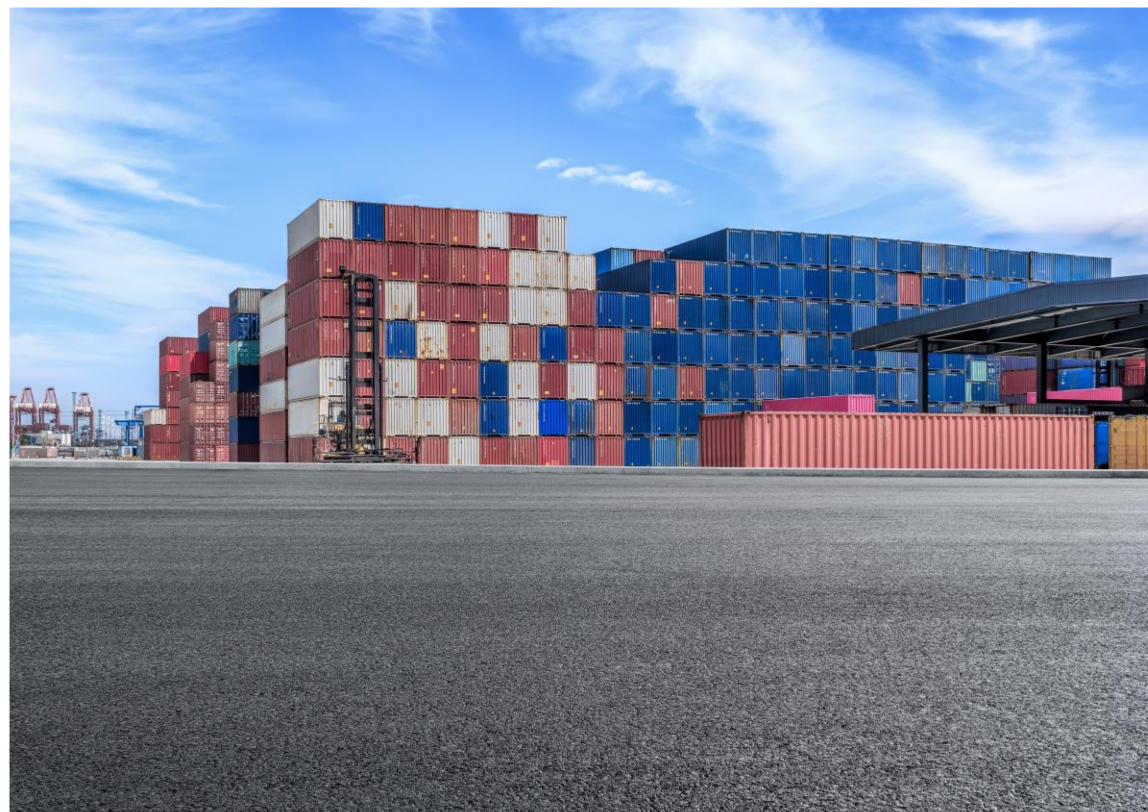
How do customs and transfer pricing interact in related-party imports?

A common question is how customs and transfer pricing (TP) interact in the import of goods from related parties. The objective of the TP and customs authorities is to ensure that goods are purchased at a value which is consistent and at a fair market value. However, the result could be conflicting due to the nature of the transaction flows. The valuation methodologies used for the purpose of customs and TP can lead to inconsistent results at times which then need to be corroborated based on the circumstances, or by way of adjustments which eliminate the differences.

The conflicting nature of the transaction flows can, at times, lead to significant year-end adjustments by taxpayers. These adjustments are not simply a compliance issue; they can impact pricing strategies, internal profitability, and the smooth flow of cross-border goods and services. As businesses adapt to these frameworks, it is important to take a holistic view, considering how TP decisions can affect other areas like customs.

In this article, we'll explore the importance of customs and TP considerations. By understanding the interplay between these pillars, businesses can manage risk and ensure smoother operations across departments.



The role of transfer pricing year-end adjustments

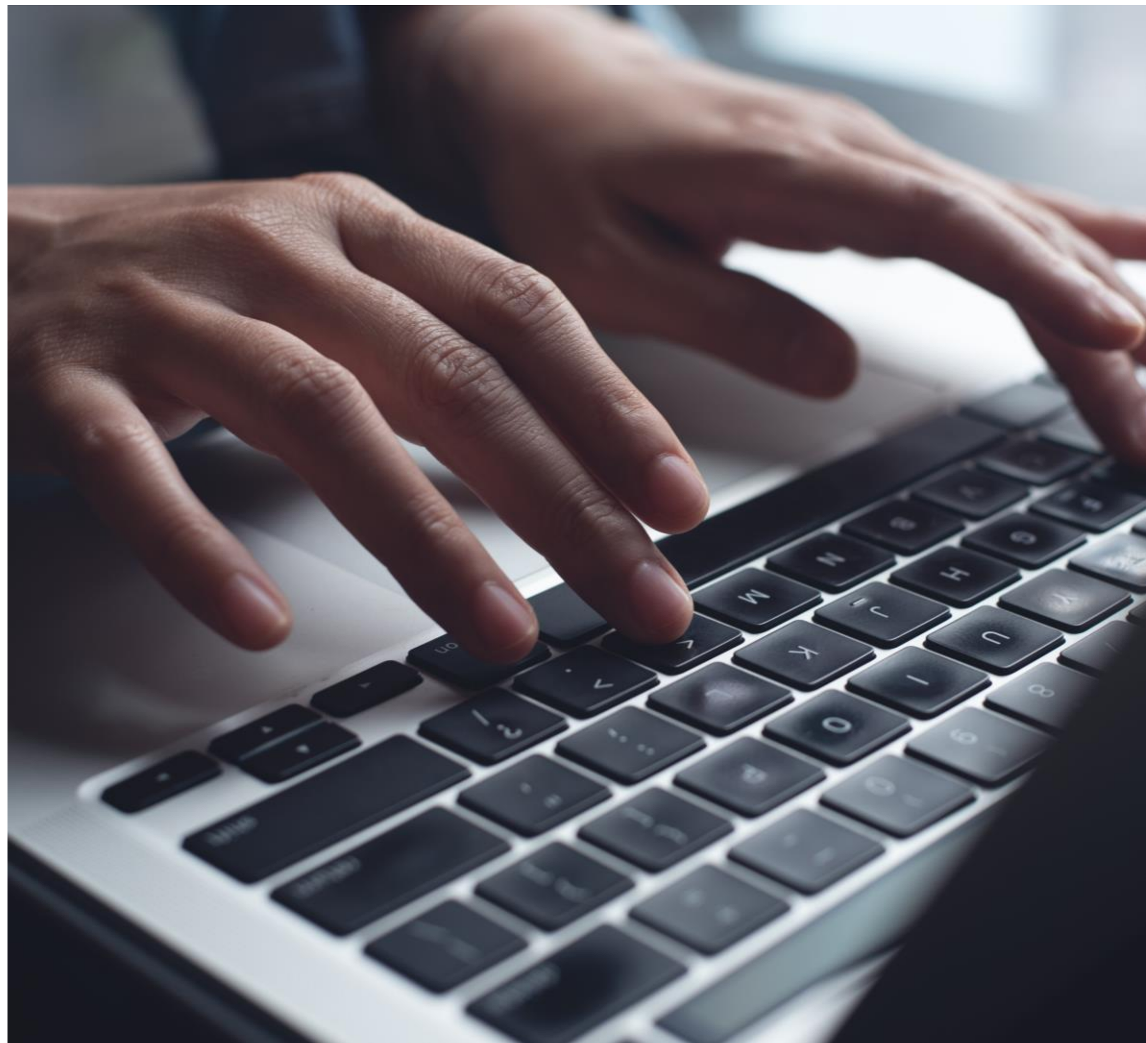
Transfer pricing (TP) year-end adjustments are often necessary to ensure that intra-group transactions remain consistent with the arm's length principle. These adjustments may be driven by a range of business factors, including shifts in profitability, changes in market conditions, or the varying performance of different group entities.

However, one of the key challenges in making TP year-end adjustments is the ripple effect they can have on customs. Adjusting transfer prices can affect the customs value of imported goods, potentially leading to changes in duties paid, which may then result in either double taxation or penalties. In some cases, this can even lead to goods being held at the border, disturbing commercial operations. It is essential that both areas - TP and customs - are aligned when making year-end adjustments to avoid compliance risks, financial penalties, or audits.

Compliance considerations: What to look out for

In both Saudi Arabia, and the UAE, businesses are required to document their TP adjustments in line with local regulations. This means that any year-end adjustments must be supported by comprehensive documentation, and companies are obligated to file TP disclosure forms as part of their compliance requirements. Additionally, these adjustments must be accurately reflected in financial statements and tax filings to prevent discrepancies.

A common challenge for businesses, particularly large MNEs, is the tight timeline for submitting these disclosure forms. In Saudi Arabia, for example, companies have 120 days after the end of the accounting period to submit their tax returns. This timeframe may not provide enough room to conduct a thorough analysis of TP adjustments, highlighting the need for sufficient preparation and planning in advance.



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Customs valuation: How transfer pricing adjustments affect import and export valuations

For transactions between related parties in the GCC, customs valuation rules and TP requirements are closely intertwined. Customs authorities generally rely on the "transaction value method," which bases the declared value of imported goods on the actual price paid, as long as it is at arm's length.

Under the Common Customs Law of the GCC States (and the corresponding Implementing Regulations in each member country), the transaction value may be rejected where the relationship between buyer and seller is found to influence the price. Article 1 of the WTO Customs Valuation Agreement (CVA), which has direct effect in the GCC through each state's WTO accession commitments, establishes this principle. Accordingly, where the parties are related, the importer must be able to demonstrate, using objective data, that the price is not influenced by that relationship. Failure to do so can lead the customs authorities to apply secondary valuation methods (such as valuation based on identical or similar goods, deductive, computed or fallback methods), potentially inflating the customs value and the associated duty costs.

Both ZATCA in Saudi Arabia and the UAE Federal Authority for Identity, Citizenship, Customs & Port Security (acting through the relevant local customs department) have issued internal guidance aligned with the World Customs Organisation (WCO) Commentary 23. In practice, this means customs auditors often request transfer-pricing documentation - especially the Local File - to assess whether the declared import price satisfies the CVA “circumstances-of-sale” criteria. Importers that can present a robust TP study, prepared contemporaneously and demonstrating that the tested party earns an arm’s-length margin, are more likely to have their transaction value accepted.

TP studies can be an effective evidentiary tool; however, only if they clearly map the tested transaction to the physical flow of goods, identify the correct tested party (typically the importer of record), and disclose any post-import pricing adjustments. Customs officials retain discretion to request supplementary data, such as intercompany agreements, contemporaneous commercial invoices, or royalty/license contracts to corroborate the TP study. Importers, therefore, benefit from maintaining a “dual use” file that simultaneously satisfies TP and customs evidentiary thresholds.

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Where a TP policy mandates retroactive year-end true ups, the importer must consider the customs impact from day one. In the GCC, for example, Article 55 of the Common Customs Law requires the submission of a supplemental declaration within 15 days of becoming aware of any circumstances that affect the customs value - including upward price adjustments. Failure to do so can trigger administrative penalties (generally up to three times the unpaid duty) and, in severe cases, even seizure of the goods.

Conversely, downward adjustments are seldom accepted by GCC Customs unless the importer can prove that the original price was provisional and subject to a formal and enforceable pricing mechanism. This makes it essential to have well-drafted intercompany contracts and clear disclosure at the time of importation.

Retroactive TP adjustments, whether upward or downward, generally need to be reported to customs authorities, which can be administratively challenging in the GCC. Upward adjustments, which increase the price paid for imported goods after the importation, may result in additional duties and penalties.

Although the GCC Common Customs Law permits duty refunds, in practice customs will only process a refund request if:

01 The importer lodges the claim within the statutory one-year limit;

02 The original import declaration explicitly referenced a provisional price; and

03 The importer can present conclusive evidence, often including TP documentation, that the revised price reflects the arm's-length value of the imported goods.

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Other factors affecting customs value

Royalties and license fees paid for intellectual property related to imported goods may be considered part of the customs value, increasing the duty liability. According to Article 8 of the CVA (incorporated verbatim into the GCC Common Customs Law) requires the addition of royalties and license fees that are "related to the imported goods" and "a condition of sale," GCC Customs routinely scrutinise trademark, technology and franchise agreements.

Importers should analyse each royalty stream against the four WCO test criteria and, where appropriate, ring-fence non-dutiable payments (such as royalties for post-import services) in separate agreements. In addition to this, certain commission payments related to the purchase or resale of imported goods may also need to be included in the customs value, potentially raising duty costs.

Only buying commissions payable to a bona fide buying agent are deductible; selling commissions and other fees are dutiable. Detailed agency agreements and contemporaneous proof of the services rendered are indispensable to sustain a buying-commission deduction during a customs audit.

When Cost Sharing Agreements (CSAs) involve R&D, design, or other activities that relate to the manufacture of imported goods, the associated costs may need to be added to the customs value. This can increase duty obligations, so companies should assess their CSA arrangements for any customs implications. Ideally, CSAs should contain a clear functional analysis, separating activities that contribute to the value of imported goods (and are therefore potentially dutiable) from group-wide stewardship or post-import services (which are not).

Payments under management service agreements between related parties may be attributed to the purchase price of imported goods by customs authorities, thereby increasing the customs value. Careful structuring and documentation of these agreements can help mitigate potential customs duty impacts. Where a management-service fee can be tied to activities performed after importation; such as local marketing or distribution support, it should remain outside customs' value. Proper invoicing and explanatory notes on the customs declaration facilitate this segregation.

07

Practical steps for businesses

For businesses operating in the GCC, aligning TP and customs strategies is no longer optional - it is a necessity. With increasing regulatory oversight in both Saudi Arabia and the UAE, managing these areas in isolation can result in compliance gaps and financial inefficiencies. An integrated approach ensures that adjustments in one area, such as TP year-end adjustments, do not inadvertently create issues in Customs valuations. It is essential for businesses to consider their cross-border transactions holistically and adopt a strategy that synchronises both pillars to avoid penalties, double taxation or discrepancies in reporting.

To achieve this, businesses must maintain robust documentation not only for TP but also for customs. This includes contemporaneous TP documentation, such as local and master files, as well as accurate import/export declarations. A practical step is to implement integrated record-keeping systems that link TP adjustments to customs values, with regular monitoring to ensure that documentation can withstand a rigorous joint audit.

Given the complexity of managing TP and Customs in the GCC, involving a tax specialist early in the process is crucial, whether it is an in-house tax professional or an external adviser. A tax specialist can help ensure that year-end TP adjustments are handled in a way that minimises the impact on customs, while maintaining compliance with local regulations. Early engagement allows businesses to design a cohesive documentation strategy that covers both areas, reducing the risk of compliance issues or financial penalties later on.

08

Navigating complexity with confidence

As businesses in the GCC - particularly in Saudi Arabia and the UAE - adapt to an evolving tax landscape, managing TP and customs effectively is more important than ever. Year-end TP adjustments will often ripple through other areas, impacting customs valuations, which makes it crucial for businesses to approach these areas in an integrated manner.

The key to navigating this complexity lies is maintaining accurate and synchronised documentation. Aligning TP adjustments with customs reporting is not just a compliance requirement, it's a way to prevent financial and operational risks. As tax regulations continue to evolve, taking proactive steps to keep strategies up to date will help businesses stay compliant and agile.

Whether by working with an in-house tax team or external advisers, involving specialists early ensures that year-end adjustments are managed smoothly. With the right planning and expertise, businesses can avoid penalties, ensure compliance, and focus on growth.

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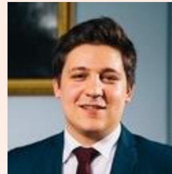

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