

25/11/2019

China - Process of Declaration of Dutiable Royalties

China's General Administration of Customs (the "GAC") issued, on March 27, 2019, the guidance on the declaration of the dutiable royalties ("Bulletin 58") effective as from May 1, 2019.

I. Background and scope

Based on a previous GAC Bulletin [2013] No. 213, the royalties that the buyer must pay, either directly or indirectly, are dutiable (i.e. being included in the dutiable value of imported goods) if both of the following conditions are fulfilled:

- ✓ The royalties are related to the imported goods; and
- ✓ The payment of royalties is a condition of the sale of the imported goods into China.

In practice, Chinese Customs usually conducted post-import inspections on the royalties and then pursued underpaid import duties if any (the "Post-Inspection").

Under Bulletin 58 (and together with the previous Bulletin 20 issued on January 23, 2019), the mode of declaration of royalties for customs purpose has been switched from the Post-Investigation initiated by the Customs to a self-declaration by the companies. Bulletin 58 has particularly clarified how importers should make voluntary self-declarations of dutiable royalties. Basically, companies shall now treat the royalties as a special type of goods and report them using the customs declaration form (the "CDF").

Please note that Bulletin 58 applies only to the royalties, while other adjustments to the dutiable value, such as commission and brokerage expenses, container expenses, etc., are out of the scope of Bulletin 58.

II. "Confirmation of royalty payments" in CDF

When an importer completes the CDF, it must fill in the section "Confirmation of royalty payment". The updates brought by Bulletin 58 on the requirements for filling in this column are shown in table below (assuming the buyer must pay the royalties directly or indirectly to the seller):

Before May 1st, 2019	As from May 1st, 2019 (Bulletin 58)
<p>State “Yes” if:</p> <ol style="list-style-type: none"> Royalties are <u>not included</u> in the price paid or payable + royalties are <u>related</u> to the imported goods; or Royalties are <u>not included</u> in the price paid or payable + taxpayer is <u>unable to determine</u> whether royalties are related to the imported goods or not. <p>State “No” if:</p> <ol style="list-style-type: none"> Royalties <u>are already included</u> in the price paid or payable; or Royalties are <u>not related</u> to the imported goods. 	<p>State “Yes” if royalties are <u>dutiable</u>.</p> <p>“Dutiable” technically means that royalties are <u>related to</u> the imported goods and which payment is <u>a condition of the sale</u> of the imported goods into China.</p> <p>State “No” if royalties are <u>not dutiable</u>.</p>

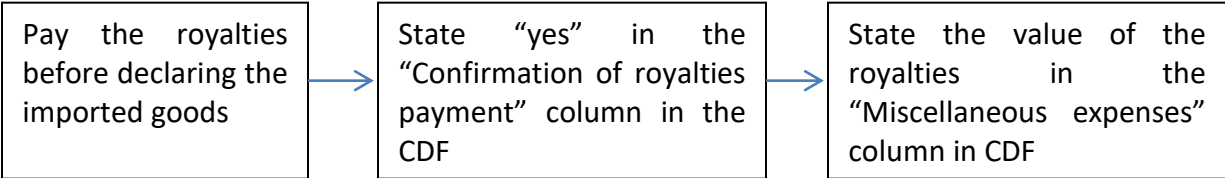
From the table, we can note the following two key differences between old guidance and Bulletin 58:

- Whether the royalties are included in the price of imported goods (paid or payable) becomes irrelevant for filing in the CDF;
- The taxpayer will however have to determine, at the moment of self-declaration, whether the payment of royalties consists in a condition of the sale of the imported goods into China**, which is often an area of debate between importers and the customs authorities. Actually, Bulletin 58 shifts more responsibility to the taxpayer, although it looks like the scenarios of “Yes” and “No” statement have been simplified and reduced compared with before.

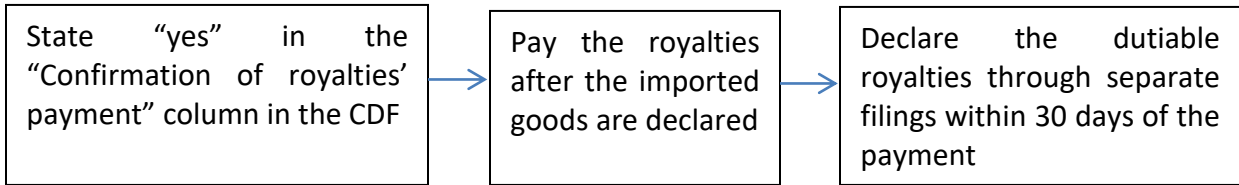
III. Self-Declaration Process

Regarding the self-declaration process, Bulletin 58 distinguishes two scenarios as follows:

- Scenario 1: Dutiable royalties are paid before declaring the imported goods**



- **Scenario 2: Dutiable royalties are not paid before declaring the imported goods**



According to our observation, in most cases taxpayers pay the dutiable royalties after the imported goods are declared.

IV. Miscellaneous points

- **Applicable duty rate and foreign exchange rate**

Pursuant to Bulletin 58:

- If the dutiable royalties are paid before declaring the imported goods, the Customs shall use the duty rate and foreign exchange rate applied on the day the Customs accepts the declaration of the goods to calculate import duties on the dutiable royalties;
- If the dutiable royalties are not paid before declaring the imported goods, the Customs shall use the duty rate and foreign exchange rate applied on the day the Customs accepts the declaration of dutiable royalties.

- **Late-payment surcharges**

Bulletin 58 has clarified, for the first time, that a daily 0.05% late-payment surcharge will be levied on any unpaid import duties if the taxpayer fails to declare the dutiable royalties, or does not declare it within the prescribed deadline. The calculation of the late-payment surcharges depend on the situation of i) taxpayer improperly fills out the “Confirmation of royalties payment” column in the CDF when declaring the imported goods; or ii) taxpayer does properly fill out the above column, but fails to declare the dutiable royalties later within the prescribed timeframe.

In addition, the late-payment surcharges could be mitigated if the company voluntarily discloses the matter in accordance with process provided for by the *Customs Audit Regulations*.

V. Suggestions

Given the regulatory changes brought by Bulletin 58, the companies are suggested to take the following actions:

- ✓ Review the dutiability assessment of the royalties implemented before and adjust it, if necessary, to comply with the requirements under Bulletin 58;
- ✓ Closely monitor the royalties declaration process to avoid any missing of deadline;

- ✓ Considering that Bulletin 58 requires many supporting documents to be submitted for the declaration of dutiable royalties, the company is recommended to start the preparation work since the beginning of planning of the remittance of the royalties.

In addition, considering the stricter scrutiny from the Chinese Customs on the dutiable royalties nowadays, other aspects relating to the royalties payment shall also be considered by companies, such as the issue of qualification of the royalty fees, the issue of transfer pricing, etc.

Contact us:

Liu Yijun-Legal & Tax Advisor

liuyijun@dsavocats.com

He Shunshan-Senior Legal Advisor

heshunshan@dsavocats.com

Jean-Marie Salva-Associé/partner

salva@dsavocats.com