

## Legal Rules for Foreign Trade and Customs Duty in China (I)

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### PRC trading rights

It consists of foreign trading right and domestic trading rights

PRC trading regime opened up in 2004.

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### PRC trading rights

Foreign trade rights:

- Import-export rights and Declaration rights

Domestic trading (distribution) rights

- commission agent, wholesale, retail, and franchise

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### Rights to make I/E declaration

1. FICE
2. Production type FIE
3. International courier / transportation company
4. Professional declaration agency

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### Registration as foreign trader

the FIE/FICE obtain I/E rights

- By completing the registration procedure as foreign trader

Why register?

- Only foreign trader can apply for customs registration & VAT export refunds

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### Types of customs registration

FIE/FICE	By obtaining a customs registration	As consignor or consignee
International courier, and transportation company	By obtaining a customs registration	As agent
Professional declaration company	By obtaining a customs registration	As agent

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## What is consignor or consignee?

- Consignor / Consignee <=> Exporter / Importer (**principle**)
- Consignor/consignee is one who has completed the registration procedure as foreign trader

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## Comparison between international courier/ transportation company with declaration company (**agent**)

1. Both provide declaration services to the consignor/consignee
2. International courier/transportation co can only declare goods for the consignor or consignee under contract of carriage
3. Declaration agent can make customs declarations for anyone who have got the I/E rights

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## Legal development Liberalization of trading rights in PRC

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## After China's WTO accession

	Administrative order by MOC	Details of the administrative order
1	Order No. 8 (2004) Effective on 2004.6.1	Chinese government opened up distribution sectors to foreign investors
2	Order No. 9 (2005) Effective on 2005.4.2	Production FIE can import, export & distribute 3rd party goods by expanding scope of business
3	Order No. 76 (2005) Effective on 2005.7.13	FIE situated in FTZ and BLP is granted distribution rights to do trading with companies situated outside FTZ/BLP
4	Order 94 (2005) Effective on 2006.3.1	MOC delegates its approval authority to provincial governments

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## PRC trading rights for FICE

1. Foreign trade right
  2. Declaration right
  3. Distribution right \*
- All above are subject to scope of business

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## Distribution rights for Trading Companies (FICE)

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## Scope of business

MOC Administrative Order No. 8 (2004): -

	Retail distribution	Wholesale distribution
1	Merchandise goods retailing;	Merchandise goods wholesaling
2	Imports of merchandise goods on the list of own trading items	Commission agent (except for auctioneering)
3	Sourcing domestic goods for export	Import and export of merchandise goods
4	Other related subordinated services	Other related subordinated services

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## PRC customs law and practices

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## Classification of imported goods under PRC customs law

	Types of goods	Customs procedure
1	General goods	General
2	Bonded goods	Special
3	Tax-exempt goods	
4	Temporarily Import-export goods	

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## Customs procedures

### General customs procedure

(a) Declaration, (b) Document examination, (c) Spot checking, (d) Payment of taxes, (e) Release of goods

### Special customs procedure

(1) Pre-importation declaration, (2) Every steps in general customs procedure (except for payment of taxes), (3) post-importation supervision procedure

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## Customs procedures

	General customs procedure	Special customs procedure
1	None	Pre-importation approval and record filing
2	Importation formality	Importation formality *
3	None	Post-importation Supervision

\* Duty and VAT not collected

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## General Import/Export Goods

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## Customs Tariff

Table contents: Category, HS code, duty rate

Goods subject to different tariff table and rates, depending on the country of origin.

Example: for a resin based paint product with HS code 32081000, the applicable duty rate can range from 0% to 50%, depending on which table it applies.

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CEPA-Hong Kong rate	0%
CEPA- Macau rate	0%
Special preferential rate	N/A
Treaty rate	8%
Preferential (MFN) rate	10%
General rate	50%

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## Certificate of Origin

1. "Nationality" of the product
2. The importing countries use this to impose duty, quantitative restrictions, or other trade measures.
3. Rules: wholly obtainable criteria, substantial transformation criteria (either change in HS code or value-added content)

Importer can apply for ruling on country of origin.

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## Application for customs pre-shipment commodity classification

- The consignee can apply for determination on product classification 45 days before shipment arrival day, per order no. 158 (2007) of the General Administration of Customs

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## Dutiable value

In general, the customs use the transaction price as dutiable value, which is the adjusted CIF value.

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## Dutiable base (transaction price)

excluding

1. Labor charges for installation, testing, training, maintenance fees for imported goods, etc;
2. Insurance premium and freight charge from port of receipt to inland destination
3. Import duty, VAT and consumption tax

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## Dutiable base (transaction price)

### Including

1. Import commission;
2. Container cost not separable from good
3. Packing cost;
4. R&D charge and design fee that the importer bears;
5. Royalty, re-sale handling fee, use or distribution fee the importer shares with foreign supplier, after importation of the goods.

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## Dutiable base

Administrative Order [2006] 148, General Administration of Customs, China

➤ Royalty payment relevant to the imported goods includes:

- (1) Patent products, or for use of patent to make the products;
- (2) For use of trade marks;
- (3) For copyrights;
- (4) For distribution of goods, which requires no further processing before sale.

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## Customs valuation

If necessary, Customs will adopt the following valuation method, in that order:

1. transaction price of same goods sold to China from the same exporting country;
2. transaction price of similar goods sold to China from the same exporting country;

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## Customs valuation

3. Cost plus profit, transportation and insurance expenses incurred in exporting country;
4. Resale price in China (after deducting taxes, transport and insurance expenses)
5. Other reasonable valuation method

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## Computation of import duty and domestic taxes

Example: lipstick imported from Japan (HS code 33041000), USD100 CIF, import VAT 17%, consumption tax 30%, the amount of total duty and taxes are given below:

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## Computation of import duty and domestic taxes

1	Duty = CIF x rate	(US\$100*7) x 10% # = RMB70
2	VAT = (CIF + duty + CT) x 17%	(700+70 + 330) ## 17% = RMB187
3	Duty + CT + VAT = total duty & tax	70 + 330 + 187 = RMB587

# MFN rate is 10%, Exchange rate: USD1 to RMB7 (assumed).

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## Computation of import duty and domestic taxes

## Consumption tax (CT) computation:

Composite value = (CIF + duty) / (1 - CT rate)  
Composite value = (700+70) / (1-30%) = 1,100

CT = Composite value x CT rate  
1,100 X 30% = 330

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## Comparison: Computation of import VAT with zero-rated duty

1	Duty = CIF x rate	(US\$100*7) x 10% # = RMB70
2	VAT = (CIF + duty + CT) x 17%	(700+70 + 330) ## 17% = RMB187
3	Duty + CT + VAT = total tax	0 + 330 + 187 = RMB517

# ASEAN rate is 0%, Exchange rate: USD1 to RMB7.

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## Duty computation

➢ Value-based duty amount will vary with following :

1. applicable tariff table
2. HS code
3. dutiable base
4. applicable rate
5. applicable exchange rate

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## Applicable duty rate

Duty rate that applies on the day customs accept import declaration

The “duty rate” on the day when the means of transportation declares entry into China, if customs has approved pre-shipment import declaration.

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## Applicable exchange rate

Customs shall adopt the base exchange rate on the Wednesday of 3<sup>rd</sup> week in preceding month as per PROC announcement, with reference to the day of applicable duty rate in that month.

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## Computation of import duty and VAT (general I/E goods)

1. Import duty rate : the date the Chinese customs accept the declaration for the import goods
2. Date of exchange rate: the date for the applicable duty rate
3. Exchange rate: the base rate the PBOC announces on the Wednesday in the third week of the preceding month

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## Two ways of duty computation

1	Dutiable value x duty rate	Ad valorem duty
2	Import quantity x rate per unit	Specific rate

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## Time for payment of duty and taxes

Within 15 days after receipt of demand for tax payment from customs  
Late payment will result in a daily surcharge, calculated at 0.05% of the amount payable.

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## Different components between accounting cost and customs valuation

1. Customs valuation includes payment for use of intangibles **and IP** rights
2. Customs valuation excludes payment for import duty and VAT, and provision of services (installation and testing charges, etc)
3. Adopting different exchange rate

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## Customs declaration and transfer pricing

- Tax mitigation vs. obligation to declare true and genuine information
- Impact of reduced export value

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## Impact of reduced export price (FICE)

- Only profit decreases, with no impact on VAT rebate amount
- Amount of VAT rebate  
= Purchase amount x VAT rebate rate

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## Impact of reduced export price (production company)

- If export price decreases, VAT refund increased and income tax reduced
- ➔ VAT refund (increase)  
= Input VAT - disallowed credit
- ➔ Disallowed credit  
= (Export – import) x (standard rate – refund rate)

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## Specific requirement for exporter

1. The goods it buys for purpose of export should not fall outside the scope of its business
2. The exporter should be a general taxpayer
3. The exporter needs to submit the application for export rebates within 180 days of the export declaration and produce prescribed documents to the tax bureau
4. If the exporter cannot do so, all the export sales are deemed to be local sales

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## VAT refund computation

	Production enterprise	Commercial enterprise (FICE)
Computation base	FOB value for export	Input VAT paid
Method	Exempt-offset-refund (ECR)	Pay-first-and-refund-later

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## VAT liability (production enterprise)

- Export sales = 2M (RMB), Local sales = 0
- Local purchase = 1.5M
- VAT rate = 17%; Rebate rate = 13%

### Computation (I) - ECR

- VAT payable
- $$= 2 \text{ m} \times 0\% - (1.5 \text{ m} \times 17\% - 2 \text{ m} \times 4\%)$$
- $$= 0 - 255,000 + 80,000 = -175,000$$
- Debit balance => VAT refund

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## Computation (II) – no refund

- VAT payable = Output VAT x 17%
- $$2 \text{ million} \times 17\% = 340,000$$
- Difference between (I) and (II) =  $340,000 + 175,000 = 515,000$

### Reason for above

- Taxpayer has not got recognized to be general VAT taxpayer, and
- Annual sales > 0.8 million (or 0.5 million)

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## Export tax

Export duty will impose on goods that will do harm to the environment protection, and the production of which consumes a lot of energy.

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## Refund of duty

Exporter can obtain refund from the customs within 1 year from tax payment day under following circumstances :

1. Goods, for which import duty has been paid, returned to overseas sellers for quality reasons

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## Refund of duty

Exporter can obtain refund from the customs within 1 year from tax payment under following circumstances:

2. Goods, for which export duty has been paid and VAT export refund has been repaid, returned by oversea buyer due to quality or specification reasons.

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## Refund of duty

3. Short shipment of bulk cargo in respect of which duty is already paid, carrier or insurance company has agreed to pay compensation, taxpayer has not applied for refund of import or export duty.

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## Refund of duty

4. Import/export goods, in respect of which consignor, carrier or insurance company has agreed to pay compensation for imperfection, poor quality, wrong specification or other situations, taxpayer has not applied for duty refunds.

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