

Implementation of the New Customs Audit Regulations



Overview

On 19 June 2016, the State Council issued Order No. 670, <Decision on the Amendments to the “Regulations of the People’s Republic of China on Customs Audits”>(the “New Customs Audit Regulations”) which will come into effect from 1 October 2016.

The New Customs Audit Regulations reflect the request for audit reform in the <Customs Comprehensive Deepening Reform Plan>. Customs audits play a significant role in Customs’ daily monitoring of import/export activities, especially in the ever-growing demand for port clearance speed and trade facilitation.

Companies should pay particular attention to some of the provisions in the New Customs Audit Regulations, such as “voluntary disclosure” and “the involvement of 3rd party firms”. This alert provides a summary of our comments to the New Customs Audit Regulations.



1. Formalising voluntary disclosure

The New Customs Audit Regulations provide a “voluntary disclosure” mechanism “where companies, directly related to the importation/exportation of goods, voluntarily report their violations to Customs and accept the corresponding customs consequences should be subject to lenient treatment or reduced administrative penalties.”

Customs has in the past been exploring the “self-assessment and reporting” supervision approach since 2015, and various self-disciplinary management programs have also been launched in the form of pilot programs for testing at different regional Customs locations since 2014. Evolving from the above, a formal “voluntary disclosure” program is now being rolled out to all importers and exporters as announced in the New Customs Audit Regulations.

The New Customs Audit Regulations as indicated above provide that, through voluntary disclosures, companies should be subject to lenient treatments or reduced penalties on their disclosed violations. Therefore one of the aims of the new regulations is to encourage companies to make use of the voluntary disclosure program as part of their routine internal control processes to improve compliance, by providing companies with a sense of direction on Customs’ position on penalties.

Notwithstanding the above, Customs may need to provide further guidance on the implementation of the program, such as clarifications on the determination of cases available for lenient treatments or reduced penalties. Furthermore, availability of the program for situations such as issues disclosed during customs audits that fall outside of the audit scope or unidentified by Customs, identification of any particular situations where lenient treatments and reduced penalties would not be applicable, etc. in order to ultimately achieve the above objective.

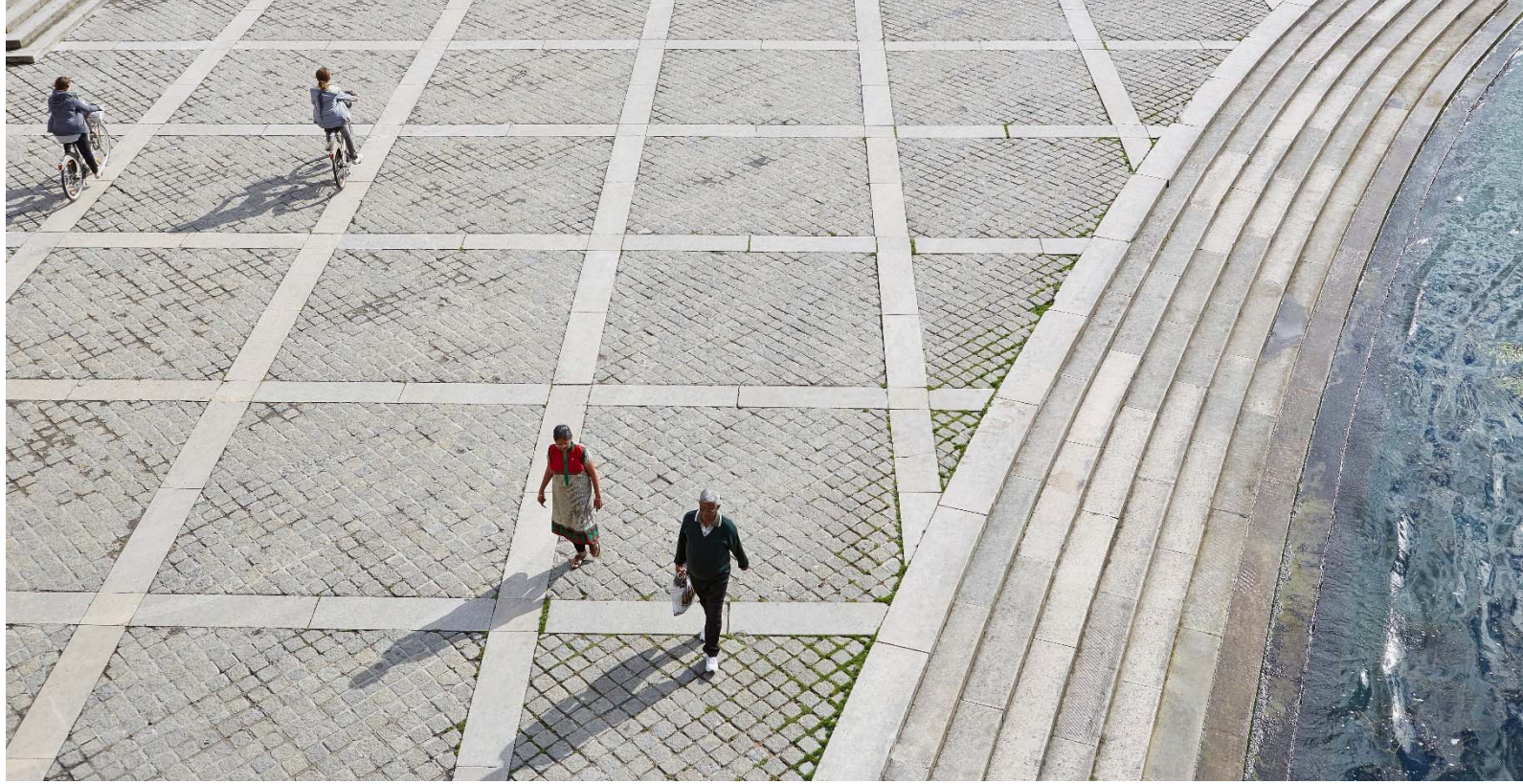
Comparison to other countries

Voluntary disclosure of significant issues commonly requires involvement of senior management at the global and/or regional headquarters level. In view of this, we provide below a high level summary of the general voluntary disclosure processes in other countries. This should help companies understand and compare the similarities and dissimilarities of these programs, so that headquarters can prioritize and determine an appropriate approach/strategy for different locations.

Country	Regulatory Reference	General Process	Treatment
China	In 2014, Shanghai Customs first launched the self-disciplinary management pilot program in the China (Shanghai) Pilot Free Trade Zone ("SPFTZ") and other Customs locations subsequently developed similar pilot programs. Progressing from the above, the voluntary disclosure mechanism is now officially announced in the New Customs Audit Regulations.	Using the SPFTZ process as an example for reference, companies would typically be required to submit a written report either prepared by themselves or by an authorized 3 rd party to Customs for voluntary disclosure purposes. Customs would then review the issues disclosed and conduct audits/investigations where necessary.	The New Customs Audit Regulations indicates generally without specific details that Customs should provide lenient treatments or reduced administrative penalties to companies on issues voluntarily disclosed to Customs.
United States	A formal voluntary disclosure mechanism is available under 19 U.S.C. 1592(c)(4).	If companies disclose historical violations in writing before, or without knowledge of, the commencement of a formal investigation of such violations, Customs would review and determine the case in line with the voluntary disclosure process as stipulated in the regulation.	Customs would alleviate or exempt penalties on self-disclosed violations resulting from negligence or gross negligence.
Australia	A formal voluntary disclosure mechanism is available under the Australia Customs Act 1901 Sections 243T and 243U.	If companies disclose historical violations in writing before the commencement of a formal investigation of such violations, Customs would review and determine the case in line with the voluntary disclosure process as stipulated in the regulation.	Customs would determine penalties under voluntary disclosures on a case-by-case basis.
Japan	A formal voluntary disclosure mechanism is available under Article 7-14 and 7-15 of Japan's Customs Tariff Act regulates mainly covering two situations: overpayment and underpayment of taxes.	In general, voluntary disclosures can be made within 5 years from the date of importation. A report with the correct dutiable amount should be submitted to the Customs where the imports were originally declared.	For the underpayment of taxes, Customs would generally exempt penalties on voluntarily disclosed items (interest are unavoidable). Customs may also consider refund of any overpaid taxes on case-by-case basis.

Comparison to other countries (Cont'd)

Country	Regulatory Reference	General Process	Treatment
Korea	Official voluntary disclosures are only applicable to companies classified as Authorised Economic Operators (“AEO”) during their annual self-assessment process. Korea Customs also accepts voluntary disclosure made by any taxpayer (even if not classified as AEO) for overpaid or underpaid amount under Article 38.3 of Korea Customs Law.	Voluntary disclosures by AEO companies are driven by Customs. Customs would provide a list of review items to the AEO companies, and the companies would conduct self-assessment of the relevant items and report back to Customs. Voluntary disclosure can be made within 5 years from the date of importation by taxpayer.	Additionally declared import VAT amount is subject to VAT draw-back. However Customs generally would not exempt penalties.
Singapore	There is no legislation providing for voluntary disclosures in Singapore, but Singapore Customs does provide formal guidance in its webpage and encourages companies to voluntarily disclose any errors under the voluntary disclosure program.	Companies are generally required to submit reports in a particular format with relevant supporting documents to Customs. Customs would initiate a formal review/investigation to determine the outcome of the issues disclosed.	Customs generally determines penalties on a case-by-case basis for voluntarily disclosed items. They are usually lower than penalties for violations discovered by Customs.
Thailand	Thailand has no official policies on voluntary disclosures. However, in practice, Thai Customs would accept companies voluntarily disclose violations at ports. In addition, Thai Customs would occasionally initiate self-assessment programs for companies to self-assess and report to Customs Headquarters.	Companies voluntary disclosure should generally be submitted to Port Customs, where Port Customs would conduct reviews as appropriate. Companies under self-assessment programs initiated by Thai Customs Headquarters would be notified and the companies involved would file the self-assessments with Customs.	In general, penalty/fines would be exempted for violations under voluntary disclosures.



Implications of the voluntary disclosure program to companies?

Companies may now make use of voluntary disclosures to deal with issues identified in internal trade compliance reviews, where in the past, they may have been more reluctant to do so without a formal process.

Companies should consider establishing a compliance program that includes voluntary disclosure of common issues resulting from normal trading activities in a timely manner, such as:

- Daily import/export declaration errors/issues
- Discrepancies in Processing Trade Customs Handbook
- Issues identified during internal audits
- Issues identified during periodic compliance reviews
- Issues identified in due diligence
- Others

A modern effective trade compliance program should build in a timely voluntary disclosure mechanism of these common trading issues, especially in an environment where more reliance is placed by Customs on self-regulation by companies in order to mitigate risks of penalties, fines and ranking downgrade.



2. Involvement of external professional firms by Customs and companies in customs audits

External professional firms acting as independent 3rd parties may provide more objectivity and technical expertise on certain issues, and therefore, the involvement of external professional firms in assisting Government’s supervision of companies is regularly used by governments in other countries and by various departments such as the Tax Bureau, SEC, etc. With the New Customs Audit Regulations confirming such an approach, the involvement of external professional firms in facilitating Customs audits is expected to be more common in the future.



In 2008, Customs initiated a pilot program to involve and engage 3rd party professional firms for audit work. According to the official data published, Customs appointed professional firms to perform compliance reviews on 5,065 companies from 2008 to 2015.



The <PRC Customs Administrative Measures for the Administration of Enterprise Credit> issued in 2014 also indicate that “*Customs or the applicant companies can appoint qualified external agencies to certify enterprises; findings from the agencies that are recognized by Customs can be used as reference for enterprise credit ranking purposes*”.



The New Customs Audit Regulations also follow this direction and provide that “*in conducting customs audits, Customs can involve 3rd party accounting, tax or other professional firms for professional comments. Where an audited party chooses to engage a 3rd party professional firm, the findings from the professional firm can be used as reference for the customs audit*”.

How to effectively utilize external professional firms?

Topics	Scope	Implications
Supply chain model planning	Obtain professional firms’ assistance in the planning and analysis of optimal strategies for new businesses or market development	Careful initial planning based on the latest technical knowledge and experience can help lower potential costs, improve efficiency and compliance, and prevent risks of future violations in the long run
Establish Standard Operating Procedures (“SOPs”)	Leverage external professional firms’ expertise and experience to assist in establishing SOPs, enhancing internal controls of ERP systems, customs declaration processes and record keeping, financial information, etc.	Establish standardized logistics and information flow processes and management system in accordance with Customs’ requirements, with effective internal controls to improve trade compliance
3 rd party compliance reviews	Utilize external professional firms’ services to review the company’s internal customs risk management processes and mitigate relevant exposures	Assist in performing self-assessments to internally identify potential issues and to formulate strategies to rectify these areas
Customs audit support	Assist in the communication with the company’s finance, logistics, purchase and legal departments; maintain seamless communication and discussion with in-charge Customs	Coordinate with different internal departments in response to Customs’ request in a timely manner, assist enterprise to clarify facts and explain enterprise’s view with Customs as well as to assist in negotiations with Customs

3. Increased importance of enterprise credit ranking

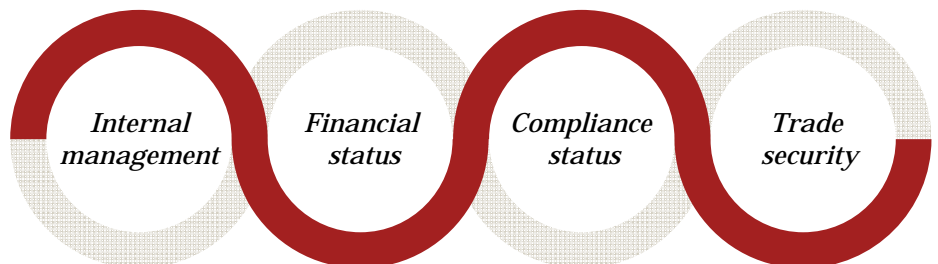
The New Customs Audit Regulations state that “*Customs will determine focus areas for customs audits based on the specific situations of the imported and exported goods, as well as the credit ranking and risk profile of the companies directly related to the import and export of goods.*”

Under the current system, Customs in general monitors companies’ compliance based on their credit ranking. Companies with higher credit ranking would be eligible for more Customs facilitation measures. Credit ranking would also have implications on the frequency and depth of customs audits performed on the companies.

As the New Customs Audit Regulations indicate that “*Customs would determine focus areas for customs audits based on enterprises’ credit ranking*”, higher credit ranking would assist companies in achieving higher clearance efficiency and thus provide a competitive advantage over competitors of lower rankings.



How does Customs evaluate enterprise’s credit ranking?



PwC's value-add

PwC can assist you in the following areas:

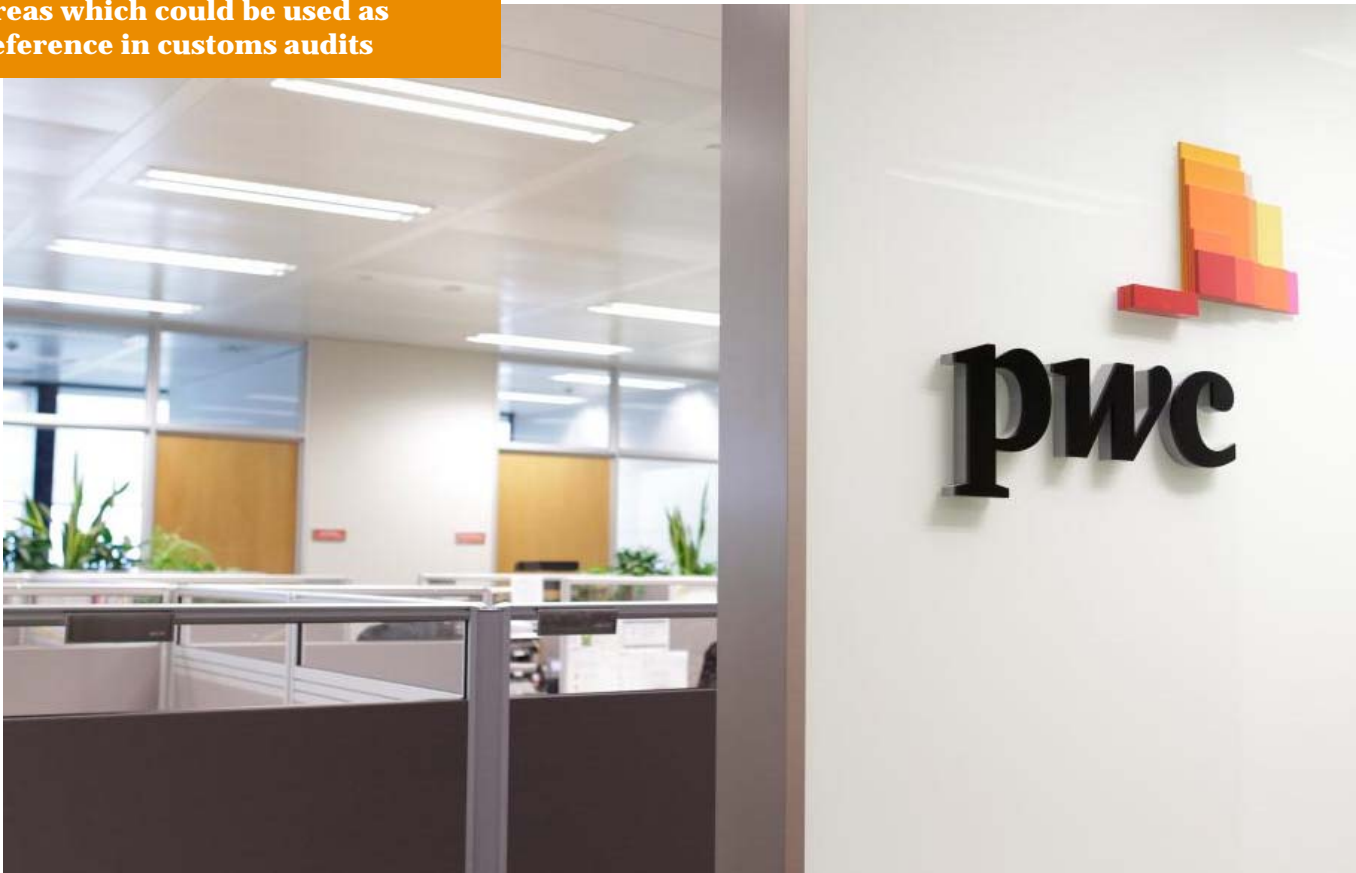
Assist in self-assessments and apply for voluntary disclosures with Customs as appropriate

Conduct compliance reviews to mitigate potential risks and improve compliance

Assist companies to improve internal management and control processes and apply for higher customs credit ranking

Facilitate explanations to Customs during Customs audits or inquiries

Provide professional advice in the accounting, tax and customs areas which could be used as reference in customs audits



Contact us



To learn more about the above or other support provided by PwC Worldtrade Management Services, please feel free to contact us.

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PwC Customs & International Trade Practice

Customs and international trade in China is complex. However, a planned and structured approach with the right resources assigned results in cost savings, higher levels of compliance and fewer unwanted surprises during an audit. PwC specialists within our Greater China customs and international trade practice provide a wide range of advice and services related to creating value, ensuring compliance, and managing risk in relation to the movement of goods into and out of China.

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