

Tax Analysis

China

Deloitte Tohmatsu Tax Co.

January 2017

GAC Issues 2017 Edition of Harmonized System Nomenclature

China's General Administration of Customs (GAC) issued the 2017 edition of the Harmonized System Nomenclature (Bulletin of GAC [2016] No. 48¹, or Bulletin 48) on 2 September 2016. Bulletin 48 becomes effective on 1 January 2017.

(1) Background

The Harmonized System (HS) is a trade tool developed by the World Customs Organization (WCO), and is known as "the common language of international trade." More than 200 countries and Customs or economic unions currently use the HS nomenclature, and more than 98% of global trade is classified based on the HS. The HS is a numerical six-digit multipurpose commodity nomenclature and is mainly used:

- As a basis for customs tariffs;
- As a basis for the rules of origin (e.g. the change of the four-digit heading in the HS is the criteria of origin);
- For the collection of domestic tax (e.g. levying consumption tax on certain imported commodities);
- As a basis for trade negotiations (e.g. the WTO schedules of tariff concessions and the tariff reductions of Information Technology Agreement (ITA) products);
- For monitoring controlled goods (e.g. waste, narcotics, chemical weapons, ozone layer depleting substances); and
- Other applications (e.g. a basis for China's export tax refund rate table).

The WCO generally makes major changes to the HS every five years. For the 2017 edition, the WCO has made a number of changes based on 2012 edition to bring the nomenclature in line with current conditions and growing trends of trade and industrial development. China will also implement the 2017 edition from 1 January 2017 and Bulletin 48 is a Chinese version of the amendments adopted by the WCO in the 2017 edition.

(2) Main changes in the 2017 edition²

The 2017 edition of the HS nomenclature contains 242 amendments that cover a wide range of sectors, such as agricultural, chemical, electromechanical, transportation, etc. Examples of products and items affected include the following:

- To address environmental and social concerns, changes have been made to fishery products, bamboo and wood products in order to better monitor and manage such resources.
- New subheadings are included for specific chemicals, hazardous chemicals and persistent organic pollutants controlled under international conventions for the monitoring and control of these products.
- Changes are made to the size criteria for newsprint, light-emitting diode (LED) lamps, multi-component integrated circuits (MCOs), hybrid vehicles and all-electric vehicles, due to advances in technology.

1 See full text in Chinese: <http://www.customs.gov.cn/publish/portal0/tab49661/info817050.htm>

2 quoted from WCO website: <http://www.wcoomd.org/>

- To adapt to changes in trade practices, certain products are separately identified in existing or new subheadings (e.g. non-alcoholic beer).

(3) Potential impact of changes

The implementation of the 2017 edition of the HS will have an impact on the import and export enterprises in terms of customs classification, tax burden, trade control, compliance, etc. The following table shows some affected goods and how these changes may impact enterprises.

Goods	Amendments	Comments
New energy vehicles	New subheadings are added for pure electric and hybrid electric vehicles	<ul style="list-style-type: none"> ■ Preferential import tax treatment is granted to encourage the import of key components of new energy cars. However, no preferential duty rate applies to new energy cars, and the current import duty rate on new energy cars remains at 25%, which is the same as that on standard cars. ■ It is uncertain whether the import duty rate on new energy cars will be reduced after the new edition of HS is implemented. Affected companies may wish to consider lobbying governments to apply for a lower import interim duty rate.
MCOs	An interpretive note is added to confirm that MCOs should be considered "integrated circuits (IC)" (which are under the heading 85.42) for Customs classification purposes	<ul style="list-style-type: none"> ■ According to prevailing practice, MCOs generally are classified as components of the goods for which the MCOs are used. Therefore, MCOs may be classified under various HS codes, which are likely to result in misclassification and disputes. ■ As from 1 January 2017, all MCOs can be classified as ICs under the heading 85.42, resulting in fewer disputes and an easier customs clearance procedure. ■ It is worth noting that, unlike other IC goods under the heading 85.42 that enjoy a zero tariff, MCOs still bear non-zero tariff rates according to the ITA, although the tariff gradually will reduce.
LED bulbs (tubes)	New subheading is added	<ul style="list-style-type: none"> ■ Customs practice is inconsistent concerning the classification of LED bulbs (tubes). Some classify the goods under the heading 85.43, while others under 94.05. The new subheading will standardize the practice. ■ The import duty rate and export VAT refund rate still are uncertain so affected companies should monitor developments.
Mixed or unmixed immunological products	New subheadings are added	<ul style="list-style-type: none"> ■ The new subheadings clarify the scope of immunological products and will standardize practice, resulting in fewer disputes and an easier Customs clearance procedure. ■ According to prevailing practice, immunological products may be classified under the subheading 3002.10 and enjoys a zero tariff. It is anticipated that the zero tariff will continue to apply to these products. Affected companies should monitor developments.

Ethylene- α -olefin copolymers, having a specific gravity of less than 0.94 (including linearity low density polyethylene)	New subheading is added	<ul style="list-style-type: none"> ■ Linearity low density polyethylene, as one of the ethylene-α-olefin copolymers, has been widely used in the manufacturing of thin films, wires and cables due to its superior property. The customs classification for this product varies in different countries. China has required this product to be classified under the subheading 3901.9020, but the US classifies it under 39011050.10. ■ The new subheading should standardize practice among countries. Affected plastics companies should monitor the import duty and export VAT refund rates for the product after the new subheading is introduced.
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(4) Deloitte's recommendations

Given that the HS is subject to a significant amendment only once every five years, the changes will have a lasting impact on enterprises. Enterprises that are engaged in the import and export businesses of the relevant goods should understand the impact of the changes, and make any adjustments, as needed. For example,

- For goods where new subheadings are added in the 2017 edition, affected enterprises should monitor any possible changes in the import duty rates or export VAT refund rates and evaluate the potential impacts.
- Potentially affected enterprises should examine whether changes have been made to the tariff codes of their products and notify the relevant internal and external departments as soon as possible.
- Enterprises that use global trade automation systems should update the tariff numbers and information.
- The adjustment of tariff codes often leads to challenges by the Customs authorities about enterprises' previous declaration of tariff numbers. Enterprises should examine the codes that currently are used and take appropriate steps to inform the relevant Customs departments.
- Enterprises may be able to use the pre-classification mechanism of commodities and communicate proactively with the Customs authorities to manage risk in advance and mitigate compliance risks.
- The new edition of the HS nomenclature may give rise to some tariff saving opportunities, so affected enterprises should take the steps necessary to benefit from tariff reductions, but ensure compliance.

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Contacts

Gao, Li Qun, Partner ligao@deloitte.com.cn

Zhang, Dolly, director dozhang@deloitte.com.cn

Issued by

Deloitte Tohmatsu Tax Co.

Tokyo Office

Shin-Tokyo Building 5F, 3-3-1 Marunouchi, Chiyoda-ku, Tokyo 100-8305, Japan

Tel: +81 3 6213 3800

email: tax.cs@tohmatsum.co.jp

Corporate Info.: www.deloitte.com/jp/en/tax

Tax Services: www.deloitte.com/jp/tax/s/en

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