Tax Newsflash

China

Deloitte Tohmatsu Tax Co.

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China Announced Changes to Consumption Tax of Cosmetics from 1 October 2016

On 30 September 2016, China's Ministry of Finance and the State Administration of Taxation issued a circular (Caishui [2016] No. 103 (Circular 103)) to remove consumption tax on non-luxury beauty and makeup products, and lower the consumption tax rate for taxable cosmetics to 15%. Circular 103 takes effect from 1 October 2016.

(1) Key changes

Taxable items – Non-luxury beauty and makeup products are no longer subject to consumption tax after 1 October 2016. Therefore, the name of the tax category is now changed from simply "Cosmetics" to "Luxury (high-end) Cosmetics," with the following items included into the taxable scope:

- Luxury beauty and makeup products;
- Luxury skincare products; and
- Cosmetics in packaged sets.

"Luxury" cosmetics are defined based on the value thereof, specifically those with selling price upon production or import (dutiable value), exclusive of VAT, being RMB 10/ml (g) or RMB 15/piece or more.

Tax rate – The consumption tax rate for cosmetics is reduced from the previous 30% to 15%.

Import taxes – The Chinese government also announced a series of import tax regulations to implement the corresponding adjustments to import tax policies for cosmetics.

The General Administration of Customs issued Bulletin 55 on 30 September 2016 to provide guidance for the import declarations of relevant cosmetics. According to Bulletin 55, cosmetics subject to import consumption tax are now covered under a list of 27 ten-digit HS code items.

Where non-luxury beauty and makeup products are transported into China through mails or as luggage or articles by passengers for self-use purposes, the regulations indicate the combined import tax computation rate (i.e. a rate covering consumption tax and other taxes upon importation, e.g. Customs duty, etc.) will be reduced from the previous 60% to 30%, if the value thereof reaches the threshold to trigger the import taxes.

(2) Deloitte's comments and recommendations

Consumption tax reform is one of the key tasks of the fiscal and tax reforms of China's thirteenth five-year plan. The changes of consumption tax policies to the cosmetics sector are not unexpected as the market has been speculating for a series of measures to reform the consumption tax for years. The adjustments reflect the government's intention to guide rational consumption.

It is expected that the government may introduce further changes of consumption tax policies in the future in terms of the scope of taxation, point of tax, tax rates, etc. In general, the major targets of consumption tax include high-energy-consuming goods, high pollution goods and some luxury goods.

Circular 103 will have a significant impact on the sector of cosmetics:

Beauty and makeup products – The costs of beauty and makeup products are expected to be significantly lowered, as non-luxury products are no longer subject to consumption tax, and the tax rate for luxury products is cut by half.

Skincare products – Although luxury skincare products remain in scope of consumption tax, previously many skincare products were not subject to consumption tax in practice due to the long absence of guidance on the determination of "luxury" skincare products. With the clarifications by Circular 103 on "luxury" cosmetics, the scope of taxable skincare products might be effectively expanded after the issuance of Circular 103.

Below is a list of examples illustrating the change of consumption tax rates:

Change of tax rate	Examples	
	Goods	Description
From 30% to 15%	Perfume or toilet water	Perfume (30ml), where the VAT-exclusive selling price by the manufacturer (or dutiable value by the importer) is CNY 300 or higher
	Lip makeup preparations	Lipstick (3g), where the VAT-exclusive selling price by the manufacturer (or dutiable value by the importer) is CNY 30 or higher
	Eye makeup preparations	Mascara (8g), where the VAT-exclusive selling price by the manufacturer (or dutiable value by the importer) is CNY 80 or higher
	Manicure or pedicure Preparations	Nail polish (15ml), where the VAT-exclusive selling price by the manufacturer (or dutiable value by the importer) is CNY 150 or higher
From zero to 15%*	Skincare products	Facial masks (10pcs), where the VAT-exclusive selling price by the manufacturer (or dutiable value by the importer) is CNY 150 or higher

*assuming the product was not subject to consumption tax (see discussions above)

As consumption tax will affect the costs of cosmetics, the affected cosmetics companies are advised to take immediate actions which shall include but not limited to the following:

- Assess the impact to the business from costs and sales perspectives, where a simulation would be necessary since the impact of the above changes could be good and bad, depending on the portfolio of the company; whether and how the change to the purchase costs should be reflected in the retail price needs to be carefully examined;
- Notify and coordinate with the suppliers and the import department/agents in order to ensure the correct and accurate Customs declaration of imported cosmetics, given Customs is responsible for collecting consumption tax upon importation and have announced the relevant changes to tariff codes, unit and other declaration elements;
- Carefully examine the import price of cosmetics and ensure its compliance from Customs valuation perspective, as it is foreseeable that cosmetics products will be an area of focus by Chinese Customs, especially in terms of import value;
- Explore supply-chain planning opportunities to optimize the costs while ensuring compliance for certain cosmetics products whose prices are close to the taxable threshold; and
- Consider transitional tax issues which could possibly arise, for example, the return or replacement of previously sold cosmetics products after the new policy come into force.

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Contacts

Sarah Chin, Partner sachin@deloitte.com.hk

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@tohmatsu.co.jp
Corporate Info.: www.deloitte.com/jp/en/tax
Tax Services: www.deloitte.com/jp/tax/s/en