

Tax

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Tax Analysis

Customs Credit Management System Revised

On 7 March 2018, China's General Administration of Customs (GAC) announced new customs credit management measures for enterprises (GAC Order No. 237) that revise and replace the current rules on the customs credit rating system that have been in effect since 2014 (i.e. GAC Order No. 225). Order 237 will come into effect on 1 May 2018.

Background

According to Order 225, an eligible enterprise may be categorized as an authorized enterprise, a general credit enterprise or a dishonest enterprise based on its customs compliance records. The introduction of the credit rating system and relevant customs administrative measures was to response to the State Council's "Outline Plan for Building a Social Credit System 2014-2020" and follows international trends relating to customs administration.

After three years, the Chinese customs credit rating system is recognized by the business community. Order 237 aims to update the rules to make them more suitable to the new business and regulatory environment. The Standard for Customs Authorized Enterprises, originally published in GAC Bulletin [2014] No. 82 (standard), also will be updated, with the new version expected to be released soon.

Main Changes

Expanded scope of eligible enterprises and information to be collected

Currently, only limited types of enterprises (e.g. importers/exporters, customs brokers, logistics companies) may apply to be recognized as authorized enterprises (the Chinese version of an Authorized Economic Operator (AEO) recognized by

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the World Customs Organization (WCO)). The new rules expand the scope of eligible enterprises so that other types of enterprises (notably, cross-border e-commerce operators, foreign trade service suppliers and cross-border courier delivery service suppliers) may be recognized as authorized enterprises; more details likely will be contained in the new standard.

The WCO allows 13 types of enterprises to qualify as AEOs. Order 237 demonstrates China's efforts to close the gap between the Chinese customs authorized enterprise and that of the AEO so that more enterprises may be able to enjoy the benefits available to authorized enterprises.

Order 237 expands the type of information the customs authorities may collect when assessing a company's customs compliance status to include basic personal information on certain key personnel, such as the legal representative, general manager, finance manager and customs manager.

The expanded scope of information collection will allow the Chinese customs authorities to examine not only the design and operation of an enterprise's internal customs compliance control system, but also relevant information on the persons responsible for monitoring and managing the system. The compliance records of such persons may have an impact on the determination of the enterprise's customs compliance rating.

Coordinated approach among government departments in granting incentives/disincentives

Authorized enterprises will be entitled to various incentives granted by customs and other government authorities in a coordinated manner.

It has been reported that more than 60 government agencies have signed 25 memoranda to share the credit information and provide more than 100 types of incentives/disincentives. An authorized enterprise recognized by customs may enjoy better and expedited government services and less scrutiny in other areas (e.g. social security, tax, foreign exchange, etc.), while a dishonest enterprise may be subject to scrutiny from other government authorities in addition to customs.

Credit information watch list

Order 237 requires enterprises to submit an annual credit information report to the customs by 30 June. An enterprise will be included on a credit information watch list in either of the following cases:

- i. The enterprise fails to submit the annual credit information report; or
- ii. The enterprise is unable to be contacted based on the contact information it has registered with customs, and its registered address or operation place cannot be verified after an onsite inspection.

An enterprise's credit rating cannot be upgraded during the period when it was included on the watch list.

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The annual credit information reporting requirement will apply in addition to the existing annual reporting of customs registration information. The customs authorities have been working with other agencies (i.e. those in charge of commerce administration, enterprise registration, etc.) to establish a cross-department information sharing platform so that the same set of information does not need to be submitted more than once to different government agencies. Enterprises should ensure that the relevant information (e.g. address, the name of legal representative, contacts, etc.) is submitted and updated in an accurate and timely manner.

Changes to criteria for dishonest enterprises

Order 237 adds two new situations where an enterprise will be deemed to be a dishonest enterprise by customs:

- It is included on the credit information watch list for 90 days based on the aforementioned circumstances in "ii" (see "Credit information watch list"); or
- An enterprise has concealed certain factual information from customs in order to affect the customs' credit rating.

Order 237 also eliminates the maximum error ratio of customs declarations under the existing rules, under which an enterprise will be considered a dishonest enterprise if its actual error ratio exceeds the maximum ratio.

A dishonest enterprise may be able to upgrade its status to general credit enterprise status if it has been compliant for two year (extended from one year under Order 225). This extension will make it more difficult for a dishonest enterprise to achieve a better customs credit rating and effectively will increase the costs of dishonest behavior and noncompliant activities.

Suspension/termination of assessment process of authorized enterprises

The customs authorities will be able to suspend the assessment process for determining whether authorized enterprise status should be granted to an applicant if a customs investigation or an audit is initiated against the applicant during the process. Order 237 also provides that if a suspension lasts for more than three months, the customs authorities will terminate the assessment process.

Enterprises should be aware of the adverse impact of customs audits or investigations on their application for authorized enterprises status. This is particularly important following the national customs integration reform launched in 2017 since more post-clearance audits are expected. Further, it should be noted that even for an authorized enterprise, some rigorous customs investigations (e.g. those relating to suspicious smuggling activities) may temporarily disqualify the enterprise for the benefits normally available for authorized enterprises. Therefore, if an audit or investigation is initiated by customs, the enterprise should cooperate with the authorities to resolve and close the case as soon as possible to minimize the potential adverse impact on an application for authorized enterprise status. Affected enterprises may wish to consider undertaking regular internal compliance reviews to identify any noncompliance in a timely manner, and leverage the Voluntary Disclosure Program (VDP). According to Order 237, noncompliance reported through the VDP will not be included in the enterprise's compliance records if the noncompliance resulted only in a warning letter or a fine of less than RMB 50,000.

More categorized customs administration measures

Order 237 introduces more categorized customs administration measures for authorized and dishonest enterprises, for example:

- **Authorized enterprises**
 - Advanced authorized enterprises
 - § Exemption from the customs deposit requirement;
 - § Lower frequency of audits and inspections;
 - § Inspection rate of less than 20% of the average inspection rate for import/export goods of general credit enterprises;
 - § Advance declaration before export goods are shipped to a designated customs area; and
 - § Prioritized customs clearance in special circumstances, etc.

- General authorized enterprises
 - § Lower customs deposits; and
 - § Inspection rate of less than 50% of the average inspection rate for import/export goods of general credit enterprises.
- Dishonest enterprises
 - Inability to apply the consolidated duty collection regime;
 - Requirement to make full customs deposits for bonded materials in processing trade relief; and
 - Average inspection rate of import/export goods will be more than 80%.

The introduction of more categorized customs administration measures will make the authorized enterprise status more attractive and increase operating costs for dishonest enterprises. The clarification of average inspection rates for different categories of enterprises will help promote the transparency of customs administration.

Recommendations

Since the introduction of Order 225 in 2014, the Chinese customs authorities have actively promoted the awareness of the customs credit rating system and encouraged qualifying enterprises to apply for authorized enterprise status. From an international perspective, Chinese customs is proactively building an AEO mutual recognition mechanism so that a Chinese authorized enterprise may enjoy reciprocal benefits in other countries. As of February 2018, China has signed AEO mutual recognition agreements with 35 jurisdictions and been negotiating with certain Belt and Road countries, such as Kazakhstan, Malaysia and Russia, and other trading partners, such as Japan and the US. According to customs statistics, the inspection rate of goods exported from Chinese authorized enterprises to countries that have AEO mutual recognition with China has been reduced by 60% to 80%, and the average time and costs spent on customs clearance has been reduced by more than 50%.

Enterprises wishing to apply for authorized enterprise status should consider taking the following actions:

Continuous improvements to compliance management: Since Order 237 sets high standard to qualify as an authorized enterprise, it is neither easy nor fast for an enterprise to enhance its compliance records in a short period of time. Companies should compare their actual status against Order 237 and the new standard to identify any discrepancies, formulate appropriate action plans and make necessary corrections in a timely manner to continuously improve compliance management.

Regular reviews to maintain sound compliance records: The customs authorities will monitor the compliance records of authorized enterprises and may revoke authorized enterprise status if certain noncompliance activities are identified. Further, increased customs post-clearance audits may put more pressure on enterprise's compliance management. Therefore, even for authorized enterprises, it is important to conduct regular (i.e. at least annually) internal self-reviews to maintain sound compliance records. Where noncompliance is identified during a review, a company should consider voluntarily reporting the noncompliance to customs in exchange for a reduction in, or exemption from, penalties.

Adoption of technology and automation tools to improve efficiency: Enterprises with high import and export volumes and diversified imports/exports under multiple trading modes may face a heavy compliance burden in their daily operations. These enterprises should consider the adoption of technology and automation tools (e.g. big data technologies) to reduce manual work and improve the efficiency of customs compliance management.

Deloitte has solid experience in assisting companies with designing and implementing IT systems to facilitate customs compliance management and applying for recognition of customs authorized enterprise status. We are able to help companies conduct internal compliance reviews against the standard of authorized enterprises, and establish a sound internal control system based on the review results. We have developed system tools that can be used by companies for daily risk screening purposes and to provide directional guidance on management improvements to enable companies to meet authorized enterprise qualifications.

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