

A Summary of China's Processing Trade System
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Processing trade refers to the business activity of importing all or part of the raw and auxiliary materials, parts and components, accessories, and packaging materials from abroad in bond, and re-exporting the finished products after processing or assembly by enterprises within the mainland. It includes processing with supplied materials and processing with imported materials. Under processing with supplied materials, the imported materials and parts are supplied by the foreign party which is also responsible for selling the finished products. The business enterprise does not have to make foreign exchange payment for the imports and only charges the foreign party a processing fee. Under processing with imported materials, the business enterprise makes foreign exchange payment for the imported materials and parts and exports the finished products after processing.

Business enterprises may import goods for processing trade from abroad or from special areas or export warehouses under customs supervision. They may also do so by transfer-in for deep processing. Business enterprises may export goods for processing trade overseas or to special areas or export warehouses under customs supervision. They may also do so by transfer-out for deep processing.

Bonded Supervision

Under the system of processing trade administration, Customs allow enterprises in China to defer payment of tariffs and import-related taxes on all materials and parts imported provided that they are purchased with foreign exchange or supplied by foreign customers. The amount of imported materials and parts actually used in the making of the finished products for export is exempt from tariffs and import-related taxes. For bonded materials and parts imported for processing or finished products which are allowed to be sold in the domestic market, Customs will levy duties and interest on deferred payment on the bonded materials and parts based on valid approval documents for domestic sale issued by relevant departments. If the bonded materials and parts are under import restriction, the business enterprise must also submit the import licence to Customs. All processed finished products for export are exempt from export tariffs.

- Full bond. Full bond is extended to the import of materials and parts by bonded factories and warehouses, the import of materials and parts under counterpart export processing contracts, as well as the import of materials and parts supplied by foreign clients.
- Fixed rate levy. For processing with imported materials not involving bonded factories, bonded warehouses or counterpart contracts, the materials and parts imported are bonded at the rates

stipulated in the Scale for Tax Levy and Exemption on Imported Materials and Parts in Processing with Imported Materials. The scale of tax levy and exemption is indicated in the Processing Handbook issued by Customs.

- Full levy and export rebate. Enterprises which have violated customs regulations or failed to complete the verification and cancellation formalities for prolonged periods are required to pay full tax on the imported materials and parts at the time of import. They may apply to Customs at the place of tax payment for rebates on materials actually used after the imported materials have been processed and the finished products re-exported.

Classification System

China adopts the customs duty deposit system on processing trade enterprises. Under this system, commodities imported for the processing trade are classified into prohibited, restricted and permitted, while processing trade enterprises are classified under four categories, namely A, B, C and D. Category A enterprises are bonded factories with no records of smuggling or violation of customs regulations, with customs officers posted on-site and online links established with the customs office; they also include processing enterprises engaged in such special trades as aircraft or ship building. Category B enterprises are those confirmed by Customs to have no record of smuggling or other violations. Category C enterprises are those confirmed by Customs to have records of violation of regulations; while Category D enterprises are those confirmed by Customs to have records of smuggling or at least three counts of violation of regulations. The Ministry of Commerce publishes a catalogue of commodities subject to management by category and a list of Category A, C and D enterprises. Category B enterprises are not listed.

Customs duty deposit system:

- Materials and parts imported by Category A enterprises, bonded warehouses, bonded areas, and enterprises in export processing zones for processing trade are exempt from customs duty deposit payment. Qualified processing trade enterprises may apply to Customs for permission to establish bonded factories. Business enterprises and processing enterprises may apply to Customs for permission to establish bonded warehouses for the storage of imported materials and parts for processing.
- Category B enterprises are required to make “nominal” payment of customs duty deposit. Business enterprise should open a customs duty deposit account with the Bank of China (BOC) where the processing enterprises are located by presenting a Customs Duty Deposit Account Opening Form issued by the local customs. Upon opening the account, BOC will issue a Customs Duty

Deposit Account Registration Notice, which the business enterprise will submit to the local customs for the registration of processing trade contracts. The enterprise does not have to pay customs duty deposit even though an account has been opened.

- For processing trade involving restricted commodities and for Category C enterprises, “actual” payment of customs duty deposit is required. Customs duty deposit has to be paid into Customs’ special account at BOC. After an enterprise has processed and exported the goods and completed the verification and cancellation procedures within the stipulated time, BOC will refund the deposit to the enterprise upon presentation of the account cancellation notice issued by Customs, with interest paid at call rate. If an enterprise cannot process and export the goods or obtain approval for domestic sales within the term stipulated in the contract, Customs will notify BOC to have the deposit and interest converted into tax payment and interest on deferred payment respectively. If an enterprise cannot pay the deposit, it may apply to BOC to open a letter of guarantee with Customs as the beneficiary. If it cannot obtain a letter of guarantee, it must pay the deposit in cash or by cheque, money order or remittance. Upon receipt of the letter of guarantee or deposit, the Customs Duty Deposit Department of BOC will issue a Customs Duty Deposit Account Registration Notice or Customs Duty Deposit Account Alteration Notice to the enterprise to be presented to Customs together with the letter of guarantee and other documents for filing the contracts.
- As for Category D enterprises, the commerce authorities should revoke their processing trade rights.

Obtaining Approval for Commencement of Processing Trade

Most processing trade activities only require the approval of commerce authorities in the place of registration of the business enterprises (which may be departments at prefecture, city or county level authorised by the provincial-level commerce authorities).

The following documentation will be required:

- A written report by the business enterprise in support of its application and a completed Processing Trade Application Form bearing its stamp.
- Photocopies of the Foreign Invested Enterprise approval certificate)and its business licence.

- Original copy of the document issued by the commerce authorities at or above county level at the place of registration of the processing enterprise certifying its production capacity, and photocopy of its business licence.
- Original copy of the import-export contract signed by the business enterprise with foreign parties.
- Original copy of the processing trade agreement (contract) signed between the business enterprise and the processing enterprise.
- Other documents and materials deemed necessary by the approval organs – for example, a Foreign Invested Enterprise would need to submit its articles of association approved by the commerce authorities stipulating the business scope and production scale of the enterprise, as well as documents proving that the production facilities have been completed and put into operation, that investment is already in place and that the enterprise has passed the necessary annual inspections.
- For processing trade using imported scrap metals or other wastes as materials, an import approval document issued by the State Environmental Protection Administration in accordance with the relevant regulations is required. In the case of processing trade where the import of materials or export of finished products involve chemicals which may be used for the production of dangerous drugs or chemicals for both civilian and military use, an approval document issued by the departments concerned is required.

Processing trade approval organs under the commerce authorities will issue a Processing Trade Approval Certificate stamped with the processing trade approval seal to business enterprises that have submitted the required documents and have proven their ability to process the imported materials and re-export the finished products. This certificate is a valid document for the opening of customs duty deposit accounts with Customs and other departments. The approval organ will examine and verify the unit consumption declared by the enterprise and prepare the “Checklist for the Filing of Imported Materials” and “Checklist for the Filing of Finished Products for Export and Corresponding Consumption of Imported Materials”. These checklists, stamped with the processing trade approval seal, are issued to enterprises for the filing of contracts with Customs.