E-commerce in Asia is booming. China alone is forecast to grow to an over US $350 billion industry by 2016. While some markets may already be considered mature (Australia, for example), the growth of internet connectivity and consumer purchasing power cannot be ignored by either small-to-medium enterprises (SMEs) or multi-national corporations (MNCs) looking to reach new consumers.

However, before a company is online and making sales, they are faced with the daunting task of setting up their web platform and deciding whether it should be hosted locally or globally. E-fulfillment should also be considered under this context. The results of these decisions lead to different customs duty or indirect tax implications. But whether it is e-commerce or traditional commerce, goods are still crossing borders to get to those consumers. So how do you manage the customs and trade implications of such e-commerce, lest they negate the opportunities on offer? This article highlights three potential distribution models that we see emerging for e-commerce transactions in relation to delivery of physical products (as opposed to electronic delivery). From a practical standpoint, we will consider some real-life implications in China, Asia’s emerging but fastest growth online retailing market, and Australia, a mature yet still growing market where shoppers continue to buy across borders.
The Organization for Economic Cooperation and Development (OECD) defines an e-commerce transaction as the sale of goods or services, whether between businesses, households, individuals or governments, conducted over the internet. The payment and delivery of the goods or services may ultimately be conducted on- or off-line. Key issues that capture the attention of companies looking to launch an e-commerce platform often begin with marketing, online branding, translation, cyber security or “localization” of their current platform. But ultimately, how will goods purchased online end up at the consumer’s location? E-commerce is changing the way consumers purchase as well as their expectations for delivery speed and convenience in the delivery location (i.e., brought straight to their door). Meanwhile, consumers are also on the hunt for high quality, aggressive prices and variety. They want to be able to browse and purchase products anywhere, any time and from any device. Ultimately, e-commerce is changing traditional distribution systems around the world. As consumers specifically direct sellers to send them certain products in a specific amount of time, a pull distribution model is emerging and companies need to determine the e-fulfillment solutions required to accommodate these changes.

What is the position in general of the World Customs Organisation (WCO) on e-commerce shipments and distribution? After all, the collection of revenue is historically one of the main cornerstones of a Customs Administration and they want to ensure that all goods have been equitably valued. The WCO is not surprisingly silent on these aspects of e-commerce. The revised Kyoto Convention allows for a country’s national legislation to define the circumstances when liability to duties and taxes is incurred. So for revenue collection, each country will need to ultimately determine its own threshold to combat smuggling and tax evasion but to ensure that tax is collected in a cost effective manner while allowing consideration for personal parcels. Australian retailers are currently embroiled in a bitter battle with the Government over their own low value parcel policies. Local retailers are calling for Customs to do away with the low value parcel exemption, as they claim it is creating an unfair advantage for overseas retailers (i.e., globally hosted websites). Australia’s parcel exemption may in the future be significantly reduced, potentially driving more consumers to shop from locally hosted websites. Personal parcel exemptions aside, perhaps from the silence about other models we can infer that from Customs’ perspective, the remaining distribution models are just that, different models of distribution.
Perhaps the simplest way to “test the waters” of e-commerce is setting up an online store supported by its global website and its server located overseas. A customer will place a purchase order (PO) directly through the website and pay through a credit card in foreign currency. The products are posted from the supplier’s warehouse via postal or express courier services. The online store or company does not at this stage establish a local presence in the market.

Initially, this sounds like a very safe and simple strategy for a company to begin to break into new markets. Additionally, some countries in Asia have a de minimis or personal parcel exemption (PPE), meaning that if a personal parcel is below a determined threshold of duty and indirect tax (e.g., VAT or GST), the PPE can be leveraged to get products to the consumer as quickly and inexpensively as possible. For example, both China and Australia have iterations of an exemption written into their national legislation subject to certain prohibited or restricted items. Both national legislations still allow for inspection or examination of personal items as deemed necessary by their Customs Administrations.

### Scenario 1 - Sales through a global website / direct shipment

<table>
<thead>
<tr>
<th>Country</th>
<th>National legislation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>Generally, no requirement to pay duty or indirect tax on imported goods valued below A$ 1,000. However, depending on the method of arrival (i.e., air vs. sea cargo) a self-assessed clearance (SAC) declaration may need to be lodged.</td>
</tr>
</tbody>
</table>
| China | Mail for personal use having customs duty payable of RMB 50 or less can be imported free of duty unless belonging to “20 commodities prohibited from duty exemption.” Additionally, mail for personal use having a total value of RMB 1,000 or less, or if the package contains 1 article with a value exceeding RMB 1,000; China Customs will use an “assessed value” approach.  
• 4 ranks of customs duty rates (i.e. 10%, 20%, 30% and 50%) are applied depending on the category of the imported articles. |
But what if the goods are moved by express courier and not via a national postal service? Who is the importer of record (IoR) in this transaction? The first issue that a company should review is whether or not an individual purchaser in the country of importation can act as the IoR if the package will need to undergo customs formalities. For example, in China an individual consumer cannot be registered with China Customs and thus will not be able to act as the IoR for importation. A shipper with import/export rights will need to be utilised to clear the goods on the consumer’s behalf.

It is crucially important then that this third party IoR is fully aware of all the relevant details required for customs declaration so as not to hold up clearing the product through customs or incur unforeseen clearance or import tax charges.

For example, it is imperative to share the proper use of INCOterms with the customers upfront when they place the order, so that the IoR knows what adjustments may need to be made to the customs value declaration. In many cases, a PPE may not be applicable and the packages will be assessed duty and tax via typical import formalities. Although the average consumer might not understand INCOterms and customs valuation, explaining very clearly that the seller will deliver the goods to a place specified by the consumer but the consumer is ultimately responsible for clearing the goods, paying any import duty and carrying out import formalities, i.e. DAP (buyer’s home) is instrumental to avoid misunderstandings at a later date.

Customers also need to understand that if they become liable to pay duty for the goods, the duty might be leveraged not simply on the declared cost of the product (i.e., FOB price) but also the shipping and insurance that they paid (i.e., CIF price) as many countries in Asia utilise the CIF price for valuation purposes. It is important to consider these issues up front as the growth of e-commerce is driven by the fact that the consumer is expecting to receive their goods faster and with less hassle than via traditional distribution models.

What happens when products are returned under this model? A return of a defective or unwanted product would technically require export formalities and subsequent re-import formalities in the country of origin making it extremely difficult for the seller to process. Companies should consider how they will handle this issue such as determining their cost threshold to simply provide the customer with a new replacement product, not expecting for the defective piece to be returned overseas.

What if the seller wants to remove some of the uncertainty, cost, and hassle of import formalities from the consumer to offer a better customer service experience? This could be accomplished by the seller using the INCOterm DDP (buyer’s home). Some sellers have begun to outsource their e-fulfillment operations to 3rd party service providers who will handle all of the shipping, clearance and delivery to the consumer for a flat fee, which is ultimately passed on to the consumer as part of the product price. This would be a good option for a seller that wants to minimise the risk and uncertainty of trying to accomplish the e-fulfillment in-house.
In this scenario, an online store is still supported by a global website where its server is located overseas. The company will make bulk shipments of inventory (i.e., lower shipping costs when shipped in bulk) to a bonded warehouse or to a warehouse within a bonded zone. The assessment of duties and other import taxes will be deferred until a PO is placed on the website by a customer. The customer will still make the payment via a credit card in foreign currency. A third-party logistics provider will manage the goods in the bonded warehouse and can post the goods to the customer via a domestic courier service once the goods are sold. The online store would not set up a local e-commerce presence in the market at this stage either.

The deferral of customs duty and tax payment until the moment that the goods have been ordered would make any seller excited. After all, the ability to consign goods as late in the supply chain as possible will save costs. But what type of bonded warehouse or bonded zone should be utilised for the storage and maintenance of goods? In China, for example, public customs warehouses are open to any person having the right to dispose of their goods and are typically run by private enterprises (i.e., 3PLs). They can be located within a bonded zone, such as a Free Trade Zone or a Bonded Logistics Park, or many are located outside of the zone such as within a Tier 1 or Tier 2 city. The warehouse operator often provides services to the seller in addition to storage or stock-keeping; they can assist with logistical support, knowledge of foreign regulations (i.e., tariff classification, valuation, origin) as well as acting as the IoR for importation. These are services that would be undeniably valuable to a SME or an MNC that does not have a local team on the ground. However, all of these services don’t come without a price. In practice, a seller will enter into a service agreement with the 3PL for such assistance. Yet according to customs valuation regulations that “assistance” may need to be factored into the dutiable value of goods at the time that they are finally imported.

What about the return of unsold inventory? A seller would still face complications when a customer wants to return defective or unwanted goods as export formalities removing the goods from commerce and back into a bonded zone would need to be completed.

Furthermore, under both of these scenarios, the seller is also assuming that the consumer has the ability to make payment via their website on a credit card in foreign currency. However, a recent study by the Australian Communication and Media Authority provided that over half of Australian consumers will purchase in either credit card or through a bank transfer. In China, incorporating Alipay, an escrow based payment system which allows a consumer to verify that they are satisfied with goods before releasing the payment, has almost become a necessity to meet consumers’ demands.

Lastly, if a company retains a global web platform, are they sure that they are reaching the maximum possible amount of consumers to generate sales?
So the seller has “gone local”. The online store is supported by a local website where the server is located in the host country. Goods are imported (duty paid) by a domestic legal entity and stored domestically until a customer places the PO through the online store. Payments would most likely be made in local currency. The ordered goods are posted from the warehouse of the domestic online store direct to the customer via a domestic courier service. The domestic online store would establish a presence in the market to support logistics, customer service, returns of the goods sold, etc. A bulk shipment of goods would be made regularly to support the sales of the domestic online store, subject to traditional import declaration and import licensing formalities (as required).

For a consumer, this is the ultimate hassle-free e-commerce experience. Customs clearance and import licensing (if applicable) have been resolved up-front, goods can be returned easily and possibly exchanged with other non-bonded goods that may be in stock, payment for goods can be charged on a local credit or debit card, bank transfer or cash on delivery, and it’s possible that the consumer can receive their goods “next day delivery”. For a seller though, the costs and the risks have just increased substantially. In Australia, for example, a seller could be facing duty +10% GST + brokerage fees + processing fees + lodgement fees + fuel surcharges on each import transaction. Not to mention the fact that returning unsold inventory to the overseas principal may require an export license in some markets or may be subject to foreign exchange controls and is thus essentially prohibitive.

In China, this might be a good option for a company that already has a strong brand presence, a local team on the ground and is looking to make a long term investment in the market. However, it will require a considerable amount of advance work in obtaining an Internet Content Provider (ICP) license from the Chinese Ministry of Industry and Information Technology, which is required to operate a website in China. In Australia, a recent study shows that many consumers have social or emotional concerns about “buying local” and thus supporting their local retailers, despite global websites being cheaper and offering more variety. Thus Australian consumers may be more willing to make purchases from a local website vis a vis an overseas website.
Although not inclusive and not covering all issues that a seller may encounter (consider for example licensing, forex controls and any state controls on e-commerce transactions), the table below some key considerations that a seller should address when thinking of the cross-border e-fulfillment implications.

<table>
<thead>
<tr>
<th>Scenario</th>
<th>Type of Transaction Model</th>
<th>Importer of Record</th>
<th>Liability</th>
<th>Non-tariff barriers</th>
<th>Free Trade Agreements (FTA)?</th>
<th>Return of unsold inventory</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Business-to-Consumer (B2C) Cross-border</td>
<td>Determine if the importing country has a low value parcel exemption that can be leveraged. If not, determine if the customer is able to act as the IoR or if an express courier with import rights will need to be utilised.</td>
<td>Research the INCOTERMS to use in transactions in the case that a package does not arrive as planned. Does your service agreement with the express courier or your 3rd party e-fulfillment provider address liability questions for import clearance in the destination country?</td>
<td>Products could require an import license or other type of certification (e.g., CITES certificate for certain apparel products) regardless of whether they are being delivered to a customer or business. Research the regulations in the destination country for whether or not a license or other import formality is determined, as well as who can apply for one.</td>
<td>If a package is required to undergo formal entry and declaration, many FTAs provide for a minimum value when a Certificate of Origin (CoO) must be provided. Compare this amount with the low value parcel exemption to determine if you should provide a CoO with the shipping documents for your consumer to gain the preferential duty benefits.</td>
<td>Will the customer have to take responsibility for export formalities?</td>
</tr>
<tr>
<td>2</td>
<td>B2C or Business-to-Business (B2B) Cross-border</td>
<td>Same as for Scenario 1</td>
<td>A 3PL can be leveraged under this model so the service contract should explicitly state when the 3PL will assume liability as the IoR for the shipments. Customs valuation needs to be considered to determine if any additions to the invoice value are required, or deductions can be made.</td>
<td>Same as for Scenario 1</td>
<td>Same as for Scenario 1</td>
<td>Note that returning products into a bonded zone (i.e., outside of commerce) may also require export formalities.</td>
</tr>
<tr>
<td>3</td>
<td>B2B Cross-border</td>
<td>Under this scenario, products will likely be imported in bulk by the legal resident entity as the IoR.</td>
<td>The legal resident entity will usually assume liability as the IoR for the transactions. However, the person holding title to the product may also carry some liability. In some Asian countries, domestic courier services are still developing. Structure the service agreement to address liability in the case that goods do not arrive at the consumer’s location following customs clearance procedures.</td>
<td>The legal resident entity should be in a position to apply for and obtain any import licenses or other certificates to comply with non-tariff requirements.</td>
<td>Provide CoOs in the shipping documents for any of the goods can benefit from preferential duty rates.</td>
<td>Return of the goods will happen locally and thus not require export or re-import formalities.</td>
</tr>
</tbody>
</table>
According to the China’s Ministry of Commerce, China’s e-commerce transactions grew 29% year on year in 2011. There are currently almost 400 million consumers shopping online. In Australia, the online spending per buyer is now estimated to be more than $2,000 per year. Ultimately, e-commerce is likely to continue to grow because it provides for lower cost products and more variety and flexibility in brands and product variation, which in turn leads to an enhanced shopping experience. Online security is also improving and an increased number of consumers are beginning to shop from their mobile devices.

However, if a seller decides to maintain a global platform, there is much more to consider than just translation. This article has addressed but a few. Shipping, customs clearance, payment methods as well as how and where to maintain a physical stock of inventory should all be considered. Despite the local versus global platform decision, consumers’ expectations in their e-commerce transactions will continue to increase and eventually sellers might discover that there is not one perfect distribution solution. Regardless, companies without an active e-commerce strategy are leaving significant growth opportunities on the table.
For further assistance about PwC’s customs and international trade services please contact:

**Damon Paling**  
Partner, Shanghai  
+86 (21) 2323 2877  
damon.ross.paling@cn.pwc.com

**Frank Debets**  
Managing Partner, WMS Asia  
+65 6236 3388  
Frank.debets@sg.pwc.com

For more information, please also visit: [www.pwccustoms.com](http://www.pwccustoms.com)

**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.