

Impact of Withholding Taxes

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Royalty Withholding Taxes

Two recent Advisory Opinion (A.O.) adopted by the World Customs Organization Technical Committee on Customs Valuation (WCO TCCV) has highlighted the requirement for withholding taxes (WHT) paid on royalty fees being included in the dutiable value of the fee paid for Customs purposes.



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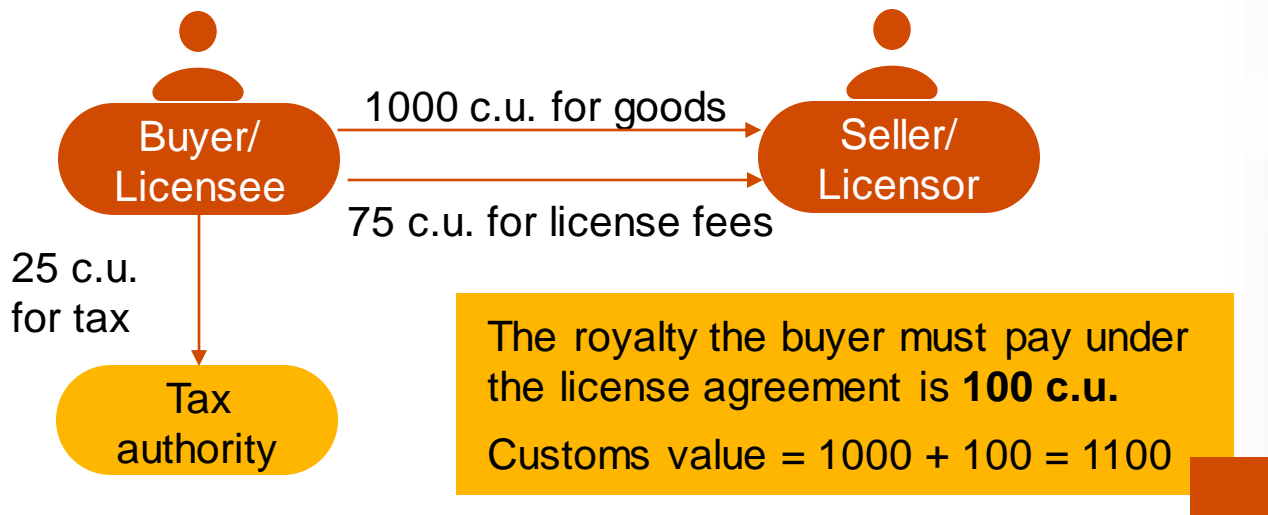
A.O 4.16 deals with withholding tax paid is deducted from the total royalty payment from the buyer to the seller, whilst A.O 4.18 the withholding tax paid is a separate payment on top of the royalty payment from the buyer to the seller.

A.O. 4.16 addressed a gross royalty payment inclusive of withholding tax paid. The Agreement called for a royalty fee of 100 currency units (c.u.) however the licensor only received 75 c.u. after the buyer paid the withholding tax of 25 c.u. on behalf of the licensor.

The technical committee deliberated whether the 75 c.u. or 100 c.u. **should be** added to the dutiable Customs value. The committee opinioned that the difference of 25 currency units does not constitute a reduction in the royalty amount, but a cost which is generated by applying income tax in the country of importation and which is born by the licensor

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In this case, there is a difference between the royalty that the buyer pays and the royalty the licensor receives, the Agreement provides that royalties payable by the buyer are part of the Customs value and does not specify that they are the royalties that the licensor will ultimately receive. In conclusion the 25 c.u. paid by the importer is part of the Customs value under Article 8.1 (c).





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The question in A.O 4.18 was if a withholding tax paid by the buyer for the seller as a separate payment on top of the royalty payment should form part of the dutiable customs value related to the royalty fee payable to the seller.

Some members of the TCCV felt that such a tax should not be included in the dutiable value as it is excluded by paragraph 3 (c) of the interpretative Note to Article 1 (WTO Article VII Valuation Agreement)

“The Customs value shall not include the following charges or costs, provided that they are distinguished from the price actually paid or payable for the imported goods:

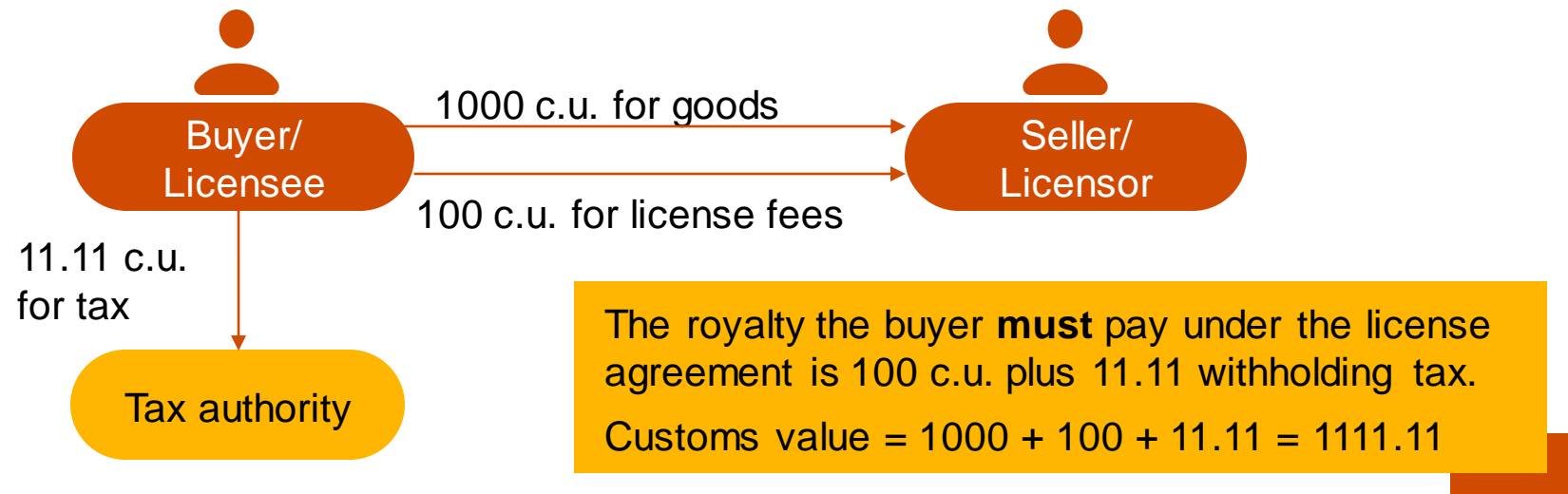
Duties and taxes of the country of importation”

In A.O. 4.16 the committee took the position that this Rule relates to domestic taxes which may be levied on the import of goods rather than taxes which may apply to royalty income. (Paragraph 12)



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Therefore, in satisfying its gross royalty obligation, inclusive of withholding tax, the buyer/licensee makes two payments for the commercial use of the patent. Both payments are made for the right to use the patent under the license agreement. Consequently, as the withholding tax paid forms part of the licensors gross royalty income, it likewise forms part of the licensee's gross royalty payment for customs valuation purposes.



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For business it is important that you know the drivers behind the goods that are being shipped. Is the payment more related to production, or the distribution of finished goods? Does the product price already capture compensation for intangibles, or whether there are separate payments required for things like, services, royalties and distribution rights. Is there a structure in place for paying such intangibles, and how is transfer pricing affected?

Review royalty and other indirect payments regularly with your tax advisors.

Reach out to us for further discussions.



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A large container ship is docked at a port, with several cranes visible in the background. The ship is white with a red hull and is loaded with colorful shipping containers. The scene is set against a bright, hazy sky.

Thank you

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