Japanese Ministry of Finance releases reports on customs audits for FY 2019

January 2021

In brief

On November 4, 2020, the Japanese Ministry of Finance released its annual report on audits conducted by Japan Customs for FY 2019, which covers July 2019 to June 2020. The main points of the report are as follows:

- Japan Customs collected a total of JPY 11.67B from importers as a result of audits, a decrease of 18.7% from the previous year. This included approximately JPY 60M in penalties for fraud or gross negligence, a 27.3% increase over the previous year.
- The top five item categories for assessments were electrical equipment, optical equipment, machinery, tobacco, and plastics. These accounted for approximately 60% of total assessments.

Examples of situations that resulted in assessment were incorrect invoicing, failure to declare additions to value, and use of preliminary invoices for declaration purposes.

In detail

1. **Top five item categories for assessments**
   As per the chart below, the top five item categories for assessments were electrical equipment, optical equipment, machinery, tobacco, and plastics. This was a change from the previous year, when the top five categories were electrical equipment, optical equipment, automobiles, machinery, and organic chemicals. As three of the top five categories are mostly duty-free, this shows that Customs actively audits even those importers whose goods are duty-free.

Rank	Item category (HTS chapter)	Assessment value (MJPY)
1	Electrical equipment (Ch. 85)	2,267
2	Optical equipment (Ch. 90)	1,919
3	Machinery (Ch. 84)	1,453
4	Tobacco (Ch. 24)	625
5	Plastics (Ch. 39)	498

2. **Examples of cases involving under-declaration**

   Case 1: Failure to declare R&D expenses paid by importer separately from invoice

   An importer imported IT devices from its overseas supplier. Per its agreement with its supplier, the importer paid R&D expenses for the imported goods separate from the payment for these imported goods.
   While these R&D expenses should have been included in dutiable value, the importer did not declare them to Customs. As a result, between the R&D expenses and other under-declarations,

the importer was found to have under-declared goods by a total of 889.54M JPY and was assessed a total of 78.26M JPY.

Case 2: Declaring based on provisional invoice value

An importer imported pharmaceuticals from its overseas supplier. The importer lodged import declarations based on provisional invoices provided by its supplier. Following importation of the goods, the price was finalized and the importer was invoiced for the difference between the final price and the provisional price. It is worth noting that declared prices that are subject to year-end transfer pricing adjustments would be considered provisional prices.

While the difference between the final price and provisional price should have been included in dutiable value, the importer failed to file amended declarations to account for these. As a result, between the above and other under-declarations, the importer was found to have under-declared goods by a total of 3.96B JPY and was assessed a total of 344.58M JPY.

The takeaway

While the total value of assessments in FY 2019 decreased from the prior year, the percentage of audits that resulted in an assessment actually increased from 79% to 81%. These results indicate how common it is for assessments to be issued and underscore the importance of performing internal audits beforehand. If importers file a prior disclosure of customs duty or JCT underpayments prior to receiving notice of an audit, they can avoid paying penalties. Conversely, disclosures filed after receipt of an audit notice will be subject to 5% penalties, or 10% if uncovered by Customs during the audit.

For this reason, importers are highly encouraged to implement an internal audit program to uncover any issues before Customs does. With the impact of the COVID-19 pandemic stretching customs revenue thin, Customs may continue to become more proactive in searching out underpayments of customs duty and JCT.

Examples of actions importers can take to prepare for future audits include:

- Ensure that all relevant documents are retained for the period of time prescribed under the Customs Act (5 or 7 years after the date of import, depending on the document)
- Review accounting records and invoices to ensure consistency between invoice amount and amount paid
- Conduct internal reviews to check if separate costs such as royalties, R&D expenses, etc. are being declared when required

Let’s talk

For a deeper discussion of how this issue might affect your business, please contact:

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