



**World Customs
Organization**

Valuation treatment of royalties and licence fees

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Adjustments



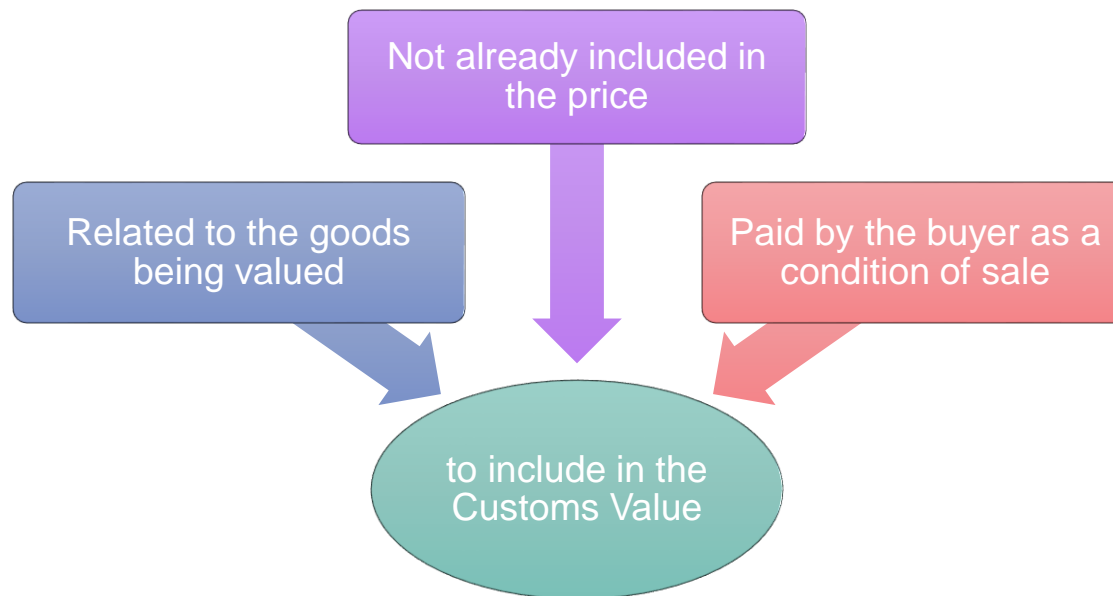
- The Customs value of imported goods shall be the transaction value, that is the price actually paid or payable for goods when sold for export to the country of importation **adjusted in accordance with the provisions of Article 8** of the WTO Customs Valuation Agreement.

Royalties & Licence Fees



- ❑ ... royalties and licence fees **related to the goods** being valued that the buyer must pay, either directly or indirectly, **as a condition of sale** of the goods being valued, to the extent that such royalties and fees **are not included** in the price actually paid or payable;

- Article 8.1 (c)



Royalties & Licence Fees

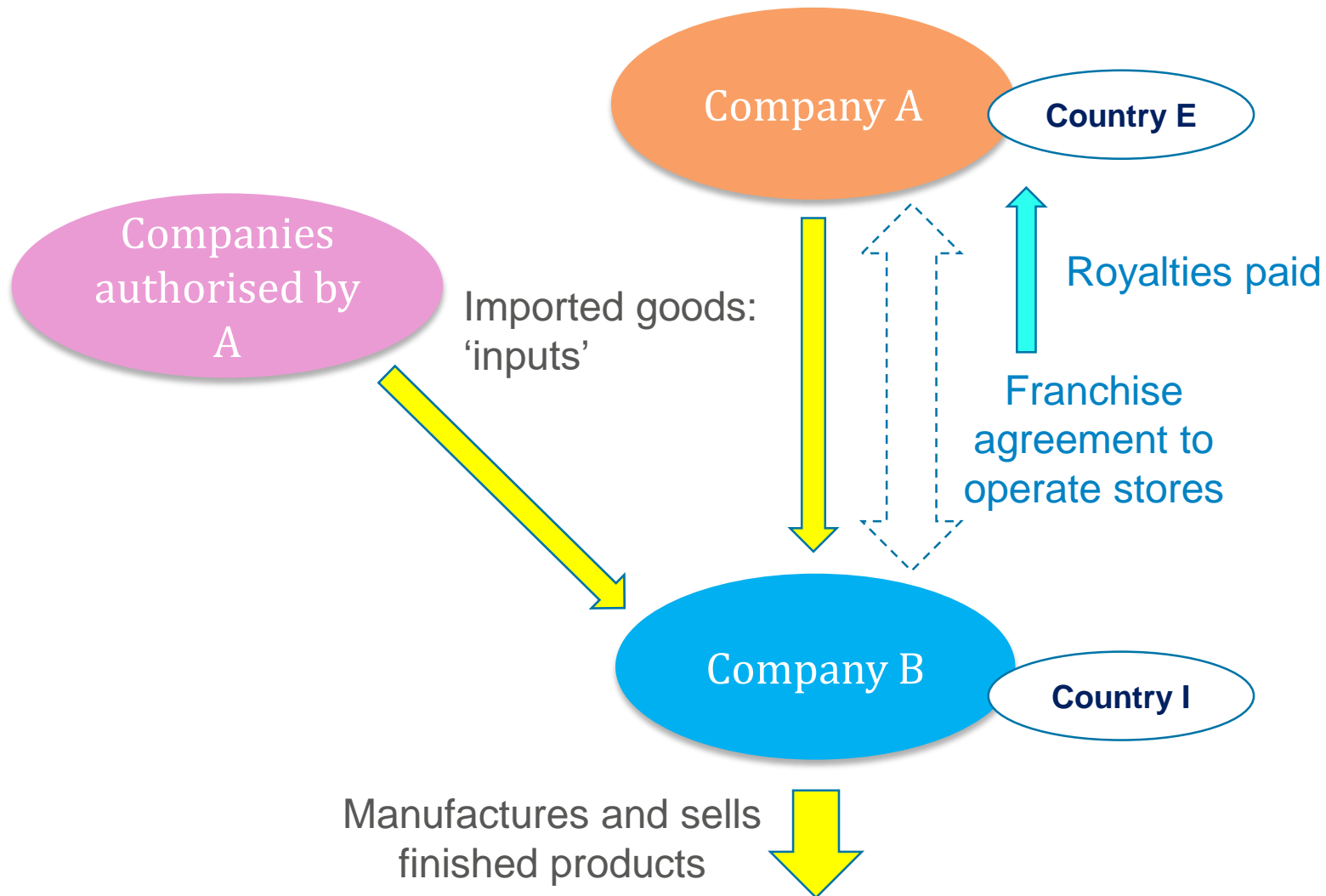


- ❑ Royalties and licence fees may include, among other **things**, payments in respect to **patents, trademarks** and **copyrights**.

- Interpretative Note to Article 8.1(c)

	Nineteen TCCV Advisory Opinions
Patent	5
Trademark	10
Copyright	1
Franchise	1
Distribution	1
Patent and Trademark	1

TCCCV Instruments - AO 4.17



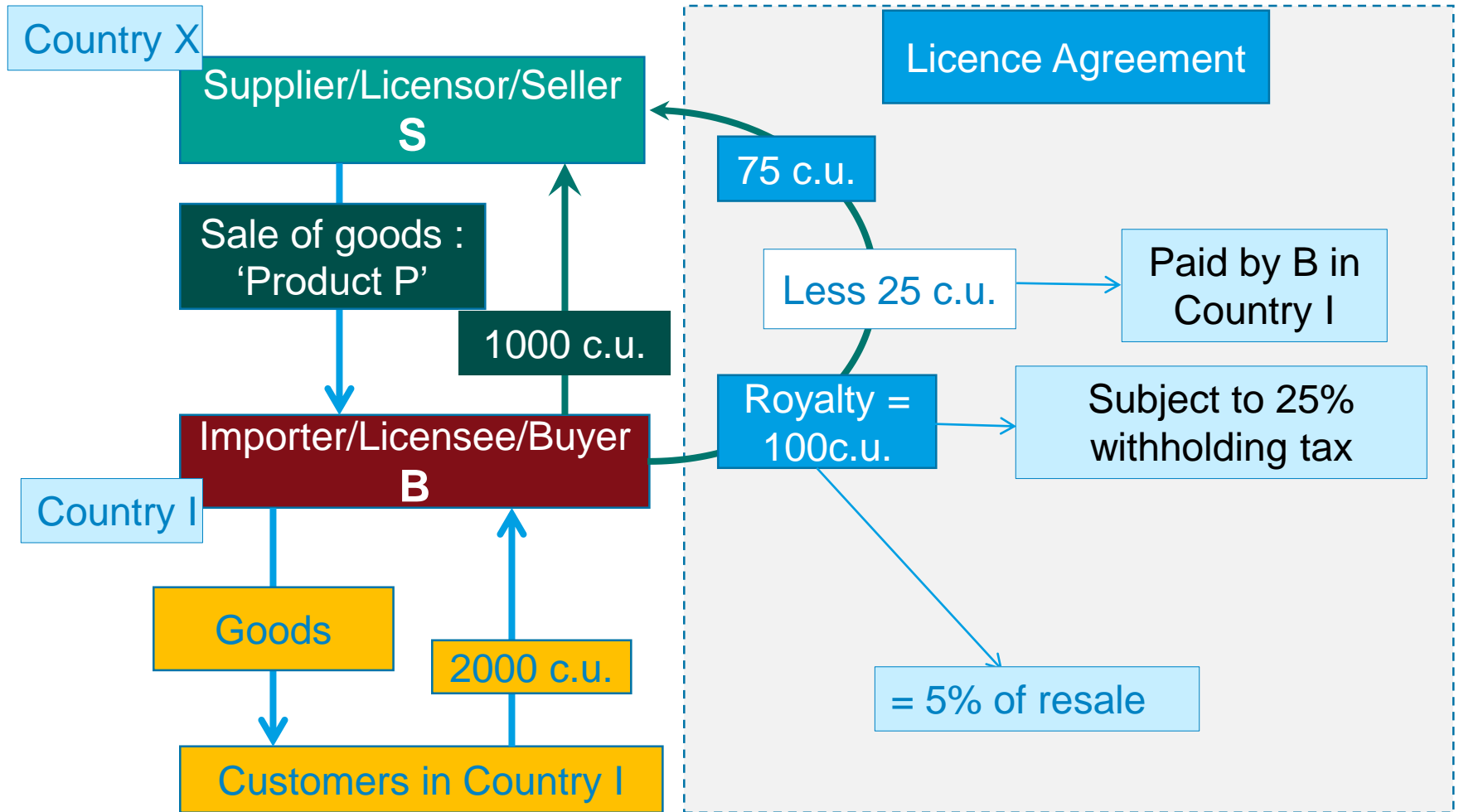
Conclusion



The Technical Committee on Customs Valuation expressed the following view :

- The imported goods, though necessary and essential to the manufacture of the products and required to be purchased from the franchisor (or a third party authorized by the franchisor to meet the quality requirements), are ***not*** branded nor patented, or manufactured under a patented process, for which a payment is made.
- The payment of royalties is not related to the imported goods but to the use of the brands and system of the franchisor in the manufacture and sale of the products bearing the intellectual property (brand) of the franchisor.
- **The royalties paid by the franchisee are not to be added to the price actually paid or payable for the imported goods under the provisions of Article 8.1(c).**

TCCV Instruments - AO 4.16



Issue brought before the Technical Committee :

- **Is the withholding tax paid to the tax authorities part of the Customs value under Article 8.1(c)?**

Analysis (I)



- Article 8.1 (c) provides that : “ ..*there shall be added to the price actually paid or payable royalties and licence fees ... that the buyer must pay, either directly or indirectly ...*”
- The Agreement does not refer to tailoring this adjustment to the royalties that the licensor will receive
- Article 8.1 (c) provides that, dutiable royalties payable by the buyer are part of the Customs value ; it does not specify that this is the amount of royalties the licensor will ultimately receive
- In this case, there is a difference between the royalty that the buyer pays and the royalty that the licensor receives :
 - Buyer/Licensee paid 100c.u.
 - Seller/Licensor received 75c.u.

Analysis (II)



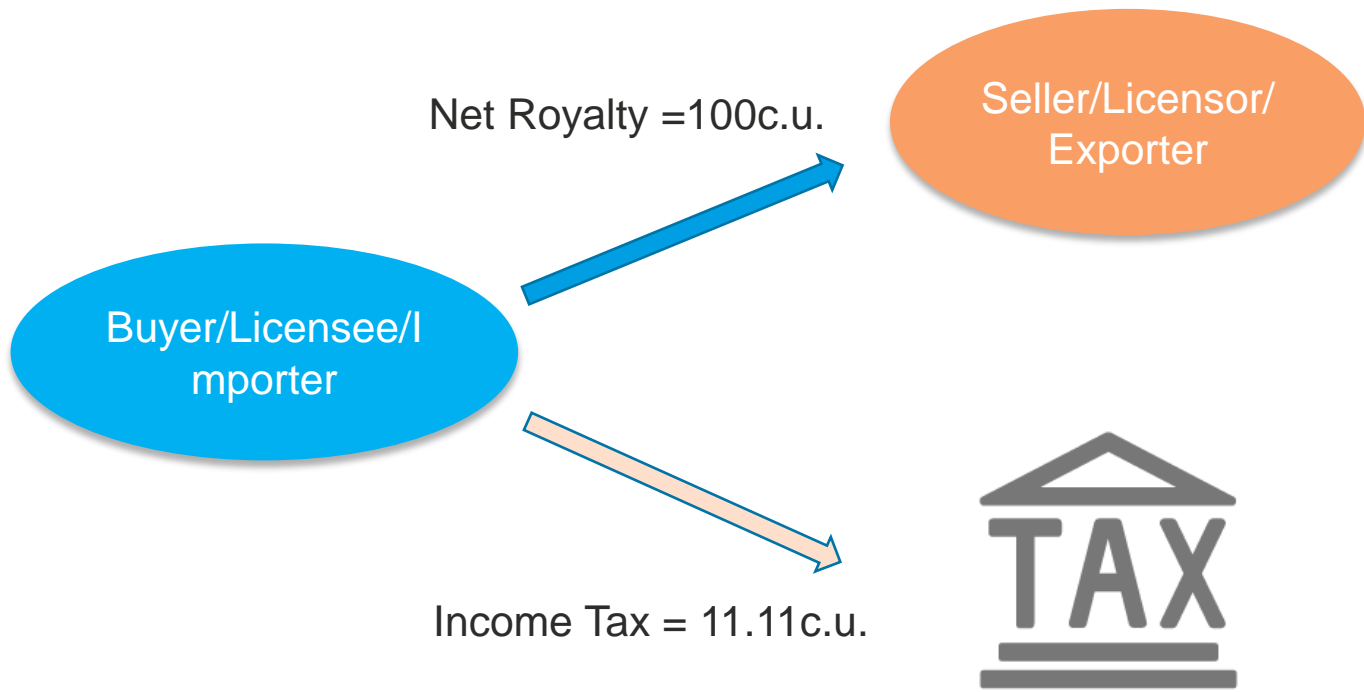
- For the reasons given, in this case, the amount of money which the importer pays, not that which the licensor ultimately receives, should be added to the Customs value of the goods.
- Para. 3 (c) of the Interpretative Note to Article 1, excludes from the Customs value the “**duties and taxes of the country of importation**”
- However, this relates to domestic taxes levied on the import of goods, rather than taxes which to royalty income. Therefore this provision is not relevant.

Conclusion



- The 25 currency units paid by importer B are part of the Customs value of the imported goods under Article 8.1 (c).
- Therefore, full amount of 100c.u. should be included.

TCCV Instruments - AO 4.18



Facts of case - I



- Importer/buyer/licensee B of country of importation I enters into a licence agreement with supplier/seller/licensor S of country of exportation X for the use of a patent. As part of this arrangement, the parties agree that:
 - the royalty payable by B to S for the commercial use of the patent licensed in the agreement will be calculated by applying a rate of five percent (5%) of the net sale price of the patented goods in the country of importation;
 - in addition to the royalty payment, **B must pay the royalty income tax on behalf of S to the Tax Authority** in the country of importation in accordance with the domestic tax rules;
 - the royalty payment must be made without any deduction.
- the royalty payment of five per cent (5 %) agreed between licensee B and licensor S is a tax-exclusive royalty, otherwise known as a **net royalty**. In other words, licensee B must pay both the royalty payment of five per cent (5 %) to licensor S, and the royalty income tax obligation of S to the Tax Authority.

Facts of case - II



- The income tax is based on the total royalty income generated by licensor S in the country of importation, which is known as **gross royalty** inclusive of income tax.

$$\text{royalty income tax} = \text{gross royalty} \times \text{income tax rate}\%$$

$$\text{gross royalty} = \text{net royalty} + \text{royalty income tax}$$

$$\text{royalty income tax} = (\text{net royalty} + \text{royalty income tax}) \times \text{income tax rate}\%$$

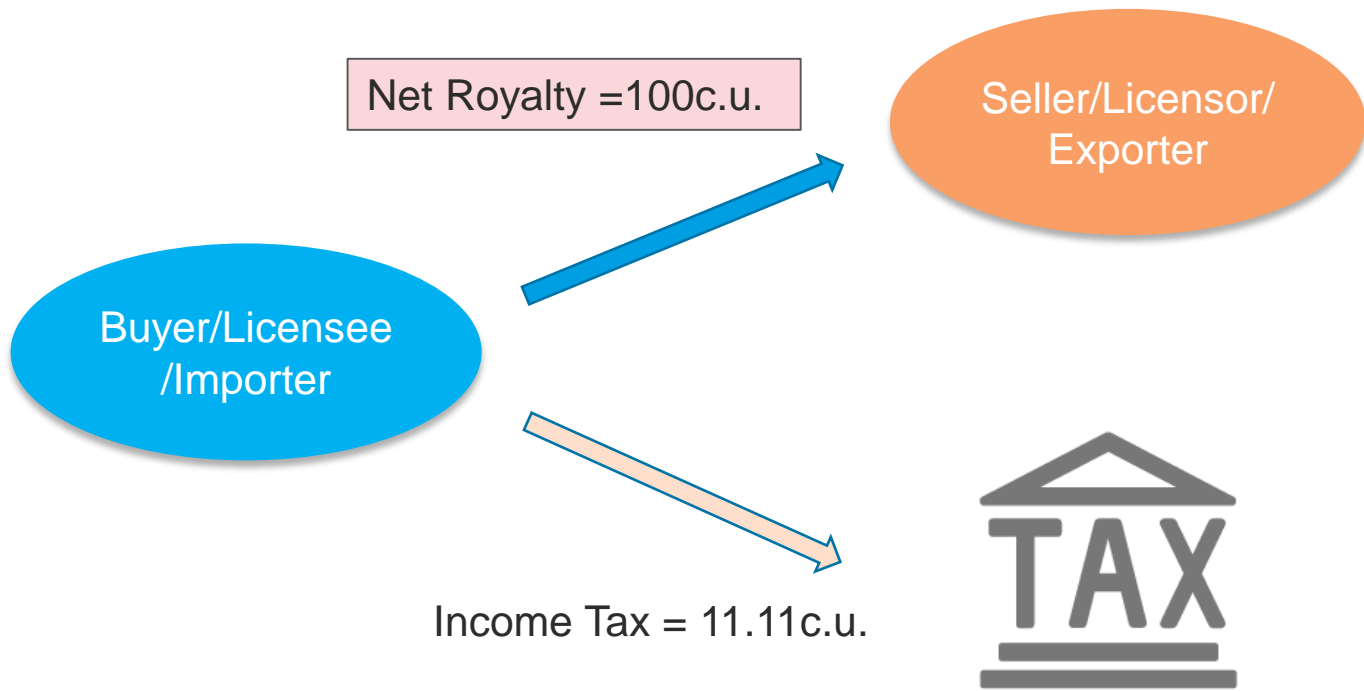
$$\text{royalty income tax} = \text{net royalty} / (1 - \text{income tax rate}\%) \times \text{income tax rate}\%$$

Facts of case - III

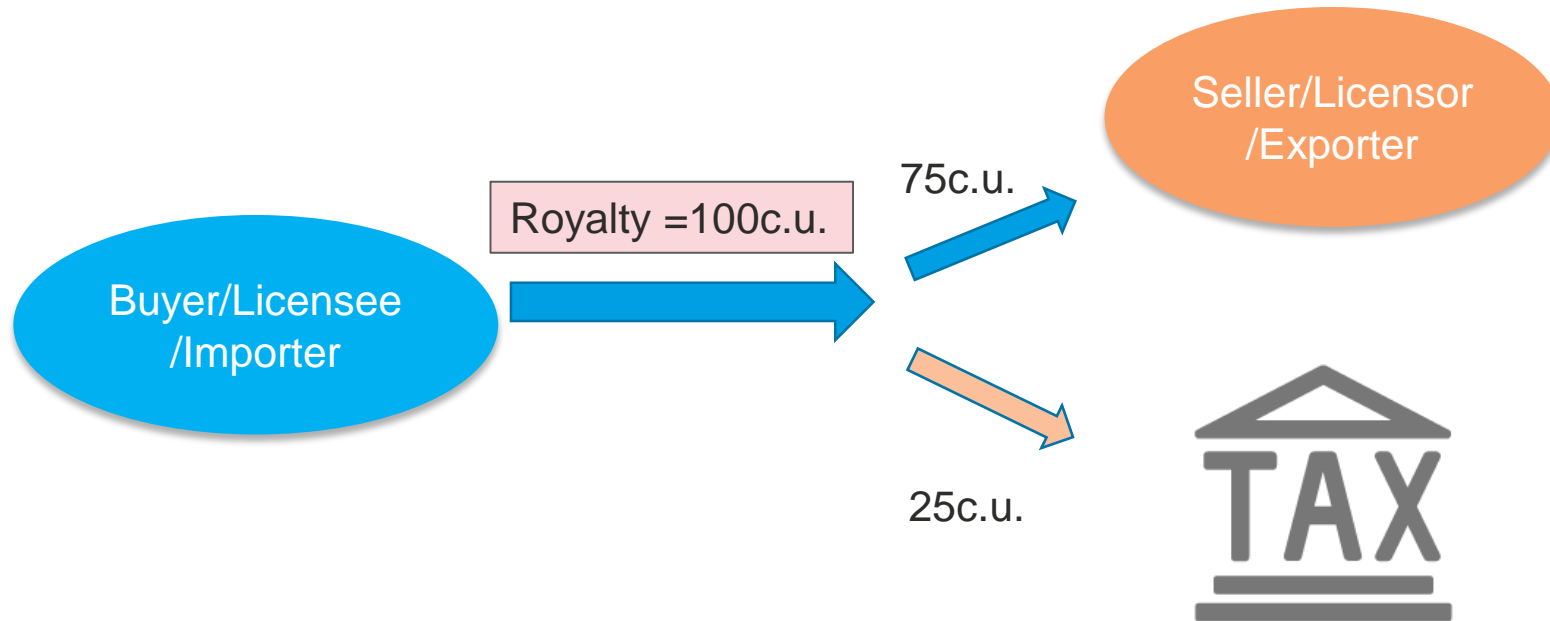


- All conditions of the application of Article 8.1(c) are met.
- The net sale price of product P in country I is 2000c.u., therefore the net royalty that B owes S for use of the patent is 100c.u.
- the royalty income tax rate = 10%
- the royalty income tax = $100 / (1 - 10\%) \times 10\% \approx 11.11 \text{c.u.}$

TCCV Instruments - AO 4.18



TCCV Instruments - AO 4.16



Analysis



- the buyer/licensee B makes two payments for the commercial use of the patent. The first is in the amount of 100 currency units for the net royalty calculated by applying the fixed rate of the net sale price of the patented goods as set out in the licence agreement. The second is in the amount of 11.11 currency units for the withholding royalty income tax.
- Both payments are made for the right to use the patent under the licence agreement. The 11.11 currency units are paid by the licensee to the Tax Authority on behalf of the licensor, and this royalty income tax is considered as part of the licensor's royalty income for tax purposes.
- Consequently, as the 11.11 currency units form part of the licensor's gross royalty income, they likewise form part of the licensee's gross royalty payment for Customs valuation purposes.

Conclusion



- Article 8.1 (c) of the Agreement provides that, in determining the Customs value, there shall be added to the price actually paid or payable royalties and licence fees “that the buyer must pay, either **directly or indirectly**”.
- Given that all the requirements provided for in Article 8.1 (c) of the Agreement are met in this case, the entire gross royalty payment, inclusive of income tax, totalling 111.11 currency units should be added to the Customs value of the imported goods.



Thank you

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