

REPORT OF THE CHAIRMAN OF THE COMMITTEE ON CUSTOMS VALUATION TO THE GENERAL COUNCIL

1. Following the meeting of the General Council in special session on 18-19 October, I carried out several rounds of informal consultations among Members, and on 7 November 2000, the Customs Valuation Committee held a formal meeting, of which a large part was devoted to discussion of the proposals. I believe that these consultations and discussion allowed the consideration of these proposals to move from a political debate to a technically in-depth analysis of the issues. The report below is based on my consultations as well as the Committee's consideration of the three proposals. While it is an overview of the analysis where much of the technical details have been necessarily summarized, it remains a technical report. I believe in order to do justice to the full technical debate, interested Members should refer to the report of the Committee's 7 November 2000 meeting (G/VAL/M/17, to be issued).

Tiret 1: A multilateral solution that enables customs administrations of importing countries to seek and obtain information on export values in a time-bound manner, in doubtful cases, shall be included in the Agreement.

2. The proponent explained, through the use of specific cases, that this proposal emanated from his delegation's experience applying the Agreement and the difficulties encountered therein in combatting fraudulent transactions, in particular under-valuation of the importer's declared price. Although his customs administration had mechanisms in place to investigate fraudulent declarations by importers, often the information obtained showing the fraud could not be used in judicial proceedings because the information was either obtained through non-official sources or on a confidential basis. The proponent was therefore seeking a formal, binding, multilateral solution which would authorize the provision of the necessary information from the customs administrations of the exporting country. If fraud was substantiated by this information, it would be admissible in judicial proceedings. Furthermore, fraudulent transactions were often in the form of third-country invoicing for which it was often necessary to go to the original source of the product to obtain an export price. In the proponent's view, a multilateral solution would ensure that all WTO Members were obliged to provide export price information which would reduce the possibilities for these fraudulent importers to escape detection and ultimately prosecution in courts. The proposal was aimed at establishing such a mechanism through which customs administrations of importing countries, when they came upon a case where they had reasonable ground for assuming a fraud, i.e. a "doubtful case", could request export price information from customs administrations of exporting countries and expect a prompt response. This information would be kept confidential unless and until such time as the fraud was substantiated and the information was necessary for proof in a judicial proceeding, in accordance with Article 10 of the Agreement on Customs Valuation. The proponent acknowledged that a situation where the exporter and importer were colluding would not be addressed by the proposal.

3. Members appreciated that fraud was a problem in international commerce and sympathized with the proponent's difficulties. Many had faced similar problems and were working with the World Customs Organization (WCO) and other providers of technical assistance to develop appropriate customs techniques and enforcement procedures. Several Members noted that this was a problem germane to developing countries where high rates of duties, reliance on customs revenue, and porous borders were realities. Some developing countries supported the proposal, particularly those that were at the pre-implementation or early stages of the transition to the WTO system of valuation.

4. The majority of Members considered that the proposal was not the appropriate solution to combating fraud. They pointed to other appropriate mechanisms which in their experience were effective. Some mentioned, as examples, bilateral agreements between customs administrations, the WCO Nairobi Convention, and the WTO Ministerial Decision Regarding Cases Where Customs Have Reasons to Doubt the Truth or Accuracy of Declared Values. The proponent considered that bilateral solutions did not work, although his customs administration was party to some such agreements, because they were difficult to enter into with all trading partners. Also, a multilateral solution would provide a solution to third-country invoicing where the goods did not undergo further transformation. In this latter case, the proponent considered a multilateral solution necessary because values from the country of origin were necessary. Furthermore, in the proponent's view, the Nairobi Convention was not signed by most delegations and of those that had signed, only 23 had acceded to the Annex dealing with exchange of information on the assessable value.

5. Many Members wondered what was particular about the proponent's problems with fraud that it could not deal with it in the country of import as was foreseen under the Agreement. The importer could deal with fraud through a variety of techniques such as record-keeping, research and analysis, risk assessment, high-risk and low-risk enforcement areas, etc. There was concern that this proposal was a substitute for using proper fraud methodologies and modern customs techniques which were important for implementing the Agreement. The proponent explained that the problem was a limited one and some goods were more subject to fraud than others. It stressed that it wished to have this additional piece of information from the customs administrations of the exporting country to support its own investigations. This raised an important concern for some Members that the proposal, if adopted, would shift the burden of proof from the importing country, where all the powers of the Agreement and necessary evidence presently lay, to the exporting country. If the proposal meant that exporting authorities would have to verify the accuracy of the information submitted to them, this would amount to shifting the investigative burden to the exporting country's authorities.

6. Other technical issues and questions concerned the meaning of the term "**doubtful cases**" in the proposal and how customs would go about determining what was a "doubtful case." Although it was acknowledged that the importing country had the right to determine what was a doubtful case for its own internal investigations, legal difficulties could arise if the determination imposed obligations on exporting countries' customs administrations.

7. Although acknowledging the proponent's reference to Article 10 of the Agreement, several Members noted that, according to their national legislation, information provided by exporters to their national customs administration was governed by **confidentiality requirements** which restricted divulging this information to other bodies. Even before exporting authorities could provide the information, there may be certain domestic procedures that might stand in the way. One Member, in support of the proposal, noted that Article 6.2 of the Agreement stated that a request could be made to the authorities of other countries in order to obtain information for determining the computed value. This was similar to what the proposal was trying to accomplish and showed a precedent for third countries assisting in verifying the customs value.

8. Some Members were concerned that the proposal might place undue burden on customs administrations to provide information to importing countries. This would be an inappropriate diversion of resources from customs' prime responsibility. **The resource implications** of the proposal would have to be analyzed and export clearance systems might have to be modified to accommodate this proposal. Questions were asked as to whether there would be an expectation that customs administrations of exporting countries would visit offices of exporting companies and would the proponent's customs administration be willing to check its own importers and exporters for such information. Although many countries did collect export price data, many Members explained that it was done primarily for statistical purposes and was not verified, nor was it on a transaction-by-transaction basis, which would be necessary for the functioning of this proposal. Further, it was not clear whether the proposal required customs administrations to examine exporters' books to determine the price data for a particular shipment. If so, it would be problematic. It was also noted that export

prices varied considerably depending on the situation. Therefore, export variables could not under the Agreement be used as a reasonable basis to determine the customs value of the imported goods.

9. Many Members questioned what was meant by the term **"time-bound manner"** and what the legal implications would be if an exporting countries' customs administration was not able to provide the information requested in a "time bound manner". The proponent explained that the term "time bound" meant promptly and without inordinate delay when an export value was requested. Another Member asked what was meant by the term **"to seek and obtain information"** and how customs authorities of importing countries would go about seeking and obtaining the information. A final question concerned whether the importing country would stop **the import clearance system pending the investigation** envisioned by the proposal. It was clarified that the idea of requesting information was to cross-check and in cases where there was no problem with the declared value, it would actually expedite the clearance. In any case, importing customs administrations would be bound by Article 13 of the Agreement to release the goods.

Tiret 2: The addition of cost of services such as engineering, development, and design work, which are supplied directly or indirectly by the buyer free of charge or at reduced cost for the production of goods under import, shall be included in Article 8:1(b)(iv).

10. The proponent explained that the objective of this proposal was to allow the inclusion of the services listed in Article 8:1(b)(iv) of the Agreement into the calculation of the customs value, even if these services were undertaken in the country of importation. Presently they are only allowed to be included if they are provided by the buyer but undertaken elsewhere than in the country of import. The goods listed under the first three items under Article 8:1(b) could be supplied either by the exporting, importing or a third country. No distinction was made and in all three cases, the costs of the listed goods would be included in the customs value. As far as the proponent was concerned, there was a logic in providing the same treatment for the services listed in item four of this Article. The proponent explained that the different treatment for goods on one hand, and for services on the other, under this Article was giving rise to bifurcation of values by fraudulent importers who often tried to deduct part of the value by claiming that such services, which comprised part of the value, were provided by the buyer and undertaken in the country of importation. Cases were often difficult to prove, since money transfers were difficult to trace.

11. It was difficult for many Members to appreciate how this proposal would alleviate the problem cited by the proponent of fraudulent importers splitting values into cost elements internally and externally sourced. They noted that fraudulent importers could always try to find other ways of evading the declaration of the value of these services or declaring lower amounts, even if they were internally sourced and required to be part of the value. Acknowledging that it could be difficult to trace financial transactions in today's world of information technology, some asked why such transactions would be found through this proposal. Importers would still have to be monitored and audited if there were problems in their declarations and there were other tools, instruments and techniques to deal with fraud and to identify the actual services involved and their costs.

12. Several Members noted that the Agreement's structure had not changed since its inception twenty years ago and that it would cause serious disruption to industry and commerce which had built up their businesses around the particular valuation treatment presently in the Agreement. Some Members wondered what the economic rationale would be for including the costs of these services performed in the country of importation. By not including internally sourced services into the customs value, the Agreement as it was presently structured, provided an economic incentive for the use of these services that were domestically sourced. Another Member explained that the exemption under Article 8.1(b)(iv) existed because the provision pertained to services carried out in the importing country.

13. Another Member was concerned that if such services were to be included in the customs value, it would be a means of inflating the import price which would in the end be paid by the domestic consumers. Another Member, while acknowledging the beneficial revenue collection

effects of this proposal for the importing country, noted that it could create a problem of double taxation for importers. The cost of a service provided by the buyer may have been subject to domestic taxation and would then be taxed again in the form of an import duty. Therefore, the importer could be paying tax on this service twice.

Tiret 3: The residual method of determining customs value under Article 7 shall be inclusive of all residual eventualities, thus allowing valuation based on domestic market price or export price in a third country with appropriate adjustments.

14. The proponent clarified that the proposal was aimed at including two presently prohibited methods of valuing imports for customs purposes as allowed methods under Article 7 of the Agreement. The first, (presently item (c) in Article 7) was the domestic market price in the exporting country, (not in the importing country); and the second (presently item (e) in Article 7) was the price of the goods for export to a country other than the country of importation. He noted that these prices were presently used in other Agreements such as the Anti-Dumping Agreement and clarified that Article 7 and these two additional proposed methods would only be used as a last resort when the other methods could not be used. One Member voiced support for the proposal, indicating that it could facilitate the work of customs administrations in establishing the customs value for new and innovative products, in the event that the other methods under the Agreement could not be used.

15. A number of questions were raised by Members regarding the necessity of changing a long-standing provision of the Agreement which prohibited the use of these two price methods under Article 7 of the Agreement. It was considered that the negotiating history as to why these methods were prohibited might be an important element to examine.

16. Several Members asked how the information necessary to determine the two proposed price methods would be obtained. In the event that a wholesale catalogue price or a shopping center price were used, there was concern that these were not reliable prices, could inflate customs values, and often were only starting points for downward price negotiation by buyers. Some Members suggested that in the domestic market of the exporting countries, the price could be considerably higher because of overhead costs, advertisement, promotion and other costs that were incurred on the domestic market. In addition, it might be necessary to examine exporter's financial books to ascertain these additional costs. This could be problematic and the end result could be the use of high, fictitious customs values. Regarding the export value to a third country, it was asked which third country would be chosen - would it be the highest priced country or the lowest. Would customs administrations shop for the best price among third countries and how would they determine which best reflected the transaction value. Furthermore, how would the information necessary to make "appropriate adjustments" be obtained? The proponent noted that explanations for establishing the proposed prices already existed in these other Agreements so he did not see the difficulty in obtaining them for use in this context. Further, he clarified that the prices could not be used directly but adjustments would have to be made, for example with respect to FOB or CIF basis, for different quantities, etc. These were all existing adjustments under the Agreement.

17. A few Members questioned the wisdom of making reference to one Agreement in the context of discussing another and the risk of mixing concepts. It was pointed out that under the Anti-Dumping Agreement, the objective was determination of price discrimination which warranted examination of the domestic price in the exporting country to compare it with the export price to the importing country or a third country. Under the Customs Valuation Agreement, the objective was determination of the value of the transaction between the exporter and the importer. These two objectives were completely different and therefore the price concepts could not be compared. The proponent explained that the proposal was not designed to bring concepts of other Agreements into the Valuation Agreement and reference to the Anti-Dumping Agreement was simply incidental. His delegation was committed to the transaction value and if that failed, to the following methods in the Agreement. If all failed and the customs administration arrived at Article 7, it wished to be able to use the two prices proposed which were presently prohibited.

18. Another Member reminded delegations of the importance of the interpretative notes to Article 7 which stressed the importance of using previously determined values and that, under Article 7, they should be used with reasonable flexibility in their application. Also, the Agreement itself clarified that such flexibility could be possible within the provisions of Article 7 and it was unnecessary to look further.

Summary

19. Some Members supported the proposals and their objectives. However, of those who spoke on the proposals, the majority acknowledged the genuine difficulties faced in addressing fraud and the problems experienced by the proponent of the tirets. That said, they failed to be convinced that the tirets themselves were appropriate solutions. Indeed, some of these Members had themselves experienced the same problems but had dealt with them by using existing mechanisms and instruments while remaining within the parameters of the Agreement.
