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ISSUES PAPER: REVISION OF CUSTOMS CODES CAN BE THE FOUNDATION FOR IMPROVED CUSTOMS ADMINISTRATION AND TRADE FACILITATION IN CENTRAL AND EAST ASIA

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The essential prerequisite for a modern customs administration is a customs code that incorporates international “best practices” and applicable international agreements. In the absence of proper legal authority, customs administrations cannot implement the international “best practices” set forth in the World Customs Organization’s Revised Kyoto Convention,² nor can they properly put into effect international treaties and agreements governing customs procedures, such as the Harmonized System Nomenclature and the World Trade Organization’s Agreement on Customs Valuation. Equally important, poorly designed customs laws create significant non-tariff trade barriers and result in a substantial loss of tax revenue.³

Problems and Goals in the Region

Trade and transport facilitation. A modern customs code should help government and society meet crucial goals. Trade and transport facilitation is one of these paramount objectives. In the C.I.S. countries of Central and East Asia (CISCE)⁴,

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² The International Convention on the Simplification and Harmonization of Customs Procedures, administered by the World Customs Organization. As of June 30, 2003, there were 14 signatories to the Convention, an insufficient number for it to come into effect. Ratification by the European Union and United States is pending.

³ Unfortunately, no internationally recognized model customs code has yet been developed that incorporates current “best practices” and applicable international conventions and agreements. The World Customs Organization (WCO) has sponsored the development of international customs administration standards and best practices, most recently the Revised Kyoto Convention, but has never developed a model customs code. The GATT and the World Trade Organization (WTO) have adopted various trade facilitation codes and agreements but to date have never attempted to negotiate a model customs code. The United Nations, through UNCTAD, ESCAP and ECE, have for decades been involved in trade facilitation work related to customs (as examples, UNCTAD has developed ASYCUDA, a modern computer system for use by customs administrations and ECE sponsors the TIR Convention), but have never undertaken the development of a customs code. The OECD has studied corruption and taxation issues in customs administrations and developed model tax and anti-corruption codes, but also has never developed a model customs code.

⁴ For the purposes of this paper, the CISCE includes Azerbaijan, Turkmenistan, Uzbekistan, Kazakhstan, the Kyrgyz Republic, Tajikistan, and Mongolia.

transport costs are at least three times higher than in the developed countries.⁵ A long list of barriers to trade and transport increase costs and make trade and transit arrangements unpredictable: small and fragmented transport markets, lack of access to sea ports and ocean transport, “unofficial” payments, poor access to reliable information with regard to international trade and transport, under-developed logistics services, the lack of the conducive environment for the development of multi-modal transport, and poor roads and other physical infrastructure impediments.

Regional and global integration. Increased regional and global integration is another important goal. The European Union is a recent example of how the harmonization of laws and procedures and the elimination of barriers at national borders can substantially increase the economic well-being of all member states in a region. GATT and the World Trade Organization (WTO) is an example of how the implementation of multilateral trade agreements can economically benefit all member countries. Unfortunately, the CISCE countries are still at the beginning stages of regional economic integration.⁶ Moreover, only two CISCE countries, the Kyrgyz Republic and Mongolia, are currently members of the WTO.

Enhanced revenue collection. More efficient and effective revenue collection is also critical. Revenue obtained from border taxes such as customs duties and VAT assessments is a major contributor to the national budgets of CISCE countries.⁷ The lack of a strong legal basis for tax assessment, authorizing post-entry audits with tax inspectors, single taxpayer numbers, computerization of tax collection and strict criteria for tax exemptions, result in major losses of tax revenue.

More effective law enforcement. In an era of international terrorism, well-organized narcotics trade, wide-spread piracy, counterfeiting and other intellectual property rights violations and health threats from AIDS and other viruses, improved law enforcement at borders is also essential. However, law enforcement may be impeded if national customs laws do not permit the free exchange of threat information and criminal activity with other countries or authorize cooperation on national borders with other law enforcement agencies.

Consultative relationships with the “trade.” Increased public participation in customs administration and transparency of customs administration is also critical to the development of democratic institutions, optimum customs administration and an effective balance between law enforcement and trade facilitation responsibilities. In CISCE countries, Kazakhstan has been in the forefront in consulting with the trading and business community and the public at large in the development and implementation of a new customs code.

⁵ See Eva Molnar and Lauri Ojala, Transport and Trade Facilitation (TTF) Issues in the CIS 7, Kazakhstan and Turkmenistan, World Bank (draft paper, 2003).

⁶ As an example, the Eurasian Economic Community, comprising the Russian Federation, Belarus, Kazakhstan, the Kyrgyz Republic and Tajikistan, is in the early stages of development.

⁷ For Tajikistan, border taxes contribute more than 40% of funds for the national budget.

Some Current Issues Regarding CISCE Customs Codes

The following comments are based upon the author's recent consulting work in connection with the development of new customs codes in Kazakhstan, the Kyrgyz Republic and Tajikistan. The comments reflect the author's views and do not necessarily reflect the viewpoint of any international or national organization or government.

Harmonization Efforts Are Focused On The Russian Federation To The Exclusion Of Other Trading Partners. For historical, economic and political reasons, Russian Federation Customs has taken the lead in assisting CISCE countries in developing new customs codes, and new codes in Kazakhstan, the Kyrgyz Republic and Tajikistan closely follow the customs code adopted by the Russian Federation in 2003. Increased integration of the customs laws and procedures of CISCE countries with each other and the Russian Federation is generally desirable from an economic point of view and has been supported by international donors such as USAID. However, regional harmonization efforts should incorporate international "best practices" and applicable GATT/WTO standards; otherwise, they may result in the creation of significant non-tariff barriers to trade with non-CISCE countries in the region and countries outside the region.

In addition to Russia, China and India are important, rapidly developing economies in Asia and Japan and Korea are major economic powers. The CISCE countries should not make the mistake of harmonizing customs laws with Russia at the expense of erecting (or maintaining) barriers to trade with China, India, and other non-CISCE countries in Asia. China in particular borders a number of CISCE countries and has the potential to be a major market - perhaps the most important market - for exports of goods and services from CISCE countries.

A Legal Question Exists Regarding The Application Of International Agreements To Customs Codes. CISCE customs codes typically provide that international agreements that have been ratified by the country prevail over inconsistent provisions of the customs code (see, for example, the draft customs code of Tajikistan, article 3(4)). However, the jurisprudence on this issue is not clear. Some CISCE jurists believe that the Principles of C.I.S. Customs Administration, adopted by C.I.S. countries in the mid-1990s, take precedence over later-enacted inconsistent provisions in customs codes. Other jurists believe that later enacted customs codes prevail over inconsistent international agreements. This issue must be clarified. If the C.I.S. Customs Principles take precedence over newly enacted customs codes, implementing WTO agreements and Revised Kyoto Convention "best practices," customs modernization efforts may be greatly impeded.

The legal status of international agreements in relation to customs codes is also relevant to the implementation of the T.I.R. Convention. If customs regulations imposing full border inspections and customs convoys supersede the expedited transit under customs seal and guarantee procedures specified by the T.I.R. Convention, the trade facilitation benefits of the T.I.R. Convention will be largely lost.

CISCE Customs Codes Are Too Complex. Customs codes closely modeled on the new Russian Federation customs code are too complex for countries such as Tajikistan and the Kyrgyz Republic, with limited economic and administrative resources and small-scale trade. Many administrative details that would be better left to administrative regulations and decrees are included in CISCE customs codes. Apparently this results in part from the legacy of the Soviet Union's legal structure and in part because of a concern that unless details are included in the customs code, traders may be subjected to arbitrary action by customs officials.

A basic principle established by the Revised Kyoto Convention for customs procedures and practices is that they should "be as simple as possible." See Revised Kyoto Convention, General Annex, Chapter 1, Standard 1.2. This principle also applies to customs codes. CISCE customs codes typically have many more articles and more detailed provisions than the European Union's customs code, and treatment of customs procedures is much more detailed. A greatly simplified code, combined with administrative regulations and decrees that set forth specific procedures, would be a preferable approach. Regulations and decrees should be published and made available on the Internet to advise the "trade," and there should also be protection against arbitrary and ex post facto changes to regulations and decrees to assure predictability and fairness.

Inadequate or No Legal Basis Exists For Bilateral Or Multilateral Trade Facilitation Measures. Many trade facilitation measures require bilateral and/or multilateral cooperation by customs administrations. These measures include: (1) harmonizing border procedures; (2) publishing up-to-date border crossing rules and their interpretations; (3) establishing and operating joint border posts and transit corridors; (4) electronic interchange of customs data and other information; and (5) cooperation on law enforcement matters. Unless there is explicit legal authority given for undertaking joint customs administration measures with other nations, the Ministries of Justice and other legal authorities in CISCE countries will likely take the position that their customs agencies cannot participate in such efforts. In some instances, Presidential decrees, memoranda of understanding (MOUs), or special legislation may be sufficient to provide the legal basis for joint trade facilitation and enforcement efforts. However, these measures may be politically difficult to obtain and may be more easily changed or revoked than customs codes, so it is preferable to have the authority to work jointly with other customs administrations included in national customs codes.

Incomplete Implementation Of GATT Principles And The WTO's Customs-Related Mandatory Agreements Is A Barrier To Trade. Only two CISCE countries, Mongolia and the Kyrgyz Republic, are currently members of the WTO. All other CISCE countries have applied for WTO membership and are in various stages of the admission process. Generally speaking, CISCE customs administrations have not yet adequately implemented basic GATT principles, such as most favored nation (MFN) and national treatment, nor have they fully implemented the WTO's customs-related agreements such as the Agreement on Customs Valuation, the Agreement on Trade-Related Aspects of Intellectual Property Rights, the Agreement on Import Licensing Procedures, and the Agreement on Pre-shipment Inspection. Full implementation of GATT principles and the WTO's mandatory customs-related agreements is a condition precedent to WTO

membership. Full implementation harmonizes customs requirements with the 146 current members of the WTO and removes unnecessary barriers to trade.

There Is Poor Implementation In CISCE Customs Codes Of Key Principles Recognized In The Revised Kyoto Convention.

Information Technology. The Revised Kyoto Convention, General Annex, Chapter 7, Standard 7.2 specifies: “When introducing computer applications, the Customs shall use relevant internationally accepted standards.” Generally speaking, the customs laws of CISCE countries do not unequivocally recognize internationally accepted standards. (For example, the draft customs code of Tajikistan, based on the Russian Federation Code, specifies that information technologies shall be “in accordance with international standards *and the current standards of the Republic of Tajikistan.*” (emphasis added) This raises the possibility that local standards will prevail over international standards.)

A United Nations agency, UNCTAD, has sponsored the development of an Automated System for Customs Data (ASYCUDA), a declaration based system now used in approximately 80 countries. The latest version of ASYCUDA, a web-based system that allows Customs and traders to handle most transactions by Internet, was recently installed in Moldova.⁸ However, of the CISCE countries, only Mongolia has adopted ASYCUDA. Other CISCE countries, such as Kazakhstan, employ proprietary systems unique to the specific country. Some CISCE countries have no automated system at all.

Post-Entry Audits And Risk Management. The Revised Kyoto Convention provides for both risk management and audit-based controls. See General Annex, Chapter 6, Standards 6.2-6.6. Some authority for use of risk management and post-entry audits has been included in several of the CISCE’s newly revised customs codes (see, for example, the new customs code of Kazakhstan and the draft customs code of Tajikistan). However, these methodologies are central to a modern, efficient customs administration and should therefore be a central component of a properly drafted customs code. Risk management allows customs administrations to focus its attention on high-risk products and high-risk importers and reward importers, brokers, freight forwarders and carriers with good compliance records with expedited clearance procedures. Risk criteria should be confidential, subject to change as appropriate, and not included in customs codes.

Post-entry audits allow customs administrations to “spot-check” declarations for completion of all elements, proper valuation and classification of merchandise, and supervise the work of “first-line” customs officials. More comprehensive audits, conducted jointly with tax inspectors, allow customs administrations to check inventory records against records of imports and duty and tax assessments. This is an extremely important tool for combating smuggling, corruption and tax fraud.

Guarantees. An effective and affordable customs guarantee is a key requirement for trade facilitation and modern customs administration. If an adequate financial

⁸ See www.asycuda.org/

guarantee has been given, Customs is assured of the payment of duties and taxes without the necessity of continuous control of imported goods prior to payment. Moreover, guarantees assure the performance of brokers, carriers and others involved with customs transactions. Guarantees may be incorporated into an entry document, such as is the case with ATA and TIR carnets, they may apply to single transactions, or they may be a general term bond, applicable to multiple transactions up to a specified value during a given time period.

Some of the CISCE customs codes provide for guarantees (see, for example, the new customs code of Kazakhstan and the draft customs code of Tajikistan), but the standards set forth in General Annex, Chapter 5 of the Revised Kyoto Convention are not specifically followed in these codes. Equally problematic, overly strict requirements imposed on sureties (see, for example, the draft Tajik customs code, articles 390, 391) may limit the availability and increase the cost of guarantees. Customs administrations are ill equipped to regulate financial institutions; this function is more properly undertaken by bank and insurance regulators.

Consultative Relationships With The “Trade.” One of the foundation principles of the Revised Kyoto Convention states that “Customs shall institute and maintain formal consultative relationships with the trade to increase co-operation and facilitate participation in establishing the most effective methods of working....” General Annex, Chapter 1, General Principle 1.3. The continuous involvement of business and trading interests, including small business enterprises and shuttle traders, should be clearly provided for in CISCE customs codes. The public should have advance notice of all regulatory initiatives so they will have time to comment on their effect. Laws, regulations and decrees should be published, as should all border procedures. Customs should meet periodically with the trade to discuss on-going issues of concern and how procedures can be improved.

An Inadequate Legal Basis Exists For A Professional, Modern Customs Service. Some CISCE customs codes contain provisions governing service in Customs Authorities and some do not. In the author’s opinion, it is preferable to include the procedures for serving in Customs as part of the country’s civil service law rather than in the customs code. Civil service procedures and pay should be subject to the same standards applied to other government agencies.

Every effort should be made to properly compensate customs officials for work performed. CISCE countries that have inadequate resources for this in the national budget may wish to consider implementing “user fees” that would reimburse Customs for various services rendered. However, any user fee imposed must meet the requirements of GATT, Article VIII – the fee must reflect the actual cost of the service rendered and if imposed on an ad valorem basis, it must be “capped” to avoid overcharging large-value imports and exports. In addition to proper compensation for customs officials, customs employees should be held to high standards of public integrity. Public integrity requirements and penalties for violations should be stated in the customs code or the applicable civil service code.

The training of customs personnel to international standards is essential. CISCE customs codes should authorize the training of customs personnel of all levels of responsibility at regional customs academies. This will facilitate cooperation between national customs administrations and make more cost/effective use of trainers and training facilities.

The Way Forward (Legal Reform Proposals)

Based upon the issues discussed above and the author's recent experience with customs code revision in several CISCE countries, the following recommendations are made for revisions of customs codes and other applicable laws:

1. At The National Level:

Adopt and fully implement all WTO customs related measures (Agreement on Customs Valuation, up-to-date version of the Harmonized System Nomenclature, Agreement on Pre-shipment Inspection, Agreement on Rules of Origin, Agreement on Import Licensing Procedures, Agreement on Trade Related Aspects of Intellectual Property Rights, GATT-consistent user fees) and basic GATT principles (MFN and national treatment).

Adopt and fully implement Revised Kyoto Convention "best practices" in customs code (simplicity, public participation in customs administration, risk management/selectivity, audits, use of guarantees, full use of ICT).

Adopt legislation that increases the level of professionalism (training, pay, standards of integrity) for customs employees. Provisions governing the pay and treatment of customs employees should be included in national civil service legislation.

Clarify any uncertainty regarding whether international agreements that are in conflict with provisions in customs codes take precedence over the code provisions.

2. At The Regional Level:

Adopt and implement regional customs codes, replacing national codes (example, the Eurasian Economic Community customs code for Kazakhstan, Kyrgyz Republic, Tajikistan, Russia and Belarus), where appropriate. Regional customs codes should include the provisions recommended above for national customs codes.

Provide clear legal authority for joint customs activities (e.g., joint border posts, transit corridors, electronic data and information sharing). This should be done in both national and regional customs codes.

Authorize joint training facilities for all levels of customs employees – regional customs academies.

3. At The Multinational Level:

Authorize full participation in the WCO, key WCO conventions, and WCO-sponsored training.

Authorize participation in all customs-related WTO matters and WTO-sponsored training.

Authorize full participation in and implementation of the TIR Convention.