

Special Report

Import procedures: shortcomings in the legal framework and an ineffective implementation impact the financial interests of the EU

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ABBREVIATIONS

AC: Administrative cooperation

ACAs: Administrative cooperation arrangements

ADD: Anti-dumping duties

AEO: Authorised Economic Operator

AFIS: Anti-Fraud Information System

B2C: Business to consumer

BTI: Binding tariff information

CIS: Customs Information System

CP 42: Customs procedure 42

CRMS: Common Customs Risk Management System

CSM: Container status message

CUP: Customs Union Performance

CVD: Countervailing duties

DG BUDG: Directorate-General for Budget

DG TAXUD: Directorate-General for Taxation and Customs Union

ENS: Entry summary declaration

EP: European Parliament

EU: European Union

FCLO: Foreign Customs Liaison Officer

GNI: Gross National Income

JRC: Joint Research Centre

MA: Mutual assistance

MAAs: Mutual assistance agreements

OECD: The Organisation for Economic Cooperation and Development

OLAF: European Commission Anti-Fraud Office

OLO: Overseas Liaison Officer

P2P: Private to private

PTA: Preferential trade arrangement

RIF: Risk Information Form

SAD: Single administrative document

SMS: Specimen Management System

TARIC: Integrated customs tariff of the Community

TOR: Traditional Own Resources

UCC: Union Customs Code

UCC DA: Union Customs Code delegated act

UCC IA: Union Customs Code implementing act

HMRC: Her Majesty Revenue and Customs

VAT: Value added tax

WCO: World Customs Organisation

GLOSSARY

Customs authorities: The customs administrations of the Member States and any other authorities which are responsible for applying customs legislation.

Customs clearance: The process of fulfilling customs formalities so that the applicant can have the goods at his disposal.

Customs controls: Specific acts performed by the customs authorities in order to ensure compliance with the customs legislation and other legislation governing the entry, exit, transit, movement, storage and end-use of goods moved between the customs territory of the Union and countries or territories outside that territory, and the presence and movement within the customs territory of the Union of non-Union goods and goods placed under the end-use procedure.

Customs declaration: The act whereby a person indicates, in the prescribed form and manner, a wish to place goods under a given customs procedure, with an indication, where appropriate, of any specific arrangements to be applied.

Customs legislation: The body of legislation made up of all of the following: the Code and the provisions supplementing or implementing it adopted at Union or national level, the Common Customs Tariff, the legislation setting up a Union system of reliefs from customs duty and international agreements containing customs provisions, insofar as they are applicable in the Union.

Customs procedure: Any of the following procedures under which goods may be placed in accordance with the Code: release for free circulation, special procedures, export.

Customs procedure 42: The regime an importer uses in order to obtain a VAT exemption when the imported goods will be transported to another Member State. The VAT is due in the Member State of destination.

Customs status: The status of goods as Union or non-Union goods.

Customs Union: Preferential trade arrangement by virtue of which trader partners grant reciprocally preferential access to their products and services in order to facilitate trade

between them. It leads to the reciprocal elimination of tariffs and quotas in the constituent territories, the discrimination of non-members trade, and the establishment of a common customs tariff among them.

Decision: Any act by the customs authorities pertaining to the customs legislation giving a ruling on a particular case, and having legal effects on the person or persons concerned.

Documentary check: A control of the correctness, completeness and validity of information entered on the customs declaration (e.g. description of goods, value, and quantity) or other documents (e.g. import licences, certificates of origin).

Entry summary declaration: The act whereby a person informs the customs authorities, in the prescribed form and manner and within a specific time-limit, that goods are to be brought into the customs territory of the Union.

Import duty: Customs duty payable on the import of goods.

Import point shopping: The act of choosing the customs point of importation with fewer controls in order to illegally pay less customs duty.

Import procedure: Application of the customs procedure 'release for free circulation' after which goods can be sold or consumed on the EU market.

Member State of importation: Member State where the goods are physically imported into the EU and released for free circulation.

Mutual assistance: Any action of a Customs administration on behalf of or in collaboration with another Customs administration for the proper application of Customs laws and for the prevention, investigation and repression of Customs offences.

Non-Union goods: Goods other than Union goods or which have lost their customs status as Union goods.

Other post-release controls: Controls of the correctness, completeness and validity of information entered on customs declarations (e.g. description of goods, value, quantity) or

other documents (e.g. import licences, certificates of origin) made after the importation of goods.

Physical check: An examination of goods including detailed counting and taking of samples to check whether they match the customs declaration accompanying the goods.

Post-release audit: Checking traders through examination of their accounts, records and systems in order to ensure compliance with customs rules and evaluate the risks linked to their business.

Presentation of goods to customs: The notification to the customs authorities of the arrival of goods at the customs office or at any other place designated or approved by the customs authorities.

Priority control areas: The part of the Common Risk Management Framework which covers particular customs procedures, types of goods, traffic routes, modes of transport or economic operators subject to increased levels of risk analysis and customs controls during a certain period.

Release of goods: The act whereby the customs authorities make goods available for the purposes specified for the customs procedure under which they are placed.

Customs Risk: The likelihood weighted by the impact of an event occurring, with regard to the entry, exit, transit, movement or end-use of goods moved between the customs territory of the Union and countries or territories outside that territory and to the presence within the customs territory of the Union of non-Union goods, which would prevent the correct application of Union or national measures, compromise the financial interests of the Union and its Member States or pose a threat to the security and safety of the Union and its residents, to human, animal or plant health, to the environment or to consumers.

Risk management: The systematic identification of risk, including through random checks, and the implementation of all measures necessary for limiting exposure to risk.

Risk profile: A combination of risk criteria and control areas (e.g. type of goods, country of origin) which indicates the existence of risk and leads to a proposal to carry out a control measure.

Union goods: Goods which fall into any of the following categories:

(a) goods wholly obtained in the customs territory of the Union and not incorporating goods imported from countries or territories outside the customs territory of the Union;

(b) goods brought into the customs territory of the Union from countries or territories outside that territory and released for free circulation;

(c) goods obtained or produced in the customs territory of the Union, either solely from goods referred to in point (b) or from goods referred to in points (a) and (b).

EXECUTIVE SUMMARY

About this report

I. Goods entering the EU from outside the European Union are subject to customs controls by Member States before they are released for free circulation within the EU. We examined whether the European Commission and the Member States ensure that import procedures protect the EU's financial interests. We found important weaknesses and loopholes which indicate that the controls are not applied effectively. This has an adverse effect on EU finances. We make a number of recommendations to the Commission and to the Member States to improve the design and implementation of the controls.

About customs controls

II. Customs controls can only ensure the protection of the EU's financial interests if they are based on common rules and if they are applied in a harmonised and standardised manner by the Member States.

III. At the time of entry, the customs authorities of the Member State of import should require the importer to pay or to secure any customs duties due on the imported goods. However, importers can deliberately reduce or evade customs duty liability by, for example, undervaluing their goods, declaring a false country of origin or shifting to a product classification with a lower duty rate.

IV. Customs duties make up 14 % of the EU budget. Their evasion increases the customs gap and must be compensated by higher GNI contributions by Member States. The cost is ultimately borne by European taxpayers.

How we conducted our audit

V. We examined whether the EU's customs controls protect its financial interests and whether the Commission and the Member States have designed robust import procedures that protect those interests.

What we found

VI. We found serious weaknesses indicating that there are shortcomings in the customs legal framework as well as an ineffective implementation of customs controls on imports and this adversely affects the financial interests of the EU.

VII. The Member States are not sufficiently financially encouraged to perform customs controls. Those which perform customs controls but are not successful in recovering losses to the revenue of the EU risk financial consequences, whereas those which do not carry out such controls may not suffer such consequences.

VIII. Member States have made progress towards the uniform application of customs legislation. But they have differing approaches in terms of customs controls to tackle undervaluation, misdescription of origin and misclassification and to impose customs penalties. Burdensome customs controls can have an impact on the traders' choice of customs office of importation and (air)ports with fewer customs controls may attract more traffic.

IX. A number of loopholes still exist in the Member States with regard to the control of imports.

What we recommend

X. We make the following recommendations to the Commission and to the Member States.

XI. The Commission should:

- (a) in order to be able to meet the European Parliament's request, develop a methodology and produce periodic estimates of the customs gap from 2019 and take into account its results for the allocation of resources and for setting operational targets;
 - (b) consider all available options to strengthen support for national customs services in their important EU role in the new Multiannual Financial Framework, including a review of the appropriate rate of collection costs;
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- (c) in the next Multiannual Financial Framework propose that the next EU action programmes, which support the Customs union, should be used to contribute to financial sustainability to the customs European Information Systems;
- (d) be more precise in the requests contained in a Mutual Assistance communication to ensure their uniform implementation by Member States; and
- (e) propose amendments to customs legislation in 2018 aimed at making compulsory the indication of the consignor in the customs import declaration.

XII. The Member States should:

- (a) make overrides of controls suggested by a particular risk filter conditional on prior or immediate hierarchical approval;
 - (b) introduce checks in their electronic release systems to block import declarations applying for duty relief on goods with declared value above 150 euros or for commercial consignments declared as gifts; and
 - (c) set-up investigation plans to tackle abuse of this relief on e-commerce goods trade with non-EU countries.
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INTRODUCTION

1. In 2018, the EU will celebrate the 50th anniversary of the Customs Union. A customs union means the absence of customs duties and quotas at internal borders between Member States, and the establishment of common customs duties on imports from third countries. The Customs Union together with the Common Commercial Policy are areas of exclusive EU competence¹ within which most of customs policy is defined and customs legislation is adopted. However, the responsibility for implementing customs legislation is primarily that of the Member States².
2. Although internal borders were abolished, goods entering Member States from outside the customs territory of the EU are subject to customs controls and payment of any customs duties before they are released for free circulation within the EU.
3. Releasing imported goods for free circulation means that the goods can move freely within the EU single market, like any product originating in the EU³. Thus, at the time of entry, the customs administration of the Member State of import should require the importer to pay or to secure any customs duties due on the imported goods.
4. Customs duties, together with sugar-production levies (collectively known as Traditional Own Resources (TOR)), are an important source of revenue for the EU budget. They are transferred to the budget, net of retention for collection costs. In 2016 TOR made up 14 % of the EU's revenue and amounted to 20.1 billion euro.

¹ Article 3 TFEU. Consolidated version of the Treaty on the Functioning of the European Union (TFEU) (OJ C 202, 7.6.2016, p. 47).

² Article 291 TFEU.

³ Article 201 of Regulation (EU) No 952/2013 of the European Parliament and of the Council of 9 October 2013 laying down the Union Customs Code (recast) (OJ L 269, 10.10.2013, p. 1), lays down that the release for free circulation will confer on non-Union goods the customs status of Union goods and entails the collection of any import duty due and other charges, as appropriate, the application of commercial policy measures and prohibitions and restrictions, and completion of the other formalities laid down in respect of the import of the goods.

5. Customs authorities pursue several objectives and scarce resources must be allocated to each. They strive to meet objectives such as the application of non-fiscal measures aimed at improving internal EU security, protecting the Union from unfair and illegal trade, and the protection of the environment. Fight against terrorism has become a priority for customs authorities. They are also responsible for the collection of customs duties, excise duties, and the value added tax (VAT) due at import.
6. It is a challenge for customs authorities to strike a balance between the need to facilitate trade with faster, seamless import procedures and the need to carry out customs controls. Burdensome customs controls can have an impact on the traders' choice of customs office of importation and (air)ports with fewer customs controls may attract more traffic.
7. The customs duty liability at the moment of the release of goods depends on three factors: (i) the customs value of the imported goods, when the duty is set as a percentage of this value (*ad valorem*); (ii) the origin of the goods; and (iii) the tariff classification of the goods which, in combination with the origin, determines the customs duty rate to be applied on the customs value.

How evasion of customs duties occurs

8. The importer can deliberately reduce the customs duty liability by:
 - (a) undervaluation , i.e. when the importer declares a value of imported goods which is lower than the actual value, often accompanied by the presentation of fake commercial documents;
 - (b) misdescription of origin, where the importer declares a false country of origin of the imported goods;
 - (c) misclassification, by shifting to a product classification with a lower duty rate; or
 - (d) a combination of the above.
 9. Finally, importers can abuse a customs duty relief by applying for the exemption for goods which are not eligible.
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The customs gap and its impact

10. Customs duties evasion increases the customs gap, defined in a study of the European Parliament⁴ (EP) as ‘the difference between the theoretical import duty level that should be collected for the economy as a whole and actual import duty collected’. Any gap in customs duties’ collection must be compensated by higher Gross National Income (GNI) contributions from Member States and ultimately borne by European taxpayers.

How to tackle customs duties evasion: customs controls and exchanges of information

11. Goods imported into the EU are subject to customs controls. Such customs controls can only ensure the proper functioning of the internal market and the protection of the EU’s financial interests if they are based on common rules and if they are applied in a harmonised and standardised manner by the Member States.

12. Customs controls on imports can be carried out:

- (a) before the arrival of goods into the EU territory or at the place of unloading, in this case they are known as pre-arrival or pre-release controls;
- (b) when the goods are imported, the so-called release controls; or
- (c) after the importation of goods, once they are in free circulation. These are the post-release controls. They can be either audit-based controls (post-release audits) or transaction-based controls (other post-release controls).

13. Since the EU does not have harmonised control and risk management frameworks, the mix and prevalence of each of these three forms of control vary from one Member State to another. Less effective controls at the pre-release and release stages mean that the remaining risks affecting the collection of customs duties should be mitigated at the post-release stage.

⁴ C.f. European Parliament, Directorate-General for Internal Policies, “From Shadow to Formal Economy: Levelling the Playing field in the Single Market”, 2013.

14. Customs authorities need to exchange information with other countries on international trade to ensure compliance with customs provisions and the completeness of revenue collection. This is known as mutual administrative assistance.

15. Exchanges of information can take place at EU level between Member States or between them and the Commission, or at international level with non-EU countries. Exchanges of information at EU level are made in the framework of either the mutual assistance regulation or the customs risk management system for risk-related information.

16. Customs authorities can also cooperate with each other and exchange information and best practices through joint actions, seminars, training courses, project groups, working visits, and cross-border operations financed by the EU action programmes. Two major EU action programmes finance the exchange of information and cooperation between customs authorities to protect the EU's financial interests: Customs 2013/2020 and Hercule II/III.

17. Customs 2013 provided nearly 325 million euro during the six years of its implementation to 'support and complement action undertaken by Member States in ensuring the effective functioning of the internal market in the customs field'⁵. Customs 2020 supports the functioning of the Customs Union. Its Regulation sets up several specific objectives aiming to support customs authorities in the protection of the EU's financial and economic interests and provides financing of nearly 525 million euro for the period 2014-20.

18. Hercule II was an EU action programme funding actions to prevent and fight fraud, corruption and any other illegal activities affecting the Union's financial interests, and made available almost 100 million euro for anti-fraud actions between 2007 and 2013. It has been succeeded by Hercule III with a Budget of 105 million euro for the period 2014-20.

19. Customs authorities exchange information and cooperate with non-EU countries under the umbrella of international agreements such as preferential trade arrangements (PTAs),

⁵ Pursuant to Article 1(1) of Decision No 624/2007/EC of the European Parliament and of the Council of 23 May 2007 establishing an action programme for customs in the Community (Customs 2013) (OJ L 154 of 14.6.2007, p. 25).

mutual assistance agreements (MAAs), and administrative cooperation arrangements (ACAs).

20. PTAs allow trading partners to grant preferential terms in the context of their trade with each other. They can be either reciprocal or unilateral. MAAs provide a legal basis to request information from non-EU countries in particular in order to prevent, investigate and combat operations in breach of customs legislation.

21. The European Commission's European Anti-Fraud Office (OLAF) concludes ACAs with non EU-country authorities and administrative investigative services of international organisations. They are intended to provide practical guidelines for OLAF's operational cooperation with partner authorities, in particular by designating a contact point.

AUDIT SCOPE AND APPROACH

22. The audit assessed whether the Commission and the Member States have designed robust import procedures that protect the financial interests of the EU.

23. We visited the customs authorities of five Member States: Spain, Italy, Poland, Romania and the United Kingdom. The selection of Member States was based in the following risk criteria: (i) the size of its TOR contribution to the EU Budget; (ii) the incidence of undervaluation in the Member State; and (iii) the proportion of audit-based controls in the total of post-release controls.

24. The audited period runs from 2007 until 2017. We carried out the audit in two stages (see more details about the audit approach in **Annex I** and **Annex II**):

(a) First stage: preparatory work in the Commission and in Member States, including a visit to the Commission services: DG Taxation and Customs Union, DG Budget, OLAF and the Joint Research Centre (JRC) and to the World Customs Organisation (WCO) in order to collect information and data that could be useful for the audit fieldwork in the Member States. This also enabled us to benchmark EU customs legislation and procedures

against the WCO standards⁶. To test whether the customs controls and risk management procedures are running smoothly, prior to each visit to a Member State, we selected four samples of risky imports and a sample of audits carried out by customs authorities.

- (b) Second stage: audit fieldwork at both the Commission (Directorate-General for Taxation and Customs Union (DG Taxation and Customs Union), the Directorate-General for Budget (DG Budget) and OLAF) and in the selected Member States, with special attention given to systems and controls.

OBSERVATIONS

The current system does not prioritize the importance of custom duties as a source of the financing of the EU budget

25. The report of the High Level Group on Own Resources⁷ highlights TOR as a benchmark of true EU revenue. However, the EU has not yet carried out an estimate of the customs gap, there are disincentives for Member States to carry out controls, and the financing of the EU customs programmes does not fully ensure the financial sustainability of the Customs Union or is not always linked to the protection of the EU financial interests.

The Commission has not made an estimate of the customs gap

26. In 2013, the EP requested⁸ the Commission to ‘collect reliable data on the customs and VAT gap in the Member States and report every six months to Parliament in this regard’. The Commission has not met this request in respect of the customs gap, whereas it regularly

⁶ The revised Kyoto Convention, the WCO risk management guide, the WCO guidelines on post clearance audits, etc.

⁷ High Level Group on Own Resources (2016), “Future financing of the EU — Final Report and recommendations”.

⁸ See Commission Staff Working Document Accompanying the document Report from the Commission to the European Parliament and to the Council on the follow-up to 2011 discharge - Replies to requests from the European Parliament (COM(2013) 668 final) (SWD(2013) 348 final).

finances studies on the size of the VAT gap. The Commission publishes an annual comparison between the additional TOR establishments resulting from its inspection activities and the actual amount collected. This can in no way be seen as the customs gap as defined in paragraph 10.

27. OLAF has made a calculation of the potential losses of customs duties and VAT due to undervaluation of imports of textiles and footwear from China into the UK. The potential losses of customs duties were calculated to be close to 2 billion euro for the period 2013-16. OLAF is assessing whether there are any potential losses in other Member States including the other four sampled by ECA.

28. An annual estimate of the customs gap would allow the Customs Union's performance in terms of the protection of the EU financial interests to be evaluated. It would also help the Commission and Member States to target resources to where they are most needed.

There is a disincentive for Member States to carry out customs controls

29. Member States' customs authorities are responsible for the collection of customs duties: they must take all measures to ensure that the duties are duly transferred to the EU Budget and protect the EU's financial interests⁹. To ensure this, the Commission inspects Member States' customs authorities every year.

30. The Commission can hold a Member State financially liable in case of administrative errors¹⁰. Member States which do not carry out customs controls may not face this risk, e.g. we found that in the UK, insolvent traders are excluded from the targeted population of a post-release control project. Indeed, one Member State complained that the more it tackles fraud the higher the risk that the Commission holds it financially liable.

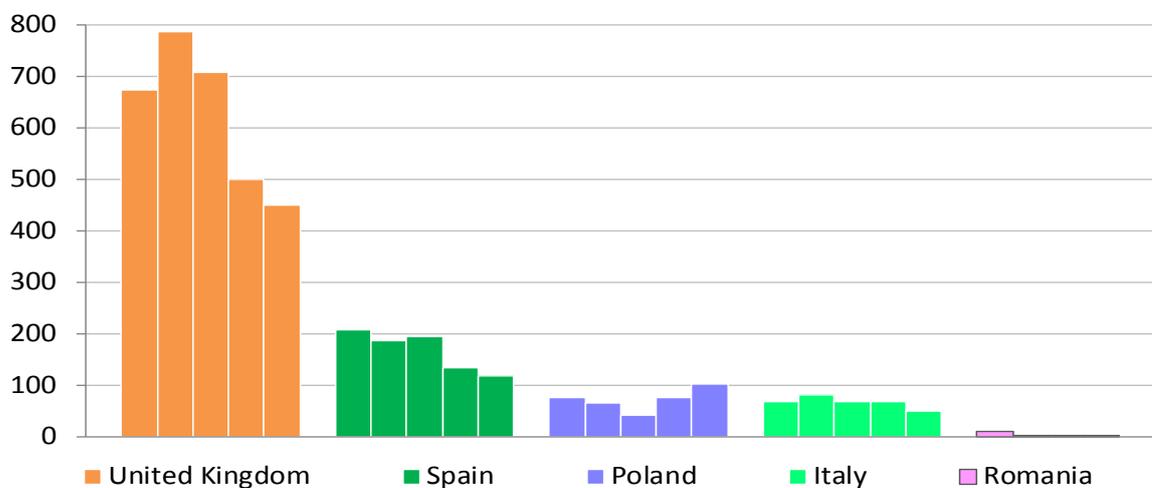
⁹ C.f. Article 2(2) of Council Regulation (EU, Euratom) No 608/2014 of 26 May 2014 laying down implementing measures for the system of own resources of the European Union (OJ L 168, 7.6.2014, p. 29) and Article 3(a) of the UCC.

¹⁰ Case C-392/02, European Commission v Kingdom of Denmark, Case C-60/13, Commission v United Kingdom.

31. If customs authorities carry out a post-release control and detect an underpayment of customs duties they must collect the duties owed. The customs authorities notify the amount due to the debtor using a post-release demand note. Statistics from the Commission show that, with the exception of Poland, the selected Member States have seen a decrease in the number of post-release demand notes¹¹ (see **Figure 1**).

Figure 1 – Number of post-release demand notes in the selected Member States (2012-16)

□



Source: OWNRES database.

32. Due to the absence of an estimate of the customs gap, it is not possible to assess whether this is due to a decreasing trend in the effectiveness of the post-release controls or a reduction in that gap.

Underfinancing of trans-European IT systems may delay the Union Customs Code implementation

33. The full implementation of the Union Customs Code (UCC) is inseparably linked to the development of the supporting IT systems. The complete deployment of all of the electronic systems required by the UCC is due to be completed by 31 December 2020. After that date,

¹¹ This data only covers cases where the amounts detected exceed 10 000 euro, regardless of whether they have been recovered.

electronic data-processing techniques must become the rule and the EU customs will move towards a paperless environment.

34. According to the final evaluation of the Customs 2013 action programme¹², insufficient national investments may delay the EU-wide deployment of customs systems. This programme financed the EU specifications of trans-European IT systems and Member States bore the costs of making national systems compatible with the EU specifications.

35. The same evaluation states that, according to Member States' officials, the costs to national administrations are of a similar degree as those borne by the Commission and that implementation and upgrades of European systems can be especially expensive for Member States if national systems are complex and if there is a lack of integration of national systems. However, some components of the European Information Systems are not financed by Customs 2020 and are borne by Member States¹³.

36. National budget constraints can jeopardize the correct implementation of European systems and some Member States reported a lack of national budget in 2015. Furthermore, Member States have confirmed the risk of delay in their replies to a questionnaire sent by the Commission in 2016.

37. As the Commission noted, in 2015 'seven Member States collect more than 80 % of TOR, and four Member States collect almost 60 % of TOR¹⁴. This should be contrasted with the amounts of collection costs retained as, for example, one Member State¹⁵ retains more than

¹² Coffey, "Final Evaluation of the Customs 2013 Programme – Final report", 2014.

¹³ Non-Union components pursuant to Article 9(3) of Regulation (EU) No 1294/2013 of the European Parliament and of the Council of 11 December 2013 establishing an action programme for customs in the European Union for the period 2014-2020 (Customs 2020) and repealing Decision No 624/2007/EC (OJ L 347 of 20.12.2013, p. 209).

¹⁴ Germany (21 %), the United Kingdom (17 %), the Netherlands (12 %), Belgium (9 %), Italy (9 %), France (9 %) and Spain (7 %).

¹⁵ Germany.

one billion euro and, on the other extreme, another Member State¹⁶ less than 10 million euro. However there is an element of fixed costs in the customs systems, for instance for what concerns IT systems'¹⁷.

38. According to the report of the High Level Group on Own Resources 'Countries where the main ports of entry are located (Belgium, the Netherlands) — and thus where significant TOR are collected — have sometimes voiced the argument that their share in TOR is too high'. In contrast, small TOR contributors are enduring a relatively greater burden in financing the components of the European Information Systems which are not paid by the Customs 2020 action programme.

Financing of Member States customs infrastructure under the Hercule action programme is not always linked to the protection of the EU's financial interests

39. We have examined examples of final implementation reports provided by the beneficiaries of Hercule II and found that there is not always a clear link between the outcome of the funded equipment and the protection of the financial interests of the EU. For example, the programme funded the confiscation of hashish by using endoscopes, and a mini spy camera used in the seizure of high value vehicles, etc.

40. In our Opinion No 3/2012 we found¹⁸ that 'the equipment co-financed is not necessarily exclusively used for the protection of the EU financial interest, but also for operations related to drugs, weapons, prison escapes, human trade, fiscal fraud, credit card fraud, money counterfeiting and corruption in national law enforcement agencies'. This may reduce the effectiveness of customs in the protection of the EU's financial interests.

¹⁶ Malta.

¹⁷ Commission Directorate-General for Budget (Minutes of the 168th meeting of the Advisory Committee on Own Resources (ACOR) of 1 December 2016).

¹⁸ See paragraph 28 of ECA Opinion No 3/2012 on a proposal for a Regulation of the European Parliament and of the Council on the Hercule III programme to promote activities in the field of the protection of the European Union's financial interests (OJ C 201, 7.7.2012, p. 1).

The EU's tools and programmes for exchanging customs information and increasing cooperation have not reached their full potential

41. Exchanges of information can take place at EU level between Member States or between them and the Commission, or at international level with non-EU countries. We have found that the EU has set up a system allowing these exchanges of information to take place but they are not fully exploited.

The EU has set up promising information channels between Member States and between the Commission and Member States but there are weaknesses in their content and use

Tools for exchanging information under the mutual assistance regulation are not fully exploited by Member States

42. Member States can exchange information related to breaches of customs legislation between each other and with the Commission using the tools and databases provided for in the mutual assistance regulation¹⁹. These exchanges are made via the secured Anti-Fraud Information System (AFIS), which is the electronic communication tool assisting Member States to fulfil their irregularity reporting obligations.

43. On the basis of the information sent by Member States the Commission may decide to open an investigation. The Commission can also decide to disseminate fraud alerts to Member States using Mutual Assistance (MA) communications.

44. We found that Member States do not implement in a uniform way the requests made by OLAF in MA communications sent to tackle fraud concerning undervaluation, misdescription of origin or misclassification. We also found cases where the audited Member States did not meet the OLAF requests.

¹⁹ Council Regulation (EC) No 515/97 of 13 March 1997 on mutual assistance between the administrative authorities of the Member States and cooperation between the latter and the Commission to ensure the correct application of the law on customs and agricultural matters (OJ L 82, 22.3.1997, p. 1).

45. Member States may use other information systems such as the Customs Information System (CIS) to assist them in the prevention, investigation and prosecution of customs infringements by making information available more rapidly. However we found that, except for Poland, the other selected Member States' customs authorities rarely use the CIS²⁰ to exchange information on customs irregularities/fraud with the competent authorities in other Member States.

46. Member States also complained about the problem of double reporting in CIS and in the exchange of risk-related information in a Risk Information Form (RIF). This low usage of the CIS database and its overlap reduces the effectiveness of these exchanges of information.

47. To overcome this overlap the Commission has created the "One Seizure One Report" project. In 2016 it invited Member States to complete a survey. The vast majority of Member States identified multiple reporting as a problem that needs to be addressed. In addition, under the framework of the Customs 2020 action programme, a project group²¹ composed of Member States and Commission representatives has been created to discuss the initial conclusions of the survey and to issue recommendations to address the question.

Exchange of information to tackle undervaluation works well

48. To overcome the risk of undervaluation, the Commission has developed a methodology to estimate "fair prices"²², applying a statistical procedure to COMEXT²³ data, in order to produce robust estimates for the prices of the imported goods²⁴. OLAF disseminates these estimates among Member States' customs authorities.

²⁰ Title V of Council Regulation (EC) No 515/97.

²¹ Project Group 'Reporting Customs seizures in CRMS and AFIS-CIS'.

²² Also known as Outlier-Free Average Prices. These are statistical estimates calculated for the prices of traded products on the basis of outlier-free data.

²³ COMEXT is Eurostat's database for detailed statistics on international trade in goods.

²⁴ Spyros Arsenis, Domenico Perrotta, Francesca Torti, "The Estimation of Fair Prices of Traded Goods from Outlier-Free Trade Data", 2015, EUR 27696 EN. doi:10.2788/57125.

49. This information on fair prices is an effective tool for risk management purposes in helping to identify potential cases of undervaluation when there are also other risks or fraud indicators, such as suspicious traders involved in the import (adversely known traders). It could also be used as a basis to estimate that part of the customs gap due to undervaluation.

Exchange of information to tackle misdescription of origin has recently improved

50. Importers can also reduce the customs duty liability by declaring a wrong country of origin of the imported goods. This way they obtain the reduced or zero customs duty rate set in a preferential trade arrangement (PTA) and/or avoid payment of anti-dumping (ADD) or countervailing (CVD) duties²⁵ established for the actual country of origin. Sometimes the real origin of the goods is disguised via fraudulent transshipment in an intermediate country where the goods are temporarily warehoused and then dispatched to the EU with false documentation. We have found on the internet several examples of companies offering this fraudulent transshipment 'service'.

51. To tackle this fraud the Commission has developed ConTraffic and the Container Status Messages (CSM). These tools provide information on container routes as well as risk assessment services to customs authorities. The system automatically sends fraud signals to Member States when it detects mismatches between the country of origin declared by the importer and the container route.

²⁵ Dumping occurs when manufacturers from a non-EU country sell goods in the EU below the sales prices in their domestic market or below the cost of production. If the Commission can establish – through an investigation – that this is happening, it may correct any damage to EU companies by imposing anti-dumping duties (ADD). Typically these are duties on imports of the product from the country in question. The duties can be fixed, variable or a percentage of the total value (ad-valorem). Subsidisation is when a non-EU government provides financial assistance to companies to produce or export goods. The Commission is allowed to counteract any trade-distorting effects of these subsidies on the EU market – after an investigation into whether the subsidy is unfair and injuring EU companies. The countervailing duties (CVD) are set on imports of the subsidised products. These duties can be fixed, variable or a percentage of the total value (ad-valorem).

Box 1 – Examples of misdescription of origin via fraudulent transshipment and its financial impact

A trader buys bicycles from China. The anti-dumping duties for bicycles from China are 48.5 % of the product value. The shipment of bicycles leaves China; it is transhipped in Singapore and again in Malaysia. In the cargo document presented at the moment of importation, the bicycles are described as coming from Bangladesh, without any indication of the prior route of the containers. According to the documents presented to customs, no anti-dumping duties should be charged for the importer. If the customs official is using the CSM or Contraffice monitoring system, it can track the route of the container and ask the importer for further documents in order to prove the real origin of goods.

OLAF carries out investigations regarding ADD evasion: “In June 2013, the EU imposed an anti-dumping duty on solar modules produced in China. Initial indications that this duty was being evaded by misdescription of origin emerged within weeks. OLAF opened investigations in December 2013 into fraudulent transshipment via Japan (misdescription of Japanese origin) and in March 2014 into fraudulent transshipment via Malaysia (misdescription of Malaysian origin). OLAF requested assistance from Japanese and Malaysian authorities and conducted investigations jointly with several Member States. OLAF has so far recommended the recovery of over EUR 50 million and has advised several Member States to use the results of OLAF’s investigations in criminal proceedings”²⁶.

52. According to the JRC, in the period 2008-2015, through an experimental pilot project run by OLAF and JRC in collaboration with 12 Member States, the declared origin of 5 million import items were analysed, using the ConTraffic system, with 1 187 fraud signals for potential origin-related fraud sent to Member States. The potential economic value of these signals was 19 million euro. Overall 2 % of the analysed goods claimed an origin and dispatch country that did not match with the route of the containers. Based on the ConTraffic project the Commission concluded²⁷ that ‘there must have been in 2011, for EU27, more than 1 500 cases of false declarations of origin which resulted in loss of revenue for the EU for the total value of at least 25 million euro and likely to exceed 100 million euro’.

²⁶ The OLAF report 2015 (https://ec.europa.eu/anti-fraud/about-us/reports/olaf-report_en).

²⁷ SWD(2013) 483 final.

53. However, ConTraffic has his limitations and cannot always determine the real origin of goods.

Exchange of risk-related information: Too much information is counterproductive

54. Customs authorities are obliged to exchange risk information related not only to observed risks but also to threats that present a high risk elsewhere in the Union²⁸ by using a RIF. However, the customs representatives we interviewed expressed their concerns about RIFs received from other Member States as they do not always contain a sufficient level of detail to be useful. The problem of double reporting in Common Customs Risk Management System (CRMS) and in the CIS was also mentioned. Moreover, Member States and OLAF do not always provide appropriate feedback.

55. According to the final evaluation of the Customs 2013 programme²⁹, some Member States filed many RIFs for relatively small and local risks. This led to an excess of information and difficulties to identify the key risks.

Cooperation and exchange of information with non-EU countries is improving

56. If a Member State has reasonable doubts about the validity and/or the authenticity of the proof of preferential origin claimed it can send an administrative cooperation request to the beneficiary/partner country of a PTA for its confirmation. Reasonable doubts may arise when the specimen of stamp used on the proof of origin or its issuing authority differs from those shown in the database Specimen Management System³⁰ (SMS) managed by the Commission. The reply from the non-EU country authorities or, under certain circumstances, its absence can justify the refusal of the preferential tariff treatment³¹.

²⁸ Pursuant to Article 46(5) of the UCC.

²⁹ Coffey, "Final Evaluation of the Customs 2013 Programme – Final report", 2014.

³⁰ The SMS is the application used by the Commission to send information electronically on origin stamps to Member State's customs administrations.

³¹ See paragraph 68 of Special Report No 2/2014.

57. We followed-up the implementation by the Commission of recommendation Nos 5 to 13 made by the Court in its Special Report No 2/2014 'Are preferential trade arrangements appropriately managed?' and found that the Commission has implemented an action plan for monitoring the functioning of PTAs³² and established a permanent monitoring routine (questionnaires, visits, etc.).

58. However, Member States have reported problems with countries such as India, Indonesia, Afghanistan, Nepal, and Bangladesh concerning late replies and insufficient quality of the replies to administrative cooperation (AC) requests. Problems concerning India and Vietnam have already been detected by the Court in the above audit³³.

59. Mutual Assistance Agreements (MAAs) or MAA Protocols to international agreements provide a legal basis to request information from non-EU countries and serve their purpose well. However we found incidents of insufficient cooperation from China: Member States reported problems in obtaining replies to requests sent using Mutual Assistance. According to OLAF, to date only 1/3 of around 150 verification requests sent after JCO Snake³⁴ to China have been answered. The UK uses its own Foreign Customs Liaison Officer (FCLO) in China to obtain information about exports to the UK. OLAF also has an Overseas Liaison Officer (OLO) in Beijing.

60. In the context of the "Action Plan on Undervaluation" accompanying the 2015 Strategic Administrative Cooperation Arrangement, the Chinese authorities have put a disclaimer on the documents submitted to the EU, which states that they cannot be used in administrative proceedings. Evidence of the prices of textiles and footwear declared at exportation, would make it easier for Member States' customs authorities to recover losses due to undervaluation when traders challenge the post-release demand notes before a court.

³² COM(2014) 105 final.

³³ See paragraph 88 of ECA Special Report No 2/2014.

³⁴ Joint Customs Operation in 2014 between OLAF and Member States to tackle undervaluation of textiles and footwear from China.

61. Based on its operational needs OLAF is currently in the process of negotiating a number of ACAs with partner authorities in non-EU countries and international organisations. ACAs between OLAF and non-EU countries' investigative authorities represent an important additional tool for the protection of the financial interests of the European Union which complement the existing legal framework.

EU action programmes have boosted knowledge-sharing and cooperation between Member States but they have not been effective in ensuring that all customs administrations act as if they were one

62. Customs 2013/2020 and Hercule II/III provide funds to enable customs authorities to cooperate with each other and exchange information and best practices through (i) communication and information-exchange systems; and (ii) participation in joint actions, such as seminars, trainings, project groups, working visits, and cross-border operations. We found that both Customs 2013 and Hercule II have been effective in fostering knowledge-sharing and cooperation among Member States.

63. However, according to the report from the Commission to the European Parliament and to the Council on the achievement of the objectives of the Hercule II programme³⁵, 'while efforts have been made to coordinate the planning of the different Union's programmes in the area of e.g. customs, more could be done to enhance cooperation between the Commission's services to benefit from synergies between programmes and to prevent overlaps between EU Programmes and initiatives'.

64. Customs 2013 has as its specific objective 'to maintain a system for measuring the performance of Member States' customs administrations to improve their efficiency and effectiveness'³⁶. However, we found no performance indicators either to measure the achievement of the Customs 2013 objective that all Member States' customs administrations 'act as if they were one single administration', ensuring controls with

³⁵ COM(2015) 221 final.

³⁶ Pursuant to Article 5(c) of the Customs 2013 Decision.

equivalent results at every point of the EU customs territory, or to measure the achievement of the Customs 2013 objective of protecting the financial interests of the EU. We have found that Customs 2013 has not achieved its objective to ensure that all customs administrations act as if they were one (see ***paragraphs 89 to 110***).

65. The conclusion from the final evaluation of Customs 2013 programme related to the protection of the financial interests of the EU was based on the feedback received from a majority of national administrations. These were positive about the customs risk management system and Surveillance² contributions to risk management. However, we found weaknesses affecting both information-exchange systems. We also found that Member States administrations do not act as if they were one.

66. Concerning joint actions, the programme has contributed to the building and sustaining of networks. According to the final evaluation, there was strong evidence that the programme contributed significantly to the spread of relevant information, good practices, and working methods and procedures between EU Member States, particularly with regard to the development of national specifications for IT systems and their implementation.

67. Regarding Customs 2020, even though the final evaluation of the Customs 2013 programme made a recommendation to 'develop a comprehensive monitoring framework to track performance and to identify issues of concern in a timely manner', we have not found any evidence that Member States are collecting performance indicators to measure the degree of convergence between Member States (i.e. working as one).

68. Pursuant to Article 1(2)(a) of the Hercule II Decision³⁷ one of the objectives of the programme was to enhance transnational and multidisciplinary cooperation between Member States' authorities, the Commission and OLAF. However, the final evaluation concludes that the Hercule II Programme primarily enhanced transnational and

³⁷ Decision No 804/2004/EC establishing a Community action programme to promote activities in the field of the protection of the Community's financial interests (Hercule II programme) as amended.

multidisciplinary cooperation between Member States³⁸. Anti-fraud training and training, seminars and conferences with a legal focus were the main drivers in achieving this.

69. Information on the degree of achievement of the impact indicators of Customs 2020 is not available. Moreover there is no information either on the achievement of the output, results or impact indicators concerning Hercule III. This prevents us from making any provisional assessment on the effectiveness of these programmes.

The EU has made progress towards the uniform application of customs legislation

70. As a Customs Union the EU needs to apply the Common customs tariff and EU customs legislation in a uniform way, ensuring the protection of the EU's financial interests and a level playing field for traders operating in the internal market.

71. The tariff is the name given to a combination of the nomenclature (or classification of goods) and the duty rates which apply to each class of goods. It is common to all EU Member States, but the rates of duty depend on the nature of the goods imported and their origin. It contains all other EU legislation that has an effect on the level of customs duty payable on a particular import, for example the common commercial policy³⁹.

Overall TARIC ensures the uniform application of tariff measures

72. TARIC, the integrated customs tariff of the EU, is a multilingual database in which all measures relating to Common customs tariff, commercial and agricultural legislation are integrated. It helps ensure their uniform application by all Member States and gives economic operators a clear view of all measures to be undertaken when importing into the EU or exporting goods from the EU⁴⁰.

³⁸ Ramboll, "Evaluation of the Hercule II programme – Final Report", 2014.

³⁹ C.f. https://ec.europa.eu/taxation_customs/business/calculation-customs-duties/what-is-common-customs-tariff_en.

⁴⁰ https://ec.europa.eu/taxation_customs/business/calculation-customs-duties/what-is-common-customs-tariff/taric_en.

73. The Commission monitors whether the TARIC database is integrated or linked to the customs release systems in the Member States in two ways: (i) by monitoring visits at the customs authorities of the Member States and (ii) by continuous monitoring of the quality/correctness (credibility checks) of the customs declarations lodged in the Member States, via the Surveillance 2 database.

74. We found that the UK is not using the current version of TARIC, TARIC 3, because TARIC 1 is the only version that the UK customs electronic release system is capable of applying. TARIC 3 data is converted into TARIC 1 manually and uploaded. Furthermore, some TARIC restriction measures are missing from the UK national TARIC system. Finally, the UK uses different customs procedure codes to those of other Member States⁴¹.

75. Moreover the UK does not report separately to the Commission, for the Surveillance 2 database, import declaration records below 1 000 euro⁴² for simplified procedures because it applies a threshold set for the provision of statistics on external trade with non-EU countries to Eurostat. Below this threshold import items are aggregated in a special commodity code agreed with Eurostat to meet this aspect of legislation. In 2014 and 2015, 88 % of import declarations at article level were submitted using simplified procedures in the UK.

76. Traders importing in the UK face a high risk of non-uniform application of EU legislation, because of:

- (a) the manual update of TARIC in the customs electronic release system, which entails a risk of inaccuracies and incomplete revenue collection;
- (b) the absence of restriction measures in the UK TARIC, which entails safety and security risks;

⁴¹ <https://www.gov.uk/government/publications/uk-trade-tariff-customs-procedure-codes/imports-home-use-with-simultaneous-entry-for-free-circulation>.

⁴² The threshold has been set at GBP 873 for 2017.

- (c) the absence of credibility checks performed on import declaration records below 1 000 euro, which further increases the risk of wrong application of TARIC; and
- (d) the use of different customs procedure codes for import, which represents a burden for traders operating in different Member States and a risk of the wrong application of customs provisions.

77. In addition, the Commission carries out TARIC updates with retroactive effect, and these can affect the financial interests of the EU. However, these updates are not systematically communicated to DG Budget so that they can follow up their uniform application in the Member States.

78. Licences and surveillance documents are essential in the application of commercial policy measures such as tariff suspensions⁴³, tariff quotas, quotas, tariff ceilings⁴⁴, and surveillance measures⁴⁵. In the application of these measures it is essential to take stock of the volume of goods imported, which in some cases cannot be exceeded or when exceeded, standard duty rates apply.

79. Licences and surveillance documents are issued for a fixed quantity of goods. In order to guarantee that no goods are released onto the EU market without a valid document, the

⁴³ Tariff suspensions entail the reduction or removal of the customs duty rate on certain categories of goods during a specified period of time in order to satisfy certain needs of raw material and goods which have insufficient EU domestic production.

⁴⁴ Tariff quotas are similar to tariff suspensions but limited to a given volume of goods. When the volume of imports exceeds the threshold then standard duty rates apply. It should be differentiated from quotas, which limit the maximum volume of import of a certain category of good to a threshold that shall not be exceeded in any case. Tariff ceilings are similar to tariff quotas but the application of the standard duty rate once the threshold of import is exceeded requires a legal act of the Union.

⁴⁵ Certain categories of goods that threaten the interests of EU producers such as agricultural and textile products need a surveillance document to be released for free circulation. The surveillance document issued by any Member State has validity in all the EU customs territory. See database of surveillance measures in the following link:
http://ec.europa.eu/taxation_customs/dds2/surv/surv_consultation.jsp?Lang=en.

quantities have to be written-down on the licence and certified by customs for each individual import at the moment of release⁴⁶.

80. The Court recommended⁴⁷ in its Special Report No 1/2010, "Are Simplified Customs Procedures for imports effectively controlled?" that the Commission should "encourage all Member States to computerize the processing of simplified procedures including the electronic management (online writing-down at the moment of release of the goods) of licences and similar documents and the use of IT-based risk profiles covering TOR and common trade policy issues".

81. This recommendation is scheduled to be implemented by the end of 2020, with the full deployment of the UCC provisions on simplified procedures⁴⁸. However, it will not cover the online writing-down at the moment of release of goods of licences and similar documents in all Member States. Imports without a valid document adversely affect the interests of the EU producers that the commercial policy measure is meant to protect. In addition, it may affect the financial interests of the EU in the case of tariff suspensions, tariff quotas, quotas, tariff ceilings.

The Commission has implemented the ECA's recommendations on Binding Tariff Information

82. A Binding Tariff Information (BTI) is an official written decision, valid for three years, issued by a customs authority which provides the applicant with an assessment of the classification of goods in the EU tariff nomenclature prior to an import (or export). The BTI is binding on all the EU customs authorities and the holder of the decision. When the importer is the holder of a BTI this should be indicated in the customs declaration importing goods of the kind included in the scope of the BTI. BTI gives certainty to traders and contributes to the uniform application of customs legislation.

⁴⁶ See paragraph 68 of Special Report No 1/2010.

⁴⁷ See paragraph 91(3) of Special Report No 1/2010.

⁴⁸ DG TAXUD, "Annual Activity Report 2015".

83. We followed-up the implementation by the Commission of our recommendations made in a previous Special Report⁴⁹. We found that, even though there are some IT developments⁵⁰ which will only be available from October 2017, all recommendations have been addressed with the entry into force of the UCC and its Implementing and Delegated Acts on 1 May 2016.

84. However, our selected Member States' customs authorities do not verify at release that the holder of a BTI actually uses it for the imports of goods of the kind indicated in the BTI. Import declarations, which declare a TARIC code different but similar to the one indicated in the BTI, are not flagged by the risk management system for a post-release control either. Thus, a BTI holder who is not satisfied with the BTI decision can misclassify imports to circumvent the decision if Member States do not verify its application, avoiding payment of the higher duties stipulated in the BTI.

There are still no EU-wide valuation decisions

85. An EU-wide valuation decision would be an official written decision issued by a customs authority which provides the applicant with an assessment of the treatment which should be applied on a certain element of the customs value, prior to an import, for a specified period. The decision would indicate how to treat, for example, a commission payment, a royalty payment or aspects of a transfer pricing agreement for customs valuation purposes⁵¹.

86. An EU-wide valuation decision would provide legal certainty and ensure a level playing field for traders operating in several Member States. We recommended⁵² the Commission to take appropriate legislative and administrative action to overcome "the absence of

⁴⁹ Special Report No 2/2008 concerning Binding Tariff Information (BTI) (OJ C 103, 24.4.2008, p. 1).

⁵⁰ E.g. validation of EORI Nos in the EBTI database.

⁵¹ C.f. WCO, Revenue Package, "Technical guidelines on advance rulings for classification, origin and valuation, and Practical guidelines for valuation control", 2015.

⁵² See paragraph 86 of Special Report No 23/2000 concerning valuation of imported goods for customs purposes (customs valuation).

Community law provisions allowing the establishment of Community-wide valuation decisions”.

87. The UCC⁵³ empowered the Commission to extend through a delegated act the scope of decisions relating to binding information to also cover ‘other factors on the basis of which import or export duty and other measures in respect of trade in goods are applied’, therefore including valuation issues. However, so far the Commission has not yet used such empowerment.

88. The Commission has not yet implemented the Court’s recommendation. 17 years on, it is still not possible to issue EU-wide valuation decisions.

Member States do not follow a uniform approach to customs control of imports, which can lead to underpayment of customs duties

89. Member States’ customs authorities are supposed to act “as if they were one”. This was one of the objectives of Customs 2013. When Member States do not follow a uniform approach to customs controls, fraudsters may choose the weakest link in the chain to perform their fraudulent imports.

90. We found that there is no harmonised and standardised application of customs controls by the Member States, to ensure an equivalent level of customs control throughout the Union so as not to give rise to anti-competitive behaviour at the various Union entry and exit points.

Lack of uniform approach to customs controls on undervaluation distorts choice of Member State of importation

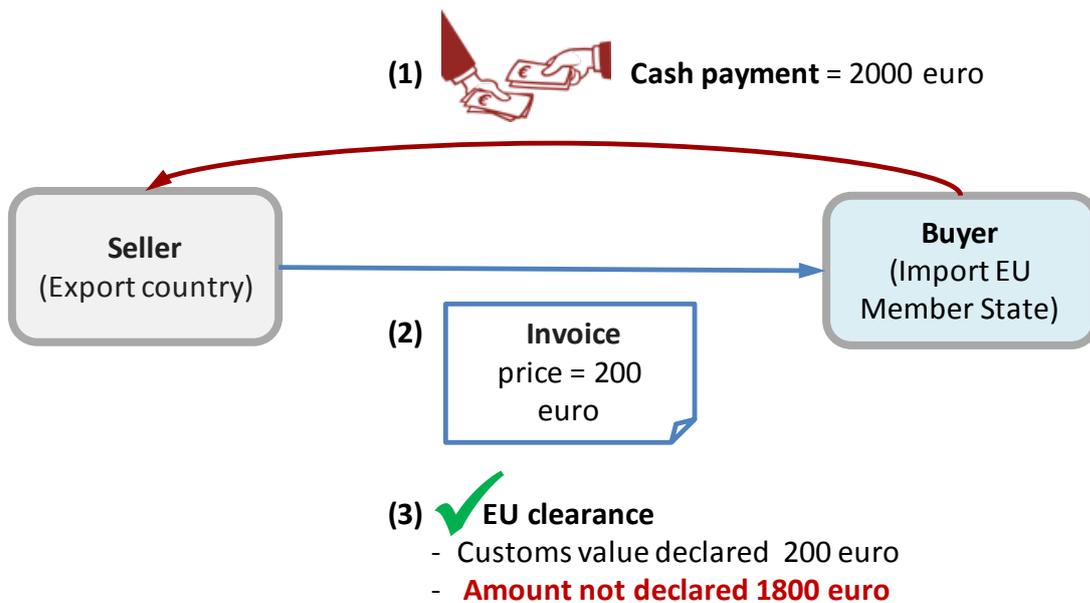
91. Member States face the challenge of tackling undervaluation fraud. Release controls should be prioritised in these cases of potential fraud because importers may subsequently become insolvent or go missing. When there are reasonable doubts whether the declared value represents the actual transaction value, customs authorities may ask, when

⁵³ Articles 35 and 36(b) of the UCC.

performing release controls, for additional information and the submission of additional documentation. Reasonable doubts may exist in particular when the declared value falls short of a defined risk threshold value.

92. For risk management purposes the risk threshold value can be determined on the basis of fair prices (see **paragraph 48**). In certain cases, importers submit supporting evidence (invoices, sales contracts, bank statements) which all match the declared (false) low values. Everything matches on the documents presented to customs and the undervaluation is difficult to detect. In such cases, there may be other payments either in cash or via third parties for the difference between the declared (undervalued) and real price. **Figure 2** below shows an example of undervaluation with an advance cash payment.

Figure 2 – Undervaluation with advance cash payment



Source: ECA based on an example of the WCO.

93. Customs procedure 42 (CP 42) is the regime an importer uses in order to obtain a VAT exemption when the imported goods will be transported onward to another Member State. In this case the VAT is due in the Member State of destination⁵⁴. When the import is made

⁵⁴ Special Report No 13/2011 “Does the control of customs procedure 42 prevent and detect VAT evasion?”

under CP 42 additional information on the actual transaction value should be requested from the customs authorities of the Member State of destination using mutual assistance because in these cases the final recipient of the goods may make a payment to, e.g. the Chinese supplier which is much higher than the invoice value shown by the customs representative to the customs authorities of the Member State of importation. However, this can be time consuming or unsuccessful because the declared acquirer can be different to the final recipient of the goods or be a missing trader⁵⁵.

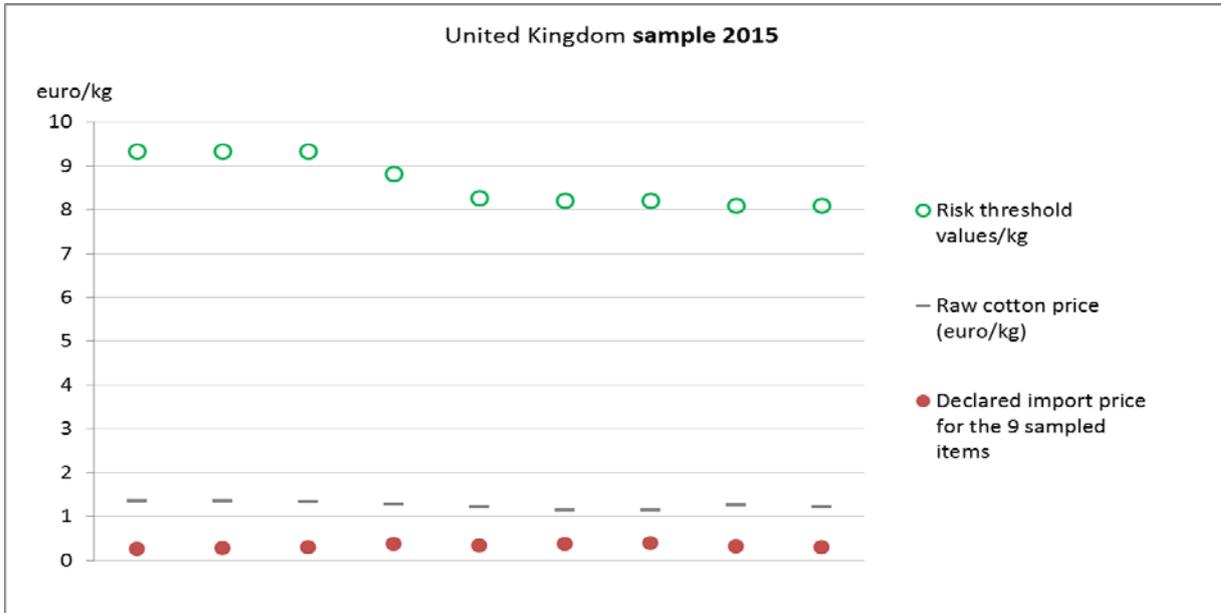
94. When doubts still persist, samples of the imported goods can be taken and a security can be requested⁵⁶ to cover the potential duty losses. The Commission has provided clear guidelines to Member States on how to tackle undervaluation during the implementation of the Priority Control Area (PCA) Discount on undervaluation of textiles and footwear from Asian countries. However, practical difficulties still persist.

95. We selected in each of the visited Member States a sample of 30 potentially undervalued imports of textiles and footwear from Asia carried out in 2015 in order to verify whether the requests contained in the OLAF MA communications relevant for undervaluation had been complied with. We found that Member States had implemented the relevant MA communications in different ways and that OLAF requests were not met in all cases. We also found that all the sample items were significantly undervalued. In some cases, the prices of the processed cotton declared at import were even below the price of raw cotton. **Figure 3** and **Figure 4** below show a comparison between the risk threshold values of processed cotton, the raw cotton prices and the prices declared at import in the samples of the UK and Poland:

⁵⁵ A trader registered for VAT purposes who, potentially with a fraudulent intent, acquires or purports to acquire goods or services without paying VAT and supplies these goods or services with VAT, but does not remit the VAT collected to the national tax authority.

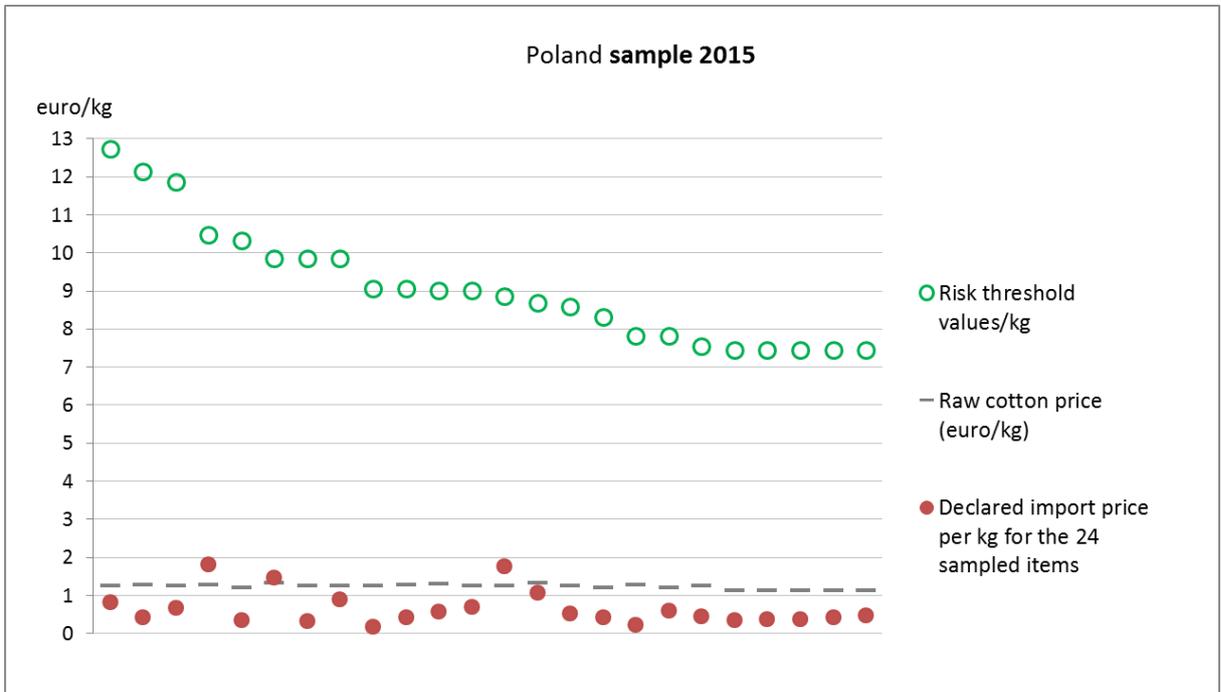
⁵⁶ Pursuant to Articles 191 of the UCC and 244 of the UCC IA.

Figure 3 – Prices of imported processed cotton goods of sample in the UK and comparison with risk threshold values and raw cotton price



Source: ECA, based on data from THESEUS web-based resource (<https://theseus.jrc.ec.europa.eu>) and from <http://www.finanzen.net/rohstoffe/baumwollpreis/euro/historisch>.

Figure 4 – Prices of imported processed cotton goods of the sample in Poland and comparison with risk threshold values and raw cotton price



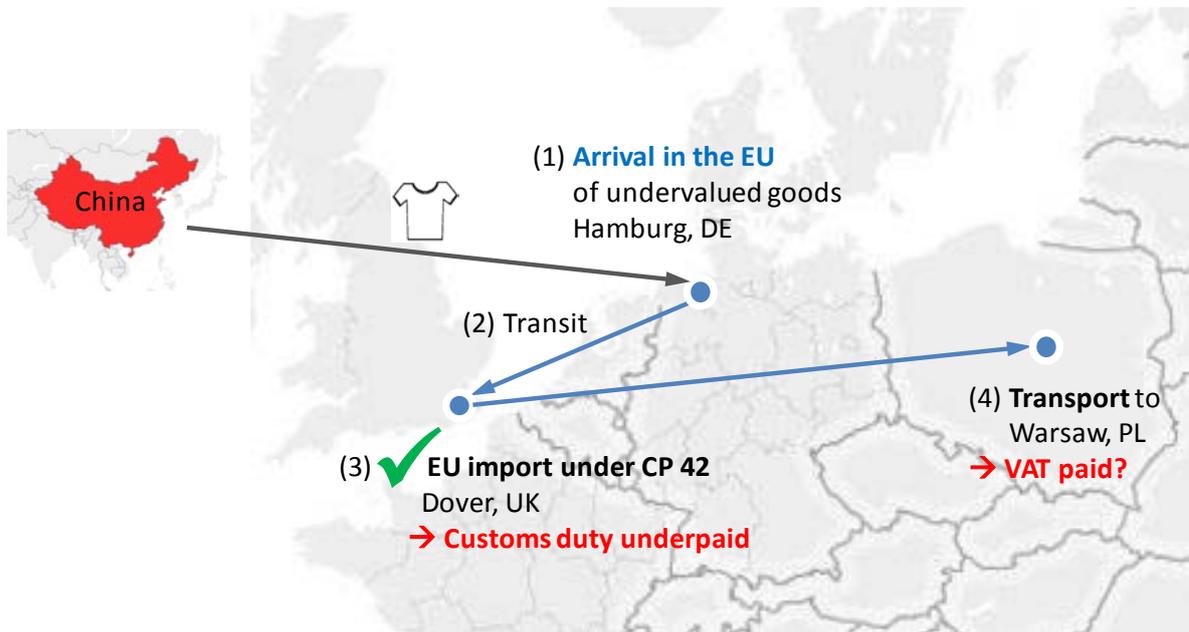
Source: ECA, based on data from THESEUS web-based resource (<https://theseus.jrc.ec.europa.eu>) and from <http://www.finanzen.net/rohstoffe/baumwollpreis/euro/historisch>.

96. We also found that Member States which carry out fewer customs release controls attract more imports. This is particularly evident in the case of controls related to undervaluation of textiles and footwear from China, where Member States which do not carry out customs release controls attract traffic from other Member States.

97. The UK does not apply the risk thresholds described in paragraph 92, nor does it request at release a guarantee for the release of goods declared with a potentially undervalued customs value in order to cover the potential duty loss. However, OLAF requested all Member States to take all appropriate precautionary measures to protect the EU's financial interests and to 'take duty on deposit on identified suspect consignments in order to prevent future loss of customs duties'.

98. We found that the lack of request for a guarantee in the UK in respect of potentially undervalued goods has led to traffic diversions: imports of significantly undervalued Chinese goods coming in transit from other Member States which, after being cleared under CP 42 in the UK, are transported back to continental Europe, e.g. textiles or footwear from China dispatched under external transit procedure from Hamburg to Dover, where they are released for free circulation under CP 42 without release controls and then transported back to, for example, Poland or Slovakia. **Figure 5** shows an example of this 'import point shopping' using CP 42:

Figure 5 – A case of ‘import point shopping’ using customs procedure 42 (CP 42)



Source: ECA.

99. Operation Octopus was carried out in 2016 by the French customs with the cooperation of OLAF. It was focussed on imports under CP 42. This administrative cooperation action highlighted that undervaluation fraud took place mainly in the UK and it was further aggravated by the fact the VAT was not paid in the Member States of destination. The values declared on the basis of fake invoices were undervalued from 5 to 10 times with a significant impact on customs duties and taxes collected⁵⁷.

100. Concerning the impact of the fraudulent use of CP 42 on VAT and customs duty losses, according to paragraph 83 of our Special Report No 24/2015⁵⁸, ‘We found in the United Kingdom two cases of undervalued imports under CP 42, which had been already identified by HMRC as a result of the OLAF’s JCO. HMRC estimated the impact on VAT collection in the United Kingdom to be GBP 0.5 million and GBP 10.6 million in other Member States. The

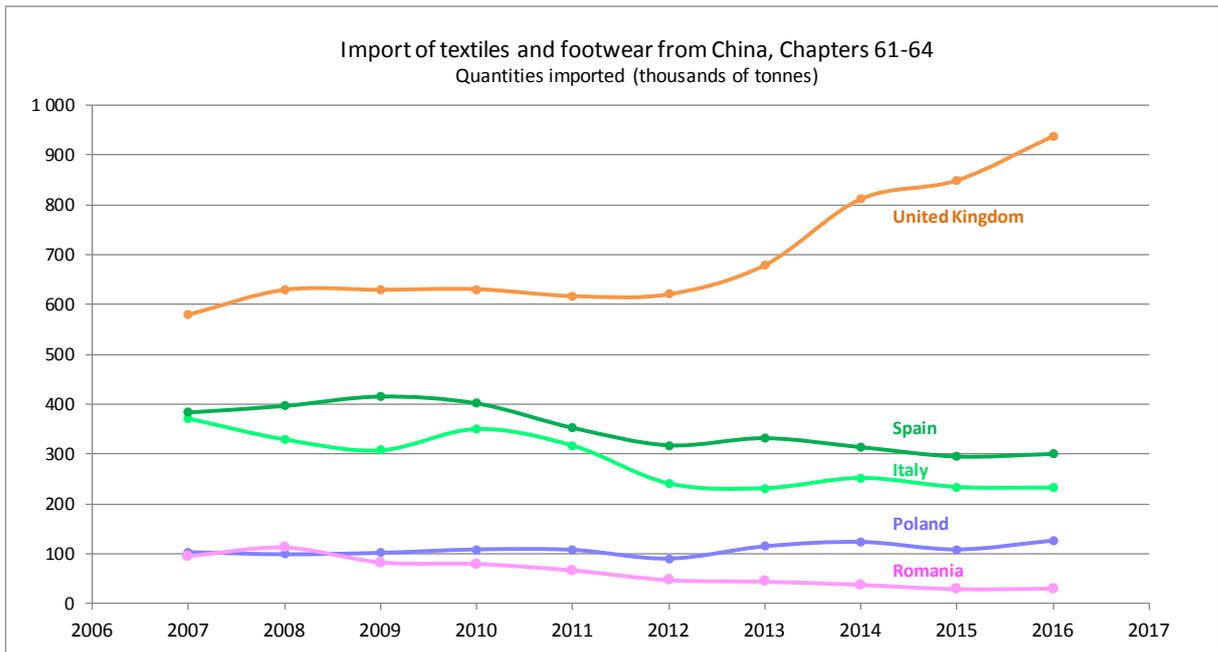
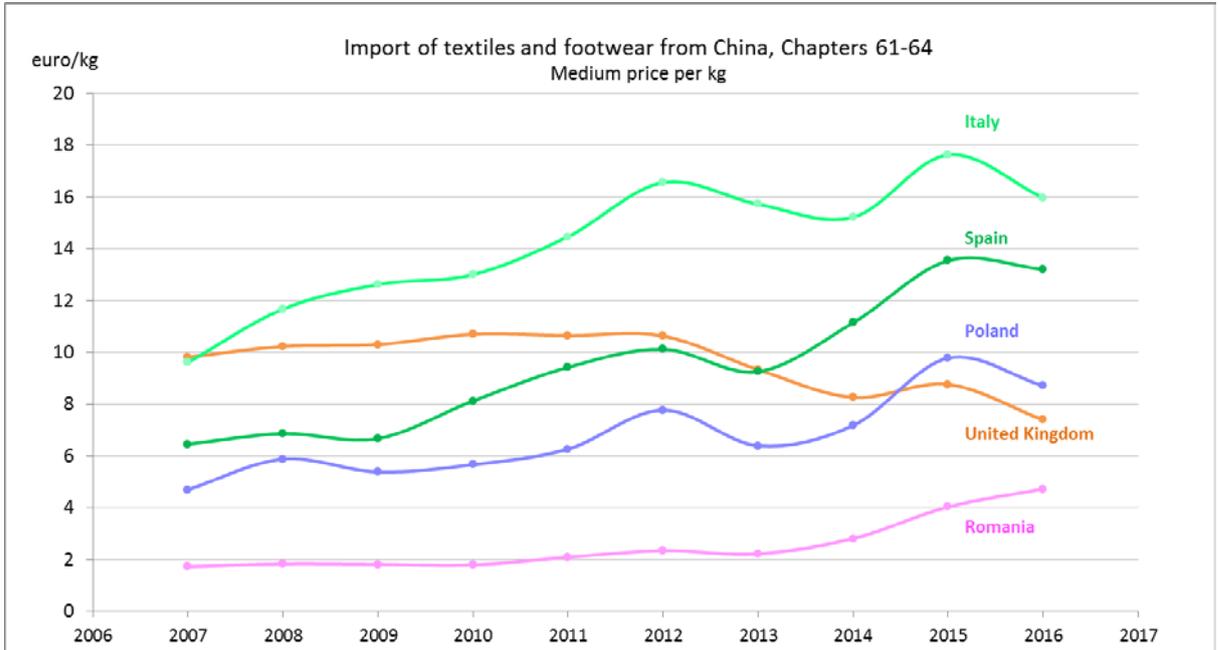
⁵⁷ See results of Joint Customs Operation ‘Octopus’ at <http://www.douane.gouv.fr/articles/a12973-la-douane-et-l-olaf-presentent-les-resultats-de-l-operation-octopus>.

⁵⁸ Court’s Special Report No 24/2015 “Tackling intra-Community VAT fraud: More action needed”.

estimated impact on customs collection in the United Kingdom amounts to GBP 81 million. These impacts have been estimated by HMRC for all items imported by the two traders identified in the sample in a three year period’.

101. **Figure 6** shows data from Eurostat from the period 2007-2016 on the five Member States selected by the Court. Member States which implemented thorough release controls on undervaluation of textiles and footwear from China saw an increase in the average declared import prices but experienced a decrease in the volume of imports. The increase in the volume of imports in the UK was 358 000 tonnes, while the overall decrease in the other four Member States was 264 000 tonnes.

Figure 6 –Medium prices and volumes imported of textiles and footwear in 2007-16



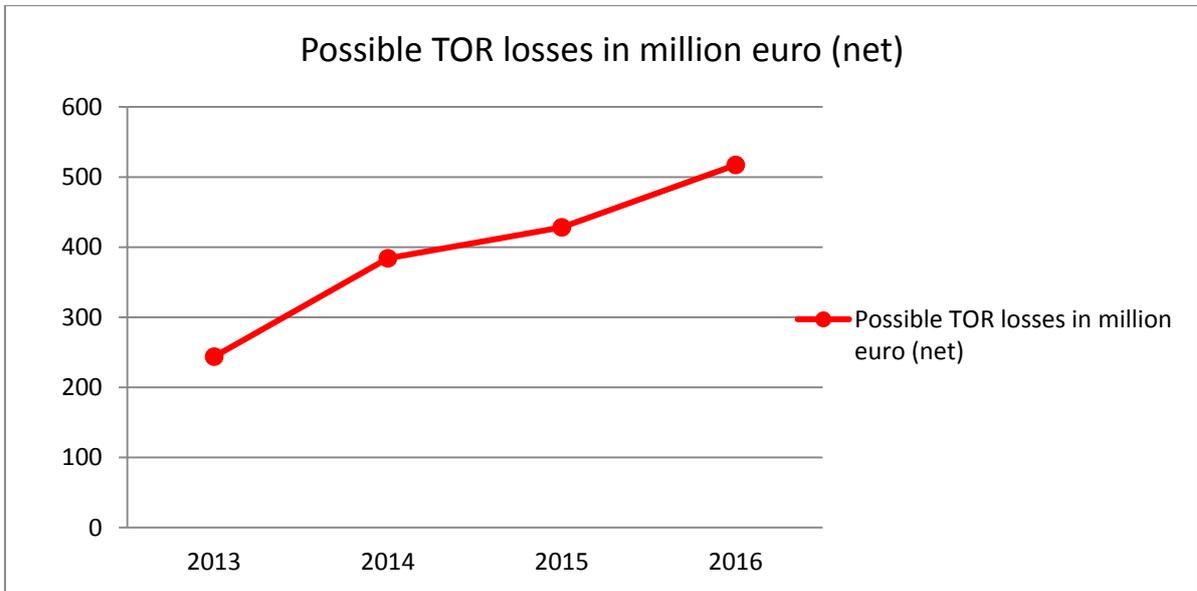
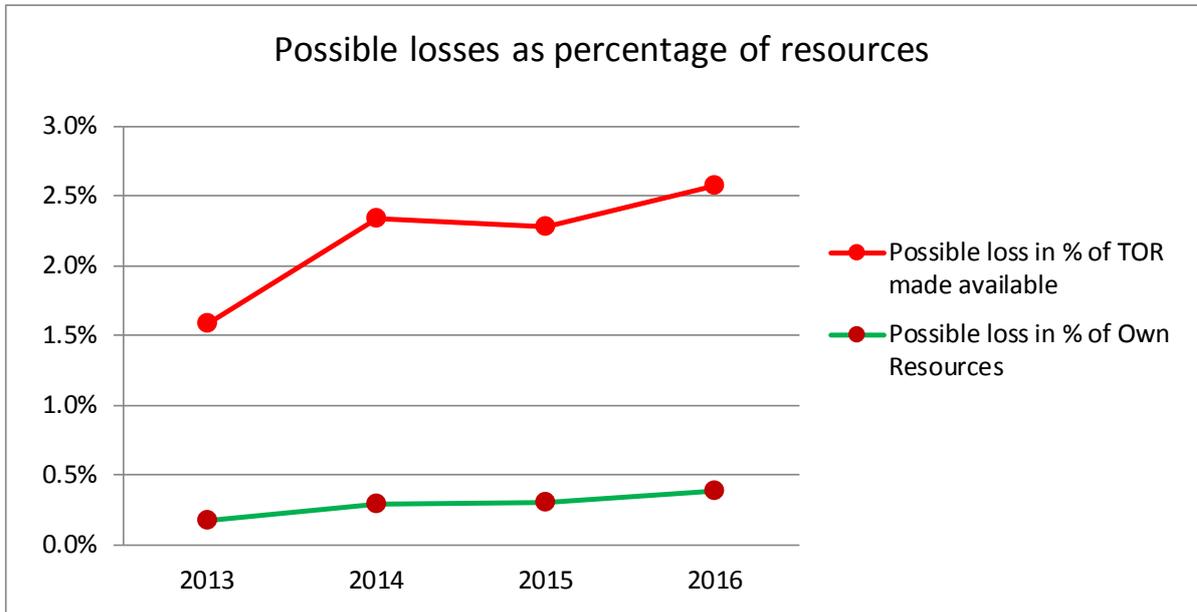
Source: Eurostat.

102. This is further corroborated by the estimates of potential duty losses due to undervaluation of textiles and footwear made for the period 2013-16 by OLAF.

103. According to OLAF⁵⁹, “the UK should have made available an estimated amount of 1.9874 billion euro (gross), or 1.5736 billion euro (net), more traditional own resources than it did from 2013 to 2016. The quantification of the possible loss (in net terms, after the deduction of collection costs) compared to the total own resources and traditional own resources actually made available by the Member States during the same period can be found below” in **Figure 7**.

⁵⁹ DG Budget, “Annual activity report 2016”.

Figure 7 – Impact in the EU Budget of the estimated amount of potential losses in the UK



Source: DG Budget, Annual Activity Report 2016.

104. This further corroborates our findings of Special Report No 23/2016 that "differences in customs control practices between Member States can make one port more attractive than others for global shipping lines"⁶⁰.

Member States have different approaches to tackle origin and classification fraud

105. OLAF can disseminate fraud alerts to Member States using Mutual Assistance (MA) communications. They contain requests to Member States' customs authorities to safeguard the EU's financial interests.

106. We found that the five selected Member States followed different approaches concerning the follow-up of OLAF MA communications 2015/15 on misclassification, and 2014/21-2015/18 concerning misdescription of origin. Dishonest traders can exploit any different approach to customs controls to evade payment of customs duties.

107. We also found that the follow-up of MA communications is easier in those Member States where the indication of the consignor is compulsory in the customs import declaration (SAD).

Member States have different approaches regarding penalty regimes

108. In the EU the enforcement of customs legislation is an obligation on the part of Member States⁶¹, which can use a diversity of civil, administrative and/or criminal penalties to deter infringements. This can distort competition in the internal market between legitimate traders while fraudsters can exploit these differences and damage the EU's financial interests.

109. We found that in Poland, Belgium and France customs infringements are considered to be of a criminal nature and systematically give rise to criminal proceedings. In Poland there are neither administrative nor civil penalties for customs infringements.

⁶⁰ See paragraphs 82 and 93 to 99 of Special Report No 23/2016 "Maritime transport in the EU: in troubled waters —much ineffective and unsustainable investment".

⁶¹ Based on Article 4(3) of Treaty of the European Union.

110. The Commission presented a proposal for a Directive laying down a Union legal framework on customs infringements and sanctions⁶², which is currently being examined by the Council and the European Parliament. The Directive proposal is the result of a study⁶³ on the Member States' legal frameworks on customs infringements and sanctions.

There are loopholes in the customs control of imports

111. Member States' customs authorities risk management includes identifying, assessing, analysing and mitigating the different types and levels of risks associated with the international trade of goods.

112. EU customs risk management operates under the principle "assess in advance, control where required". Depending on the risks involved, they can be addressed prior to the loading of the goods in the exporting country, before their arrival in the EU territory or at the place of unloading, at the time of importation or after the goods have been released for free circulation⁶⁴.

113. Imports can take place using normal or simplified procedures. Importing goods using simplified procedures facilitates trade by increasing the speed of release of goods. The Commission produces every year a report on the Customs Union Performance (CUP), which shows an overview of the frequency and effectiveness of the different types of customs controls carried out.

Member States do not carry out pre-arrival controls to protect the EU's financial interests

114. At the pre-arrival stage, customs authorities can obtain advance information on imminent cargo arrivals via shipping manifests and other sources. In the EU, carriers or their authorised representatives can lodge electronic entry summary declarations (ENS) at the first (air)port of entry into the customs territory of the EU at a prescribed time ahead of the

⁶² COM(2013) 884 final.

⁶³ Report from the Customs 2013 Project Group on Customs Penalties.

⁶⁴ C.f. COM(2014) 527 final of 21.8.2014.

arrival of the goods. Customs risk analysis teams can analyse this data and make preliminary targeting selections. However, limited information is available at that stage to enable detailed checks for fiscal purposes, e.g. regarding valuation or classification of the imported goods⁶⁵.

115. The five selected Member States' customs authorities argued that they cannot carry out pre-arrival checks on ENS for fiscal purposes due to the absence of relevant data. However, suspicious (adversely known) traders can trigger pre-arrival checks relevant for fiscal purposes if the ENS shows data on the consignor and consignee. While this is regularly the case, such data can be missing⁶⁶.

Member States do not always carry out the controls suggested by their risk management systems

116. Release controls suggested by the risk management system can be either physical, documentary, or consist of the taking of a sample of goods for further analysis, including laboratory analysis.

117. We found that in the Member States visited by the Court, except for the UK, a customs officer can override a control measure suggested by a risk filter without any hierarchical approval or confirmation. This represents a gap in the internal control system which erodes the effectiveness of the customs risk management system.

118. In the UK, documentary and physical checks apply only to normal import procedures, which represent 12 % of import declarations. We found that 99.77 % of imports declared under normal procedures in 2015 were cleared within one hour; and that documentary controls to tackle misdescription of origin at release do not check either the original proofs of origin or the ConTraffic database for mismatches. This calls into question the effectiveness

⁶⁵ C.f. WCO, Revenue Package, "Technical guidelines on advance rulings for classification, origin and valuation, and Practical guidelines for valuation control", 2015.

⁶⁶ This happens when carriers submit the ENS with the master bill of lading data and not with the house bill of lading data from the freight forwarders.

of release controls in the UK. The remaining 88 % of import declarations were submitted using simplified procedures and were not subject to release controls.

The level of post-release controls does not compensate for the decrease in release controls on simplified procedures

119. Traders who are authorized to use simplified customs procedures for imports benefit from an accelerated customs release process. Customs place reliance on the correctness of their import declarations and carry out fewer controls before release. This should be compensated by pre-authorisation and ex-post audits⁶⁷. In 2015, nearly four fifths of all EU imports were made using simplified procedures, of which 0.2 % were subject to release controls.

120. However, we found that in Spain and in the UK there are no release controls performed on simplified procedures. This is particularly serious in the case of the UK because the vast majority of import declarations are submitted using simplified procedures.

121. An Authorised Economic Operator (AEO) is a reliable trader who benefits from fewer physical and document-based controls at clearance. The AEO authorisation is granted by customs provided that the trader meets certain criteria⁶⁸.

122. One of the simplifications provided for in the UCC allows the submission of an import declaration by means of an entry in the records of the holder of the authorisation. In this case, the trader is obliged to notify the presentation of the goods to customs but no data related to the origin, tariff classification and value of the goods are included in this notification⁶⁹ which would allow customs to carry out a meaningful risk analysis for fiscal

⁶⁷ Special Report No 1/2010 'Are Simplified Customs Procedures for imports effectively controlled?'

⁶⁸ Article 39 of the UCC sets up the criteria for the granting of the status of authorised economic operator (AEO).

⁶⁹ Message I2 of notification of presentation of goods to customs in case of entry in the declarant's records pursuant to Annex B of the UCC DA.

purposes. In addition, customs authorities may waive the AEO from the obligation to present the goods to customs⁷⁰.

123. We found cases of AEOs operating in the courier sector that abuse the customs relief for low value consignments, and other cases of AEOs that did not fulfil the AEO conditions at the time of our visit, or who submitted undervalued imports of textiles and shoes from China as either declarant or representatives.

124. We found that Italy does not carry out post-release audits as defined in the Customs Audit Guide, not even in respect of AEO. In the UK we examined 10 post release audit files related to AEOs but none was actually a post-release audit but rather an assessment or monitoring carried out on the continued fulfilment of the AEO conditions.

125. Finally, in July 2016 the Commission noted that six Member States⁷¹ either did not carry out any post-release audits or did not provide any information about these audits. These Member States were the source of about 20 % of the total amount of customs duties collected in the EU⁷². Post-release audits are meant to tackle residual risks after release and other post-release controls but when they are not carried out these risks remain.

Post-release controls rarely cover imports in other Member States

126. Where an importer with its headquarters in one Member State (Member State 2) performs an import operation in another Member State (Member State 1), customs controls must be carried out by the latter⁷³.

⁷⁰ In accordance with Article 182 of the UCC.

⁷¹ Belgium, Estonia, Italy, Portugal, Romania and Slovenia.

⁷² See paragraph 4.18 of ECA Annual Report 2016.

⁷³ The Customs Code Committee (Section for General Customs Rules) concluded during its 30th meeting on 19.5.2000 that "...it was for the Member States where the goods were cleared to do checks. They acknowledged that there could be difficulties when the accounts and the goods were elsewhere, but considered Member States should liaise appropriately".

127. We found that the customs authorities of Member State 1 do not address the customs authorities of Member State 2 to request the accounting records, bank accounts, etc. of the trader situated in its territory and that the customs authorities of Member State 2 are not aware of the imports made as there is no obligation for the authorities of Member State 1 to notify them.

128. This is aggravated by the fact that the information included in the existing database of imports in Member States, "Surveillance2", is of limited use for post-release audits, as it does not include the name of the importer and/or declarant. The full deployment⁷⁴ of a database named "Surveillance3", which includes this and other relevant information, is not expected until 1 October 2018.

129. We found that this situation particularly applies to CP42. Under this procedure, the importer based in Member State 2 can appoint a representative in Member State 1 to carry out the import there, making it more difficult to carry out the post-release control.

130. According to OLAF, around 57 % of all suspected undervalued imports from China in the area of textiles and footwear are cleared under CP42, even though only 16 % of imports are cleared under this procedure.

131. The Commission has also found, during an inspection carried out in Slovakia in December 2016, that the main risk of undervaluation was detected in imports covered by CP42 where the importer is usually located in another Member State, making it more difficult to fight it via post-release controls.

The lack of checks on customs relief for low value consignments is leading to underpayment of customs duties

132. Customs legislation provides for an exemption or duty relief for consignments of negligible value. Goods whose value does not exceed a certain threshold are exempted from

⁷⁴ Pursuant to Commission Implementing Decision (EU) 2016/578 of 11 April 2016 establishing the Work Programme relating to the development and deployment of the electronic systems provided for in the Union Customs Code (OJ L 6, 15.4.2016, p. 6).

customs duties and other taxes. This is because the small potential revenue collection of low-value consignments does not make up for the administrative and business costs needed to ensure the compliance with customs rules.

133. The rapid expansion of e-commerce has altered this picture. As the Organisation for Economic Cooperation and Development (OECD) acknowledges⁷⁵, “at the time when most current low value import reliefs were introduced, internet shopping did not exist and the level of imports benefitting from the relief was relatively small”.

134. Business to consumer (B2C) supplies of goods purchased from non-EU countries have a low value consignment relief of VAT (and customs duties) when their value does not exceed the threshold of 10 or 22 euro. In addition to VAT, when the value of goods is higher than 150 euro customs duties must be levied. A gift sent from one private individual to another private individual (P2P) is exempted from customs duties and VAT when its value does not exceed 45 euro. When its value exceeds 45 euro but is not higher than 700 euro, excluding VAT, a standard flat customs duty rate of 2.5 % can be applied. All these reliefs apply also to goods purchased on-line from non-EU countries.

135. We found that the electronic customs release systems in the selected Member States accepted (i) imports applying for a relief of customs duties for goods of negligible value even though their declared value⁷⁶ was higher than 150 euro, and (ii) imports of commercial consignments declared as gifts.

136. We also found that even couriers holding an AEO authorisation abused these customs reliefs on imports carried out after the entry into force of the UCC Delegated and

⁷⁵ OECD, “Addressing the Tax Challenges of the Digital Economy”, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, 2014.

⁷⁶ Intrinsic value defined as the item value without freight and insurance charges.

Implementing Acts⁷⁷ on 1st May 2016. This is particularly serious as AEOs are required to have internal controls capable of preventing and detecting illegal or irregular transactions⁷⁸.

137. Evidence gathered by the UK on e-commerce points to massive undervaluation of goods imported from the Far East and increasingly the USA, by a factor of anywhere between 10 - 100 times below the correct valuation.

138. According to the Belgian Customs, goods purchased via certain non-EU websites are systematically declared as goods with a value below 22 euro, while the consumer actually paid more⁷⁹.

139. Finally, according a study by Copenhagen Economics⁸⁰, import duties are only levied on 47 % of dutiable postal shipments and this incomplete levying of import duty directly translates into a loss of customs duties in the EU of approximately 0.25 billion euro.

140. Therefore, customs duty losses take place in two ways: (i) via undervaluation of goods, so the goods are wrongly declared as eligible for the low value consignment relief; and (ii) via application of the relief for non-eligible goods, e.g. goods declared with a value higher than 150 euro and accepted by the customs release system because there is a loophole therein or commercial consignments (B2C) declared as gifts (P2P) because they are not controlled by customs.

141. In the case of couriers holding an AEO authorisation, this is all the more possible because they benefit from fewer physical and document-based controls and this includes

⁷⁷ Commission Implementing Regulation (EU) 2015/2447 of 24 November 2015 laying down detailed rules for implementing certain provisions of Regulation (EU) No 952/2013 of the European Parliament and of the Council laying down the Union Customs Code (UCC IA) (OJ L 343, 29.12.2015, p. 558).

⁷⁸ Pursuant to Article 25(1)(f) of the UCC IA.

⁷⁹ See e.g.: "Cel Cybersquad spoorde al 858 frauderende webshops op", article in De Standaard of 27 July 2015, available at: http://www.standaard.be/cnt/dmf20150727_01793127.

⁸⁰ Copenhagen Economics, E-commerce imports into Europe: VAT and customs treatment, 2016.

fewer controls at the point of importation and can be taken into account for post-release controls as well⁸¹.

CONCLUSIONS AND RECOMMENDATIONS

142. The audit addressed the question of whether the EU import procedures protect its financial interests. We found serious weaknesses indicating that there are shortcomings in the legal framework as well as an ineffective implementation of customs controls by Member States on imports, which adversely affect the financial interests of the EU.

143. The absence of an estimate of the customs gap adversely affects the evaluation of the performance of the Customs Union in terms of the protection of the EU's financial interests and prevents an efficient allocation of resources to areas e.g. undervaluation, or Member States where the highest potential losses are identified (see **paragraphs 26 to 28**).

Recommendation 1

In order to be able to meet the European Parliament's request, the Commission should develop a methodology and produce periodic estimates of the customs gap from 2019 and take into account its results for the allocation of resources and for setting operational targets.

Target implementation date: 2019.

144. The Member States are not sufficiently financially encouraged to perform customs controls and to improve the collection of customs duties for the EU Budget: Member States which perform customs controls but are not successful in their recovery action risk to bear the financial consequences of these losses, whereas perversely Member States which do not carry out such controls may not suffer any negative consequence. Moreover, one Member State complained that the more it tackles fraud the higher the risk that the Commission holds it financially liable (see **paragraphs 29 to 32**).

⁸¹ C.f. Commission Directorate-General Taxation and Customs Union, "Authorised Economic Operator Guidelines", 2016.

145. Even if financing is provided through EU action programmes, it is not always linked to the protection of the EU's financial interests. Member States do not always provide the necessary financial resources for the implementation of non-Union components of the European Information systems which are not financed by the action programmes, leading to a possible delay in the UCC implementation. Some Member States where the main ports of entry are located accept that their share of TOR retention is too high (see **paragraphs 33 to 40**).

Recommendation 2

The Commission should consider all available options to strengthen support for national customs services in their important EU role in the new Multiannual Financial Framework (MFF), including a review of the appropriate rate of collection costs.

Target implementation date: for the start of the next MFF.

Recommendation 3

The Commission should propose that the next EU action programmes, which support the Customs Union should be used to contribute to financial sustainability to the customs European Information Systems

Target implementation date: for the start of the next MFF.

146. Information exchange and cooperation in customs matters works smoothly. But the audit showed that there are still weaknesses in the information exchange tools, both in terms of content and their use (see **paragraphs 41 to 69**).

Recommendation 4

The Commission should:

(a) propose amendments to customs legislation in 2018 aimed at making compulsory the indication of the consignor in the customs import declaration (SAD); and

(b) be more precise in the requests contained in a Mutual Assistance communication to ensure their uniform implementation by the Member States.

Target implementation date: immediately.

Recommendation 5

The Commission should appoint in 2018 an OLAF overseas liaison officer in non-EU countries where most fraudulent transshipments in free zones occur.

147. In terms of uniform application of EU customs legislation, the integrated Tariff of the European Union (TARIC) is uniformly implemented in four of the five audited Member States. However, there are retroactive changes in TARIC which have financial impact and need to be carefully implemented by Member States. Member States do not properly check whether the Binding Tariff Information (BTI) decisions issued are actually used at the moment of import by the holders. Although the UCC gave a remit to the Commission to make the issuance of EU-wide valuation decisions possible, the Commission has not done so (see ***paragraphs 70 to 88***).

Recommendation 6

The Commission should:

- (a) carefully follow-up in Member States their checks on BTI decisions' compliance by 2020; and
- (b) make the issuance of EU- wide valuation decisions possible without further delay, as recommended by us in Special Report No 23/2000.

148. Member States have differing approaches in terms of customs controls to tackle undervaluation, misdescription of origin and misclassification and to impose penalties. It is a challenge for customs authorities to strike a balance between the need to facilitate trade with faster, seamless import procedures and the need to carry out customs controls. Burdensome customs controls can have an impact on the traders' choice of customs office of importation and (air)ports with fewer customs controls attract more traffic. The Court found cases of "import point shopping", i.e. traders choose to import the undervalued goods in Member States with lighter controls (see ***paragraphs 89 to 110***).

Recommendation 7

The Commission should propose legislative changes allowing it to impose financial corrections, from 2021, on those Member States which are not adequately addressing the risks and possibly encouraging “import point shopping”.

149. Due to lack of sufficient data, Member States do not carry out risk analysis for fiscal reasons at the pre-arrival stage or on traders’ notification of arrival of goods at their premises. Moreover, in the five audited Member States, customs officials can ignore the checks suggested by the national risk management system, without any hierarchical approval. Concerning simplified procedures, Member States do not compensate for the reduced level of release controls with post release controls. Furthermore, if a trader imports in a Member State other than the one it is based in, such imports are rarely checked ex-post. Member States face difficulties in ensuring traders’ compliance with the customs duty relief for low value consignments, leading to losses for the national and EU Budgets. We found that AEOs operating in the courier sector are abusing such relief (see **paragraphs 111 to 141**).

Recommendation 8

The Commission should in 2018:

- (a) propose legislative action to make mandatory the provision of additional data elements allowing the performance of financial risk analysis at pre-arrival stage and on traders’ notification of arrival of goods at their premises;
 - (b) improve the Surveillance database to identify the recipient of the goods when customs procedure 42 is used; and
 - (c) investigate the abuse of the low-value consignment reliefs on e-commerce trade of goods with non-EU countries.
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Recommendation 9

Member States should immediately:

- (a) make overrides of controls suggested by a particular risk filter conditional on prior or immediate hierarchical approval;
- (b) introduce checks in their customs electronic release systems to block the acceptance of import declarations applying for a duty relief for low-value consignments of goods with declared intrinsic value higher than 150 euro or for commercial consignments (B2C) declared as gifts (P2P);
- (c) verify ex-post traders' compliance with customs duty relief for low-value consignments, including AEOs;
- (d) set-up investigation plans to tackle abuse of these relief on e-commerce trade of goods with non-EU countries.

This Report was adopted by Chamber IV, headed by Mr Baudilio TOMÉ MUGURUZA, Member of the Court of Auditors, in Luxembourg at its meeting of 7 November 2017.

For the Court of Auditors

Klaus-Heiner LEHNE

President

ECA audit approach at the level of the Commission

We performed the audit at the Commission in two stages, a preparatory stage and the audit fieldwork.

1. During the preparatory stage we carried out information-gathering visits to DG Taxation and Customs Union, DG Budget, OLAF and the Joint Research Centre (JRC).

We discussed the audit methodology with the Commission (audit questions, criteria and standards), including the audit methodology in the Member States and the Commission's replies to our pre-visit questionnaire. We also received feedback and suggestions concerning undervaluation, misdescription of origin and misclassification, the main inherent risks affecting the release of goods for free circulation and collected the relevant documents.

At the JRC the Commission presented its scientific projects concerning container tracking (ConTraffic) and estimation of fair prices (THESEUS). The JRC granted the auditors access to ConTraffic database and THESEUS web-based resource.

DG Taxation and Customs Union granted the auditors access to Surveillance 2, the database on import declaration records, and Specimen Management System (SMS), the database on authentic stamps and authorities which can issue a preferential origin or a movement certificate.

Finally, DG Budget granted the auditors access to OWNRES, the database of on cases of fraud and irregularities involving amounts exceeding 10 000 euros, and WOMIS, the database that contains reports concerning irrecoverable amounts above a certain threshold where Member States have not made the respective amounts available to the EU budget, as they consider that the reasons for which the amounts could not be recovered cannot be attributed to them. The Commission issues its comments on the reports within six months from their receipt.

We examined pertinent performance information, such as the annual activity reports, DG Taxation and Customs Union's customs union performance reports, and progress and evaluation reports related to the EU action programmes Hercule II/III and Customs

2013/2020. We also examined the database containing up-to-date information on the follow-up of previous ECA recommendations, the RAD database.

We visited the World Customs Organisation where we presented our audit, discussed its role, responsibilities and challenges concerning undervaluation, valuation rulings, origin, revenue gap and e-commerce. We discussed the relevant international standards such as the Agreement on the Implementation of Article VII of the General Agreement on Tariffs and Trade (GATT), the so-called Customs Valuation Agreement; the WCO Revised Kyoto Convention on the simplification and harmonization of Customs procedures; and the WCO guidelines. The purpose of this visit was to assess whether the Commission follows international best practices. We examined the most relevant and recent WCO guidelines, in particular the Revenue Package. This was used as a benchmark for the preparation of the questionnaires sent to the selected Member States on valuation, origin and tariff classification.

2. During the audit fieldwork we sent a general questionnaire to the Commission. This addressed the question of whether the Commission ensures that import procedures protect the EU's financial interests. We also gathered evidence of the current developments and the Commission's activities in the areas as the customs gap, EU action programmes concerning cooperation between Member States' customs administrations, mutual assistance, follow-up of Member states' uniform implementation of customs provisions and whether the Commission had designed robust import procedures to avoid loopholes leading to TOR underpayments.

This general questionnaire was replied to by DG Budget, OLAF and DG Taxation and Customs Union. In addition, we sent two supplementary questionnaires to each of them and we organised interviews with representatives of the Units in charge of the different areas addressed in the questionnaires.

We have followed-up the implementation by the Commission of Special Reports relevant for the current audit, such as the Special Report No 2/2008 concerning Binding Tariff Information (BTI); the Special Report No 1/2010 'Are Simplified Customs Procedures for imports effectively controlled?', and the Special Report No 2/2014 'Are preferential trade arrangements appropriately managed?'

ECA audit approach in Member States

We carried out the audit in two stages, a preparatory stage and the audit fieldwork.

1. During the preparatory stage, we selected five Member States: Spain, Italy, Poland, Romania and the United Kingdom. The selection of Member States was based in the following risk criteria: (i) the size of its TOR contribution to the EU Budget; (ii) the incidence of the undervaluation in the Member State; and (iii) the proportion of audit-based controls in the total of post-release controls.

We sent a questionnaire to the selected Member States. This addressed the question of whether the Member States ensure that import procedures protect the EU financial interests. We received written replies from all the selected Member States.

Prior to each visit to the Member States we selected:

- (a) 30 potentially undervalued import transactions. For this selection, we applied Visual Data Analysis to the population of imports recorded in Surveillance 2 by each Member State in 2015, using *Tableau*. The potential undervaluation was then benchmarked with the fair prices per kg published by the Joint Research Centre in THESEUS and with the average price per unit reported in Surveillance 2;
 - (b) 30 import transactions subject to Mutual Assistance (MA) communications issued by OLAF to tackle misclassification of goods. We randomly selected imports recorded in Surveillance 2 by each Member State in 2015 by using ACL;
 - (c) the whole population of imports affected by a MA communication to tackle misdescription of origin in 2015, according to Surveillance 2;
 - (d) a risk-based sample of 10 audit files related to Authorised Economic Operators (AEOs) carried out by the Member States in the last 6 years;
 - (e) a risk-based sample of 10 summary declarations for temporary storage to trace them onwards to the release of goods for free circulation and verify compliance with the rules
-

concerning maximum deadline for discharging the goods, valuation, customs reliefs and flat rate taxation, carried out by a typical AEO of the courier sector in 2016 after the entry into force of the Union Customs Code's provisions on 1 May 2016; and

- (f) a risk-based sample of 10 items released for free circulation by this AEO in 2016 after the entry into force of the Union Customs Code's provisions on 1 May 2016 to trace them backwards to the summary declaration for temporary storage and verify compliance with the rules concerning maximum deadline for discharging the goods, valuation, customs reliefs and flat rate taxation.

2. During the audit field work we visited the customs authorities of Spain, Italy, Poland, Romania and the United Kingdom. In each selected Member State we discussed the replies received in advanced to the questionnaire and carried out interviews with the officials in charge of the different areas tackled by the questionnaire and, in particular, in charge of valuation, origin, tariff classification, risk management, AEOs, post-release controls, and Customs 2013/2020.

Based on international standards we checked whether: (i) Member States' post-release controls managed residual risks after release controls; (ii) Member States post-release controls covered imports carried out in other Member States; (iii) Member States' customs administrations performed duties as if they were one; and (iv) Member States' customs administrations paid due attention to courier shipments. We analysed and discussed the outcome of the preselected samples based on a checklist.

We paid special attention to the systems and controls including a test in the dummy environment of the customs release systems related to credibility checks on low value consignments.

REPLIES OF THE COMMISSION TO THE SPECIAL REPORT OF THE EUROPEAN COURT OF AUDITORS

"IMPORT PROCEDURES: SHORTCOMINGS IN THE LEGAL FRAMEWORK AND AN INEFFECTIVE IMPLEMENTATION IMPACT THE FINANCIAL INTERESTS OF THE EU"

EXECUTIVE SUMMARY

I. The Commission notes that essential findings included in this report concern Member States' control shortcomings and implementation tasks which are carried out under the full responsibility of national authorities. The Commission inspects however the collection and making available of traditional own resources by the Member States which has a corrective impact.

When the Commission finds that the Member States' controls are not effective and lead to losses of traditional own resources, the Member States are made liable for those losses, with very significant interest applied for belated payment. This means that the adverse effect on EU finances of ineffective controls by Member States is countered by the Commission's inspections. Interest for belated payment more than compensates for the delays in making available to the EU budget, so the Commission's inspections ensure comprehensive protection of the EU financial interest.

The Commission welcomes all suggestions to improve the control.

VI. Shortcomings in the customs legal framework are being addressed via the Union Customs Code (UCC) which took effect from 1 May 2016. Its full benefits will be obtained when all the electronic systems for its implementation are operational. The UCC has as a main objective that of better protecting the Union financial resources (own resources) by i) fraud-proofing European customs legislation (i.e. closing loopholes, eliminating inconsistent interpretation and application of rules and providing electronic access for customs authorities to relevant information), ii) ensuring more harmonised and standardised application of customs controls by the Member States, based upon a common risk management framework and an electronic system for its implementation, and iii) introducing a common system of guarantees. These measures are intended not only to better protect the EU's financial interests and the security and safety of EU citizens but also to prevent anti-competitive behaviour at the various EU entry and exit points.

VII. The Commission is of the view that Member States do have sufficient financial incentives to perform custom controls. Member States that apply the EU customs legislative framework diligently do not face financial liability for TOR that become irrecoverable for reasons beyond their control.

VIII. According to Article 46(1) of the Union Customs Code it is up to the customs authorities of the Member States to carry out any customs controls they deem necessary. Practices will therefore differ to some extent between Member States in this regard. Customs controls shall, however, be based primarily on risk analysis. In order to contribute to the uniform application of risk criteria and standards, an implementing act on EU common risk criteria for financial risks is being prepared. The necessary guidance to support a common understanding and implementation is now underway. A pilot implementation by Member States is envisaged in 2018.

XI.

(a) The Commission does not accept the recommendation.

The European Parliament requested the Commission to 'collect reliable data on the customs ... gap in the Member States'. The Commission already provides annual calculations of the gap in customs duty collection identified in its TOR inspections. The amounts at stake are claimed from the Member States and collected in favour of the EU budget.

The Commission's calculation, based on hard data, is the most reliable methodology to establish such gap and is used for operational purposes, namely for preparing its annual inspection programme of Member States.

The Commission is not aware of any other suitable methodology but would consider positively any suggestions for a feasible methodology that could complement the Commission's calculations.

See also replies to paragraphs 25 and 26.

(b) The Commission accepts the recommendation. The Commission is currently assessing options to improve the financing of national customs services in the next MFF. The Commission considers that the Customs operations of Member States and the related working costs are a function of multiple factors including the structural makeup of the Member State's customs administration, the resources available to the national customs service, and the pattern and volume of trade resulting from the geographic situation of the Member State. Currently the Commission is executing a Customs Union Impact Assessment study to investigate, inter alia, customs investment funding possibilities from the EU funding instruments.

(c) The Commission can partially accept the recommendation to the extent that it shares the objective of the ECA's recommendation, but notes at this stage that it is not in a position to make specific commitments in relation to its proposals for the next MFF.

(d) The Commission accepts the recommendation to be more precise in the actions asked of Member States in Mutual Assistance communications, noting that the main goal will remain having equivalent results. OLAF requests of mutual assistance are covered by Regulation 515/1997 and, consequently, legal and compulsory. The actions proposed to Member States are a set of recommendations which not necessarily fit for all Member States in every case.

(e) The Commission accepts the recommendation. While the indication of the consignor in the customs import declaration is already compulsory in Member States that did not make use of the option to waive the data requirement, the Commission will follow up with Member States in 2018 with a view to making this indication compulsory in all Member States. This may entail significant costs for those Member States that do not yet collect it. The actual date of adoption will depend on the negotiations with Member States.

INTRODUCTION

11. According to Article 46(1) of the Union Customs Code it is up to the customs authorities of the Member States to carry out any customs controls they deem necessary. Practices will therefore differ to some extent between Member States in this regard. Customs controls shall, however, be based primarily on risk analysis. In order to contribute to the uniform application of risk criteria and standards, an implementing act on EU common risk criteria for financial risks is being prepared. The necessary guidance to support a common understanding and implementation is now underway. A pilot implementation by Member States is envisaged in 2018.

13. The Common Risk Management framework (CRMF) was introduced in the EU customs legislation by Regulation 648/2005 and has included several actions to support Member States in addressing financial risks in a systematic way:

- Provision of Customs Audit Guide dealing comprehensively with the conduct of audits and post clearance (now: post-release) checks;
- Provision of the Handbook on operational customs controls addressing controls at the time of clearance and compiling best practices identified in the Member States including for financial risks related to tariff classification, valuation, origin and anti-dumping measures;

- Priority Control Actions dealing intensively with specific subjects to identify how Member States can best address the risk and customs control challenges in a systematic way.

14. Mutual administrative assistance intends to ensure revenue collection through preventing, investigating and combatting breaches of customs legislation.

15. At EU level: The electronic Customs Risk Management System (CRMS) to support real-time electronic exchange of risk information among Member States and between Commission and the Member States connects 841 customs offices including all international ports and airports, major land frontier posts and all national risk analysis centres with currently some 4000 users. Various Commission services have direct access to CRMS: TAXUD, OLAF, SANCO, TRADE, BUDG, JUST, ENV, AGRI, GROW.

Exchange of information at EU level is done on the basis of Regulation 515/97 and at international level on the basis of international agreements.

19. Indeed the legal bases are quite numerous. By way of example, 51 MAA provisions/protocols are in place relating to 79 countries/territories. Negotiations with others, e.g. Mercosur, are ongoing and some are pending entry into force (some EPA countries).

ACAs do not as such provide a separate legal basis for the exchange of information.

20. MAA provisions are a part of bilateral preferential arrangements (FTAs) but also autonomous preferential regimes like GSP require that beneficiary countries provide assistance which allows preventing fraud or irregularity with regard to granting tariff preference.

Effective anti-fraud measures – such as a clause allowing suspending a tariff preference in case of lack of assistance – aim to ensure a sufficient level of MAA from third countries benefiting from tariff preference at import to the EU.

OBSERVATIONS

25. The Commission already calculates a gap in the collection of TOR based on the shortcomings in customs duty collection identified as a result of DG BUDG's inspection activities.

The own resources legislation provides powerful incentives, in the form of very significant interest for belated payment for Member States to carry out controls.

The financing of the EU Customs programmes was agreed by Member States for the current MFF and is under review for the next.

26. The Commission already provides annual calculations of the gap in customs duty collection identified in its TOR inspections. The amounts at stake are claimed from the Member States and collected in favour of the EU budget. The VAT is a revenue source of a different nature, so the approach used for estimating the VAT gap is not applicable to the "customs gap".

The Commission's calculation, based on hard data, is the most reliable methodology to establish such a gap.

The Commission is not aware of any other suitable methodology but would consider positively any suggestions for a feasible methodology that could complement the Commission's calculations.

27. The potential losses calculated by OLAF for the United Kingdom are being followed up in an ongoing contradictory procedure with that Member State. The Commission cannot comment on such ongoing procedures. The Commission is looking at potential undervaluation in other Member States.

28. The Commission uses systematically its calculation of the gap, together with all other relevant risk indicators, to allocate resources for its inspections efficiently. Please see replies to paragraphs

25 and 26. The Commission is not aware of any other suitable methodology but would consider any suggestions for a feasible methodology which would complement the Commission's calculations.

30. The Commission carries out inspections in order to ensure a consistent application of EU customs legislation across the Member States and to ensure that the financial interests of the Union are protected. Member States that do not carry out controls and thereby cause losses of traditional own resources face the risk of liability for the losses, which provides an incentive for them to be diligent in order to avoid liability.

Debts owed by insolvent traders should be followed up diligently taking into account the remaining assets and the priority of Member State's customs authorities in case of liquidation. The UK customs authorities have no priority in the case of liquidation.

As part of the preparation for the next Multiannual Financial Framework, the Commission will consider whether amendments to the current own resources' legal framework can improve the incentives for effective controls by Member States.

31. The EU customs legislation in place does not give preference to post-release controls and the reduction of post-release demand notes may be explained by several factors, among them the carrying out by those Member States of controls other than at post release.

The Commission notes that in the countries mentioned by the ECA the number of import declarations examined post-release has shown an increase in 2016.

32. As pointed out before (see reply to paragraph 26) the Commission already produces a gap calculation. Moreover, an increase/decrease of the customs gap could be due to many factors. It would be difficult, if not impossible to identify cause/effect relationships with individual factors.

33. By December 2020, 80% of the UCC systems work will be delivered. Nevertheless, the electronic customs Multi-Annual Strategic Plan (MASP) revision 2017 under preparation has established the need for a date beyond the date of 31 December 2020 for the entry into operations of six UCC systems, due to human and financial resources constraints. This approach is currently under discussion with Member States and the Commission will consider appropriate legislative action.

38. The Commission is not aware of any Member State accepting that their share of TOR collection costs is too high. The current system of collection costs was unanimously adopted by Member States.

40. Technical assistance grants awarded under the Hercule Programmes enable national and regional administrations in the Member States to purchase equipment for use during operations in support of investigations into transgressions, such as irregularities, suspected fraud and corruption, perpetrated against the financial interests of the EU. These operations include, for example, activities to identify and detect OC-groups involved in smuggling of cigarettes and tobacco, but also drugs, Trafficking in Human Beings or weapons. It is not possible to restrict beforehand the use of this equipment to operations relating to the protection of the EU's financial interests.

41. The Commission is currently reflecting on possible initiatives to strengthen the exploitation of the available data sources.

44. Member States enrich the requests of MA communications with their own intelligence work. In some cases, there may be justification for non-uniformity in the actions as long as the results are equivalent.

The Commission's TOR inspections regularly examine Member States' follow-up of OLAF's MA communications. When failure by Member States to follow them up appropriately results in TOR losses, the Commission holds Member States financially responsible for the losses.

45. The Customs Information System (CIS) is available to all Member States Customs Authorities. Even if all Member States use the system for the purposes it has been conceived, its usage varies according to each Member State.

OLAF is currently working, in close cooperation with Member States, on a new version of the CIS to incorporate the changes brought by the amendment of Regulation 515/97 and address the requests for improvement from Member States.

46. CRMS supports real-time electronic exchange of risk information among Member States and between the Commission and Member States.

A full overview of the systems, their scope, objectives and time plan is provided in the Multi-Annual Strategic Plan version 2016 published on the Europa web site¹.

The systems serve their own objectives and purposes and have different legal bases. Member States identified the multiple reporting as a major problem. Synergies and links between systems are documented in the Business Process Models also available on the Europa web site².

47. In the meantime the project group which had been created to address the problem presented its report, which revealed the complexity of multiple reporting and that this problem cannot be solved with a 'simple' IT solution by transferring data between the two systems. The recommendations of the group are currently being addressed.

50. Member States are using risk management and have created risk profiles to select consignments that might be misclassified or declared with a wrong origin.

The Commission will shortly propose an implementing act on common risk criteria for financial risks in order to address those issues (see also reply to paragraph 11 above).

The Commission regularly examines Member States' procedures to avoid and combat such fraud mechanisms in its TOR inspections.

51. Regarding the issue of fraud based on mis-declaration of the origin of imported goods the Commission has conducted research in order to identify cost-effective support tools. The identified solution, based on Container Status Messages (CSM) data, has been prototyped and tested through the ConTraffic system. This technology allows for an automated cross-checking of the origin declared by importers against the container route and the flagging of mismatches.

Box 1

It should be noted that since 1 September 2016, a new application allowing the trace and track of containers is available by means of the AFIS platform. The application called AFIS-CSM, contains movements of containers entering and leaving the EU territory reported directly to a central repository by sea-carriers.

52. With regard to the analysis of origins in import declarations in 2008-2015 and the mentioned 1187 signals sent to Member States, the Commission would like to clarify that this analysis was done in the framework of an experimental pilot project run with the collaboration of 12 volunteering Member States and the signals produced identified cases of potential customs fraud. This information was provided to the Member States to better target their post-clearance controls.

¹ https://ec.europa.eu/taxation_customs/general-information-customs/electronic-customs_en

² https://ec.europa.eu/taxation_customs/business/union-customs-code/ucc-bpm_en

Common reply to paragraphs 54 and 55.

The legal obligation to exchange risk information via CRMS is mentioned in Article 46(5) UCC, which stipulates the type of information to be exchanged. In addition, the Commission produced guidelines available in all EU languages to support Member States' decision on relevant information to be put in a RIF and in particular new risk and targeting elements. The Commission has not received complaints in recent years, notes a considerable improvement in the quality of RIFs in the last five years and believes that the system of national contact points for CRMS, the extensive training being provided and guidelines will ensure the necessary quality. See also Commission reply to paragraph 46.

58. In the framework of the "Action plan for monitoring the functioning of preferential trade arrangements" (COM(2014)105 final), monitoring questionnaires were sent in 2016 and monitoring visits were carried out in 2017 in India and Indonesia. A questionnaire was sent to Vietnam in 2016, the follow-up of which clarified all identified issues. Nepal and India started the self-certification system with Registered Exporters (REX System) as from 1st January 2017. Specific training sessions were provided to these countries by the Commission (an additional session for India was held in September 2017). New appropriate monitoring actions may be decided once the REX System is fully implemented in these countries. Bangladesh is to be considered as being monitored on a regular basis through exchanges of letters and close contacts with the Commission. In order to reduce the high number of requests for verification of certificates for textiles, access and use of the Bangladeshi database GSP-tracker by EU national customs authorities is possible and is going to be promoted. Regarding Afghanistan, the Commission is not aware of the problems reported by a Member State to the ECA. Clarification will be sought from this Member State and appropriate action will be decided. In any event the REX System will be implemented in this country as from 2018. Specific training action has been proposed to the authorities of this country and took place in September 2017.

59. Cooperation from China in response to MAA requests should be further strengthened; too many requests from the Member States remain unanswered, or the answers are delayed or incomplete or documents provided by the General Administration of China Customs (GACC) are stamped with a disclaimer (see below). OLAF monitors the flow of information in the context of such MAA requests between EU and China.

The following actions were already undertaken: better prioritising of requests by the EU, reinstating Liaison Officer in Beijing, offering China a secured AFIS email connection to exchange information smoother. In spite of these initiatives, co-operation with China remains insufficient.

60. OLAF considers that the disclaimer is in breach of Article 17.3 of the EU-China Agreement on co-operation and mutual administrative assistance in customs matters:

[...] the Contracting Parties may, in their records of evidence, reports and testimonies and in administrative proceedings use as evidence information obtained and documents consulted in accordance with the provisions of this Agreement.

However, the Chinese authorities have a different interpretation of these provisions.

OLAF has repeatedly (two last meetings of the Anti-Fraud Working Groups, last meeting of the JCCC) raised this issue with China/GACC in the competent bilateral fora.

64. The final evaluation of the Customs 2013 programme was positive with regard to the programmes contribution to policy level objectives and in terms of helping customs authorities to work as one. The evaluation further noted that acting as one administration is a gradual process that cannot be completed overnight, but that the programme helps the customs administrations in achieving its objectives.

With the beginning of the Customs 2020 programme, the Commission has developed a methodology for performance measurement of the functioning of the Customs Union within the project called the Customs Union Performance (CUP). The main aim of the CUP is to show how customs activities and operations support achieving strategic objectives of the Customs Union³. A set of key performance indicators (KPIs) and data collection indicators (DCIs) have been established within the CUP per strategic objective (protection, customs controls, facilitation/competitiveness, co-operation plus basic parameters); they are described in detail in the CUP Guidance Notes⁴.

The CUP project is being developed as a joint action under the Customs 2020 Programme. Although the CUP aim is broad and linked to strategic objectives of the Customs Union, as referred above, some CUP indicators can also be used for measuring the achievement of the Programme's general and specific objectives. It needs to be noted, however, that several CUP indicators are marked as 'EU limited' and their use is therefore restricted.

65. In application of articles 55 and 56 of Commission implementing regulation (EU) 2015/2447 (and, previously, article 308d of the CCIP), Member States administrations send data extracted from the customs declarations for release into free circulation to the Surveillance 2 system. This transmission is closely monitored by the Commission and no noticeable weakness was noted.

69. According to the Performance Measurement Framework for Customs 2020, impact level indicators for the programme are collected at the time of the mid-term and final evaluations. The mid-term evaluation of the programme will publish its results, including impact indicators, in June 2018. On Hercule III: The mid-term evaluation will address the points raised by the ECA in a comprehensive manner, notably the achievement of the specific objective of the Hercule programme as measured by the Key Performance Indicators listed in Article 4 of Regulation 250/2014. The Commission will submit the report on the mid-term evaluation to the European Parliament and to the Council by the end of 2017. Information on outputs and short-term results is already available and reported upon in the Annual Overviews on the Implementation of the Hercule III programme.

74. The problem of not properly using TARIC data was strongly underlined during the TARIC monitoring mission and led to several recommendations addressed to the UK in the report of this monitoring action.

UK has taken note of these recommendations and informed the Commission about the development of a new release system.

75. As from 2013 data extracted from customs declarations with a value below 1000 Euro have been sent to the Surveillance 2 database by the UK.

76. The Commission has analysed the issues raised here by the ECA within the scope of the monitoring visits taken place between 2010 and 2014 and is, consequently, currently investigating this topic within the remit of a possible infringement procedure against the UK.

³ Strategy for the evolution of the Customs Union COM(2008) 169 of 1.4.2008; strategic objectives set out in 2008 were confirmed 'as still valid and appropriate' by the Council conclusions on the progress on the Strategy for the Evolution of the Customs Union (2013/C 80/05 of 19.3.2013).

⁴ Document TAXUD/A1/DB/D(2015) 394984 Rev 1 of 3 Feb 2016); please note that this document is being annually reviewed in January/February each year; the 2017 revision is under preparation and will include necessary amendments based on the implementation of the UCC.

(c) The absence of the said credibility checks is linked to the partial application of TARIC. Credibility checks are not applied fully by the UK (see also reply to paragraph 74).

77. The cases where TARIC is retroactively updated relate to legislation published in the EU Official Journal with retroactive application. These specific cases are directly communicated to the Member States' administrations in order for them to undertake the necessary financial action (reimbursement, recovery).

81. Under the UCC which applies since 1/5/2016 there is an overall obligation to use electronic means for data exchange and storage, including for simplified procedures. All systems are being developed and deployed according to the UCC work programme.

As regards licenses and similar documents, the Commission is since June 2017 working on a legal proposal for the "EU Customs Single Window program", encompassing the "EU Customs Single Window: Certificates exchange" interface.

This interface connects the national customs clearance systems with databases hosted centrally at the Commission that supports the electronic execution of business processes. It includes a functionality to allow automatic checks on the availability of certificates that should be provided to customs when goods are being presented. A future version of this interface that will be operational by the end of 2018 will expand this functionality, in particular to increase the number of certificates supported and to cater for quantity management and write-offs at EU level.

This interface is already available to all Member States on a voluntary basis since 2014 (currently seven Member States use it) and the Commission is confident that this number will expand in future alongside the increase in functionalities. Several Member States have expressed their interest and intention to join the project in the coming years.

84. The Commission has upgraded its EBTI & Surveillance systems in order to assist the Member States in their BTI usage control. As the national systems are not yet upgraded - under the UCC Member States have a transition period until 2020 to fulfil this obligation - this control is not yet possible by using the Surveillance system.

It can only be followed up by manual checks of the customs declarations.

The Commission will follow up the implementation of the new UCC provisions once there is sufficient data available.

For this type of misclassification see also reply to paragraph 50.

86. At the time of special report 23/2000, a legal basis for establishing a system of advance rulings in the field of valuation did not exist in the EU.

88. The Commission has undertaken a joint assessment with Member States customs administrations and the business community of the relevance, feasibility and implications – in terms of costs/benefits, etc. – of the introduction and application in the EU of the concept of Binding Valuation Information (BVI). The Commission expects to conclude this work and decide on any further course of action by early 2018.

89. The fact that Member States do not follow a uniform approach does not necessarily lead to underpayments of customs duties, but can potentially do so. The different approaches applied may have similar effects.

See reply to paragraph 11.

92. The threshold value can only be used as a risk indicator to target a consignment, however it is not a proof of the price paid (see also reply to paragraph 11).

95. The Commission has already carried out inspections on undervaluation, including missions to the UK in November 2016 and May 2017 and a mission to Slovakia in 2016, and it is currently following up the related reports. The Commission has also been requesting information from all Member States inspected in 2017 on their procedures to counter the undervaluation risks and intends to give high priority to this issue going forward.

96. The issue of undervaluation of textiles and footwear from China is currently being investigated further by the Commission.

97. The Commission inspected undervaluation in its UK TOR inspections of November 2016 and May 2017. It will continue to do so in its UK TOR inspection of November 2017. The Commission is also actively following up the OLAF report on undervaluation in the UK. The Commission will keep following up very closely undervaluation in the UK and will take all appropriate measures to protect the financial interests of the Union including, where appropriate, the legal action envisaged by the Treaties. See also reply to paragraph 96.

100. Customs procedure 42 is an important facilitation for legitimate businesses. However, for several years, the Commission, same as the Court of Auditors, have been signalling to Member States that the procedure can be abused by fraudsters; and recommendations have been formulated towards customs and tax administrations on control and exchange of information. Member States have the legal and operational tools to verify transactions from the customs and VAT risk point of view; however, such control requires good cooperation between customs and tax administrations at national level.

104. See Commission's reply to paragraphs 82 and 93 to 99 of the Special Report No 23/2016.

106. The Commission is generally satisfied with the level of cooperation provided by most Member States, regardless of the existence of punctual problems.

The Commission has been devoting particular attention to inspecting Member States' customs procedures to stop and combat mis-declaration of origin and/or misdescription of goods with special focus on the MA communications quoted by the ECA. It will continue to do so.

107. Currently, the indication of the consignor in the customs import declaration is a data element which may be waived by Member States. It is mandatory in Member States that did not make use of this option. The Commission will follow up with Member States in 2018, and depending on the outcome, may consider taking legal action to make the indication of the consignor compulsory in all Member States. It has to be borne in mind that collecting this information will imply significant costs for those Member States that do not yet collect it. The actual date of adoption will depend on the negotiations with Member States.

112. It has to be taken into account that this quote equally refers to risk management for security and safety purposes, and does not substantiate the usefulness of risk analysis for financial purposes prior to arrival of the goods in the EU territory.

113. The Commission will continue to prepare a Customs Union Performance report on annual basis. This report will also cover the area of customs controls.

The UCC maintained the possibility for using simplifications. A dedicated project group has elaborated guidance on the application of simplified procedures.

114. Risk analysis for fiscal purposes is not carried out on the basis of data generally available to the carriers lodging the entry summary declaration (ENS) at the pre-arrival stage but on the basis of the customs declaration data. However, the ENS data available can be used to flag a certain consignment upon its arrival in the EU. See also reply to paragraph 115.

115. The purpose of the ENS is primarily to carry out risk analysis on Safety and Security (Art. 128 UCC). Risk analysis for fiscal purposes is only possible where a customs declaration is lodged together with the ENS in accordance with Article 130 UCC. Traders that make use of this option normally benefit from an accelerated clearance of their goods upon arrival. Introducing an obligation for the ENS to include in all cases data on the consignor and consignee is not necessary because the ENS is not used for fiscal purposes (see reply to paragraph 114).

118. The Commission takes the view that documentary and physical checks, based on risk analysis, must also apply to goods that are declared through a simplified procedure.

Any persisting practice which would appear to be incompatible with applicable EU customs legislation will be examined by the Commission within the remit of a possible infringement procedure.

Please see reply to paragraph 106.

119. Authorisations to use simplified customs procedures for imports depend on prior checks by customs. They are given to traders who provide detailed information on their business practices.

122. The Commission is currently examining whether the notification of presentation in the framework of the entry in the declarants records procedure can be enhanced or not. However, the possibility to waive AEOs from this obligation under certain circumstances should be maintained in order to take account of the fact that those economic operators have to subject themselves to more stringent criteria.

Article 233 UCC IA furthermore mitigates possible abuse of EIDR by providing for a robust pre-audit of applicants, a close monitoring of the authorisation, and the regular supervision of the operations through a tailor-made control plan.

123. The AEO authorisation is subject to continuous monitoring. In case of non-fulfilment of the AEO criteria the Member States' customs authorities must either suspend the AEO authorisation or revoke it. Where the Commission has detailed knowledge that a Member State is failing to implement EU law, it may take appropriate legal action against that Member State.

The Commission is currently studying the impact of the risks of specific business models, including express couriers, during the AEO application and monitoring process.

124. The Commission is encouraging the Member States to use the Customs Audit Guide bearing in mind that these guidelines are not legally binding.

125. Several Member States have indeed either not reported post-release audits or reported data that required clarifications. The Commission regularly provides methodological clarifications to all Member States, insists on accurate and reliable reporting and invites them to provide missing information and/or clarify the information provided when necessary. The Commission's analysis is typically shared and discussed with Member States in the meetings of the Advisory Committee on (Traditional) Own Resources.

The Commission will continue to assess Member States' reports and impress on them the need to perform proper controls, including post-release audits. Moreover, in its traditional own resources inspections, the Commission recommends always to Member States that they follow the Commission's Customs Audit Guide, though neither the Guide nor post-release audits are mandatory.

127. This issue is already being followed up in several Member States, where the Commission requests increased efforts to broaden mutual assistance cooperation between the Member States affected.

128. The Surveillance 2 database is covering all the customs declarations for entry into free circulation as from 2011. An important extension of data elements to be collected is, indeed, included in the Surveillance 3 project that should be implemented by October 2018.

131. The Commission is of the view that post-release controls are much less effective tools to prevent and combat undervaluation than controls prior to release. It has systematically encouraged Member States to address undervaluation with controls prior to release.

132. The fact that administrative and business costs would outweigh revenue collected has been the rationale up to now for the exemption of duty relief for consignments of negligible value.

However, the Commission remains open to the possibility of exploring other relevant factors and assessing the effectiveness and efficiency of the legislation in force. This issue will be addressed in particular by a project group.

134. Some other exemptions from customs duties exist besides those referred to in the ECA report.

These reliefs and the impact of their application are currently under discussion in a project group.

135. As regards the acceptance of applications for relief of customs duties for goods of negligible value in respect of goods of a declared value higher than 150 euros, the Commission takes the view that Member States should adjust their national import systems so as to reject such applications.

Commercial consignments which are incorrectly declared as gifts may be subject to customs controls because customs authorities may decide to check whether the conditions for granting the import duty relief are met.

136. See reply to paragraph 123.

137. Undervaluation is one of the most significant issues. A project group will explore various possibilities to optimise customs formalities to address all relevant concerns.

138. The Commission is aware of the problem of under-valuation of goods. The problem is particularly acute in the context of e-commerce. A project group will provide an opportunity to explore how these issues are addressed in Member States and how the problem should be resolved.

139. The issue of the customs incomplete levying of import duty concerning dutiable postal shipments will be addressed in a project group.

140. A project group on low value consignments will address the issue of customs duty losses as referred to by the ECA.

The Commission also notes that commercial consignments which are incorrectly declared as gifts may be subject to customs controls because customs authorities may decide to check whether the conditions for granting the import duty relief are met.

141. The AEO status provides an opportunity to balance trade facilitation and customs controls.

See also reply to paragraph 123.

CONCLUSIONS AND RECOMMENDATIONS

142. The issues with the legal framework are being addressed via the Union Customs Code (UCC) package (the Code plus its Delegated and Implementing Acts) which took effect from 1 May 2016. Its full benefits will be obtained when all the electronic systems for its implementation are operational. The UCC has as a main objective that of better protecting the Union financial resources (own resources) by i) fraud-proofing European customs legislation (i.e. closing loopholes, eliminating inconsistent interpretation and application of rules and providing electronic access for

customs authorities to relevant information), ii) ensuring more harmonised and standardised application of customs controls by the Member States, based upon a common risk management framework and an electronic system for its implementation, and iii) introducing a common system of guarantees. These measures are intended not only to better protect the EU's financial interest and the security and safety of EU citizens but also to prevent anti-competitive behaviour at the various EU entry and exit points. Furthermore, this legal package is constantly being updated to tackle errors and inconsistencies that arise, in particular if these are causing non-harmonised application of the rules.

143. See reply to paragraphs 25 and 26.

Recommendation 1

The Commission does not accept the recommendation.

The European Parliament requested the Commission to 'collect reliable data on the customs ... gap in the Member States'. The Commission already provides annual calculations of the gap in customs duty collection identified in its TOR inspections. The amounts at stake are claimed from the Member States and collected in favour of the EU budget.

The Commission's calculation, based on hard data, is the most reliable methodology to establish such gap and is used for operational purposes, namely for preparing its annual inspection programme of Member States.

The Commission is not aware of any other suitable methodology but would consider positively any suggestions for a feasible methodology that could complement the Commission's calculations.

See also replies to paragraphs 25 and 26.

144. The Commission maintains that Member States that do not carry out controls run considerable risks of facing financial liability, including of interest for belated payment, for losses to the EU budget. The Commission holds that the possibility that Member States may be held financially liable for administrative errors or failure to recover debts is a strong encouragement for them to carry out controls and be diligent in order to avoid liability. Failure by Member States to recover amounts due and to make them available to the EU budget would not comply with the own resources regulations and the European Court of Justice's relevant case law.

As part of the preparation for the next Multiannual Financial Framework, the Commission will consider whether amendments to the current own resources' legal framework can improve the incentives for effective controls by Member States.

145. The Commission is not aware of any Member State accepting that their share of TOR collection costs is too high, the current system of retention costs was unanimously adopted by Member States.

Recommendation 2

The Commission accepts the recommendation. The Commission is currently assessing options to improve the financing of national customs services in the next MFF. The Commission considers that the Customs operations of Member States and the related working costs are a function of multiple factors including the structural makeup of the Member State's customs administration, the resources available to the national customs service, and the pattern and volume of trade resulting from the geographic situation of the Member State. Currently the Commission is executing a Customs Union Impact Assessment study to investigate, inter alia, customs investment funding possibilities from the EU funding instruments.

Recommendation 3

The Commission can partially accept the recommendation to the extent that it shares the objective of the ECA's recommendation, but notes at this stage that it is not in a position to make specific commitments in relation to its proposals for the next MFF.

146. The Commission has improved its ways of working in the development of new/updated customs applications by involving the Member States from the early stages of development. The issue of the multiple reporting of customs information, already referred to in paragraphs 47 and 54, has been largely discussed with Member States in order to make the exchange of customs information at EU level more cost-effective. In addition, in current IT projects the Commission pays particular attention to their connectivity with other AFIS and external IT systems, to minimise the Member States' efforts and optimise the data quality, usage and purpose of these systems.

A strong effort is also put in providing efficient tools for the analytical and statistical usage of the data stored.

Recommendation 4

(a) The Commission accepts the recommendation. While the indication of the consignor in the customs import declaration is already compulsory in Member States that did not make use of the option to waive the data requirement, the Commission will follow up with Member States in 2018 and depending on the outcome may consider taking legal actions to make this indication compulsory in all Member States. This may entail significant costs for those Member States that do not yet collect it.

(b) The Commission accepts the recommendation to be more precise in the actions asked of Member States in Mutual Assistance communications, noting that the main goal will remain having equivalent results. OLAF requests of mutual assistance are covered by Regulation 515/1997 and, consequently, legal and compulsory. The actions proposed to Member States are a set of recommendations which not necessarily fit for all Member States in every case.

Recommendation 5

The Commission accepts the recommendation subject to available resources, investigative priorities and the willingness of the third country to cooperate. At present OLAF has liaison officers in China, the United Arab Emirates and Ukraine.

147. The cases where TARIC is retroactively updated relate to legislation published in the EU Official Journal with retroactive application. These specific cases are directly communicated to the Member States administrations in order for them to undertake the necessary financial action (reimbursement, recovery).

The Commission will assist Member States in the monitoring of BTI usage. The upgraded versions of EBTI & Surveillance systems facilitate this monitoring since October 2017. With the use of several predefined reports missing or invalid usage can be detected. The quantities imported under extended use will be tracked as well in a regular report.

However, Member States need to adjust their national systems as well and need to send the new data elements via Surveillance in order to carry out meaningful control. Under the UCC Member States have a transition period until 2020 to fulfil this obligation.

See also reply to paragraph 88.

Recommendation 6

(a) The Commission accepts the recommendation. It has upgraded its EBTI and Surveillance systems in order to assist the Member States in their BTI usage control. As the national systems are

not yet upgraded - under the UCC Member States have a transition period until 2020 to fulfil this obligation - this control is not yet possible by using the surveillance system.

It can only be followed up by manual checks of the customs declarations.

The Commission will follow up the implementation of the new UCC provisions once there is sufficient data available.

(b) The Commission does not accept the recommendation at this stage.

The Commission is currently conducting a study, involving Member State experts and business representatives, in particular through a public consultation, in order to assess the interest and feasibility in the Union of a system of decisions relating to Binding Valuation Information (BVI).

148. The Commission is very actively addressing the undervaluation, mis-declaration of origin and mis-description of goods in its TOR inspections, with special emphasis for the UK. It is also following up the OLAF undervaluation report concerning the UK. It will continue to do so with high priority.

Recommendation 7

The Commission does not accept this recommendation, as the current legislation already includes very strong incentives for Member States to address adequately risks of losses for the EU budget, in the form of high interest for belated payment.

The Commission will, however, examine all possible improvements of the system of the incentives in the next Multiannual Financial Framework.

149. Currently, the risk management system does not require mandatory checks in every case. The Commission is examining possible ways to improve risk management.

See replies to paragraph 114 and to paragraph 123.

Recommendation 8

(a) The Commission does not accept the recommendation but it is prepared to examine the issue raised by the ECA in the context of an ongoing examination of how to strengthen the control approach in the case of simplified procedures. As far as performance of financial risk analysis at pre-arrival stage is concerned, the Commission refers to its replies to paragraphs 114 and 115.

(b) The Commission accepts the recommendation; in fact the proposed improvement has already been defined in the framework of the development of the Surveillance 3 system to be implemented by October 2018.

(c) The Commission accepts the recommendation concerning the investigation of the abuse of the low-value consignment reliefs on e-commerce trade of goods with non-EU countries. This is one of the areas of undervaluation fraud being investigated by OLAF.

The Commission has set up a project group-comprised of Member States and trade representatives that will, inter alia, analyse the challenges customs face to ensure correct implementation of legal requirements-in this area.

Event	Date
Adoption of Audit Planning Memorandum (APM) / Start of audit	31.5.2016
Official sending of draft report to Commission (or other auditee)	13.7.2017
Adoption of the final report after the adversarial procedure	7.11.2017
Commission's (or other auditee's) official replies received in all languages	23.11.2017

Goods entering the EU from outside the European Union are subject to customs controls by Member States before they are released for free circulation within the EU. We examined whether the European Commission and the Member States ensure that import procedures protect the EU's financial interests. We found important weaknesses and loopholes which indicate that the controls are not applied effectively. This has an adverse effect on EU finances. We make a number of recommendations to the Commission and to the Member States to improve the design and implementation of the controls.

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