

WTS Customs Newsletter

Editorial

Dear Reader,

It is our pleasure to present you with the latest edition of the WTS Global Customs newsletter.

We are all experiencing the weakening of the global economy, with increasing prices and rather pessimistic forecasts for almost everywhere in the world. For this reason, customs topics become increasingly important as (savings) opportunities in global trade should be higher on companies' agendas. At the same time, compliance with the rules must not lose its traction.

That said, our colleagues from across the global network have given examples of exactly these opportunities.

In **Brazil**, the government has approved a law intended to strengthen the economy, in particular the manufacturing industry, by extending the application of the drawback customs regime. This regime allows for the suspension of various levies for imported goods that are used for the manufacturing of products that will be re-exported again. With the new law, certain services can be included in the regime that will lower the costs for companies and hopefully strengthen the economy.

In **China**, customs have issued a notice relaxing the rules concerning voluntary disclosure for companies that have breached the law. While our colleagues point out the – of course – positive aspects of this development, they also point out that this is a temporary situation. Affected companies should take note of this particular aspect.

Paolo Dragone of WTS R&A **Italy** also writes about a situation where a company infringed the law by underpaying duties following the misclassification of the imported good. The positive aspect of the Italian Supreme Court's decision is that the fine to be paid was limited. Hopefully, this decision will have a positive effect on similar cases in Italy in the future.

In the **UK**, the new Customs Declaration Service (CDS) was planned to be mandatorily used from 1 October 2022. Arjen Odems gives an overview of some of CDS's key features, explains why the mandatory applicability was postponed, and, above all, states that CDS is much better than the old CHIEF system.

As you may know, in the **US**, the First Sale For Export (FSFE), which was abolished in the EU some years ago, still applies. Now the Court of Appeals for the Federal Circuit has ruled that the FSFE applies for the non-market economy (NME), which strengthens the FSFE principle again.

Finally, in **Germany**, the Federal Fiscal Court in September 2022 published its judgment in the famous *Hamamatsu* case and has given some very interesting statements in the field of customs valuation. It will be interesting to see how this judgment will influence the world of customs for intra company transactions where a margin-based transfer price is used.

As you can see, we have yet again compiled court decisions, legal and technical developments for you, and we trust that they are interesting for you.

Enjoy reading our newsletter.

Yours sincerely,

Kay Masorsky

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Brazil



Benefits of the drawback regime extended to some services

On 5 September 2022, the Brazilian government approved Law 14440/2022, which, by amending Law 11945/2009, authorises the inclusion of certain services in the suspension drawback regime as from 1 January 2023.

The drawback customs regime aims to boost the export of Brazilian manufactured products by exempting the acquisition of inputs or refunding customs duties, which thus reduces the manufacturing costs. As a rule, the legal system provides for three types of drawbacks: suspension, exemption, and refund.

The suspension drawback allows the suspension of the payment of Import Duty (II), Exercise Tax (IPI), Social Contribution on Revenues (PIS and COFINS), Social Contribution on imports of goods and services (PIS-Import and COFINS-Import), whether or not combined with the acquisition, in the domestic market, of goods to be used or consumed in the manufacturing of the product to be exported. A State VAT (ICMS) exemption also applies, but only to imports.

As for the exemption drawback, it allows the exemption from the II and the reduction of IPI, PIS, COFINS, PIS/PASEP-Import and COFINS-Import on imports to zero, whether or not combined with the local acquisition of goods equivalent to those used or consumed in the manufacturing of the exported product.

Finally, in the refund drawback, the total or partial refund of the taxes paid on the import of inputs used in the manufacturing of goods exported, or used in the manufacturing, complementation or packaging of another product that is exported is allowed. Due to the broader scope of the benefits granted by the other two modalities, the drawback refund is generally not used anymore.

As can be seen, the three main drawback modalities seek to relieve the acquisition costs of goods to be used or consumed in the manufacturing of products that are to be exported. No reference is made to services required for completing the exports.

With the changes brought by Law 11440/2022, as from 1 January 2023, it will be possible to acquire services, in the domestic market and upon import, directly and exclusively linked to the export of products resulting from the use of the drawback regime, with the suspension of the PIS, COFINS, PIS-Import and COFINS-Import.

The suspension of PIS/COFINS and of PIS/COFINS-Import will apply, among other things, to: (i) intermediation in the distribution of goods abroad; (ii) cargo insurance; (iii) customs clearance; (iv) storage of goods; (v) road, rail, air, waterway, or multimodal cargo transportation; (vi) cargo and container handling; (vii) freight forwarding services. Furthermore, the Executive Branch may provide for its application to other services associated with exported products.

This measure will reduce the tax burden on export-related services, which account for 35.7% of the value added to Brazilian exports of manufactured goods, according to the Organization for Economic Cooperation and Development (OECD). Thus, it is expected to further reduce the export costs of Brazilian manufactured products and so boost the economic recovery following the Covid-19 pandemic.

To make the new law operational, the Federal Government will issue an ordinance regulating the criteria for granting, using, monitoring, and inspecting the drawback suspension regime for services, and will provide for adjustments on the drawback systems.

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China



China's customs relaxes voluntary disclosure rules

China's customs has relaxed the rules for the voluntary disclosure of breaches in customs matters through a recently released circular, GAC Notice [2022] No.54 (Notice 54). This relaxation is valid for a limited period of time from 1 July 2022 to 31 December 2023.

Voluntary disclosure refers to the self-initiated disclosure of breaches by importers/exporters, and is intended for China's customs to make lenient treatments, especially for exempting or reducing administrative penalties. In principle, voluntary disclosure does not apply to cases already known to the customs prior to the voluntary disclosure.

China's customs first explained voluntary disclosure in principle in 2016, and then in more detail in 2019 via a rule GAC Notice [2019] No. 161 (Notice 161) on the conditions for a waiver of administrative penalties. The latest changes made by circular Notice 54 are highlighted below.

	Relaxations to the voluntary disclosure rules	
	2019 (Notice 161)	2022 (Notice 54)
No-penalty conditions	Disclosure must be made within 3 months from the offence/breach.	Disclosure must be made within 6 months from the offence/breach.
	Tax underpayment is under: <ul style="list-style-type: none"> > 10% of the total tax liability; or > CNY 500,000. 	Tax underpayment is under: <ul style="list-style-type: none"> > 30% of the total tax liability; or > CNY 1 million.
	No such provision.	Interest charges can also be waived or reduced if punishment is exempted.
Disclosure location	To one of the customs that is: <ul style="list-style-type: none"> > Collecting the taxes concerned; or > At the location of the company. 	To one of the customs responsible for: <ul style="list-style-type: none"> > Customs declaration; > Port of import/export; or > Customs registration of the taxpayer(s).
Blacklisting (discrediting) in the customs system	No blacklisting if a case is: <ul style="list-style-type: none"> > Only subject to a warning; or > Fined under CNY 500,000. 	No blacklisting if a case is: <ul style="list-style-type: none"> > Only subject to a warning; or > Fined under CNY 1 million.
	No such provision.	Companies with "senior AEO status" will not be suspended during the customs inspection period in the case of a voluntary disclosure.
Exclusion	No such provision.	Repeated offence/breach for the same issue cannot be accepted as voluntary disclosure.

As shown above, these relaxed conditions offer more benefits/lenient treatment to taxpayers. More filing locations also help facilitate the reporting. However, the short period of validity (of eighteen months) also implies that the concession is temporary. Companies should consider their need for an internal audit and voluntary disclosure before 31 December 2023.

Italy



Penalties for customs violations must be proportionate: the Italian Supreme Court takes a clear position against the more than proportional increase in penalties for customs law violations

With its ruling of 11 May 2022 (n.14908), the Italian Supreme Court stated the principle that penalties must be proportional to the Customs Law violation committed; otherwise, the courts can re-determine such penalties.

The case submitted to the Italian Supreme Court concerned the Customs Agency's correction of a customs classification for an imported product, which resulted in the application of a higher duty rate; on the basis of the penalty range provided for by Article 303 of the Italian Customs Code, the Customs Agency imposed a fine of 33,000 Euro on the importer, which was a substantial increase from the initial 9,000 Euro duty.

Considering that this increase infringed the European principle of proportionality enshrined in Article 42 of EU Regulation n.952 of 2013 (Customs Code of the Union, so-called CDU), the Regional Tax Court then decided in favour of the importer, re-determining the penalty to an extent equal to the duty evaded (of 9,000 Euro).

The Customs Agency, considering the Regional Tax Commission's decision to be against the law, appealed it to the Italian Supreme Court.

However, the Supreme Court confirmed that, to ensure the individual Member States comply with European principles, the European Court of Justice has repeatedly stated that it is up to the national courts to assess whether, taking into account the imperatives of repression and prevention, the penalties actually imposed appear disproportionate to the gravity of the infringement. If this were the case, then the national courts may disapply any national provision conflicting with directly applicable European regulations.

The Italian Supreme Court endorsed the restatement of the penalty applied by the Regional Tax Court. It correctly noted how the penalty range system outlined by Article 303 of the Italian Customs Code, given the rigidity of the minimums provided, does not allow the penalty to be contained by adjusting it to the actual value of the violation and to any collaborative effort made by the importer since, even if Article 303 provides for the possibility of grading the penalty, this cannot fall below 30,000 Euro for the sole fact that the customs duty not paid was equal to or greater than 4,000 Euro.

The Italian Supreme Court has confirmed an important principle that operators can assert when seeking to obtain reductions in the penalties decided by the Customs Agency, when the particular circumstances show the disproportionate nature of such penalties regarding the violation committed and the operator's collaborative behaviour.

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United Kingdom UK developments on CDS



The Customs Declaration Service (CDS) has now officially replaced CHIEF as the customs declaration system for imports into the UK.

Although CDS has replaced CHIEF from 30 September 2022, and HMRC announced on multiple occasions that 30 September 2022 was a hard deadline, many companies were not ready for CDS by this deadline.

Technical challenges

In light of the high number of companies that were not ready for CDS, HMRC has allowed an extension of CHIEF's use for companies that have requested such an extension. Extensions until 31 October 2022 have automatically been accepted, and additional evidence and arguments need to be provided for extensions that go beyond 31 October 2022.

Although HMRC appears to be scrutinising extensions that go beyond 31 October 2022, only time will tell when HMRC will finally 'switch off' CHIEF for imports into the UK.

A number of technical challenges have contributed to the situation in which some companies have not been ready for CDS, including software solution providers experiencing 'teething' problems with both the new communication protocol and CDS data requirements as well as operators that have not sufficiently and in time familiarised themselves with the changes that CDS has introduced.

For traders that rely on their forwarders and/or customs clearing agents for customs declarations in the UK, it is extremely important that they ensure that their forwarders and/or customs clearing agents have implemented CDS and are able to lodge customs declarations for imports into the UK using CDS.

New codes

In addition to these technical challenges, it should be noted that CDS has also introduced a large number of new codes and data elements that need to be included in the import declarations.

For example, CHIEF provided the option of applying an overwrite code that effectively avoided that individual references and licences had to be included. However, under CDS this is no longer possible and any relevant document references need to be included at the product item level. Additionally, the codes and references themselves have changed and operators need to familiarise themselves with the new codes and references.

Additional information documentation

Another aspect to consider is that traders need to provide additional information and documentation to complete customs declarations in CDS. This might require traders to update their invoices, provide additional documentation and/or provide further details regarding the products that they import into the UK.

CDS encourages compliance

Despite the challenges that CDS is providing at the moment, it is a significant improvement compared to CHIEF. The additional codes and references as well as the additional data elements provide for an opportunity to provide HMRC with clarity relating to the products that are being imported and their compliance with customs and other related import or entry requirements.

CDS has also introduced additional fields allowing the various parties that are involved with the trade, export, import and lodging of the customs declarations all to be identified individually. This provides much better insights for the parties involved. Overall, CDS allows for an opportunity to better reflect the particulars concerning the import of products and the parties involved. Companies that have invested in a (customs) compliant import process should be able to benefit and should be scrutinised less during customs audits, whilst it should also be easier for HMRC to detect non-compliant imports.

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United States**Applicability of the First Sale Rule for Non-market Economies**

On August 11, 2022, the U.S. Court of Appeals for the Federal Circuit ("CAFC") issued its decision on *Meyer Corporation v. U.S.*¹ This case addresses the use of the first sale price for affiliated entities, specifically within a non-market economy ("NME") and the court ultimately holds that first sale prices may apply in NME's.

This decision rejects potential limitations of the first sale rule proposed by the Court of International Trade's ("CIT") original 2021 decision of the same matter.² The lower court's decision relied on the *Nissho Iwai American Corp. v. U.S.*³ holding and required Meyer to prove four elements to rely on the first sale price for transaction value. The CIT required: (1) a bona fide sale, (2) goods that are clearly destined for the U.S., (3) an arm's length transaction between the related parties, and (4) the transaction to be absent any distortive non-market influences.

On appeal, the CAFC held that the lower court misinterpreted *Nissho Iwai* and improperly imposed requirements beyond those relevant for an arm's length transaction.⁴ The CAFC stated that considering the effects of a NME on transaction value is baseless.⁵ In reaching this decision, the CAFC reemphasized the statutory language only requires determining an arm's length transaction⁶ and explains the focus of the analysis is limited to the relationship between buyer and seller and not governmental intervention in an NME.

The U.S. is one of the few jurisdictions that still allows the use of a first sale price for customs valuation in multi-tiered transactions. While transaction value is typically the price actually paid for the merchandise when sold for exportation to the U.S.,⁷ the first sale rule addresses which purchase price in a multi-tiered transaction is an acceptable basis of appraisal. This price is key to meeting the transaction value requirements

1 *Meyer Corporation v. United States*, Case No. 21-1932 (Fed. Cir. Aug. 11, 2022)

2 *Meyer Corporation v. United States*, No. 13-00154, 2021 WL 777788 (Ct. Int'l Trade Mar. 1, 2021)

3 *Nissho Iwai American Corp. v. United States*, 982 F.2d 505 (Fed.Cir. 1992)

4 19 U.S.C. § 1401a(b)

5 *Meyer Corporation v. United States*, Case No. 21-1932 (Fed. Cir. Aug. 11, 2022) at 11

6 19 U.S.C. § 1401a(b)(2)(B)

7 Codified in 19 U.S.C. § 1401a(b)

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and supporting duty mitigation strategies. In *Nissho Iwai*, the CAFC stated that the use of the first sale rule would only be applicable in a related party setting with proof of the first three elements above, with no mention or consideration of NME influence.⁸

Pending the outcome of the CAFC's *Meyer* decision, U.S. importers were left questioning whether the continued use of the first sale rule for imports from NME's, such as China and Vietnam, would be viable or subject to burdensome due diligence. Fortunately, the appellate court's decision largely maintains the status quo and provides some certainty to existing first sale programs relying on the *Nissho Iwai* standard. Given this positive result, we expect a renewed interest in development and expansion of first sale programs. If you have any questions about the applicability of the first sale rule and related benefits, please reach out to any of the authors for more information.

Germany



Appeal in "Hamamatsu" case rejected by German Federal Fiscal Court

In its Judgment of 17 May 2022 (published on 29 September 2022), in Case VII R 2/19 "Hamamatsu", the German Federal Fiscal Court (Bundesfinanzhof, BFH) rejected the appeal filed on points of law (*Revision*) relating to an application for refund of customs duties; at the same time the Court made a number of fundamental determinations which could have a substantial impact on the future assessment under customs valuation law of transactions between affiliated group companies.

The case concerned the German subsidiary of a Japanese parent company; when declaring the customs value of imported goods, the German entity used the sales price for the definition of the transaction value. It was agreed between the group companies and with the German tax authorities (without the involvement of the customs administration) within the framework of an advance pricing agreement (APA) that the intra-group transfer price would be established on the basis of the "residual profit split method". Accordingly, at the end of each financial year, balancing payments were made which were either credited to or debited from the German company. The dispute was based on a situation in which the German subsidiary retroactively received flat-rate price reductions. These led to an application for the refunding of customs duties due to a retroactive reduction in the declared import customs values.

The refund was ultimately refused by the Fiscal Court (Finanzgericht) based on the ECJ Judgment of 20 December 2017 in Case C-529/16, which has attracted a great deal of attention in the customs world.

The Claimant filed an appeal on points of law (*Revision*) against the decision of the Fiscal Court, which has now also been rejected.

In this context, the following fundamental determinations by the German Federal Fiscal Court are highly noteworthy:

- › The **transaction value method**, i.e. determination of customs value based on invoice amount, **is precluded** in such cases in which the value of the imported goods cannot be determined at the time of importation, since such value consists of the invoice

amount and a flat-rate adjustment, which cannot be determined at the time of importation. This position is based on the aforementioned ECJ Judgment and is thus not new, but in our view is no less noteworthy as a result.

- › The so-called **fall-back method for determining customs value** is in this instance **precluded** for the same reasons:
"It follows from this that the verdict of the ECJ, in accordance with which the Customs Code does not permit an agreed transaction value to be used as a basis for calculating the customs value where such transaction value consists partly of an amount initially invoiced and reported and partially of a flat-rate adjustment following the end of the accounting period, without it being possible to tell whether, at the end of the accounting period, such adjustment will take place up or down, is in any event ultimately also definitive with regard to determining the customs value under the fall-back method pursuant to Article 31 of the Customs Code." (Judgment, para 49).
- › According to the German Federal Fiscal Court, **retrospective price adjustments are irrelevant as regards determination of customs value**:
"In any event, within the framework of all customs value determination methods, such a transfer pricing adjustment which, as an instrument for income tax purposes, serves the prevention of disputes and the reduction of transfer pricing risks (see Liebchen in Mössner et al., Steuerrecht international tätiger Unternehmen, 5th ed., marginal ref. 13.50; cf. also Drüen in Wassermeyer MA Art. 25 MK, marginal ref. 110), has no impact on the definitive customs value – due to the demonstrated goods-related and record-date-based nature of customs value determination." (Judgment, para. 59).
- › The above determination relates not only to retrospective downward adjustments but, according to the German Federal Fiscal Court, expressly **also to upward adjustments**. As a result, retrospective price increases which would also entail an increase in customs value would also have to be disregarded.

It must be stressed that, of course, judgments by the German Federal Fiscal Court – unlike those of the European Court of Justice (ECJ) – do not have a direct effect as regards the entire European Union. Nevertheless, it will be very interesting to observe the future impact of these determinations, which relate to EU-wide customs valuation law (and, in terms of basic principles, indeed customs valuation law virtually around the world).

The Court took the general point of view that any retroactive price adjustments, i.e. even if effected outside implementation of an APA based on application of a transfer pricing mechanism with balancing payments, have "no influence on the definitive customs value"; this is due to the unclear effects in terms of amount and impact at the time of importation. This statement made by the Court could be potentially explosive since, consequently, this would also preclude retrospective levying of customs duties.

In the present case, at the time of importation the customs administration was not aware that price adjustments would retrospectively be applied. It remains to be seen whether this means that the assessment would be different if a prior arrangement were to be made with the customs administration. Since, however, also in the event of a prior arrangement to the effect that retroactive balancing will be undertaken, the lack

of clarity in terms of the amount of the balancing payment, and whether adjustment would be upwards or downwards, would remain, any differing assessment in such an instance must be considered unlikely.

The German Federal Fiscal Code and the European Court of Justice moreover criticised the fact that the Claimant and Appellant did not undertake a precise allocation of the balancing payment across the respective imported goods. In this regard too, we very much doubt that the assessment would be different if a more precise apportionment, for instance through an invoice correction, were possible, since it would remain the case that this would not be clear at the relevant time of importation.

It consequently remains to be seen how the German customs administration and those of the other EU Member States respond to this Judgment. We would advise companies in a comparable situation to appeal against any notices from the customs administration concerning retrospective levying of customs duties based on retroactive price adjustments. We would recommend those who have in the past regularly and proactively submitted corrective reports for the retroactive adjustment of customs values based on transfer pricing adjustments to get in touch with the customs administration and proactively clarify the impact of the Judgment. If the administration insists on a correction notification and then issues retrospective demands for payment of customs duty, again an appeal should be filed in order to prevent the notice taking legal effect until the matter has been definitively clarified.

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Events

Upcoming webinars

Global developments and trends in customs and foreign trade law

Thursday, 10 November 2022, 14:00 – 15:00 CET

[Register here](#)

Speakers

- › Kay Masorsky, Partner and Head of Global Serviceline Customs, WTS Germany
- › Arjen Odems, Managing Director, Customs and Trade Consultancy Ltd., UK
- › Alexandra Klein, Senior Manager Customs, WTS Germany
- › Dr. Gregor Sobotta, Partner and Managing Director, Customs Operations, WTS Germany

Global developments and trends in export controls

Thursday, 17 November 2022, 16:00 – 17:00 CET

[Register here](#)

Speakers

- › Kay Masorsky, Partner and Head of Global Serviceline Customs, WTS Germany
- › Jim Huish, Managing Director Export Controls, Sanctions & Trade, FTI Consulting, UK
- › Stephen Wilcox, Managing Director Export Controls, Sanctions & Trade, FTI Consulting, USA
- › Markus Wieners, Senior Manager Customs, WTS Germany

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About WTS Global

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