Customs valuation

Interpretation of the definition of the EU last sale for export

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Preface

In March 2015 we started with the Executive Master Customs and Supply Chain Compliance. 27 students with a variety of backgrounds were ready to share and get knowledge. After modules related to supply chain, logistics, customs and IT, the time to write our master thesis came.

In my master thesis I examine the interpretation of the last sale rule. The last sale rule is used for determining the customs value in the EU. In the EU there is a lot of discussion which transaction value has to be taken for determining the customs value in a chain of transactions. In Canada the last sale rule has been used for many years, so the comparison is interesting.

To compare the Canadian interpretation with the EU interpretation, I have interviewed Mr Bédard. I would like to thank Mr Bédard again for his cooperation. I would also like to thank prof. mr. dr. de Wit and dr. Hulstijn for their supervision. Next to that I want to thank my colleagues mr. ing. Boersma and mr. Van Lent for their review and input.

Finally, I want to thank my family and friends for their support during my studies.

I hope you will enjoy reading my thesis.

Samantha Speelman

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Executive summary

Since May 1st, 2017 the first sale rule has been abolished in the European Union. The first sale rule has been replaced by the last sale rule. Companies and customs authorities do experience legal uncertainty when applying the last sale rule. The definition of last sale for export is not clear, especially in a chain of transactions.

In Canada the last sale rule has been applied for several years now. The Canadian customs authorities do have experience with applying this rule, therefore a comparison with the Canadian interpretation of the last sale rule is useful. The central question in this research is: *Against the background of the objective of the abolition of the first sale rule, is the interpretation of the last sale rule in the EU effective? And how does this interpretation compare to the Canadian version of the rule?*

In order to narrow down the research, the following sub-questions are discussed:
- Why did the EU change from first sale to last sale rule and what are the main characteristics of the current interpretation of the EU last sale for export rule?
- What are the main characteristics of the Canadian last sale rule?
- In which way do these characteristics of the EU and Canadian last sale rule differ?
- Are there any issues in the EU interpretation and can these issues be solved or prevented by another interpretation, e.g. by using the Canadian interpretation?

This research has a purpose to build and evaluate a more efficient interpretation of the definition for the last sale for export in the EU by taking into account the interpretation of the last sale for export definition in Canada. To interpret and study the Canadian customs law, an observational case study is performed by conducting an interview with a customs officer, Mr Jean-Francois Bédard, specialized in customs valuation in Canada. After this first phase, two other interpretations of the definition of the last sale rule have been prepared. All of the interpretations have been compared with scenarios.

The results of the research shows that the current EU interpretation causes uncertainty, especially in case of domestic sales (sales between two EU parties) or when invoices of previous transactions are not available. The Canadian interpretation seems to be more predictable in some of the cases. Two new interpretations have been compared to the current EU and Canadian interpretation. The first interpretation, combining the EU and Canadian interpretations, shows that predictability increases, but additional provisions, policy papers and other documents are necessary to solve all of the issues.

The alternative interpretation, which includes also domestic sales, is most predictable of all interpretations. The issue of not having the right invoice is not applicable, as the sale between the importer and the its supplier is the sale that should be used when determining the customs value.

Concluded, the EU interpretation is not effective in terms of predictability and impact on customs value. The Canadian version of the last sale rule is more predictable and seems more effective. This is partly caused by a high amount of policy papers and memoranda. A combination of both interpretations would result in a higher predictability. By using one of the alternative interpretations, the legal certainty of companies and customs authorities can be increased. Also companies do know how to restructure their supply chain when legal certainty is higher.

A recommendation is to investigate both alternative interpretations, especially regarding real impact on customs values and European trade. The time to adjust the legislation should also be taken into account. Policy papers and guidance documents can be released much faster than adjusting legislation. Case law may be faster than adjusting the legislation.

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1. Introduction

Globalisation allows countries to benefit from sources around the world without high barriers. One way to accomplish globalisation is by trade agreements. Negotiations in the last years between the European Union (EU) and Canada have resulted in the Comprehensive Economic and Trade Agreement (CETA). The agreement has been signed on October 30th, 2016. The expectation is that trade barriers should be diminished or at least lowered by the CETA. The EU and Canada are both members of the World Trade Organization (WTO).

The WTO also takes responsibility to minimize trade barriers. Therefore, several agreements have been agreed upon, like the Valuation Agreement. To minimize the differences between the members of the WTO, the WTO members each agreed to implement the rules in the Valuation Agreement in their local legislation.

Customs valuation is relevant for trade, because of the fact that the customs value is needed to import goods into countries. Valuation in a more broad sense is also relevant for taxation principles. Change in valuation rules and interpretation of these changes therefore is relevant for valuation for customs purposes, but also for taxation purposes. Trying to harmonise the valuation rules therefore has its impact.

1.1. Earthquake in EU customs environment

Also the EU follows the rules in the Valuation Agreement. One of the rules, the transaction value method for determining the customs valuation, needed clarification. Therefore, in April 2007 the Technical Committee on Customs Valuation of the WCO adopted Commentary 22.1 in which the Committee gave clarification on the meaning of article 1 of the WTO Valuation Agreement. This Commentary has led to a change in the interpretation of the transaction value from the first sale rule to the last sale rule, which is adopted in the "new" EU legislation.

May 1st, 2016 is a memorable day for a lot of people in the customs field in the European Union. The "new" EU customs legislation, the Union Customs Code (UCC), is applicable from that day. Several changes in the customs field have been adopted in the UCC. One of the main changes is the abolishment of the first sale for export rule. An earthquake for the EU customs environment? No, only a little shock, because there is a lot of fog still in the air. Companies are not certain which transaction value they have to take for determining the customs value.

The change from the first sale rule to the last sale rule is not a big shock. As mentioned before, in April 2007 the Technical Committee on Customs Valuation of the WCO adopted Commentary 22.1 in which the Committee gave clarification on the meaning of article 1 of the WTO Valuation Agreement. Desiderio and Desiderio (2010) and Ruessmann and Willems (2009) explained the consequences of Commentary 22.1. Ruessmann and Willems (2009) state: "Experience has shown that the WTO Valuation Agreement leaves room for interpretation. While the Commentary serves as a valuable guide towards achieving uniformity in the Agreement's interpretation and application, its reasoning in the case of the first sale rule, as the analysis above illustrates, is rather inadequate."

Although Ruessmann and Willems state that the reasoning is rather inadequate and the first sale rule should not be abolished, the EU has adopted the interpretation and has changed its legislation into the "last sale for export" rule.

1.2. Customs valuation in Canada

Canada and the EU have signed the CETA. This means both parties do want to lower trade barriers. By using the same valuation rules, trade barriers will be lowered too. Therefore, both countries adopted the Customs Valuation rules of the WTO. In contrast to the EU, Canada has abolished the first sale for export rule for a while now.

As Ruessmann and Willems (2009) comment in a footnote: "When the Canadian customs authorities lost in Harbour Sales (Windsor) Ltd v. D/MNR [1994] 4647 ETC., they succeeded in getting the valuation law changed to require a transactional value based on a sale to a purchaser in Canada."

The first sale for export rule is not being used in Canada anymore. Therefore, it is useful to compare the last sale for export rule in the EU with the last sale for export rule in Canada. The Canadian customs valuation is the case in this research.

1.3. Research

The research question that will be addressed in this thesis is:

Against the background of the objective of the abolition of the first sale rule, is the interpretation of the last sale rule in the EU effective? And how does this interpretation compare to the Canadian version of the rule?

Investigating this topic may lead to a higher effective interpretation of the last sale rule in the EU. This research aims to build an interpretation and evaluate that interpretation of the last sale rule in the EU. In this research the Canadian interpretation of the last sale rule will be taken into account.

Mr Jean-Francois Bédard of Canada Border Services Agency has been interviewed to gain knowledge regarding the Canadian interpretation of the last sale rule. The results from the interview have led to an adjusted interpretation. This interpretation is compared with the Canadian interpretation and the current EU interpretation.

1.4. Summary conclusions and recommendations

The effectiveness of the current EU interpretation is quite low. Customs authorities and companies do experience legal uncertainty. Especially in case of a situation that an earlier sale should be used, the availability of the previous invoice causes issues. Also the definition of a domestic sale (according to the guidance document a sale between two EU parties) causes issues. The Canadian version of the last sale rule is more predictable and seems more effective. This is partly caused by a high amount of policy papers and memoranda.

The predictability of the alternative interpretation including the domestic sales is the highest, but the impact on the customs value is also the highest. In most cases the relevant invoice will be available, so the issue of not possessing the relevant invoice will be solved immediately.

The combined interpretation provides higher predictability than the current EU interpretation and would be best of all interpretations in terms of impact on the customs value. By using this interpretation policy documents should be added or legislation should be changed to solve the issue of companies that do not have the invoice of an earlier sale than the sale between the party and its supplier.

A recommendation is to investigate both options, especially regarding true impact on customs values and on the European trade. The time to adjust the legislation should also be taken into account. Policy papers and guidance documents can be released much faster than adjusting legislation. Another recommendation would be, even when the European Commission does not want to adjust the interpretation, to explain the current interpretation in more detail.

2. Problem definition

Before May 1st, 2016 the first sale for export rule was applicable in the EU. This meant that an earlier sale in a chain of transactions could be used for determining the customs value. From May 1st 2016, the last sale for export rule is applicable. Companies and customs authorities in the EU are, however, not certain which transaction value they have to take for determining the customs value.

The European Commission realized there were some issues regarding determining the customs value under the UCC. Only few days before May 1st 2016, the European Commission (2016) has drafted a guidance document to give some clarification on the UCC and the implementing acts dated April 28th, 2016. This document has no legal status and still leaves room for interpretation. Companies and customs authorities still have questions with regard to the transaction that should be used in chains of transactions for determining the customs value. This results in a lack of legal certainty.

Without legal certainty, companies cannot act upon the legislation and structure their supply chain to make it as efficient as possible, keeping in mind the customs valuation rules. Therefore, this is a real strategic and operational problem for companies. Also customs authorities do not know how and when to act.

Customs valuation is relevant for trade, for the collection of customs duties and has also its impact on the taxation rules, especially transfer pricing. Subtle differences in legal rules and interpretations can have influence on strategic and operational decisions. The goal to harmonise customs valuation rules has impact in several ways.

2.1. Research objectives

Companies and customs authorities are not certain – in a chain of transactions – which transaction should be used for determining the customs value. This research aims to build and evaluate a more efficient interpretation of the definition for the last sale for export in the EU.

The research will lead to an interpretation of the last sale for export definition in the EU by taking into account the interpretation of the last sale for export definition in Canada. This interpretation can be used for further research or for litigation.

2.2. Research design

Qualitative research is the basis for this thesis. To compare the EU and Canadian situation, case study research has been performed. Since Canada has implemented the last sale rule for many years, it is useful to use Canada as a case. The interpretation of the last sale for export definition in Canada will be used for building an interpretation of the EU definition for the last sale for export. Because of the fact that the last sale rule has been implemented in May 2016, there is not yet quantitative information available to research.

By comparing scenarios with the current interpretation in the EU, the Canadian interpretation and the “new” interpretation, the effectiveness of the new interpretation can be evaluated. The effectiveness has been assessed in terms of predictability, the transaction value that should be used and the impact on the customs value compared to the first sale transaction value.

2.3. Structure of thesis

In chapter 3 the literature and current legal frameworks of the WTO / WCO, the EU and Canada will be examined. This literature will be the basis for the research itself. Chapter 4 includes a presentation of the research methods that have been used. In chapter 5 the current, Canadian and “new” interpretations are described and evaluated.

The implications for research and the contributions for practice are set out in chapter 6 and 7. In chapter 8 the conclusions and recommendations following from the research are embedded.

3. Literature review

The first sale for export rule has been abolished by the EU. Before and after the announcement of the changes in the legislation, several authors have written about the abolishment. This chapter reviews the articles written. In this chapter also the legal framework at WTO level, in the EU and in Canada are described.

3.1. Articles

The change from the first to the last sale rule has been discussed in several articles in the past. Ruessmann and Willems (2009) have elaborated on the impact of Commentary 22.1 of the WCO and the impact of the abolishment of the first sale for export rule in the EU and US. Desiderio and Desiderio (2010) also discuss the interpretation of the transaction value method regarding the Commentary. Truel and Maganaris (2015) described the changes caused by the Union Customs Code.

Ruessmann and Willems (2009) discuss the first sale rule in the EU and the US. They elaborate on Commentary 22.1 of the WCO regarding the WTO Valuation Agreement. Ruessmann and Willems state that the Commentary increases the chances of abolishing the first sale rule in the EU and the US. The impact of the abolition of the first sale rule in the EU and/or the US would be:

- At the micro level: increase the dutiable value of imports and restructure trade lanes.
- At the macro level: other countries will be less likely to implement the first sale rule in the future.

Desiderio and Desiderio (2010) considers the position of the EU taken regarding the first sale for export. Desiderio and Desiderio discuss the impact of that position and the impact of the first sale rule. The first sale rule in the US and the EU is being discussed in the article. The authors state: “To reduce such complexity [different valuation methods], the World Customs Organization (WCO) recently tried to harmonise the interpretation of some of the customs valuation rules, namely those of which relate to multi-tiered transactions.” The WCO has adopted Commentary 22.1. The authors state that the WCO Technical Committee was wrong. They state that “the customs authorities bear no greater burden in the first sale scenario than they would if ‘last sale’ rule were applied.” The authors end with the hope that the US and EU will continue the first sale rule.

In Truel and Maganaris (2015) the changes caused by the Union Customs Code have been described. The impact on the customs authorities and companies is being discussed. The change from first sale for export to last sale for export is introduced. Truel and Maganaris (2015) state that the impact on companies is that “companies using the first sale rule will see their taxable basis and therefore their amount of duties and taxes increase”. Trade organisations, especially multinational companies, were dissatisfied with this change. As Truel and Maganaris (2015) declare: “it has been argued that this decision could result in fairer trading environment for SMEs”.

3.2. Legal framework WTO / WCO

The members of the WTO have agreed upon the Valuation Agreement. All of the members have committed to implement the valuation rules. The interpretation of these rules can differ. Therefore, the WCO has drafted Commentary 22.1 regarding the interpretation of the transaction value method.

3.3. Legal framework EU

Despite the impact of the abolishment of the first sale for export rule, the EU has implemented the last sale for export rule. The EU customs law consists of several regulations. The Union Customs Code (UCC) applies from May 1st, 2016. The UCC Delegated Act (UCC DA) is a supplement for non-essential elements of the UCC. The UCC Implementing Act (UCC IA) aims to ensure equal conditions for implementation and uniform application of procedures of the UCC.

The transaction value method has been described in article 70 UCC. This article has been elaborated in article 128 UCC IA. Several member states have requested clarification of the new valuation rules under the UCC. The European Commission (2016) has drafted a guidance document. This document has no legal status.

3.4. Legal framework Canada

In Canada the Customs Act (R.S.C. 1985, c. 1 (2nd Supp.)) is applicable. The Customs Act describes – amongst other subjects – the transaction value method. The Ministry of Justice (1986) clarifies some of the concepts in the Customs Act in the Valuation for Duty Regulations. The Canada Border Services Agency (CBSA) has drafted several memoranda to clarify the “goods sold for export to Canada”, “purchaser in Canada” and the “transaction value method of valuation”.

The memoranda are only policy documents. These documents do not have a legal status, but do reflect the interpretation of the last sale of the CBSA.

4. Research methods

This chapter describes the research questions and the research methods. Also the scenarios for evaluating the different interpretations are elaborated in 4.4.

4.1. Research question

Companies and customs authorities struggle with the interpretation of the last sale for export rule. This research focusses on the following question:

Against the background of the objective of the abolition of the first sale rule, is the interpretation of the last sale rule in the EU effective? And how does this interpretation compare to the Canadian version of the rule?

The effectiveness is analysed in terms of predictability, the transaction value that should be used and the difference between this value and the first sale transaction value.

The predictability is relevant in this case, since companies and authorities do need legal certainty to anticipate in certain situations. Legal certainty is one of the key elements of law. Predictability is one way to measure the legal certainty of an interpretation. The transaction value that should be used and the impact of the interpretations are relevant to display the financial impact for companies and customs. It also shows the extent of abolition of the last sale rule.

4.2. Sub-questions

In order to narrow down the research scope, the following sub-questions will be discussed:

- Why did the EU change from first sale to last sale rule and what are the main characteristics of the current interpretation of the EU last sale for export rule?
- What are the main characteristics of the Canadian last sale rule?
- In which way do these characteristics of the EU and Canadian last sale rule differ?
- Are there any issues in the EU interpretation and can these issues be solved or prevented by another interpretation, e.g. by using the Canadian interpretation?

4.3. Methods

To diagnose the problem, the literature and regulations are reviewed. To interpret and study the Canadian customs law, an observational case study is performed by conducting an interview with a customs officer, Mr Jean-Francois Bédard, specialized in customs valuation in Canada (see appendix A).

After this first phase, an interpretation of the definition of the last sale for export has been prepared. To evaluate this interpretation, descriptive methods have been used: informed argument and scenarios. By comparing these scenarios with the current interpretation, the Canadian interpretation and the “new” interpretation, the most effective interpretation has been suggested.

4.4. Scenarios

The scenarios used for evaluating the different interpretations are based on cases in practice and cases in the guidance document of the European Commission (2016). The scenarios are as follows.

Scenario 1

Company A, located in China, sells goods for EUR 1.000 to company B, located in Brazil. Company B sells goods for EUR 1.100 to company C, located in the US. Company C sells the goods for EUR 1.200 to company D in the EU. All of the aforementioned transactions take place before the goods have been brought into the customs territory of the EU. The goods are shipped directly from China to the EU.

The flow of goods can be displayed as:

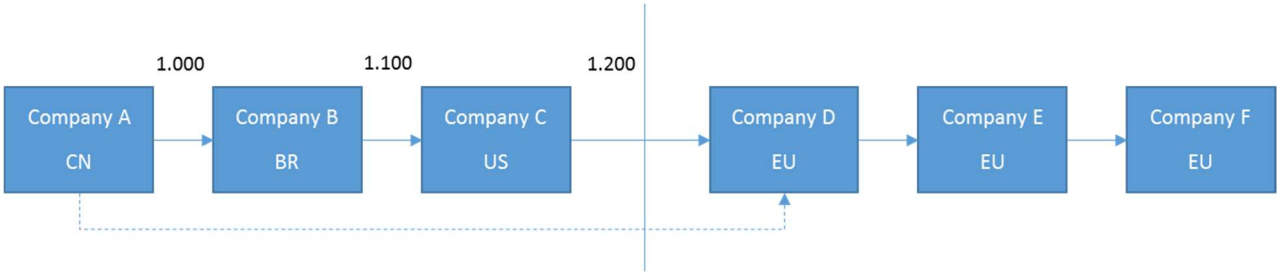

Figure 1: Scenario 1 - general

Scenario 2

Company A, located in China, sells goods for EUR 1.000 to company B, located in Brazil. Company B sells goods for EUR 1.100 to company C, located in the EU. Company C sells the goods for EUR 1.200 to company D in the EU. All of the aforementioned transactions take place before the goods have been brought into the customs territory of the EU. The goods are shipped directly from China to the EU.

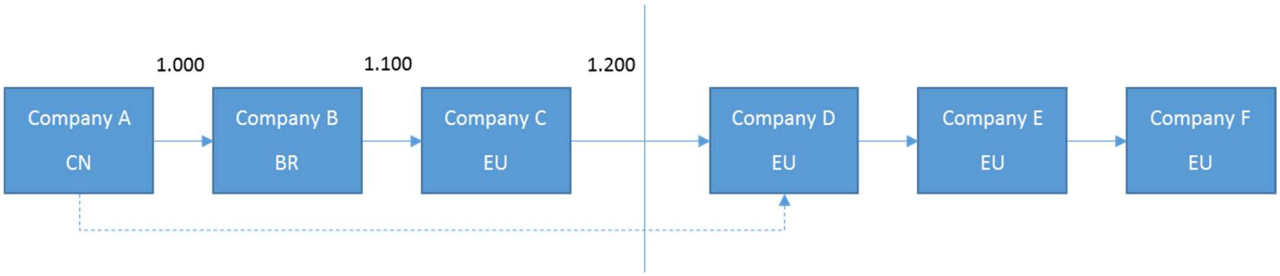

Figure 2: Scenario 2 - general

Scenario 3

Company A, located in the US, sells goods for EUR 1.000 to company B, located in the EU. Company B sells goods for EUR 1.100 to company C, located in the EU. Company C sells the goods for EUR 1.200 to company D, located in Switzerland. All of the aforementioned transactions take place before the goods have been brought into the customs territory of the EU. The goods are shipped directly from the US to the EU. Some companies located in Switzerland do import goods into the EU, without having a subsidiary in the EU.

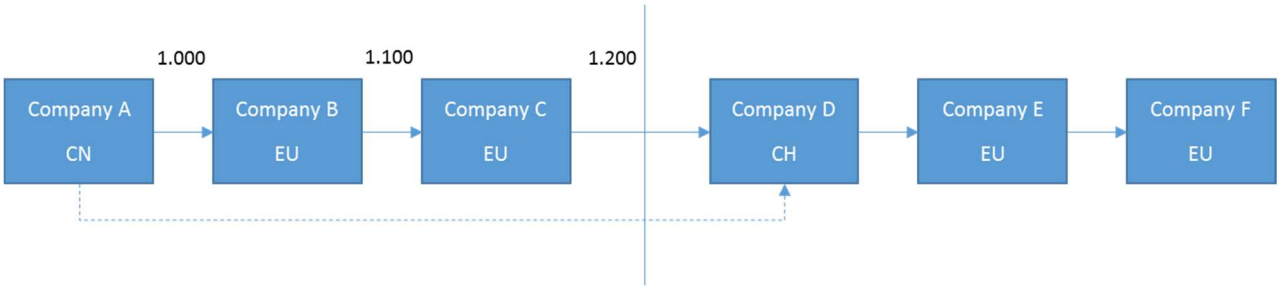

Figure 3: Scenario 3 - general

Scenario 4

Company A, located in the China, sells goods for EUR 1.000 to company B, located in the US. Company B sells goods for EUR 1.100 to company C, located in Switzerland. Company C brings the goods into the EU customs territory and places the goods in a warehouse of company C. All of the aforementioned transactions take place before the goods have been brought into the customs territory of the EU. The goods are shipped directly from China to the EU.

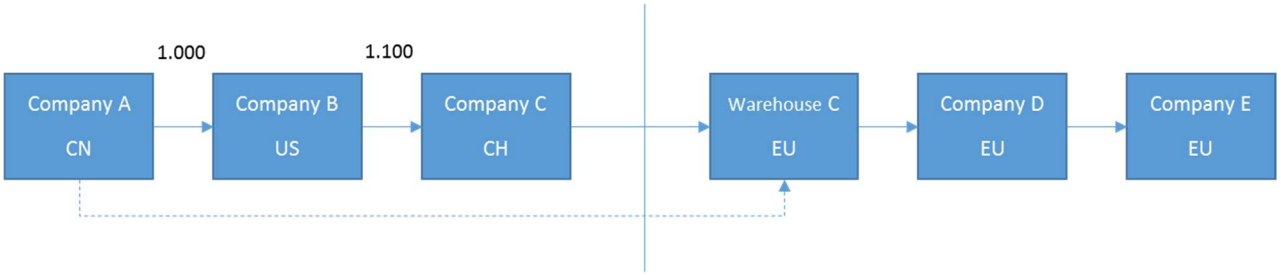

Figure 4: Scenario 4 - general

For comparing the scenarios with the Canadian interpretation, the location of the companies in the EU has to be replaced by Canada.

The outcome of the scenarios (which transaction value is the relevant value) will be discussed in chapter 5.

5. Effectiveness of the interpretation of last sale for export

The first sale for export rule is abolished in the EU with the application of the UCC. In this chapter the background of the objective of the abolition of the first sale rule is discussed. Also the effectiveness of the current interpretation of the last sale rule in the EU is examined in 5.1. In 5.2 the EU interpretation and in 5.3 the Canadian interpretation will be discussed. The differences between the Canadian interpretation and EU interpretation are being elaborated on in 5.4. Also another interpretation will be compared with both interpretations in 5.5. A conclusion follows in 5.6.

5.1. Background abolition first sale rule

In previous years the abolishment of the first sale for export rule has been subject of discussion many times. First we do have to take a step back. The old legislation of the European Union clarifies the background of the abolition of the first sale rule. Also the WTO valuation agreement and the Commentary of the WCO on the valuation rules do contribute to understanding the abolition of the first sale rule.

CCC / MCC

The Community Customs Code (CCC), Regulation (EEC) No 2913/92, was applicable from January 1st, 1994. The implementing provisions of the CCC (IPCC), Regulation (EEC) No 2454/93, were also applicable from January 1st, 1991. After several years the European Commission started to write new legislation to modernize the customs legislation. This attempt was called the Modernised Customs Code (MCC), Regulation (EC) No 450/2008. The MCC was adopted in 2008, but never became applicable.

In the implementing provisions of the Modernized Customs Code the transaction value related to the last sale was the only value allowed to be used for determining the customs value. The first sale was abolished in the implementing acts of the MCC. These implementing acts never became applicable however, like the MCC itself. In the MCC the interpretation of the WCO was adopted.

WTO valuation agreement / Commentary WCO

The WCO valuation agreement is applicable from January 1st, 1995. In article 1, paragraph 1, the following has been determined:

> "The customs value of imported goods shall be the transaction value, that is the price actually paid or payable for the goods when sold for export to the country of importation adjusted in accordance with the provisions of Article 8, provided: […]"

The meaning of "the price paid or payable for the goods when sold for export" was not completely clear, especially not in a chain of transaction. On April 27th, 2007 the WCO adopted Commentary 22.1 regarding the meaning of the expression "sold for export to the country of importation" in a chain of transactions.

According to the WCO Technical Committee in Commentary 22.1, in a chain of transactions the price paid or payable for the goods when sold for export is the price paid "in the last sale prior to the introduction of the goods into the country of importation". The last sale rule is applicable according to the WCO.

As Desiderio and Desiderio (2010) state: “Experience has shown that the WTO Valuation Agreement leaves room for interpretation. While the Commentary serves as a valuable guide towards achieving uniformity in the Agreement’s interpretation and application, its reasoning in the case of the first sale rule, as the analysis above illustrates, is rather inadequate.” They believe the WCO Technical Committee has interpreted the valuation agreement insufficient.

Although some authors do not agree with the WCO Technical Committee, the EU has taken into account this interpretation. In preamble 26 of the IA UCC, the European Commission has stated:

> “In order to ensure uniform and harmonised application of the provisions on customs valuation, in compliance with international rules, procedural rules should be adopted specifying how the transaction value is determined. For the same reasons, procedural rules need to be adopted specifying how the secondary methods of customs valuation are to be applied and how the customs value is determined in specific cases and under specific circumstances.”

Especially the sentence “in compliance with international rules” is worth mentioning. The European Commission mentions in this sentence the international rules of valuation and refers – assumed at least – to the Commentary of the WCO.

The first sale for export rule has been used in an extensive way. Many early transactions in a chain of sales have been used for determining the customs value. To narrow the definition down and to clear the definition of the sale for export, the European Commission has abolished the first sale for export rule.

5.2. EU interpretation last sale rule

The last sale for export has been introduced in the EU from May 1st, 2016. The current legal framework will be discussed first. Then the scenarios mentioned in paragraph 4.4 will be compared with the legislation and interpretation by the European Commission.

EU legal framework

As mentioned before, the transaction value method for determining the customs valuation is described in the UCC and the UCC IA. Article 70 UCC states:

1. The primary basis for the customs value of goods shall be the transaction value, that is the price actually paid or payable for the goods when sold for export to the customs territory of the Union, adjusted, where necessary.
2. The price actually paid or payable shall be the total payment made or to be made by the buyer to the seller or by the buyer to a third party for the benefit of the seller for the imported goods and include all payments made or to be made as a condition of sale of the imported goods.
3. The transaction value shall apply provided that all of the following conditions are fulfilled:
   a) there are no restrictions as to the disposal or use of the goods by the buyer, other than any of the following:
      i. restrictions imposed or required by a law or by the public authorities in the Union;
      ii. limitations of the geographical area in which the goods may be resold;
      iii. restrictions which do not substantially affect the customs value of the goods;
   b) the sale or price is not subject to some condition or consideration for which a value cannot be determined with respect to the goods being valued;
   c) no part of the proceeds of any subsequent resale, disposal or use of the goods by the buyer will accrue directly or indirectly to the seller, unless an appropriate adjustment can be made;
   d) the buyer and seller are not related or the relationship did not influence the price.

Paragraph 1 fixes the transaction value as the price actually paid or payable for the goods when sold for export to the customs territory of the Union. This definition does not abolish the first sale for export rule immediately. The first sale for export rule is abolished explicitly by article 128 UCC IA.

Article 128 UCC IA gives some clarity on the last sale rule:

1. The transaction value of the goods sold for export to the customs territory of the Union shall be determined at the time of acceptance of the customs declaration on the basis of the sale occurring immediately before the goods were brought into that customs territory.
2. Where the goods are sold for export to the customs territory of the Union not before they were brought into that customs territory but while in temporary storage or while placed under a special procedure other than internal transit, end-use or outward processing, the transaction value will be determined on the basis of that sale.

Several member states have requested clarification of the new valuation rules under the UCC, since the new legislation caused many questions and did not simplify the legislation. The European Commission (2016) has drafted a guidance document. This document has no legal status. The European Commission states in the document that domestic sales "do not qualify as sale for export to the EU". Domestic sales are defined as a sale between parties in the EU. The residence of a party is suddenly important for determining the transaction that should be used for determining the customs value.

On page 5 of the guidance document the European Commission (2016) tries to clarify the last sale rule, but in practice there is even after publishing the guidance documents still uncertainty. It stipulates that "the relevant moment is when goods are brought into the customs territory of the Union" and "the relevant sale for goods brought into the Union is the sale when crossing the border, i.e., the ultimate sale taking place, in performance of the contract at sale, at that time". This should clarify the rule, but as mentioned before, the sales between to EU parties does not qualify, even though this sale could be the ultimate sale taking place. In the guidance documents several practical examples have been described to illustrate the relevant sale for export.

The European Commission is currently integrating the guidance document in the Customs Valuation Compendium of the Customs Code Committee. The Customs Valuation Compendium only reflects the view of the Customs Code Committee and has no legal status.

In the Netherlands the interpretation of the last sale rule has been described in the Handboek Douane (a national guide of Dutch Customs to explain and clarify procedures). In section 9.00.00 the transaction value method, especially the sale for export, is elaborated on. Some of the examples in the guidance document of the European Commission (2016) have been included in this section. In this section Dutch Customs has stipulated that in case the invoice of the sale for export is not available for the importer, another valuation method should be used. The implications of this statement will be discussed together with the scenarios.

Interpretation and scenarios

The legal framework can be compared with the scenarios mentioned before. These scenarios are common cases in international trade. In concluding which transactions have to be taken, first the latest transaction will be discussed before bringing the goods into the territory of the EU. In case this sale qualifies as sale for export to the EU, the other transactions will not be discussed as the last sale for export is applicable for determining the transaction value for the customs value.

As aforementioned, there are still several discussions regarding the interpretation of the legal framework in certain situations. When interpreting the legal framework and taking into account the guidance document, the following conclusions can be drawn.

Scenario 1

This scenario is the most "simple" scenario. As company C, located in the US sells the goods for EUR 1.200 to company D in the EU, this transaction qualifies as the last sale for export to the EU. The transaction value of EUR 1.200 forms the base for the customs value.

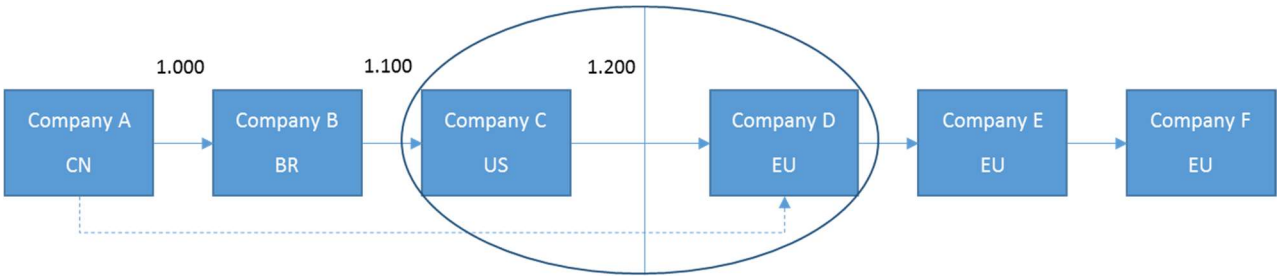

Figure 5: Scenario 1 - EU

Scenario 2

In scenario 2 the sale between the two EU parties, company C and company D, cannot qualify as sale for export to the EU, as mentioned by the European Commission. Therefore the sale between company B, located in Brazil, and company C, located in the EU, is the sale for export. The transaction value is EUR 1.100. The interpretation is clear, because of the guidance document of the European Commission (2016), but there is still some unclarity regarding the "domestic sale". Practice shows that the invoice of the sale between B and C is not always available, especially when the sales occur between nonrelated parties. According to Dutch Customs this means that another valuation method should be used.

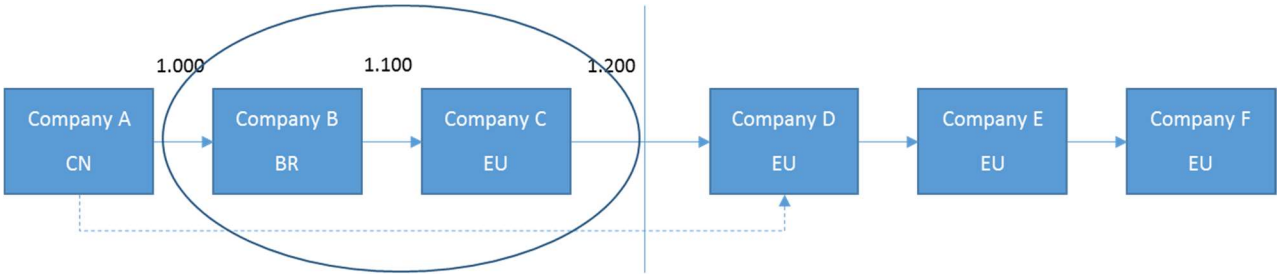

Figure 6: Scenario 2 - EU

Scenario 3

The transaction between company B and C cannot qualify as sale for export to the EU, as this sale is a sale between to EU parties. The sale between company A and company B and the sale between company C and company D can qualify as sale for export. The last sale should be used, so the sale between company C and D, for EUR 1.200, is the transaction for determining the customs value.

The predictability in this scenario is low, because of the fact that the location of the parties is suddenly relevant in this scenario. Just like in scenario 3 it is likely that the invoice of the sale between B and C is not available for company D. In some cases, for example when related parties are involved in the chain of transactions, the invoice may be available. It is however possible that another valuation method should be used according to Dutch Customs.

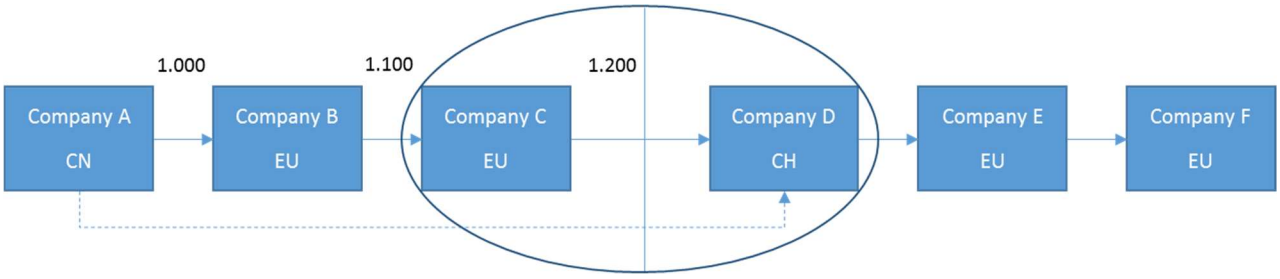

Figure 7: Scenario 3 - EU

Scenario 4

The transaction between warehouse C and company C cannot be qualified as sale for export to the EU. There is no sale, the transaction is a movement of stock. The transaction between company B and C is a sale for export to the EU. The goods have been shipped from China to the EU, so the transaction between company B and C of EUR 1.100 is the sale for export to the EU. The guidance document is clear in this scenario, so the predictability is high.

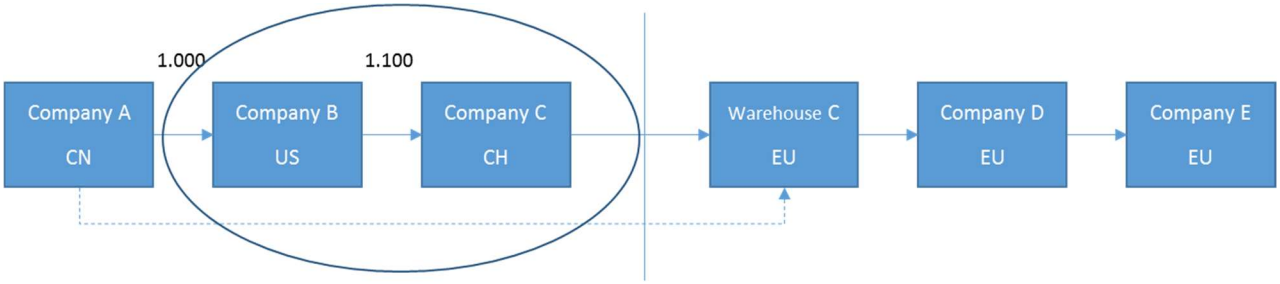

Figure 8: Scenario 4 - EU

Summary EU interpretation

Before May 1st, 2016 the first or an earlier sale could be used for determining the customs value (in the scenarios the transaction value of EUR 1.000). The current interpretation is being compared for Customs and companies with the first sale rule. The following conclusions have to be drawn for each scenario:

	EU interpretation				
Scenario	***Predictability***		***Value used***		***Impact customs value***
1	++	€	1.200,00	€	200,00
2	+	€	1.100,00	€	100,00
3	--	€	1.200,00	€	200,00
4	++	€	1.100,00	€	100,00

Table 1: Summary EU interpretation

For scenario 2 and 3 the issue exists that the invoice of the sale for export that should be used for determining the customs value is not available. The importer does not always have the invoices of earlier sales. Companies do not want to share their invoices with supply chain partners for competitive advantages.

In practice Dutch Customs already maintains this position. Dutch Customs demands companies to use another valuation method when only an invoice of a later sale, between two EU parties, is available. The statement of Dutch Customs is not based on the UCC or the UCC IA. Therefore, the question arises whether or not this statement will be tenable in court.

5.3. Canadian interpretation last sale rule

In Canada the first sale for export rule has been abolished many years now. Mr Bédard mentioned during the interview that in Canada the requirements of the GATT Valuation Agreement have been implemented in 1985. The Canada International Trade Tribunal accepted in Harbour Sales a sale between two foreign entities as a sale for export to Canada. The judgement of the Tribunal broadened the definition of sale for export to Canada.

As Ruessmann and Willems (2009) have mentioned, the first sale for export has been abolished after the Canadian customs authorities lost in Harbour Sales (Windsor) Ltd v. D/MNR [1994] 4647 ETC.

Canadian legal framework

In order to abolish the first sale for export rule, the Canadian legislation has introduced the requirement to use the price paid or payable by the first purchaser in Canada. This requirement is determined in section 48 of the Customs Act Canada (R.S., 1985, c. 1 (2nd Supp.), s. 48; 1994, c. 47, s. 71; 1995, c. 41, s. 18; 2002, c. 22, s. 336; 2009, c. 10, s. 7.):

> "Transaction value as primary basis of appraisal 48 (1) Subject to subsections (6) and (7), the value for duty of goods is the transaction value of the goods if the goods are sold for export to Canada to a purchaser in Canada and the price paid or payable for the goods can be determined and if […]"

Section 48 of the Customs Act describes that the transaction value is the value for duty of goods "if the goods are sold for export to Canada to a purchaser in Canada". These concepts have been elaborated on in the Valuation for Duty Regulations.

Especially the meaning of purchaser in Canada of subsection 45(1) of the Customs Act is relevant for the interpretation of the last sale rule. Based on the Valuation for Duty Regulations, a purchaser in Canada means:

A. A resident;
B. A permanent establishment;
C. A person (neither a resident nor a permanent establishment) who imports the goods:
    a. for consumption by the person itself (no sale); or
    b. for sale by the person, without having sold the goods to a resident.

Mr Bédard explained: "There are three kinds of purchaser in Canada. In Canada we accept non-resident importers, because of the US. The US are our biggest trade partners and they accept non-resident importers of Canada. So, we do accept non-resident importers as purchaser in Canada, from every country as long as they have not entered into an agreement to sell the goods to a Canadian."

In Canada only sales for export to Canada to a purchaser in Canada can qualify as the transaction value to determine the customs value. Several memoranda have been issued by the CBSA.

The CBSA gives its interpretation and application of several phrases regarding customs valuation, especially several interpretations of phrases in the Valuation for Duty Regulations. These memoranda are not legally binding, but reflect Canada's policy on valuation. Importers are not bound to follow the memoranda, but the memoranda indicate the position of the CBSA.

Interpretation and scenarios

Also the Canadian legal framework can be compared with the scenarios mentioned before. In Canada the sale that triggers the importation of the goods into Canada is the sale that should be used for determining the customs value. The scenarios are discussed with Mr Bédard. Following the results of the interview and interpreting the legal framework, the following conclusions can be drawn.

Scenario 1

Also when comparing the Canadian legal framework with the scenarios, this scenario is the most "simple" scenario. As company C, located in the US sells the goods for EUR 1.200 to company D in Canada, this transaction qualifies as the last sale for export to Canada. The transaction value of EUR 1.200 forms the base for the customs value.

It is important that a company carries on business in Canada. Mr Bédard emphasized that Company D must have more than people working in a warehouse, unloading and reloading a truck. A company has to be involved as a purchaser in Canada and cannot be an empty shell. The transaction in which a person in Canada is directly involved, is the sale for export to Canada.

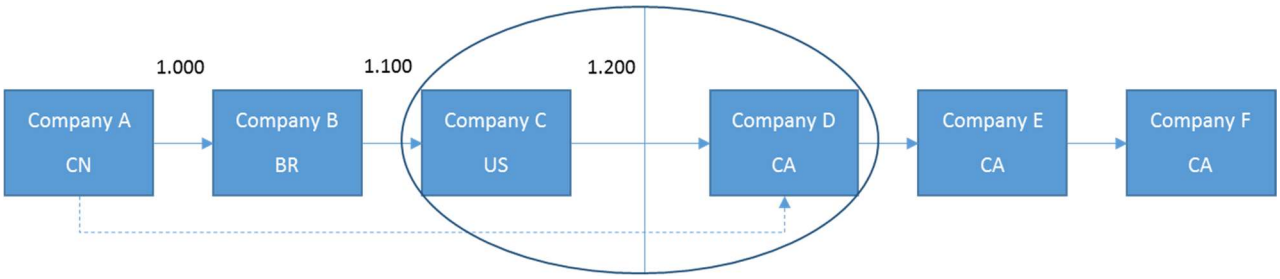

Figure 9: Scenario 1 - Canada

Scenario 2

In scenario 2 the sale between the two Canadian parties, company C and company D, does not qualify as the sale for export to Canada. This sale is being considered as a domestic sale. The sale between company B and C triggers the importation of the goods in Canada. Therefore the sale between company B, located in Brazil, and company C, located in Canada, is the sale for export. The transaction value which should be used is EUR 1.100. The predictability in this scenario is high.

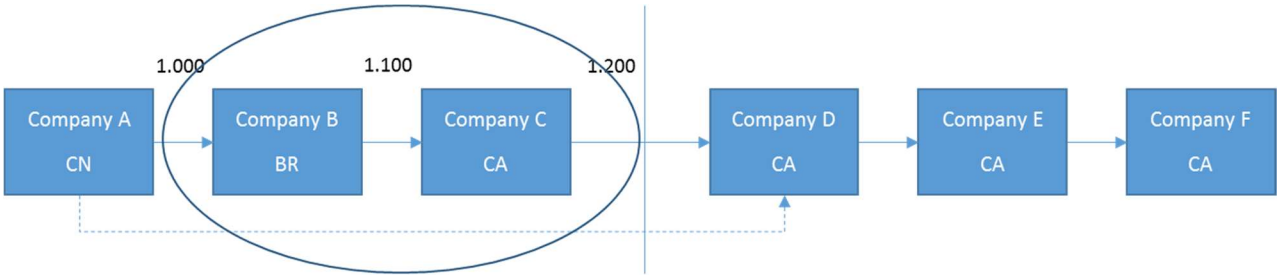

Figure 10: Scenario 2 - Canada

Scenario 3

In scenario 3 the sale between company A and company B triggers the importation of the goods into Canada. In case the goods are shipped directly to Canada, this sale is the sale for determining the customs value. The sale between company B and company C is a domestic sale.

In case the goods are not shipped directly to Canada, but company B stores the goods first in the US and after that the goods are ordered by company C in Canada, the sale between company A and B cannot be considered as sale for export to Canada. There is no guarantee that the goods are destined for Canada. The location of the goods is important in this scenario. The interpretation in this scenario is quite predictable.

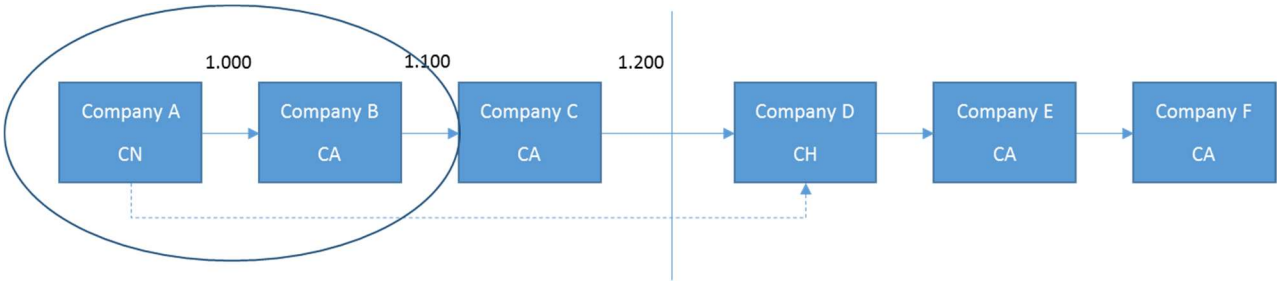

Figure 11: Scenario 3 – Canada

Scenario 4

In the Valuation for Duty Regulations the definition of purchaser in Canada is included. A non-resident company without a permanent establishment can be a purchaser in Canada in case the goods are imported for consumption, use or enjoyment by the company in Canada but not for sale *or* when the goods are imported in Canada for speculation.

Therefore, if the Swiss company – as a non-resident importer – ships the goods on speculation for the Canadian market, without a previous agreement to sell the goods to a resident, the sale between company B and C is accepted as sale for export to Canada. If there is already an agreement between company C and D, that sale has to be used as sale for export to Canada.

Mr Bédard emphasized during the interview that in the Cherry Stix 1 case a similar situation applied (AP-2004-009):

"In that decision Walmart Canada had an agreement to sell with Cherry Stix. Cherry Stix was the non-resident importer. Cherry Stix declared their sale with their Chinese supplier, but there was an agreement between Cherry Stix and Walmart, so Cherry Stix could not be a purchaser in Canada. We took the other sale between Walmart and Cherry Stix. We won that decision."

In conclusion, the sale between company B and C would be applicable in case there are no following sales at the moment of importation. In case there is a sale between a resident in Canada and the non-resident importer, that sale has to be used for determining the customs value. Companies have to take following transactions into account. This distinction makes the interpretation in this scenario less predictable.

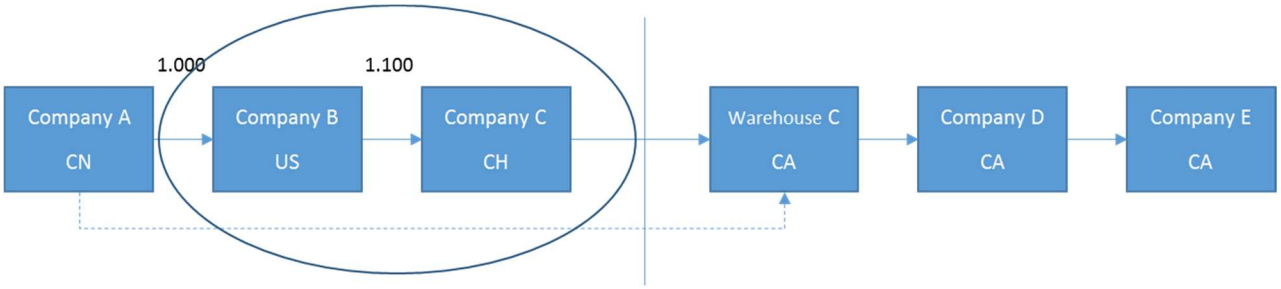

Figure 12: Scenario 4 – Canada

Availability invoice previous sale

It may be possible that in scenario 2 and 3 the importer does not possess the invoice of the relevant sale. In that case the CBSA allows companies to use that invoice of the following sale. In case the relevant sale is the sale between company A and B, but company C only has an invoice of the sale between company B and C, the following applies. Mr Bédard states:

"Since company C has only its invoice to provide in support of its declaration, the application of another method would result in the same customs value. This is the main reason why the CBSA accepts the sale between B and C as the customs value under the transaction value method. However, if company C is able to get the invoice between A and B afterwards, company C will be eligible for amending its declaration and request a refund of duties."

There are no issues in case a company does not have the invoice of the relevant sale.

Summary Canadian interpretation

The current interpretation is being compared for Customs and companies with the sale that would be used in case the first sale rule was applicable. The following conclusions have to be drawn for each scenario:

	Canadian interpretation		
Scenario	***Predictability***	***Value used***	***Impact customs value***
1	++	€ 1.200,00	€ 200,00
2	++	€ 1.100,00	€ 100,00
3	+	€ 1.000,00	€ -
4	+-	€ 1.100,00	€ 100,00

Table 2: Summary Canadian interpretation

The predictability is higher than in the EU interpretation, because of the fact that the CBSA has approximately 45 documents that explain specific valuation issues.

5.4. Differences EU and Canadian interpretation

The EU and Canadian interpretation differ in several ways. In this paragraph the differences are discussed. First several differences in the legal frameworks are listed, after that other differences are elaborated on.

Legal frameworks

The EU legislation regarding the last sale rule is relatively new. Therefore, the interpretation of the last sale rule is also new. With one guidance document and no case law, the legal framework is quite narrow. Also the definition in the legislation leaves room for interpretation. Companies do not have the certainty that they use the right transaction value.

In Canada the legal framework is more extensive. Especially the high amount of memoranda regarding the valuation rules contributes to a higher predictability. Also the Canada International Trade Tribunal has ruled in several cases on the definition of sale for export.

Other differences

One of the main differences between the Canadian interpretation and the EU interpretation is the definition of the sale for export. As discussed with Mr Bédard in Canada "the sale that triggers the importation into Canada" is the sale for export. This means other following sales can be left unspoken.

In the EU the last sale for export is – based on article 128 IA UCC – "the sale occurring immediately before the goods were brought into that customs territory". The definition "sale occurring immediately before" leaves room for interpretation.

Another difference is the requirement of a sale for export to a "purchaser in Canada". In the EU there is no similar requirement. This Canadian requirement narrows down the number of transactions that can qualify as "sale for export", but also ensures more discussion between CBSA and companies.

Especially in scenario 3 the differences in interpretation result in another transaction value for determining the customs value. By using the Canadian interpretation, the transaction value of EUR 1.000 should be used. By using the EU interpretation, the transaction value of EUR 1.200 is applicable.

The Canadian interpretation that in case a non-resident importer sells the goods before importation and does not bring the goods on speculation to Canada, has been introduced in the EU too when discussing the MCC. Also in an earlier stage, before the UCC was applicable, this situation was discussed and came up. The interpretation of the EU is however not the same currently. The subsequent sales are not important for determining the customs value at the moment.

5.5. Alternative EU interpretation

The current interpretation of the EU last sale rule may not be tenable, because of the fact that the place of establishment is important for determining the transaction value, as shown by scenario 3 in paragraph 5.2. This criterium may be interpreted as discriminatory. By combining the EU and Canadian interpretation, this problem could be solved. In this paragraph an alternative EU interpretation will be discussed. Another option would be to drop the exclusion of domestic sales. This option will be discussed too.

Alternative combined interpretation

When combining the EU and Canadian interpretation, the alternative interpretation would be to:

1. use the last sale for export definition of the EU; and
2. add the principle that the sale for export is the sale that triggers the importation into the EU.

There will be no requirement to be a "purchaser in the EU", as this is a complicating factor. In this case a following sale between an EU company and a non-EU company is not relevant and therefore the location of companies is not relevant either. This combined interpretation will (more or less) lead back to the first sale rule, which was not the intention of the European Commission.

To make the interpretation more predictable, several policy papers, guidance documents or other guidelines should be published by the EU.

This combined interpretation does not solve the issue of companies that do not possess the invoice of the earlier sale than the domestic sale. It is possible to solve this issue by introducing the statement that a domestic sale can be used for determining the customs value in case the invoice of the earlier sale is not available. This would simplify the application of the last sale rule.

The summary would be as follows:

Scenario	Combined interpretation				
	Predictability	*Value used*		*Impact customs value*	
1	++	€	1.200,00	€	200,00
2	++	€	1.100,00	€	100,00
3	+	€	1.000,00	€	-
4	++	€	1.100,00	€	100,00

Table 3: Summary combined interpretation

Interpretation including domestic sales

Another option would be to keep the EU interpretation like it is at the moment, but to drop the exclusion of domestic sales. The last sale for export would be the sale which should be used for determining the customs value. The definition in article 128 IA UCC could be unaltered ("the sale occurring immediately before the goods were brought into that customs territory").

This interpretation would solve the issue of the availability of the invoice of a sale between other parties in the supply chain than the party submitting the customs declaration. The last sale will be the relevant sale and in most cases this is the sale between the supplier and the importer. The importer does not need information of parties in the supply chain other than its own information.

The following summary would apply:

Scenario	Interpretation (including domestic sales)				
	Predictability	*Value used*		*Impact customs value*	
1	++	€	1.200,00	€	200,00
2	++	€	1.200,00	€	200,00
3	++	€	1.200,00	€	200,00
4	++	€	1.100,00	€	100,00

Table 4: Summary interpretation including domestic sales

This interpretation would be most predictable, but would result in a lot of resistance of companies. The transaction value used would be higher in all situations. The goal of the European Commission will be accomplished by adopting this interpretation, namely the abolishment of the first sale rule.

5.6. Conclusion

The interpretation of the last sale rule is not the same in the EU and Canada. Especially the legal frameworks and definitions differ. Comparing two new alternative interpretations of the last sale rule and the current interpretations, would result in the following overview:

Interpretation	*Predictability*	*Value used*		*Impact customs value*	
EU	+-	€	4.600,00	€	600,00
Canada	+	€	4.400,00	€	400,00
Combined	+	€	4.400,00	€	400,00
Including domestic sales	++	€	4.700,00	€	700,00

Table 5: Comparison interpretations

The predictability of the interpretation including the domestic sales is the highest, but the impact on the customs value is also the highest. In most cases the relevant invoice will be available, so the issue of not possessing the relevant invoice will be solved without adding policy documents or changing any legislation.

The combined interpretation seems better in terms of predictability than the current EU interpretation and best in terms of impact on the customs value of all interpretations. It is however necessary to add policy documents or change legislation to solve the issue of companies that do not have the invoice of an earlier sale than the sale between the party and its supplier.

When the interpretation including the domestic sales would be used, companies could be forced to restructure their supply chain to cope with the higher burden caused by the higher customs value. Companies should structure their supply chain in the most efficient way to avoid higher customs values.

6. Contribution for research

After the abolishment of the first sale rule and together with the introduction of the last sale rule in the EU, the interpretation of the last sale for export in the EU was not clear. Companies were and are not certain which transaction value they have to take for determining the customs value. Especially the interpretation regarding domestic sales causes confusion. Domestic sales are excepted as sale for export, as stated by the European Commission (2016) in a guidance document.

In Canada, the last sale rule has been used since 1985. The Canadian customs authorities have explained the customs valuation rules in many policy papers. By using these policy papers the definition of last sale for export in Canada is clearer, as shown by the research.

The research performed has indicated several differences between the Canadian and EU interpretations. Especially taking into account subsequent sales in the Canadian interpretation and "domestic sales" in the EU interpretation are important differences.

The goal of this research was to build a new interpretation of the last sale rule and to evaluate that interpretation. Two new interpretations for the EU have been built and evaluated using the same scenarios as used when displaying the current interpretations in the EU and Canada.

In earlier research the implications of the abolition of the last sale rule have been discussed. Also, the changes in the legislation have been discussed by Truel and Maganaris. The research performed takes the legislation and guidance documents in the EU into account and gives more insight in the efficiency of the EU interpretation by comparing the EU and Canadian interpretations. Four scenarios have been used to evaluate the current and new interpretations in terms of predictability and impact on customs value.

The research performed adds new knowledge regarding the interpretation of the first sale rule in the EU and Canada to the literature. The new interpretations, especially the combined EU and Canadian interpretation, show that the interpretation of the last sale for export can be simplified. These interpretations can be used to further develop the last sale rule in the EU.

7. Contribution for practice

Companies and customs authorities are not certain which value they have to take for determining the customs value. This problem is especially relevant for companies, customs authorities and the legislator, as the legal certainty is low at this moment.

Research of Desiderio and Desiderio (2010) shows that the change from first sale rule to last sale rule leads to an increase in the dutiable value of imports for companies. With a decrease of legal certainty companies (and customs authorities) do not benefit at all from the change in legislation.

As follows from the research performed, the Canadian interpretation gives more legal certainty. This is caused by many policy documents. The Canadian interpretation has a less complicated definition of sale for export.

Under the current interpretation in the EU, companies do have issues when only having the invoice of a domestic sale. Domestic sales do not qualify as sale for export. These sales (and therefore invoices) cannot be used by companies for determining the customs value. Dutch Customs states that another valuation method should be used.

By combining the two interpretations (the EU interpretation and the Canadian interpretation), the predictability would be better. Companies and customs authorities in the EU would be more certain about the transaction value for determining the customs value. The issue of not having the invoice of the relevant sale will not be solved. One option could be to make an exception when the relevant invoice is not available to use the invoice that is available to determine the customs value. This exception should be defined in legislation or policy documents.

The alternative interpretation, including also the domestic sales, is the most drastic interpretation. This interpretation will lead to complaints by companies, as the customs value will be higher in most of the scenarios. The invoice issue will be solved however, as domestic sales do qualify as sale for export.

Also so-called “backorders” will contribute to much higher customs values. When using backorders, an order by a customer cannot be delivered directly. The seller has to order the products first. Backorders are common in the automobile industry. A customer orders a car and the distributor orders after this sale the car from its supplier. The first transaction value is higher than the second transaction value. In case domestic sales are included when determining the customs value, the sale between the customer and the seller has to be the sale for export. This sale may be much higher than the sale between the seller and the supplier.

In case one of the new interpretations will be used, the legal certainty will be higher. Companies and customs authorities will benefit from a higher legal certainty. The combined interpretation will lead to higher legal certainty and the customs value will not change a lot.

It is possible that the interpretation of the European legislation does not change. In that case companies do have to restructure their supply chain in order to avoid higher customs values. Non-EU residents may choose to establish an EU located company. Companies could also choose to sell the goods only after bringing the goods into free circulation.

In summary, the research gives insight in the issues when determining the customs value when following the current interpretations. The scenarios show the issues for practice. The new interpretations could provide higher legal certainty.

By combining the two interpretations, the predictability would be better. Companies and customs authorities in the EU would be more certain about the transaction value for determining the customs value. The other interpretation, including domestic sales, is not the most efficient interpretation for companies, but does result in the highest legal certainty.

8. Conclusions and recommendations

This research focussed on the following question:

Against the background of the objective of the abolition of the first sale rule, is the interpretation of the last sale rule in the EU effective? And how does this interpretation compare to the Canadian version of the rule?

The answer to this research question is substantiated by answering the sub-questions.

Sub-question 1: *Why did the EU change from first sale to last sale rule and what are the main characteristics of the current interpretation of the EU last sale for export rule?*

By applying the Union Customs Code the EU changed from first sale to last sale rule. The first sale rule was applicable under the Community Customs Code. The Community Customs Code was modernized and during this modernization, the abolition of the first sale rule came up. The Modernized Customs Code never became applicable however. In April 2007 the WCO adopted Commentary 22.1 in which the definition "sold for export to the country of importation" in a series of sales was explained. The WCO Technical Committee explained the last sale rule was applicable.

The EU considered this interpretation – like expressed in the preamble of the implementing acts of the UCC – and abolished the last sale rule.

The last sale rule is included in Article 128 IA UCC. The definition in the legislation was however not clear enough, therefore the European Commission (2016) explained the definition in a guidance document. This document has no legal status.

In this document several cases have been explained. The European Commission (2016) states in the guidance document that domestic sales do not qualify as sale for export, but the document is only a guide. Companies and customs authorities are not certain about which value should be used for determining the customs value.

The invoice is necessary to determine the transaction value. The invoice of earlier sales – in case of domestic sales – is not always available to the importer. Dutch Customs interprets the definition at the moment in a way that an alternative valuation method should be used in that case.

Sub-question 2: *What are the main characteristics of the Canadian last sale rule?*

In Canada the last sale rule has been used for many years. In Canada the last sale rule is defined in the Customs Act and Valuation for Duty Regulations since the GATT Valuation Agreement has been implemented in 1985. To explain the definition the Canada Border Services Agency has issued several memoranda. These memoranda are not legally binding, but the give an indication of the position of Canadian Customs.

In Canada the sale that triggers the importation into the territory of Canada is the relevant sale for export. As follows from the definition in the legislation, the sale for export to a purchaser in Canada is the relevant sale for determining the customs value. Canada accepts non-resident importers, but only if these importers did not enter into an agreement to sell the goods to a Canadian party.

Sub-question 3: *In which way do these characteristics of the EU and Canadian last sale rule differ?*

The EU and Canadian interpretation differ in several ways. The EU legislation regarding the last sale rule is relatively new. There is only one guidance document and no case law. The definition in the legislation leaves room for interpretation. The legal certainty is quite low therefore.

In Canada the legal framework is more extensive, especially the high amount of memoranda regarding the valuation rules causes higher predictability. Also case law is available in Canada.

One of the main differences between the Canadian interpretation and the EU interpretation is the definition of the sale for export. The sale that triggers the importation into Canada is the relevant sale for determining the customs value. The EU definition leaves room for interpretation.

Another difference is the requirement of a sale to a "purchaser in Canada". In the EU there is no similar requirement. This Canadian requirement narrows down the number of transactions that can qualify as "sale for export", but also ensures more discussion between CBSA and companies. The EU accepts non-resident importers. In Canada non-resident importers are only allowed when there is no agreement with a Canadian party.

Sub-question 4: *Are there any issues in the EU interpretation and can these issues be solved or prevented by another interpretation, e.g. by using the Canadian interpretation?*

The current EU interpretation does not seem to be tenable. The place of establishment is relevant for determining which transaction value is the relevant transaction value. This finding seems discriminatory. Also the statement of Dutch Customs that another valuation method should be used in case the invoice of the relevant sale for export is not available, does not seem to be tenable (based on the UCC and UCC IA).

In this research the combination of both interpretation and an alternative interpretation including domestic sales are examined.

A combined EU and Canada interpretation would be to use the last sale for export definition of the EU and add the principle that the sale that triggers the importation into the EU is relevant. The requirement of a sale to a purchase in the EU will not be implemented, as this complicates the definition and does not contribute to a higher predictability. Policy papers, guidance documents and guidelines should guide companies and customs authorities. These documents could also solve the issue of not having the relevant invoices.

Another option would be to keep the current EU interpretation but include the domestic sales. This would result in higher customs values, but will increase the predictability. The issue of not possessing the relevant invoices will be solved in this way.

Based on previous findings, the answer to the research question *Against the background of the objective of the abolition of the first sale rule, is the interpretation of the last sale rule in the EU effective? And how does this interpretation compare to the Canadian version of the rule?* Should be:

The effectiveness of the current interpretation is quite low. Customs authorities and companies do experience legal uncertainty. The current EU interpretation is not predictable and seems to be discriminatory in especially aforementioned scenario 3. In case the relevant information of the sale is not available, the current EU interpretation and the consequences of the interpretation are unclear at the moment.

The Canadian version of the last sale rule is more predictable and more effective. This is caused by a high amount of policy papers and memoranda. A combination of both interpretation would result in a higher predictability.

In my opinion the EU interpretation needs either more explanation of the European Commission or another definition of the last sale for export. The legal certainty is too low at the moment.

The predictability of the alternative interpretation including the domestic sales is the highest, but the impact on the customs value is also the highest. In most cases the relevant invoice will be available, so the issue of not possessing the invoice will be solved without adding policy documents or changing any legislation.

The combined interpretation provides higher predictability than the current EU interpretation and would be best of all interpretations in terms of impact on the customs value. It is however necessary to add policy documents or change legislation to solve the issue of companies that do not have the invoice of an earlier sale than the sale between the party and its supplier.

A recommendation following from the research is to investigate both options. The true impact on customs values and on the European trade should be calculated. The time to adjust the legislation should also be taken into account. Policy papers and guidance documents can be released much faster than adjusting legislation. In case adjusting legislation would take several years, case law regarding the definition of last sale for export may be available too.

Another recommendation would be, also in case the European Commission does not want to adjust the interpretation, to explain the current interpretation in more detail. The scenarios mentioned in the memoranda of the Canadian customs authorities could be useful for explaining the interpretation.

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10. Appendix A – Interview Canadian interpretation last sale rule

Before May 1st, 2016 the first sale for export rule was applicable in the European Union (EU). From May 1st, 2016, the last sale for export rule is applicable. Companies and customs authorities in the EU, in some situations in a chain of transactions, are not certain which transaction value they have to use to determine the correct customs value.

In Canada, the last sale rule is applicable for many years now. It could be that the Canadian interpretation is also suitable for the EU. This interview with Mr Bédard focusses on the Canadian interpretation of the last sale rule. To be clear: this interview is only used for research purposes.

1. Could you tell something about your background?

   "I have been working for the Canada Border Services Agency for the valuation program for eleven years now, since 2006. I am a senior program advisor, so I am responsible to develop, create and review policy on valuation. I am also responsible for training materials, because we train our own officers, the auditors who are conducting post-clearance audits. In Canada, a large country, we have different regions responsible for auditing importers. I am also responsible for reviewing the procedures that they have to follow and any regulations or legislation associated with the administration of the valuation program. I am based in Ottawa, the capital of Canada. At headquarters we are responsible for the policy, the administration of that program. I have also been the Canadian delegate at the Technical Committee on Customs Valuation since 2010. In May it will be my fourteenth session, so I am used to discuss international policies or different interpretations of the customs valuation agreement."

2. Regarding the background of the Canadian switch from the first sale to the last sale rule: why did Canada switch to the last sale rule?

   "In Canada we have implemented the requirements of the GATT valuation agreement in 1985. Since then Canada's policy has always been that the relevant sale for export for establishing the customs value, is the transaction in which the person in Canada is directly involved. However, the Canada International Trade Tribunal (CITT), in Harbour Sales, accepted a sale between two foreign entities as a sale for export to Canada. Following that decision the purchaser in Canada criteria was introduced in order to use again the last sale. It has always been our position to use the last sale rule. The definition has been introduced in the Valuation for Duty Regulations. Section 45 of the Canadian Customs Act contains all our definitions and the definition of 'purchaser in Canada' is referred to the regulation."

Section 48 of the Customs Act describes that the transaction value is the value for duty of goods "if the goods are sold for export to Canada to a purchaser in Canada". These concepts have been elaborated on in the Valuation for Duty Regulations.

Especially the meaning of purchaser in Canada is relevant for the interpretation of the last sale rule. A purchaser in Canada means:

A. A resident;
B. A permanent establishment;
C. A person (neither a resident nor has a permanent establishment) who imports the goods:
    a. For consumption by the person itself (no sale); or
    b. For sale by the person, without having sold the goods to a resident.

Also memoranda are published by Canada Border Services Agency.

3. What is the legal status of these documents?

"The memoranda are clearly Canada's policy on valuation. Importers are not bound to follow them, but at least they know what is our position or our interpretation of the agreement. So, for us it is easier to have importers compliant, because sometimes – as you probably know – valuation rules can be complex. That is why we try as much as possible to develop instruments for importers in order to understand how they have to declare their customs value. When we are challenged at the Tribunal, it is in respect of those policies. When importers disagree with our used policy, then they go to the CITT. The policies are not legislation. Companies can disagree, challenge us and go to the Tribunal, when they disagree."

4. Do you consider the valuation rules complex – especially regarding the last sale rule – in Canada? Why?

"There are three kinds of purchaser in Canada. In Canada we accept non-resident importers, because of the US. The US are our biggest trade partners and they accept non-resident importers of Canada. So, we do accept non-resident importers as purchaser in Canada, from every country as long as they have not entered into an agreement to sell the goods to a Canadian. The biggest issue we have with the purchaser in Canada is with non-resident importers. When we conduct post-clearance audits, sometimes importers declare the earlier or first sale and not the last sale. The difference in value can be significant."

5. How do companies experience the valuation rules?

"When businesses are located in Canada, they have management control activities, a fixed place of business in Canada and they are well located and especially when they are not related to another party, the valuation rules are not so complex to determine the relevant sale for export. It may be more complex for them when they have an assist (services provided free of charge to a vendor). Sometimes companies forget to declare the assists as part of the customs value in their declaration. Or, if there is a buying agent involved for example in China, companies are not adding the right value in their declaration.

Normally, our importers are compliant with the rules, maybe because we have a lot of valuation policies available to them. I think we have right now 45 or 46 documents that explain specific valuation issues. So, companies can rely on those documents, but we have been challenged several times on the purchaser in Canada. We have lost at the Tribunal on the last sale rule.

We have two specific cases:

1) Ferragamo USA (AP-2005-053) was a non-resident importer, but they had an agreement with Ferragamo Canada. They challenged us with our regulations, because a non-resident importer can be a purchaser in Canada if that non-resident importer has not entered into an agreement with a Canadian resident. Ferragamo USA argued that Ferragamo Canada was not a resident, because they were not 2.A of the definition of resident in the regulation, but more 2.B, a permanent establishment. Ferragamo USA won on this. In this case Ferragamo USA could use the sale between them and Ferragamo SpA in Italy, so a lower sale.
2) In Cherry Stix there are three decisions. They were in all of the cases involved with Walmart. We won the first one, but we have lost Cherry Stix 2 (AP-2008-028). There were two sales for export. The Tribunal determined that we could not use either of those sales. In those two cases the importers were located outside Canada. The Tribunal determined that another valuation method should be used. The Tribunal relied on the used incoterms (CIF or DDP). Cherry Stix still had the title of the goods at the time of importation, so the Tribunal said there was no sale for export, even though they had an agreement to sell with Walmart Canada. Some companies want to rely on Cherry Stix 2, but we do have another policy on this, because at the end the value would be more or less the same.

   Advisory opinion 1.1 of the Customs Valuation Agreement, an instrument from the Technical Committee, says we must interpret sale in its widest sense. For us an agreement to sell is a sale for export. A purchase order is an agreement to sell. In our memorandum D13-4-2 we explain that that is our policy.

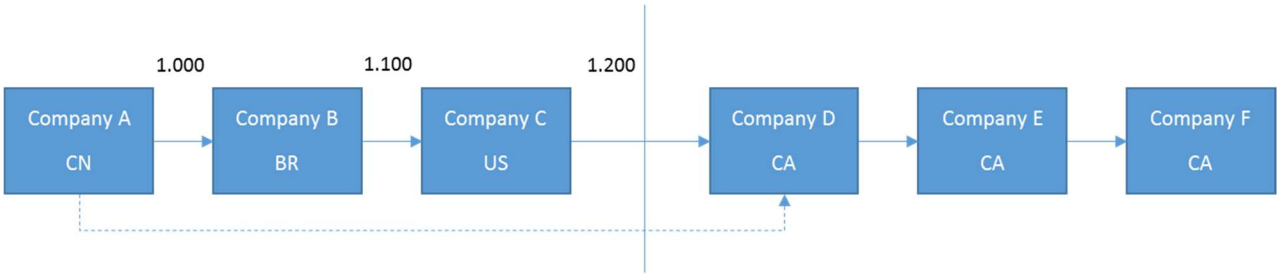
   The valuation rules are complex, but that is why we have decided to publish policies for importers."

As mentioned before, in the EU, many questions regarding the use of the last sale rule remain. In this context, I would like to discuss the following scenarios with you.

Scenario 1

Company A, located in China, sells goods for USD 1.000 to company B, located in Brazil. Company B sells goods for USD 1.100 to company C, located in the US. Company C sells the goods for USD 1.200 to company D in Canada. All of the aforementioned transactions take place before the goods have been brought into the customs territory of Canada. The goods are shipped directly from China to Canada.

The flow of goods can be displayed as:

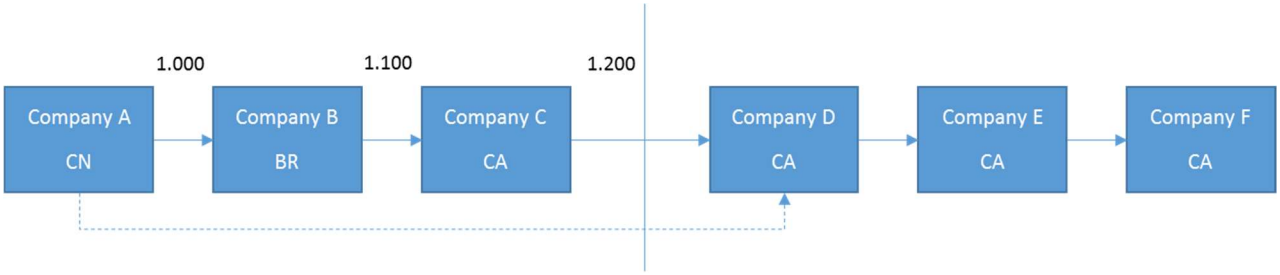


6. In this scenario the sale between company C and D is the sale for export, right? Can you elaborate on the reasoning behind this?

"Yes, that is right if the person in Canada qualifies as a purchaser in Canada. Most of the time, when a Canadian has a fixed place of business through which it carries on business and not only having two people working in the warehouse, just looking at the goods, unload a truck and reload a truck. That is not carrying on business. They must be involved as a purchaser in Canada. When a person has agreed with another person located outside Canada to purchase goods, then I believe it is the agreement between C to D and the goods are exported to Canada as a direct result of that agreement. The transaction in which a person in Canada is directly involved, constitutes the sale for export to Canada. Clearly in this situation it is the sale between C and D."

Scenario 2

Company A, located in China, sells goods for USD 1.000 to company B, located in Brazil. Company B sells goods for USD 1.100 to company C, located in Canada. Company C sells the goods for USD 1.200 to company D in Canada. All of the aforementioned transactions take place before the goods have been brought into the customs territory of Canada. The goods are shipped directly from China to Canada.

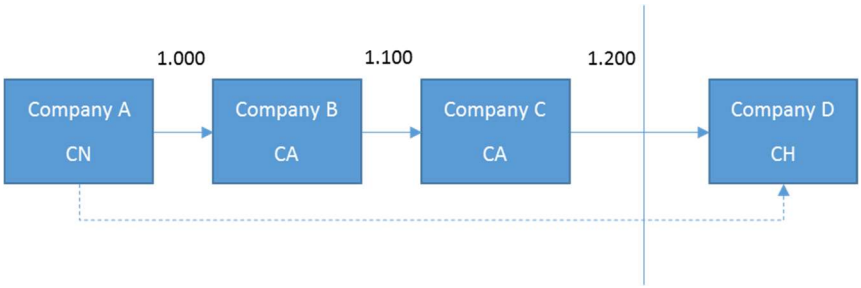


7. In this scenario, the transaction between company B and C is the price used for determining the customs value I believe. Is this correct? Why?

"On the same principle it would be between B and C. The relevant sale is the sale in which the goods were sold for export to Canada, the "over the border sale". The sale between C and D is a domestic sale. The sale between B and C is the sale that set off the chain of events, which causes the goods to be shipped to Canada. Sometimes you can have an order between two Canadians, but the goods are not physically located in Canada. The Canadian vendor can contact a foreign vendor to ship the goods directly to the Canadian purchaser. The sale between the two Canadians is considered to be a domestic sale.

Scenario 3

Company A, located in China, sells goods for USD 1.000 to company B, located in Canada. Company B sells goods for USD 1.100 to company C, located in Canada. Company C sells the goods for USD 1.200 to company D, located in Switzerland. All of the aforementioned transactions take place before the goods have been brought into the customs territory of Canada. The goods are shipped directly from China to Canada.

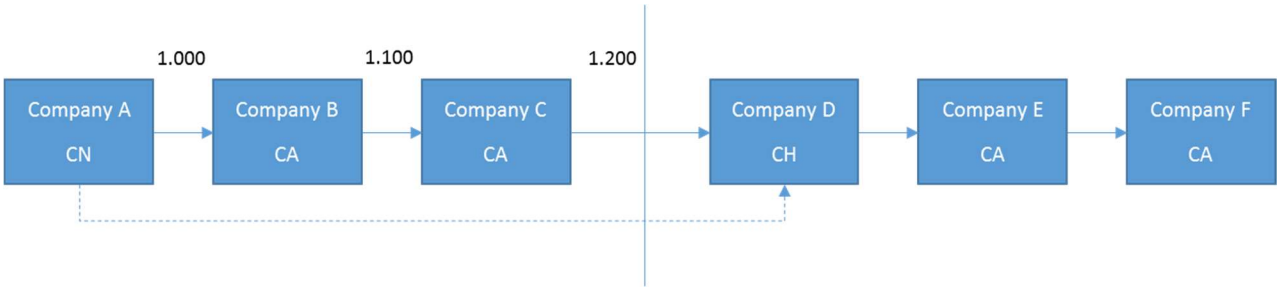


8. Which transaction should be taken in this scenario?
   A. Transaction A-B
   B. Transaction B-C
   C. Transaction C-D

   Can you explain your answer here?

"The sale between A and B is the transaction that triggers the importation of the goods into Canada. The transaction between B and C is a domestic sale, because it is a sale between two Canadian companies. Last week we had a case that is similar to this case. A person located in Canada ordered goods from Mexico, but he shipped the goods to the US in a bonded warehouse. Then another Canadian ordered the goods from that person located in Canada. The first buyer directed the goods directly to the other entity in Canada. So, in that situation the first sale between Canada and Mexico was not a sale for export to Canada, but a sale for export to the US. We took the other sale, the sale between the two Canadians as the sale for export. We used advisory opinion 14.1, which says that the location of the vendor is irrelevant. It is the sale that triggers the importation. The goods were not shipped directly to Canada, but to the US. The goods could have been sold to a US entity as well. There was no guarantee that the goods were destined for Canada. Obviously the importer disagrees with our position. He asked for a ruling. Canada has a program for valuation rulings. In this ruling the importer wanted us to confirm that the sale was between Canada and Mexico. We rely on advisory opinion 14.1 and our policy, it is scenario C in D13-4-2."

9. And what if the flow of goods is as follows?



"If we have a non-resident importer, who is shipping goods on speculation for the Canadian market, with no previous agreement to sell the goods to a resident, we accept that sale as a sale for export. The issue that we have is to follow the sequence of the transactions. The goods must be shipped clearly on speculation, just waiting for a sale. If company B already ordered the goods to company A, therefore there was an agreement to sell and we are going to use that sale for export. We will take the sale at the next level, because we disqualify company A and D as purchasers in Canada.

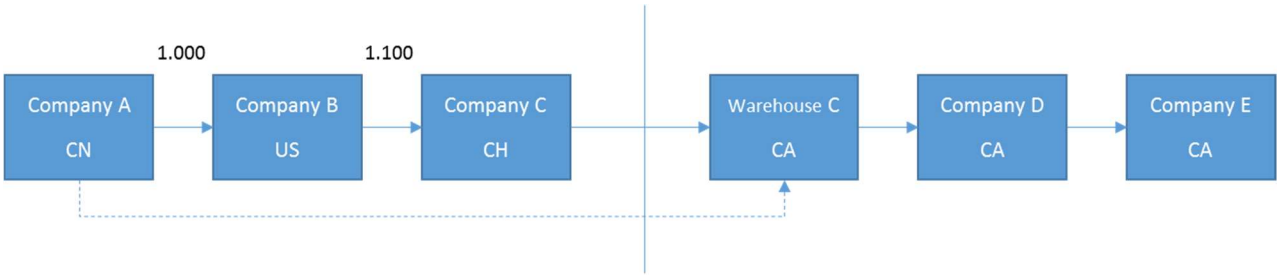
Cherry Stix 1 was a similar situation. In that decision Walmart Canada had an agreement to sell with Cherry Stix. Cherry Stix was the non-resident importer. Cherry Stix declared their sale with their Chinese supplier, but there was an agreement between Cherry Stix and Walmart, so Cherry Stix could not be a purchaser in Canada. We took the other sale between Walmart and Cherry Stix. We won that decision.

We do not have a company in the middle, like Switzerland in the EU. Therefore we do not have the same issues you have in the EU.

In Canada we have some issues with the qualification of a sale as a sale for export to Canada. We have a requirement that the label of the goods should have a description in two languages, French and English. Nowadays many goods are shipped with a description in six or more languages. The qualification of sale for export to Canada is easier in that way, but goods are not always destined for the Canadian market. Importers always try to find a way to get a lower value obviously, because that is their business. The only way to find out whether the goods are destined for the Canadian market is to do post-clearance audits and that is where we are focussing on. We target companies that are part of a multinational group, as we experienced that these companies do use in some cases an earlier sale for determining the customs value."

Scenario 4

Company A, located in the China, sells goods for USD 1.000 to company B, located in the US. Company B sells goods for USD 1.100 to company C, located in Switzerland. Company C brings the goods into the Canadian customs territory and places the goods in a warehouse of company C. All of the aforementioned transactions take place before the goods have been brought into the customs territory of Canada. The goods are shipped directly from China to Canada.



10. Which transaction qualifies as sale for export to Canada? Why?
    A. Transaction A-B
    B. Transaction B-C
    C. Transaction C-D

"You could use the transaction between B and C in case the goods are shipped to Canada without a prior agreement between company C and D. If the goods have been brought to Canada for speculation, the sale between company B and C is the sale for export to Canada. If we see that D orders the goods to C and then C orders goods to B, then the sale between C and D should be used for determining the customs value."

11. What do you think of the complexity of the last sale rule in the discussed scenarios?

"The evidence to demonstrate that a previous sale agreement to sell the goods existed between a Canadian and foreign entity before the importation of goods is the most complex scenario. We have been challenged when a non-resident importer has not transferred the title of the goods by using the incoterm DDP. The CITT ruled that the goods were not sold before the importation of the goods in Canada. In the EU you are using the "transaction value of the goods sold for export to the customs territory of the Union", so you could be challenged in the same situation. Every time we are challenged by companies, our defence is that we use the sale in its widest sense, the interpretation of advisory 1.1. In Canada we would like to make some amendments to legislation and regulations in order to avoid that kind of argument, but it is hard to change legislation. We would like to have a definition of 'sale for export'. We consulted our legal services at the Department of Justice and the importing community on this, but the issue that we are facing is that we have to quantify the monetary impact of changing the legislation. We have been working on this for six years now, but it may still take a while."

12. What if there is a sale between company A (US) and company B (Canada) and a sale between company B (Canada) and company C (Canada). Company C brings the goods into free circulation and submits the declaration. Under normal circumstances the sale between company A and B is the relevant sale for export and the transaction value of this sale should be used for determining the customs value. In this situation company C does not have the invoice of the sale between company A and B. Should company C use the transaction value of the sale between company B and C? Or does company C have to apply another valuation method?

"In this situation, since company C is responsible for declaring the imported goods and the only information available is the invoice between B and C, the Canada Border Services Agency (CBSA) will accept that sale for export as the basis for the calculation of the customs value under the transaction value method.

One of the reasons is that the CBSA does not have the authority to "force" company B in Canada to provide the invoice between them and company A. There is also a possibility that company B already purchased the goods and stored them outside of Canada prior to selling those goods to company C. In such a situation, the sale between A and B would not be considered a sale for export to Canada. The relevant sale for determining the customs value in this situation is the one that sets off this chain of events resulting in the goods being exported to Canada, i.e., the sale between B and C. This last situation often occurs when the goods are stored in a free trade zone outside of Canada waiting for a sale to a Canadian customer and closely resemble Example 2 of Advisory Opinion 14.1 (see attachment).

Since company C has only its invoice to provide in support of its declaration, the application of another method would result in the same customs value. This is the main reason why the CBSA accepts the sale between B and C as the customs value under the transaction value method. However, if company C is able to get the invoice between A and B afterwards, company C will be eligible for amending its declaration and request a refund of duties."