

Reform of Customs Transit in the European Community



This report has been prepared under Section 6 of the National Audit Act 1983 for presentation to the House of Commons in accordance with Section 9 of the Act.

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Executive summary

1 In December 1995 the European Parliament exercised for the first time their new powers to examine “alleged contraventions or maladministrations in the implementation of Community law”, given by the Treaty of European Union, by setting up a temporary Committee of Inquiry to investigate the problems occurring in the Community transit system, the main form of customs transit within the Community. Customs transit is a set of procedures which enable customs duties, excise duties and VAT on imported goods to be suspended until those goods reach either their point of destination in the Community or are exported out of the Community. The suspended duty and tax is protected by a guarantee provided by one of the organisations involved in the movement of the goods.

2 Since 1992, there had been a growing concern about the level of fraud in the customs transit systems within the Community and the apparent ease with which fraud could be perpetrated. The European Commission and the European Court of Auditors had reported on the problems, but the European Parliament noted that reports from both these bodies did not seem to specify why “shortcomings and cases of maladministration, or even breaches of the relevant provisions of Community law, occur and increase over the years”. The European Parliament Committee of Inquiry was set up therefore with a view to clarifying the nature and causes of the problems. The Committee put forward 12 main recommendations relating to customs transit, on which this report is based.

3 Customs transit is one of the cornerstones of European integration for facilitating trade both within the European Union, and with the European Free Trade Association (EFTA) and Visegrad countries. It comprises the Community transit (for the European Union), common transit (for the extension to the EFTA and Visegrad countries) and the TIR systems. This report is concerned with the first two transit systems; the main differences between them relate primarily to their legal base and the countries to which they are applicable. Common transit is based upon an international convention whereas Community transit has been framed within Community regulations. Community transit covers the Community; common transit extends the Community transit system to include EFTA and Visegrad countries.

4 Under customs transit procedures someone has to take responsibility for ensuring the goods reach their final destination and, in the event of an irregularity, for the payment of the suspended customs and excise duties and taxes. This person is known as the Principal. In most cases Principals are required to provide a guarantee. The main form of guarantee is known as a comprehensive guarantee

and covers an amount corresponding to up to 100 per cent of customs duties, excise duties and VAT liability on an average of one week's transit movements. For so-called "sensitive" goods, for example those with a high excise and tax value such as cigarettes and alcohol, Principals are required to provide individual guarantees covering 100 per cent of the potential liability for each transit movement.

5 The Community transit and common transit systems are based on a multi-part form, the Single Administrative Document. One copy is retained by the customs office at which the goods enter the transit system. The haulier presents the remaining documents and the goods at the customs office where the goods enter into use or consumption in the Community, or from where they are to be exported. The customs office endorses the transit document with its own stamp and returns one copy to the customs office where the movement started. The two copies are matched to confirm the movement has been properly completed. If, after a prescribed length of time, the first copy remains unmatched an inquiry procedure is initiated to establish what has happened to the goods.

6 In their report the European Parliament noted that there were a number of major identified problems within the current customs transit systems which have facilitated their misuse. They recommended a series of reforms to establish a framework for addressing these weaknesses. They did not however deal with short term measures or the technical details of how the transit regulations and procedures might be amended. They saw this as the function of the European Commission's review which was being undertaken alongside the Committee's inquiry. The European Commission produced a plan of reforms which took account of many of the recommendations of the European Parliament, as well as suggesting detailed interim measures. The European Commission subsequently incorporated many of these proposed reforms into draft legislation which is now passing through the normal legislative process.

7 Transit fraud occurs when goods, on which customs duties, excise duties or VAT have not been paid, are placed (or diverted) onto the internal Community market. The fraudster's profit lies in the difference between the duty-free price at which the goods were obtained and the price obtained for them on resale, usually on the black market. This latter price will be lower than the tax-paid price, in order to create an incentive to buy, but can still be considerably higher than the duty-free price.

8 The United Kingdom's involvement in customs transit is relatively minor with it accounting for approximately two per cent of Community movements. The United Kingdom is unlikely to have suffered from fraud to the same extent as some other Member States. Nevertheless the present weaknesses in the system have a significant impact upon the Community budget and are therefore a concern to all Member States. In addition the administrative arrangements for customs transit represent a significant burden for HM Customs and Excise, so it is important that the arrangements should become both more efficient and effective.

9 This Report examines the recommendations of the European Parliament and the European Commissions' proposals for reform. It focuses on the impact of the problems in the United Kingdom and the extent to which the United Kingdom has contributed to the reform of the transit arrangements and any United Kingdom views on constraints to progress. The Report covers:

- access to the Community transit system and debt recovery;
- preventive control measures;
- fraud investigation and prosecution of offenders;
- computerisation;
- streamlining administrative procedures.

Access to the Community transit system and debt recovery

10 The European Parliament made the following recommendations:

- "admission to the transit system should be limited, particularly in relation to sensitive goods, such as cigarettes and alcohol, with reliable operators being granted reduced guarantee obligations;
- the guarantee system must be reformed, spreading responsibility to owners and transporters of goods, refining the mechanism to take account of the degree of security provided for the goods, and extending it to cover forms of transport other than road, especially sea transport;

- customs administrations should agree a suspension of outstanding claims of repayment dating before the introduction of the 100 per cent guarantee for sensitive goods, pending agreement on a proposal for writing off outstanding debts where these can be shown to be the result of maladministration”.

11 The European Commission are in the process of redefining who can use the Community transit system and what criteria operators must satisfy to become authorised Principals. They will also be seeking to assign more fairly the liability for revenue debts. They have rejected the blanket writing off of revenue debt, suggesting that each Member State should instead use its discretion and consider each case on its own merits.

12 HM Customs and Excise see the authorisation procedure as an appropriate means of identifying reliable Principals who will have access to simplified procedures and reduced guarantees. They have already put in place debt recovery operations which they believe are equitable within the bounds of cost effectiveness and current regulations. HM Customs and Excise support the Commission’s review of air and rail movements but would, in the absence of evidence to the contrary, wish to retain the current arrangements which provide major benefits to Community traders and customs.

13 In general transit fraud does not appear to be as great a problem for the United Kingdom as it does for some other Member States. Significant cases may arise, however, and at the time of this report HM Customs and Excise had detected, and were participating in the multinational investigation of a complex case of cigarette fraud centred on Germany. In pursuing this case HM Customs and Excise identified the fact that existing measures for securing United Kingdom excise duty for movements of goods in the Single Market did not adequately cover certain Community transit procedures. To rectify this situation the Excise Duty Point (External and Internal Community Transit Procedure) Regulations 1998 were made on 3 February 1998. The Regulations are not retrospective and therefore do not apply to the case mentioned above.

Preventive control measures

14 The European Parliament made the following recommendations:

- “a system of physical checks must be developed which is based on a common system of risk analysis, with comparable facilities being made available in EU ports as well as at important land frontier crossing points; and

- the customs code should be amended to permit spot checks anywhere within the territory of the EU rather than only at frontiers”.

15 The European Commission are proposing several measures to ensure secure movement of goods and setting up a Community risk analysis unit to compile risk profiles and thus enable customs services to define precise criteria for targeting inspections. They are also proposing to evaluate and coordinate customs services’ resource management, and to conduct a study of the role and power of customs officials.

16 HM Customs and Excise are in favour of some aspects of the Commission’s proposals on risk analysis and resource management but have some concerns over the loss of national prerogative in these areas. They are more in favour of encouraging best practice and greater efficiency across Member States. They are also concerned that some of the Commission’s proposals for secure movement may prove impractical. HM Customs and Excise consider they have an adequate range of powers, unlike some other customs services which, for example, are unable to conduct investigations.

Fraud investigation and prosecution of offenders

17 The European Parliament made the following recommendations:

- “the European Union must establish a framework for customs services leading to national customs services functioning as if they were one; a common customs investigation service should be created, based on the existing anti-fraud unit of the Commission (UCLAF);
- contacts between national prosecutors must be intensified with the creation of a European legal directory of contact prosecuting officers in the Member States, with formal procedures applying to requests for legal assistance between Member States being simplified and accelerated; in this context UCLAF should be able to initiate criminal proceedings and to give evidence in court on the same basis as national authorities;
- mechanisms must be established to ensure the “mutual recognition of evidence” across the European Union; to this end a European legal “clearing house” could and should be established at the earliest opportunity; and

- the 10 per cent retained by Member States to cover the collection costs of own resources should be directly set against their efforts to protect the financial interests of the European Community”.

18 The European Commission are proposing to address the problems of detecting and dealing with transit fraud through setting up Community level investigative bodies; greater customs co-operation; the ratification of the convention for the protection of Community financial interests by mid 1998; and a study of judicial systems. The Commission have yet to set out in detail their proposal regarding the Community investigative bodies. The UK Government’s position, which was explained to Parliament in Explanatory Memorandum Reference No. 7862/97, is to oppose the creation of a single Community investigation service. Given the potential difficulties such a service would have operating across 15 different legal and judicial systems, the UK Government believes the problems within customs transit could be better addressed through improved co-operation between Member States.

19 The Commission’s study of European judicial systems would cover the European Parliament’s recommendations for a directory of prosecuting officers, mutual recognition of evidence, a clearing house pending mutual recognition, questions of jurisdiction and the legal recognition of UCLAF. Under UK law, HM Customs and Excise already have jurisdiction over serious offences committed elsewhere and they are particularly interested in the mutual recognition of evidence. Although they recently experienced some failed prosecutions on technical grounds, due to the inadmissibility of other Member States’ certificates of corresponding law, HM Customs and Excise are confident these difficulties will be overcome and that they will achieve a successful prosecution in the future. HM Customs and Excise have appointed fiscal liaison officers in a number of other Member States to facilitate the solution of problems in fraud investigation and prosecution.

Computerisation

20 The European Parliament recommended that:

- “comprehensive computerisation of the transit system, long overdue, must be implemented as rapidly as possible, whilst recognising that it is not in itself an anti-fraud measure: greater attention should also be paid to complementary technological options for the management of transit”.

21 Computerisation of the Community transit system was initially proposed by the European Commission in 1991. It is an essential part of the Commission's reform of transit and is fully supported by HM Customs and Excise. When fully and appropriately implemented, it will solve many of the procedural problems associated with transit and will provide an opportunity for introducing new and better controls. It will also remove much of the scope for existing fraud, though it cannot be expected to eliminate fraud. Although current difficulties with the project may lead to only partial implementation initially, nonetheless this should enable Member States to apply resources more effectively to remaining paper transactions and to those aspects of the system where problems of illegal diversion had previously been experienced.

Streamlining administrative procedures

22 It was not the intention of the European Parliament Committee of Inquiry to consider and recommend short-term corrective measures. They saw their rôle as identifying areas in which reforms could be proposed, and establishing the framework for such reforms. They saw interim reforms to minimise the level of fraud as the function of the Commission. Many of the problems of transit stem from a failure to properly apply current procedures. These are likely to be eliminated once the system is computerised, but computerisation is a medium to long term project. In the meantime action needs to be taken to make the current procedures more effective.

23 The European Commission have made proposals with respect to:

- the reorganisation of customs administrations;
- clarifying Principals' responsibilities for supervising transit operations;
- cooperation between customs administrations;
- the training of customs officials; and
- the drafting of a transit handbook.

24 These proposals are in general supported, and in some cases reflect action already taken, by HM Customs and Excise. HM Customs and Excise currently employ some 52 staff in their Central Community Transit Office, at a cost of about £775,000 per annum, to run the key aspects of the administration of the customs transit systems within the UK. HM Customs and Excise have taken a number of

initiatives to further improve administrative procedures, but are concerned that any actions sought by the Commission should be geared to an assessment of risk and avoid undue constraint over national procedures.

Other recommendations of the European Parliament

25 The European Parliament also recommended that:

- “the Joint Committee on Common Transit bringing together 23 countries should establish a working group to examine the ways in which the trade in cigarettes can be made more transparent particularly in terms of the chain of ownership, as well as what sanctions should be taken against those involved in the illicit trade in cigarettes; and
- firm Community action is required with regard to the countries whose legislation contributes to the problems encountered in the transit system, in particular Switzerland and the issues of ensuring adequate levels of control should feature in accession negotiations with the countries of Central and Eastern Europe and Cyprus”.

26 As these recommendations are considered by the Commission to require further input at the political level within the Community, they have not addressed them in their current action plan. The National Audit Office have therefore excluded them from the scope of this review.

General conclusions

27 When the Community transit system was originally set up it covered six countries, three of which were already in a customs union, and a volume of trade which was far less than it is today. Since then the system has been extended to a further nine countries of the European Community, and through the common transit system to four EFTA and four Visegrad countries. At the same time the volume of trade has increased substantially. The system was never designed to cope with these circumstances and as a consequence it suffers from inherent weaknesses, in particular its dependence on the return of documents, recognition of the many thousands of customs stamps used to endorse them, and the operation of the procedure for following up missing documents. Weaknesses in the system have permitted fraud, resulting in losses to national and Community budgets. In their report the European Parliament recommended a series of reforms to the customs transit systems. These were taken forward by the European Commission in their action plan, though not all of their proposals are yet fully developed.

28 The National Audit Office agree with HM Customs and Excise that, in the medium to long term, computerisation has the potential to solve many of the procedural and security problems of the customs transit systems whilst improving the anti-fraud operations, and that, in the short term, customs services need to apply the transit procedures properly, in particular the return of key documents and the operation of the procedure to follow up missing documents.

29 The National Audit Office also support HM Customs and Excise's view that improved cooperation between customs services is essential if the limitations imposed by differing legal systems are to be overcome. Combined action is frequently necessary to identify the organisations committing the frauds, to collect sufficient, reliable evidence to convict them and to bring about successful prosecutions through national courts. Progress has been made in mutual assistance between customs services, new investigative powers have been given to the Community's fraud investigation body, UCLAF, and a target set for the ratification of the convention for the protection of European Community financial interests. Mutual recognition of evidence, however, remains a major issue to be considered by the Commission's proposed study.

30 Whilst the United Kingdom's involvement in customs transit is relatively minor and the impact of fraud is less of a problem than for some other Member States, major cases of fraud can arise and HM Customs and Excise have stated that they will continue to devote appropriate resources to supporting the transit system and will remain vigilant in the fight against fraud.

Part 1: Introduction

The European Parliament's inquiry

1.1 From early 1995, the European Parliament, the European Commission and the European Court of Auditors became increasingly concerned about the level of customs transit fraud within the Community and the ease with which it could be perpetrated. As a result in December 1995, the European Parliament set up a Committee of Inquiry to examine alleged contraventions or maladministration in the Community transit system, the main form of customs transit. This was the first such committee of inquiry established by the European Parliament. During the 13 months from January 1996 to February 1997 the Committee of Inquiry investigated the reasons for the perceived crisis in the transit system, the shortcomings and loopholes in procedures and the measures to be taken to improve those procedures. The Committee of Inquiry took evidence from all Member States, including detailed questionnaires, and canvassed both oral and written views from other interested parties.

1.2 In their report, which was adopted by the European Parliament on 19 February 1997, the Committee sought measures to restore the economic advantages of customs transit whilst providing mechanisms to ensure better protection against the risks involved. They concluded that:

- the transit system is an archaic paper-based procedure, vulnerable to fraud;
- transit fraud is committed by international crime, whose main target is cigarettes, and has caused losses of several billion ECU to national and community revenues;
- some customs services are using the Principals' guarantees solely as a form of insurance and are failing to tackle the defects in the system. As a result Principals are suffering losses;
- efforts to control customs transit fraud have displaced criminal activity into more traditional forms of customs crime; and
- differences in national and legal systems and diverging standards of evidence make prosecutions across frontiers difficult.

The European Parliament put forward 12 main recommendations relating to customs transit, on which this report is based.

1.3 The European Commission have also addressed the transit problems. This started with their comments, in the 1994 annual report, on the fight against fraud with particular reference to the Community transit system. In March 1995, the Commission issued a document to the Council and the European Parliament entitled “Fraud in the Transit Procedure, Solutions Foreseen and Perspectives for the Future”. It drew attention to the serious level of fraud taking place in transit and described the action already being taken to tackle it. Then, alongside the work of the European Parliament, the Commission undertook their own major policy review of customs transit. In October 1996 they produced an interim report setting out further possible reforms of the system. A six month consultation period followed after which, in April 1997, the Commission drew up a plan to translate the European Parliament’s recommendations into a “thoroughgoing, balanced and realistic reform of customs transit systems”. The plan takes account of many of the recommendations of the European Parliament. The plan was also seen as “providing a basis and permanent point of reference for the range of proposals that the Commission will put forward and initiatives that it will take”. Many of these proposals were taken one step further through draft legislation introduced by the Commission in July 1997. Although the fraud problems affect all Member States, it appears they principally have their cause and effect outside the UK. The UK does, however, contribute to the resolution of the Community problems and offers views on any constraints to progress.

What is customs transit?

1.4 In normal circumstances goods entering a Member State of the Community are liable for charges of customs duties, excise duties and VAT in line with the Community’s customs policy and the Member States’ fiscal policies. These charges would normally be paid on import. In order to facilitate trade a system known as customs transit allows goods to be imported with the temporary suspension of these charges until those goods reach either their point of destination in the Community or are exported from the Community. The charges are safeguarded, however, by the imposition of guarantee arrangements, which enable the customs authorities to collect the duties and taxes, if the goods are subsequently used or consumed within the Community. The goods are considered to be under customs control whilst in transit and they have to be strictly accounted for. The rate of national duties and taxes is determined by the country of final destination. The suspension of duties and taxes remains in place until the goods:

- enter into free circulation within the Community and are available for use or consumption after the payment of the appropriate national duties and taxes; or

- arrive at their EFTA or Visegrad destination and are similarly available for use or consumption; or
- are exported from the Community to other countries. Where certain Community agricultural goods leave the Community, export refunds under the Community's Common Agricultural Policy may be payable.

1.5 Customs transit has two main functions. Firstly, it tries to reconcile the needs of honest traders, with their aims of competitiveness and reducing operating costs, with the effective control of international transactions aimed at protecting the internal economy of the Community. Without such a process, it would not be possible, for example, for goods coming from outside the Community and destined for another country also outside the Community to pass through the Community untaxed. The unattractive alternative is for the goods to be subjected to duty and tax at the appropriate rates for each member country at import and for the appropriate refund to be claimed at export. The avoidance of this alternative is an international commitment originally framed under the General Agreement on Tariffs and Trade. Secondly, with customs clearance facilities available away from borders, customs transit enables customs controls to be concentrated at the inland office of destination or the importer's premises. This thus avoids congestion at the Community's external border crossings and ports.

1.6 Customs transit was first introduced at the international level by the Transport Internationaux Routiers (TIR) Convention of 1948. When the Community's Common Customs tariff was created in 1968, the TIR system had to be supplemented so that a distinction could be made between three classes of goods:

- those imported for use or consumption in the Community on which customs duties had been paid;
- goods produced in the Community in free circulation and available for use or consumption after payment of duties and taxes; and
- imported or community goods, travelling through the Community, on which both customs duties and indirect taxes were potentially due but not yet paid.

Thus the Community transit system was set up for the then six (now 15) Member States of the Community. It is currently framed under Council Regulation (EEC) 2913/92 which established the Community Customs Code and Commission Regulation (EEC) 2454/93 implementing that Code. Over the years the Community transit system has been extended in the form of the Common Transit Convention to encompass the EFTA and Visegrad countries.

1.7 Typical examples of transit movements are detailed below. These cover goods imported for use in the Community and goods carried through the Community.

Example 1 Goods imported into the Community for use

Goods originating in Japan, imported by a retailer in Rome enter the Community at Hamburg. In Hamburg they would be loaded into a lorry for road transport to Rome. Under customs transit, duties and taxes are not payable in Hamburg, but in Rome where and when the goods are entered into free circulation for use in the Community.

Example 2 Goods imported into the Community for export

Goods, imported from the United States by sea, enter the Community at Rotterdam for onward transport to North Africa. In Rotterdam they would be loaded onto a lorry for road transport to, say, Marseilles for shipment to North Africa. Under customs transit no duties and taxes would be payable where re-export of the goods is confirmed.

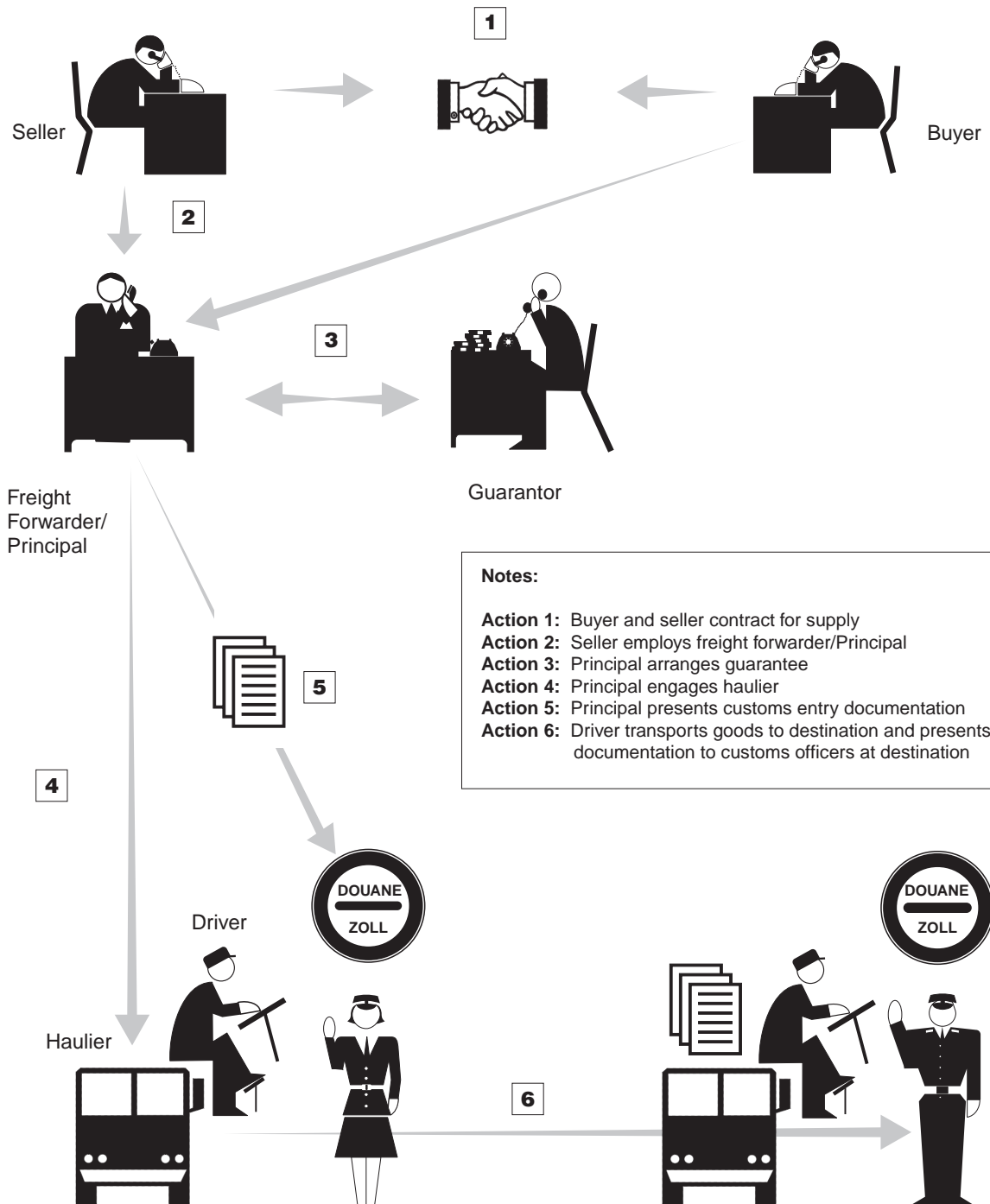
How the transit systems work

1.8 The Community and common transit systems operate in the same basic way. The goods are transported free of duty and taxes until their final destination. Under Community regulations customs authorities require the transit movement to be the responsibility of an individual or company, usually a freight forwarder, who is known as the Principal. The Principal is responsible for arranging the appropriate level of guarantee with a bank or an approved guarantor to cover the consignment, and for the submission of the appropriate transit and supporting consignment documents.

1.9 Although customs transit takes place as a result of a normal trade purchase and sale transaction, it will have little impact on the existing or intended owners of the goods, unless they also have a dual capacity with one of the other main roles; ie Principal, guarantor or haulier. Typically the seller or buyer of the goods will employ a freight forwarder as an agent to act as the Principal for the transit movement. The Principal will arrange for the goods to be physically moved from a port or warehouse by a road haulier. As previously mentioned the Principal is also responsible for

Figure 1

Main participants in Community transit procedures



arranging the guarantee and submitting the necessary paperwork for the movement to the customs office of departure. The drivers employed by the road haulier have the responsibility of carrying the transit documents for the movement and ensuring that the appropriate parts are handed in at the office of destination, although the ultimate responsibility falls back upon the Principal. The final participants in the transit chain are the customs officials at the offices of destination for the stamping of the documents and at the office of departure for the matching of the documents (see also Figure 1).

1.10 The transit document is a multi-part form, commonly called the Single Administrative Document (SAD). One copy (copy 1) is kept at the customs office from where the goods enter the transit system (the office of departure) and a further copy (copy 5) is subsequently returned from the customs office where the goods enter into use or consumption or are exported (the office of destination), duly stamped. These two copies are matched at the customs office of departure to confirm the completion of the transit movement, as detailed in Figure 2.

Inquiry procedures

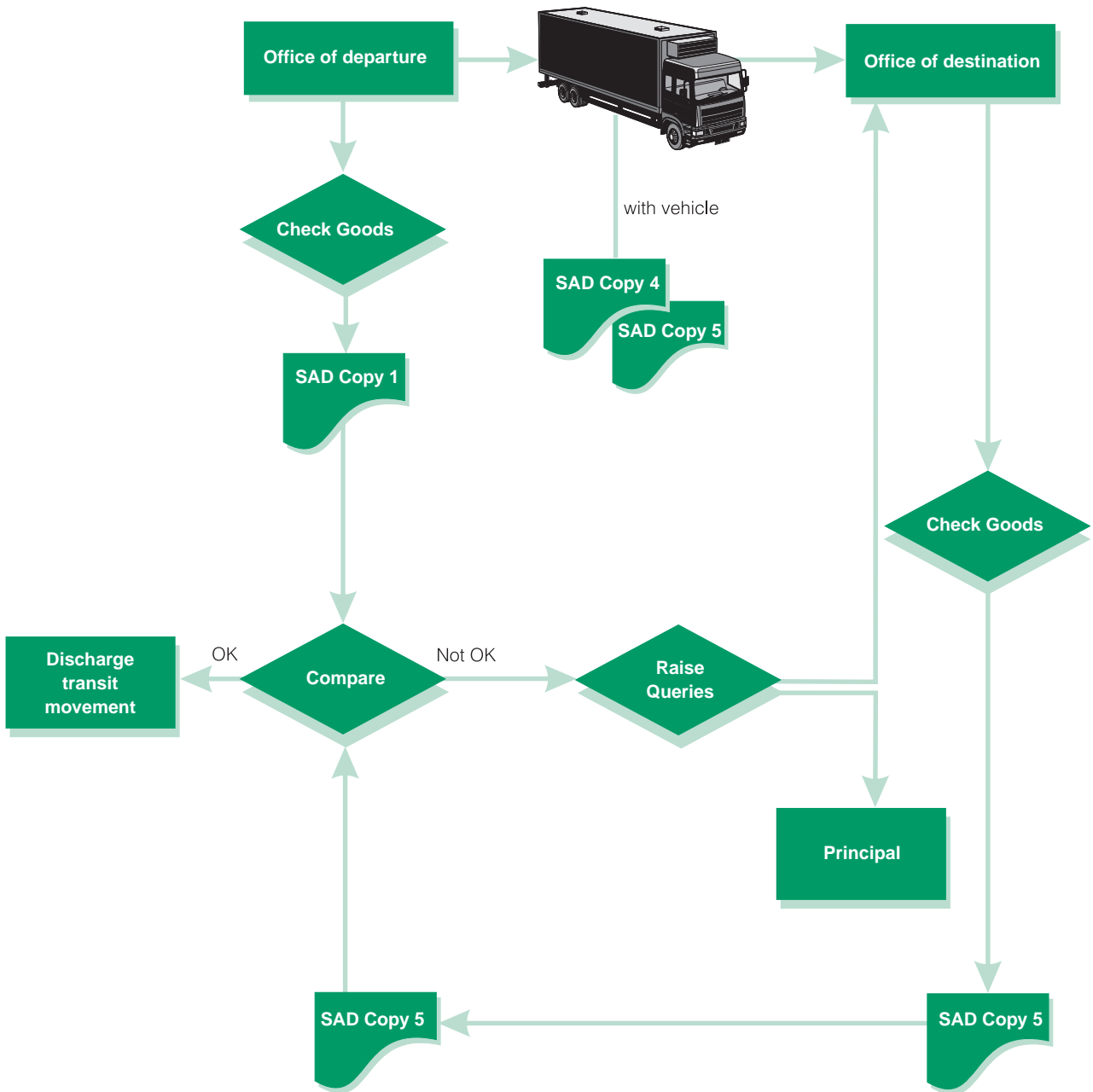
1.11 If, after prescribed lengths of time, the office of departure has not received notification that the transit movement has been completed, or there are doubts about the veracity of the completion, for example where a false or inappropriate customs stamp appears to have been used, then queries are raised with the customs office of destination and the transit Principal.

1.12 The inquiry procedure starts with the office of departure asking the office of destination for confirmation that the goods have cleared customs. If it is unable to do so, the office of departure then has the responsibility for establishing what has happened to the goods: for instance there may have been a change of destination. If it appears they have not cleared customs in a regular fashion, they are assumed to have improperly entered the Community market.

1.13 At this point, the office of departure has the responsibility of establishing where the irregularity took place, because the responsibility for investigating the irregularity and recovering the lost revenue lies with the Member State in which the goods were diverted. If it proves impossible to identify where the irregularity took place, the office of departure takes action to recover the lost revenue from the Principal and/or guarantor.

Figure 2

Schematic diagram of customs transit movements



Source: National Audit Office

1.14 The procedures for carrying out an inquiry are set out in the European Commission compendium of administrative arrangements. These can be seen diagrammatically in Appendix 1.

Guarantees

1.15 Under Community transit and common transit the guarantee can be:

- **comprehensive**, to cover any number of transit movements by a single Principal. In response to the worsening transit fraud situation, a regulation was adopted in October 1996 to raise the existing comprehensive guarantee from 30 per cent of the duties and other charges payable in one week up to 100 per cent of the duties and charges payable. However, the text of the regulation still allows the 30 per cent comprehensive guarantees for less sensitive goods where, for example, there have been no infringements by the Principal within the last two years;
- **individual**, to cover a single movement comprising the total tax value of the goods involved. Early in 1996 a decision was taken to prohibit the use of comprehensive guarantees for so called “sensitive goods”, for example, those with high excise and tax value such as cigarettes and alcohol. It introduced the requirement for an individual guarantee for each movement of these goods covering the full amount of customs excise, duty and VAT payable; or
- **flat-rate vouchers** of ECU 7,000 each.

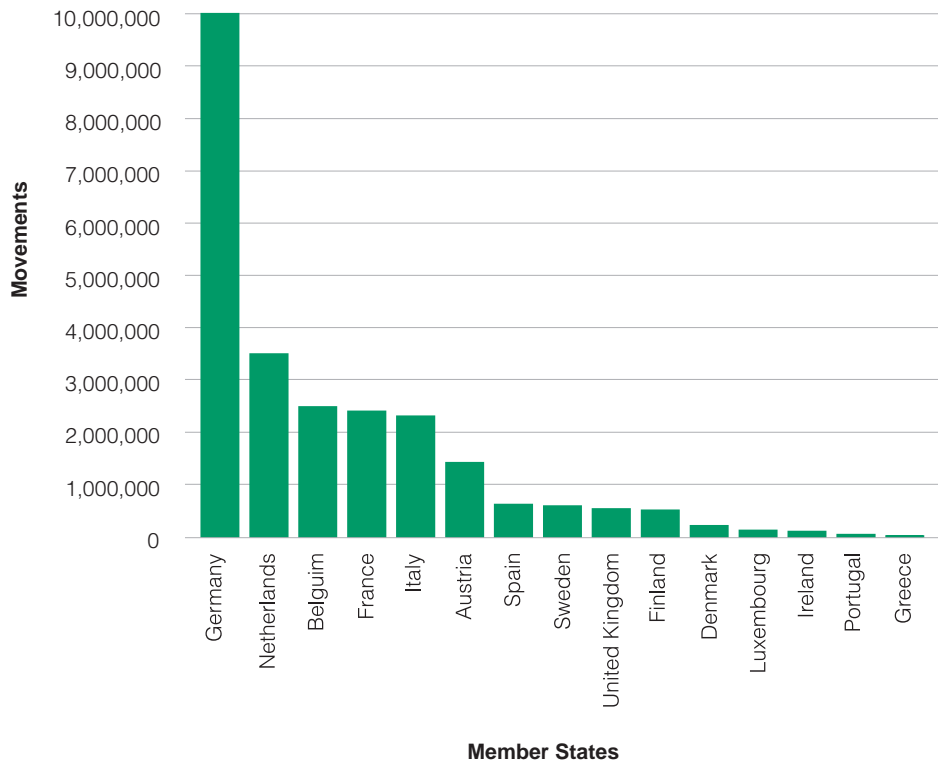
A guarantee may take the form of a cash deposit at the office of departure or, more usually, a legally enforceable undertaking by a third party guarantor (usually a bank or insurance company).

Transit activity

1.16 Whilst the main principles of the transit system have remained unchanged since it was set up, the European Community has expanded to include 15 Member States and the volume of trade between European countries increased dramatically. There are some 15 to 18 million Community transit documents issued in Europe every year. These documents cover vast quantities of goods, account for billions of ECU in duty and taxes destined for both Community and national budgets, and include both goods entered into free circulation in the Community and those passing through the Community. However the distribution

Total community transit movements during 1995 by Member State

Figure 3



Source: European Parliament Committee of Inquiry Report

There is an uneven incidence of transit movements in the Community.

United Kingdom transit movements 1993 to 1997

Figure 4

Year	Transit movements finishing in the UK ('000)	Transit movements commencing in the UK ('000)	Total ('000)
1993	189	249	437
1994	201	368	569
1995	177	343	520
1996	177	376	553
1997	201	261	462

Source: HM Customs and Excise

UK transit movements have been approximately 500,000 in each of the last 5 years.

of the transit movements across Member States is uneven. Owing largely to patterns of trade and geography, two Member States, Germany and the Netherlands, accounted for some 13.4 million transit movements in 1995, or approximately half of the total movements, (Figure 3). By comparison, the UK experiences relatively little transit traffic with around 500,000 annual movements, or some two per cent of total transit traffic in the Community, (Figure 4).

Transit fraud

1.17 Transit fraud exploits the difference between the duty free and duty paid price of goods being transported. Thus goods with a ready market including the shadow economy and subject to higher rates of duty, such as alcohol and tobacco, carry a greater risk of fraudulent diversion. Other factors such as the avoidance of licensing controls may also increase the risk of transit fraud.

Who pays?

Public revenue

1.18 Customs duties are payable to the European Community budget, less 10 per cent “collection fee” for Member States’ customs services. Excise duties and VAT are payable to the Member State in which the goods are placed in free circulation or use. A proportion of the VAT is payable to the European Community. The cost of transit fraud is borne partly by the Member States and partly by the Community, but ultimately by the generality of Community tax payers.

1.19 Where frauds are detected, the lost revenue can theoretically be recovered through the Principal’s guarantee. However the guarantee may not always cover the full amount outstanding, particularly if a comprehensive guarantee is used and a number of frauds have been committed against it. Also, it may be impractical to recover the full amount from the Principal and the guarantor and so the customs authority may have no alternative but to write off the loss.

The trade

1.20 In addition to the perpetrators of a fraud, the Principal is equally liable for the customs duties, excise duties and VAT regardless of the amount of the guarantee. If he does not pay, the customs authority call on the guarantee, though the Principal remains liable to the guarantor for the full amount of the guarantee. The Principal remains liable to the customs authority for any amount not covered by the guarantee.

Transit fraud mechanisms

Non-completion of transit procedure

1.21 The simplest method of committing a transit fraud is to cause the goods to “disappear” somewhere between the office of departure and the office of destination. Many of the frauds perpetrated have involved the repeated non-completion of a series of similar transit movements before the customs inquiry procedures begin. Given the openness of Community borders, and the absence of prescribed itineraries, a vehicle may travel anywhere within the Community and not be committing an irregularity. Vehicles have up to eight days to complete their journey and customs authorities normally allow a minimum of ten weeks before initiating enquiries. For goods classified as high risk there are additional procedures which should enable Member States to identify non-completion of procedures earlier.

Fraudulent completion of transit procedures

1.22 This involves using either a forged customs stamp or a stolen customs stamp on the copy 5 of the Single Administration Document. Factors which facilitate this fraud are:

- there are thousands of different customs stamps, so a forged or stolen stamp is unlikely to be detected, allowing the fraud to be repeated indefinitely; and
- unless discovered, it will not give rise to any claim in the Principal’s guarantee.

Again the fraud may involve a series of similar transit movements.

Fraud involving the guarantee

1.23 This takes the form of a forged guarantee certificate. In these cases, the customs authorities have no valid guarantee from which to collect any duties and taxes evaded.

Fraud involving the misdescription of goods

1.24 Since the introduction of the individual guarantee for sensitive goods, a further type of fraud is re-emerging: the misdescription of goods such as to place them in a lower risk category. This avoids the financial liability arising from sensitive goods and the extra attention of customs services which such goods attract.

Who are the fraudsters?

1.25 Evidence to the European Parliament showed that most transit fraud is considered to be carried out by organised crime. The same persons, the same routes and the same methods are used to commit transit fraud as are used in the traffic of drugs and arms. The organisers of the fraud usually work through shell companies operating from “brass plate” addresses. Frequently the organisations behind these companies are based in non EU countries offering favourable tax regimes and secretive banking laws. Consequently it is difficult to trace and investigate large scale fraud. A successful fraud usually involves one or more of the following: drivers, hauliers, freight forwarders, warehousekeepers or customs officials.

Effect of transit fraud

1.26 The European Commission have estimated that over ECU 1.27 billion was lost to revenue in the seven year period 1990-1996 of which ECU 784 million was in national taxes. In 1996 alone ECU 294 million was lost of which ECU 216 million was in national taxes (mostly due on cigarettes). The Commission believe, however, that the full extent of fraud is almost certainly far greater than these estimates.

The Single Market

1.27 The completion of the Single Market, with effect from 1 January 1993, with the removal of internal customs frontiers has had a major impact on the control of customs transit. Prior to 1993 it was possible to monitor the passage of transit vehicles through Member States by the paper documents presented at each border crossing. This is no longer possible and the freedom of movement can be used to exploit weaknesses in the transit systems for financial gain. For some time, the gains from doing so were sufficient to bring about a switch from the more traditional smuggling of high value excise commodities such as cigarettes and

alcohol, to transit fraud with these commodities. There is now evidence to suggest that, following the tightening up of guarantee procedures in 1996, there has been a reversion to more traditional smuggling methods.

Scope of examination and audit approach

1.28 Against this background the National Audit Office examination has followed up the issues raised by the European Parliament Committee of Inquiry report on the Community transit system and the European Commission's action plan for Transit in Europe. The examination has focused on the impact of the problems of customs transit; the extent to which the United Kingdom has contributed to the solutions; and the constraints to progress as seen from the United Kingdom perspective.

1.29 The examination has been concerned with customs transit systems addressed by the European Parliament's report and the Commission's action plan: Community transit and common transit. It has focused on the following main areas which have been identified in the two European reports and these are covered in Parts 2 to 6 of the report as follows:

- Part 2: access to the Community transit system and debt recovery - changes to the facilities for Principals, including the guarantee arrangements and the constraints to be imposed on them, based on the degree of risk involved;
- Part 3: preventive control measures - the regime of physical checks applied by Member States;
- Part 4: fraud investigation and prosecution of offenders - the treatment of detected fraudsters and other legal reforms required to harmonise powers across the Community;
- Part 5: computerisation - the replacement of the paper documentation by national computer transit systems; and
- Part 6: streamlining administrative procedures - changes to the current transit procedures.

For completeness, Part 7 details the other two main European Parliament recommendations which have not been taken forward directly by the Commission's action plan.

1.30 The National Audit Office examination highlights the extent to which the United Kingdom is committed to the implementation of the reforms and can demonstrate that commitment through actions already taken and proposals for future action. The examination has also taken into account consultations with some UK trade associations.

Part 2: Access to the Community transit system and debt recovery

The European Parliament recommendations were:

- "admission to the transit system should be limited, particularly in relation to sensitive goods, such as cigarettes and alcohol, with reliable operators being granted reduced guarantee obligations;
 - the guarantee system must be reformed, spreading responsibility to owners and transporters of goods, refining the mechanism to take account of the degree of security provided for the goods, and extending it to cover forms of transport other than road, especially sea transport;
 - customs administrations should agree a suspension of outstanding claims of repayment dating before the introduction of the 100 per cent guarantee for sensitive goods, pending agreement on a proposal for writing off outstanding debts where these can be shown to be the result of maladministration."
-

Problems

2.1 Much of the thrust of Community policy over the last two decades has been to favour free trade and facilitate the easy exchange of goods between Member States and with other countries. In implementing procedures such as Community transit there has to be a balance between facilitating business while limiting the risks and retaining a degree of control.

Access to the Community transit system

2.2 Under the Community transit procedures, someone has to take responsibility for producing the goods, and the relevant documentation, to a customs office in another Member State. This person is known as the Principal. The transit regulations do not specify who a Principal should be, as long as they can provide a sound guarantee. Freight forwarders act as Principals as one of the services they provide to importers and exporters. The European Parliament stated that in the past it was possible to criticise freight forwarders for accepting business without due care as to the identity of their clients or the purpose of the transit movements. Since the introduction of the individual guarantee, however, freight forwarders have become more cautious about acting as Principals.

Guarantees: concerns of the trade

2.3 Under the regulations, when a fraud has been committed the Principal is equally liable for the revenue debt as is the perpetrator of the fraud or his accomplices. Principals claim, however, that some Member State customs services are not fully investigating suspected frauds, with the result that Principals are being called upon to meet the total liability. Moreover, the Principal is liable for the total amount of customs duties, excise duties and VAT regardless of the amount of the guarantee. Even where the authorities recover the amount of the guarantee from the guarantor, the Principal remains liable to the guarantor for the full amount of the guarantee.

2.4 The trade are concerned that, even for the majority of movements where no claim is made against a guarantee, the arrangement costs of guarantees are an extra financial burden without the benefit of combating fraud. They feel they are suffering the consequences of defects in the transit system and in the customs services managing it. Evidence given to the European Parliament, however, suggested that the introduction of individual guarantees for high risk goods such as tobacco and alcohol, has led to a substantial fall in the level of transit fraud, although the European Parliament observed that this mechanism appears “to be a sledgehammer to crack a nut”.

2.5 Under the current regulations the Principal is wholly responsible for any revenue debt arising out of the movement of goods, whereas those organisations with a major financial interest in the goods, the seller, the buyer and the transport companies, have no legal responsibility for the debt. Consequently when giving evidence to the European Parliament, Principals recommended a wider spread of liability for suspended taxes, duties and excise amongst those with a financial interest in the goods being moved.

Debt recovery

2.6 If a customs office of departure has not received a returned copy 5 within about 10 weeks, it should initiate an inquiry to establish what has happened to the goods. The European Parliament have described the inquiry procedure as slow and cumbersome. Simple inquiries can take months to process and thus a series of frauds can be committed before the inquiry procedure detects the first fraud, by which time the fraudsters may have covered their tracks. Also delays in returning copies 5 have led to unnecessary inquiry procedures and a waste of customs time and resources.

2.7 Where an irregularity has occurred, the practical difficulties of establishing and proving where an offence took place are immense. Vehicles are generally considered to have up to eight days to complete their journey, do not have to follow a prescribed route, and usually have the option to change the office of destination without prior notice to the customs authorities. In these circumstances, a vehicle may “disappear” at will almost anywhere in the Community. In such cases, the customs services usually claim the lost revenue from the Principal and failing that from the guarantor.

2.8 Where action is taken against the perpetrators of a fraud, there have been problems in interpreting those parts of the Customs Code dealing with the recovery of the revenue debt. The Code does not make clear how, and to what extent, recovery action should be taken against fraudsters as opposed to the Principal.

Other related concerns

2.9 **System weaknesses** - The inherent weaknesses in the transit system make it susceptible to a degree of administrative error, which can lead to a substantial waste of time and resources spent chasing up lost documentation.

2.10 **Movements by air, rail and sea** - The majority of transit movements are made by road but some are made by air, rail and sea. Most non-road movements are carried out under simplified procedures not requiring a guarantee because the risks of irregularities are considered to be greatly reduced. The European Parliament believe that fraud is extending to non-road transport although little is known about the extent to which it exists.

Impact on the United Kingdom

2.11 On the basis of transit frauds which they have been involved in investigating in the period 1991 to 1996, HM Customs and Excise have estimated that fraud against the United Kingdom and other Member States' revenues is over £321 million (or ECU 406 million) calculated at the appropriate rates of national taxes. Just over £22 million (or ECU 27 million) of this amount (or seven per cent) related to fraud arising in the United Kingdom, mostly for cigarettes (see Figure 5). At 31 December 1997, HM Customs and Excise recorded a potential liability of some £6.6 million of customs duty and VAT outstanding under Community transit arrangements.

**Transit fraud
investigations involving
HM Customs and Excise
1991 to 1996**

Figure 5

Revenue evaded in:	Total Duties/Taxes		Cigarettes
	£ million	per cent	£ million
United Kingdom	22.1	7	21.7
Other Member States	299.3	93	241.0
Total	321.4	100	262.7

Transit frauds having an impact on United Kingdom revenues have been a small proportion of the total for the Community and there has been a high preponderance of cigarettes as the commodity on which the fraud was based. Some of these cases are still under investigation or awaiting prosecution.

Source: HM Customs and Excise

2.12 HM Customs and Excise calculate and record outstanding liabilities for customs duties, excise duties and VAT at the point at which they write to Principals requesting payment. The early stages of the inquiry procedure may produce little response from Principals, and it is often not until a letter requesting payment of liabilities is issued that Principals produce evidence to show that the movement of goods was properly completed. HM Customs and Excise have told us that in 1996-97, they issued around 800 letters requesting the payment of outstanding liabilities. During the same period, there were 600 cases where liabilities were cancelled after a letter was issued because evidence was produced to demonstrate the liabilities had already been paid.

2.13 In general transit fraud does not appear to be as great a problem for the United Kingdom as it does for some other Member States. Significant cases may arise, however, and at the time of this report HM Customs and Excise were participating in a multinational investigation of a complex case of cigarette fraud centred on Germany. Having detected the fraud, the United Kingdom remains involved because about a quarter of the 100 or so transit movements in question were consigned from the United Kingdom and, under European legislation, where an irregularity is known to have occurred but the place cannot be established, the irregularity is then deemed to have occurred in the country where the transit began. The movements consigned from the United Kingdom were valued at some £2 million customs duty and some £50 million excise duty and VAT calculated at United Kingdom rates. The German customs investigators have established that 10 out of the United Kingdom movements were diverted in Germany and have taken steps to recover charges.

2.14 In pursuing the above case HM Customs and Excise identified that the measures, taken in 1992, for securing United Kingdom excise duty for movements of excise goods in the Single Market did not adequately cover certain Community transit procedures. To rectify this situation the Excise Duty Point (External and Internal Community Transit Procedure) Regulations 1998 were made on 3 February 1998. The Regulations are not retrospective and therefore do not apply to the case described above. In a small number of other cases where excise duty may have been charged erroneously and, subject to consideration of whether unjust enrichment would arise, claims for repayment will be invited. The total sum involved is unlikely to exceed £300,000 even if full repayment is made.

Proposed improvements

Controlling access to the transit system and tailoring the guarantee arrangements

2.15 To boost security, but still maintain open access to the transit system, the European Commission have proposed, in draft legislation, a two tier arrangement:

- that authorised Principals, who demonstrate they have met certain criteria (for example, they have not committed serious or repeated offences against customs or tax legislation), use the comprehensive guarantee which need not cover the full liability for customs duties, excise duties and VAT; and
- that other Principals will be expected to take out an individual guarantee covering the full liability.

The draft regulations also give customs services the legal framework to vet applicants for authorisation and to stipulate on the authorisation the amount of the guarantee. The Commission have also proposed:

- a feasibility study be carried out into providing access to information, Community wide, on unreliable Principals; and
- a study to establish the extent to which an insurance scheme for duties and taxes might be a substitute for guarantees.

2.16 HM Customs and Excise have advocated authorisation as a means of differentiating equitably between Principals. They see this as a solution to the complaint that anti-fraud measures, such as individual guarantees for the movement of sensitive goods, are applied across the board irrespective of the

known reliability of the Principal. Some UK traders, in particular the cigarette manufacturers, found the move from comprehensive guarantees to individual guarantees a heavy financial burden and would welcome such changes.

2.17 The National Audit Office agree with HM Customs and Excise that any screening criteria would need to be clear, specific, identifiable and measurable, so that Member States could apply them equitably to all Principals. Those unable to meet the criteria would have to obtain an individual guarantee for each and every movement of goods, which is costly to the Principal and an administrative burden to the customs services. HM Customs and Excise recognise that the criteria should not unduly favour large traders.

2.18 HM Customs and Excise do not advocate the creation of a black list of unreliable operators but have no objection to the Commission's proposed feasibility study. We share HM Customs and Excise's view that whereas the idea of creating a list of unreliable Principals is simple, it carries the risk of legal and practical problems such as:

- what level of involvement in fraud would justify listing (active participation, passive complicity, involvement of an employee);
- what proof of involvement would be required (conviction, customs intelligence); and
- what redress would be available to a Principal who was wrongly listed and whose business might suffer as a result.

Assigning liabilities for revenue debt

2.19 The Commission have not taken forward the European Parliament's recommendations of spreading the responsibility for revenue debt to owners and transporters. Instead the Commission have made legislative proposals for:

- setting out the Principal's responsibilities for controlling and monitoring transit movements;
- stating more clearly the Principal's liability for revenue debts, the exception being where goods have been unlawfully removed from the transit system by a third party;

- stating that where goods are unlawfully removed from the transit system, recovery should be taken first against the persons involved; and
- making the Principal liable for the balance, if the debt is not fully recovered from these persons.

The Commission have also recommended streamlining the debt recovery procedures by making a single office in each country (the Guarantee Office) responsible for debt recovery.

2.20 HM Customs and Excise accept their responsibility under the current arrangements for identifying fraud and pursuing the relevant parties. In particular, where frauds have been masterminded from the UK but committed elsewhere, they have been keen to assist other customs services in identifying and arresting the criminals involved. HM Customs and Excise already have a single office responsible for debt recovery: the Central Community Transit Office. HM Customs and Excise believe, however, that customs services must have regard to the cost of operations, and should not be expected to undertake disproportionate recovery action against those involved in irregularities before pursuing the Principal. The National Audit Office support that view.

Movements by air, rail and sea

2.21 To improve the security of transporting goods between Member States by sea, the Commission have adopted new legislation which enables authorised shipping services to be treated similarly to road transporters, with goods moving under the Community transit guarantee. The new legislation comes into force in July 1998.

2.22 For air and rail, the Commission have started a review of the current procedures to establish the risks they present and consider whether the procedures should continue in their current form. HM Customs and Excise support the review but, in the absence of evidence to the contrary, would wish to retain the current arrangements which provide major benefits to traders and customs.

Administrative errors

2.23 The European Parliament asked the Commission to consider writing off outstanding debts “where these can be shown to be the result of maladministration” and pending such arrangements, “a suspension of outstanding claims of repayment dating from before the introduction of the individual guarantee for sensitive goods”. The Commission rejected the blanket

writing off of customs duties debts. They stated that it is possible “to deal with debtors’ individual circumstances under existing provisions of the Community Customs Code covering circumstances in which no deception or obvious negligence can be attributed to the trader”. They also suggested Member States use their discretion in relation to time to pay arrangements and consider each case on its own merits. The National Audit Office believe that any blanket remission on customs debt might undermine recent progress in encouraging Principals to take their responsibilities more seriously, and note that HM Customs and Excise will operate within the Commission’s suggestions with respect to the exercise of discretion by Member States. With regard to national taxes HM Customs and Excise have discretion to write off debts.

Part 3: Preventive control measures

The European Parliament recommended that:

- "a system of physical checks must be developed which is based on a common system of risk analysis, with comparable facilities being made available in EU ports as well as at important land frontier crossing points; and
 - the customs code should be amended to permit spot checks anywhere within the territory of the EU rather than only at frontiers."
-

Problems

3.1 Goods in transit under the Community transit regime are deemed to be under customs control. They are required to be strictly accounted for and at the start of the movement are scheduled for transport to a defined destination. For sensitive goods there are Community legal requirements for providing a specific itinerary and setting the time to be taken in reaching the destination, but these have not yet been finalised and included in the Community administrative arrangements. Even if they were to be in use, variance from an agreed route, taking too much time to reach a destination, or changing the destination whilst the goods are en route may be indicative of illicit behaviour but may also be entirely innocent. The only culpable irregularity is the actual diversion into free circulation in the Community without payment of the appropriate duties and taxes.

3.2 Physical inspection of all goods would be the only way to ensure that what is declared on the transit documents is an accurate reflection of the transaction and to disclose misdeclarations. Following inspection, the sealing of containers is the preferred way to ensure identification of the goods throughout their transit movement. Not all goods are inspected, however, and the European Parliament found that the various customs services had different approaches to physical checks. They noted, from a questionnaire response from the Member States, that the level of physical inspection of transit transactions varied from 0.5 per cent to some 11 per cent. Even with risk analysis and scanning of vehicles, which increase the efficiency of the controls, physical checks were not generally conducted on a scale to deter fraudsters.

3.3 Prior to the Single Market, inspections could take place at the office of departure, the office of destination and at any of the intermediate borders. They are now primarily limited to the offices of departure and destination, although some customs services do have powers of stop and search en route. The European Parliament found that the inspection control measures were in need of improvement. To a large extent these measures are concerned with:

- checking the veracity of the customs declaration i.e. that the actual goods being transported are correctly recorded on the paper documentation;
- discovering irregularities en route as early as possible;
- locating where the irregularity has occurred; and
- taking effective remedial action as soon as possible with the consequent greater chance of success.

3.4 There has to be an appropriate balance between necessary controls and the demands of operators for the facilitation of trade. The European Parliament found that the powers of the different customs authorities to carry out inland inspections were diverse, ranging from almost unlimited powers to very heavy reliance on cooperation with the police. The European Parliament felt that the removal of internal borders within the Single Market has been used by many of the Member States to reduce customs resources to such an extent that controls were below acceptable levels.

Impact on the United Kingdom

3.5 HM Customs and Excise carry out about a two per cent physical examination of all imported goods based upon national and local risk profiles for identification of selections. This figure includes goods arriving under customs transit. These examinations can take between 10 minutes and 4 hours depending upon the degree of check. HM Customs and Excise also have powers to examine goods en route but only where they have reasonable grounds for suspicion.

Proposed reforms

3.6 The European Commission in their action plan have suggested a number of improvements to control. These include:

- several measures to ensure secure movement of goods;
- coordinated risk management and targeted checks on operations; and
- harmonisation of customs officials' powers and coordination of means and resources.

The National Audit Office agree with HM Customs and Excise that any proposed measures should be judged on the grounds of practicality and the cost effective use of resources.

Secure movement of goods

3.7 The current TIR system includes the sealing of vehicles and the display of TIR plates on vehicles. To improve the secure movement of goods under Community and common transit, the Commission have proposed in draft legislation:

- sealing for transit goods; and
- affixing “T” plates to approved vehicles.

3.8 HM Customs and Excise believe that sealing all vehicles would be burdensome and not very effective. Sealing of sensitive goods and goods attracting export refunds is mandatory under Community and common transit and HM Customs and Excise would be prepared to accept sealing for other designated high-risk goods. Some trade bodies have serious reservations about affixing “T” plates to vehicles. HM Customs and Excise also have reservations about this proposal and would not favour a system of approving vehicles as the costs of such an approval system could, they believe, outweigh the benefits.

3.9 Other measures for improving security in the movement of goods proposed in draft legislation by the Commission include:

- the Principals detailing the proposed itineraries;
- not being able to change the office of destination without prior customs approval; and
- more accurate time limits for the journeys.

Deviation from a proposed itinerary is not an irregularity and may be justified by prevailing traffic conditions at the time of the journey. But a specified transit itinerary would aid en route checking and deviations would be a prima facie indication of suspicious activity or intent. The Commission recognise, however, that this would not be practical for non-sensitive goods given the volume of such movements.

3.10 Journey times have decreased in recent times in line with the improved roads infrastructure throughout the Community. HM Customs and Excise have accordingly instructed their offices to set more realistic times for the journeys.

3.11 Some hauliers use satellite based systems to maintain their own security control over their vehicle and consignment movements. The Commission see benefit in coordinating customs surveillance measures with the haulier's own security systems. HM Customs and Excise agree but would prefer such use of hauliers' tracking to be limited to investigations rather than as a day to day control measure, since surveillance tracking of all vehicles by the Commission or Member States on the lines of air traffic control would scarcely be practical.

Coordinated risk management and targeted checks

3.12 To coordinate risk management and provide target checks on operations, the Commission proposed:

- establishment of a Community risk analysis unit;
- Commission coordination of risk management policies at national, regional and local level;
- six-monthly national control plans setting out targets, priorities, resources, etc, coordinated at European level; and
- organisation of one-off joint control operations at European level.

3.13 The Commission have proposed the establishment of a Community risk analysis unit and the central coordination of risk management policies. HM Customs and Excise already use similar techniques for their documentation and physical examination selections under their Customs Handling of Imports and Exports Freight (CHIEF) system and in connection with the selection of VAT traders to be visited. While they would welcome input from the proposed Community risk analysis unit, which they feel would enhance the analyses carried out at the local and national level, they would not wish the Commission to assume a management role which could impinge on national management discretion in the use and allocation of resources.

3.14 The Commission have proposed the provision of six-monthly control plans setting out targets, priorities and resources by national custom services and coordination of these national plans at the European level. HM Customs & Excise support in principle the drafting of these control plans and their coordination by the Commission. They provided the Commission with their plans in December 1997.

3.15 HM Customs and Excise also support the organisation of one-off joint control operations. Some are planned on a national basis and some with other Member States through the Customs Cooperation Working Group. For example, HM Customs and Excise have recently been involved in an exercise looking at two weeks' cigarette trade with the Canary Islands. Further exercises are planned with Spain and France and with other Member States. In addition, they have been carrying out customs checks on vehicles stopped by the police at checkpoints throughout the UK for 24 hour periods. They have found these exercises to be effective and feel that there could be scope for all of these types of checks, where they are not already carried out, to be extended to other Member States.

Harmonisation of powers and resourcing of customs controls

3.16 To harmonise customs officials' powers and to coordinate means and resources, the Commission have proposed:

- studying the role and powers of customs officials;
- evaluation and coordination of customs administrations resource management; and
- Community planning to ensure external borders are properly resourced.

3.17 There are considerable differences in customs officials' powers for example with regard to the prosecuting and fiscal powers, en route checking, involvement in immigration and bearing arms. A Commission study on the role and powers of customs officials in the different Member States is currently schedule to start in 1998 as programmed in the Customs 2000 action plan. The National Audit Office agree with HM Customs and Excise that rather than concentrating on harmonisation of roles and powers, with the attendant problems associated with rationalising employment contracts and conditions of service, it should be more cost effective to improve customs cooperation.

3.18 The Commission's actions relating to resource management are currently scheduled for the second half of 1998 and for 1999. They include not only human resources aspects but also provide for equipment to be partially funded by the Community. HM Customs and Excise have recognised the scope for redeploying resources to transit in the light of current problems and increased risk, and staff have been duly assigned to risk areas in the United Kingdom. The National Audit Office agree with HM Customs and Excise that both national and Community cost/benefit considerations should be taken into account before further or different resources are allocated.

Part 4: Fraud investigation and prosecution of offenders

The European Parliament made the following recommendations related to fraud investigation and the judicial process:

- "the European Union must establish a framework for customs services leading to national customs services functioning as if they were one; a common customs investigative service should be created, based on the existing anti-fraud unit of the Commission (UCLAF);
 - the 10 per cent retained by Member States to cover the collection costs of own resources should be directly set against their efforts to protect the financial interests of the European Community;
 - contacts between national prosecutors must be intensified with the creation of a European legal directory of contact prosecuting officers in the Member States, with formal procedures applying to requests for legal assistance between Member States being simplified and accelerated; in this context, UCLAF should be able to initiate criminal proceedings and to give evidence in court on the same basis as national authorities;
 - mechanisms must be established to ensure the "mutual recognition of evidence" across the European Union; to this end a European legal "clearing house" could and should be established at the earliest opportunity."
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Problems

4.1 Elsewhere this Report discusses measures to mitigate the effects of fraudulent diversion of goods in transit. These measures cover the documentary administration of the transit movements including computerisation, guarantees, and physical measures for control and checking. The improved systems, with the enhanced data collection through computerisation, risk analysis techniques, resultant targeted checking and closer cooperation between customs authorities both within the Community and outside (EFTA and Visegrad) should bring about the detection of frauds more efficiently. Even if fully and effectively implemented, they are, however, unlikely to completely prevent the occurrence of fraud. Where frauds are detected, it is then important to ensure that effective sanctions are taken against the offenders, including those benefiting from the frauds.

4.2 There are two main issues in the area of fraud investigation and the prosecution of offenders:

- the need for a high level of cooperation between the customs services to underpin the success of investigation and prosecution; and
- constraints presented by the diversity of the legal systems and procedures between the various Member States.

4.3 The European Parliament found that transit fraud was not easy to investigate or prosecute because it was complex and crossed national borders. The person or persons behind the fraud may be in one Member State, or even outside the Community, but the offence will often be committed in a different or undetermined Member State. The European Parliament noted that most prosecutions were made in the Member State where the transit movement began. Some Member States were content to prosecute the drivers of the vehicles and collect the duty and taxes from the Principal (usually the freight forwarder) or the guarantor without going after the person behind the fraud. The European Parliament concluded that it was impossible to investigate the frauds in a meaningful way because of the weaknesses in the system. They noted that only the United Kingdom and Germany had legislation which expressly permitted the prosecution of an offence not committed within their borders.

4.4 The European Parliament noted that prosecution was also hampered by the slow, formalistic and unresponsive approach to judicial cooperation, where delays are often occasioned by requests having to be processed through diplomatic channels. The European Parliament noted that the legal systems in the Member States varied considerably and there were different legal structures, which could result in non-conformity of treatment even within the Community, especially with regard to rules of evidence. Sanctions for similar offences vary depending upon the Member State in which the prosecution takes place. There are no prescribed penalties for offences against the Community budget except those available under the Member States national legal systems.

4.5 The European Parliament noted that the statistics on prosecutions for the Member States were not wholly comparable. For instance, some Member States (including the United Kingdom) had reached some out of court settlements comprising the revenue lost and administrative penalties. These would have been court cases in those Member States where no such out of court settlement facilities exist. They further observed that the smuggling of cigarettes in Italy might not be classified as a serious offence, and that Switzerland did not offer cooperation for fiscal evasion. Even where judicial and investigative cooperation have been good enough to bring about prosecution, there have been problems in recent court cases with the acceptability of evidence provided from other Member States.

Impact on the United Kingdom

4.6 Whilst the United Kingdom is not one of the main Community transit countries, transit fraud is an international Community wide problem requiring concerted actions from all Member States and also from the EFTA and Visegrad countries. HM Customs and Excise investigation services are keen to bring to book the people behind the frauds; they see this as one of the most effective ways of tackling transit fraud. This requires considerable cooperation between national customs services to ensure successful investigation. It also requires some coordination of legal arrangements to ensure that the perpetrators are prosecuted successfully, wherever the offence has occurred. HM Customs & Excise have the requisite legal powers to effect a prosecution of an offence which has been committed outside the United Kingdom, under section 71 of the Criminal Justice Act 1993.

Suggested reforms

Community level investigative bodies

4.7 To increase investigative efficiency, the Commission have proposed the setting up of the appropriate Community level bodies. It is expected that these would cover both investigation and prosecution. The Commission have proposed the establishment of a crime unit staffed by the Member States' experts on crime and the setting up of a joint investigation agency. The UK Government's position, which was explained to Parliament in Explanatory Memorandum Reference, Number 7862/97, is to oppose the creation of a single Community investigative body. Given the wide variation in the powers of customs officials and their working methods the UK Government is not in favour of any centralised investigation, intelligence or prosecution body. It believes that improved cooperation between the customs services, enhanced intelligence sharing and the reform of the judicial system with particular reference to acceptability of evidence would enable successful investigations and prosecutions to be accomplished.

Customs cooperation

4.8 To improve cooperation between national customs authorities, the Commission have proposed:

- incorporation of provisions on customs cooperation into European Union treaty; and

- implementation of Regulation 515/97 on mutual assistance between customs administration, of Regulation 2185/96 concerning on the spot checks; and of Regulation 2988/95 on administrative penalties.

4.9 The European Union Treaty, signed at Maastricht in 1992, has been revised by the Treaty of Amsterdam. This was agreed in June 1997, but has not yet been ratified by Member States. The new Treaty includes a new article on customs cooperation within the Community provisions and a revised Article 209A which relates to countering fraud affecting the financial interests of the Community and coordinated action by Member States.

4.10 Mutual assistance between customs services has been in existence since 1981. Regulation 515/97 which comes into effect in March 1998 will update the original Regulation 1486/81 to meet the current needs of the Community following the completion of the internal market and to take account of the experience gained over the years of application of the Regulation. The UK Government fully supports the new regulation which will also cover the implementation of the Customs Information System for intelligence sharing and data protection in line with the UK Data Protection Act 1984.

4.11 Regulation 2185/96, approved in June 1996, gives the Community's fraud investigation body, UCLAF, powers in certain circumstances to carry out inspections at the premises of traders, which may include transit operators. HM Customs and Excise contributed to the drafting of an operational protocol setting out conditions with which the Commission officials will comply in exercising these powers. No inspections to UK traders have yet been made under the Regulation. HM Customs and Excise intend to accompany the Commission officials carrying out these inspections where they concern customs matters.

4.12 Penalties for transit irregularities are determined nationally and currently depend upon where the prosecution is undertaken. The Community has established an enabling framework for future Community legislation on civil penalties for infringement of the Community Customs Code and other Community regimes (Regulation 2988/95), but has yet to proceed from this to the introduction of Community penalties. HM Customs and Excise are supportive of the principle of administrative or civil penalties at Community level as long as such penalties will not undermine the application of national criminal sanctions in cases where such sanctions are warranted.

Convention for the protection of European Community financial interests

4.13 To combat fraud in the European Union, the Commission have proposed ratification by Member States of the convention on “protection of financial interests”, and protocols on corruption and on cooperation in criminal cases.

4.14 The senior customs officials who form the inter-governmental High Level Group on Organised Crime have recently produced an action plan which sets the target date for ratification of the convention for the protection of European Community financial interests as mid 1998. While no Member State has currently ratified this convention the United Kingdom fully intends to ratify within the target date. Additional protocols have also been proposed to cover corruption and cooperation in criminal cases, for ratification in 1998.

Study of judicial systems

4.15 The Commission have proposed the conduct of a study of European judicial systems. This would cover the European Parliament’s recommendations for a directory of prosecuting officers, mutual recognition of evidence, a clearing house pending mutual recognition of evidence, the question of jurisdiction and the legal recognition of UCLAF. These items are not specifically mentioned in the Commission’s action plan. The United Kingdom, as previously mentioned, do have jurisdiction over offences committed elsewhere under the Criminal Justice Act 1993. HM Customs and Excise particularly see the need for the mutual recognition of evidence. Although they recently experienced some failed prosecutions on technical grounds, due to the inadmissibility of other Member States’ certificates of corresponding law in an English court, HM Customs and Excise are confident these difficulties will be overcome and that they will achieve a successful prosecution in the future. HM Customs and Excise have introduced fiscal liaison officers in some other Member States to facilitate the solution of problems, including consultation with investigation and judicial contact points within the Member States.

Part 5: Computerisation

The European Parliament recommended that:

- "the comprehensive computerisation of the transit system, long overdue, must be implemented as rapidly as possible, whilst recognising that it is not in itself an anti-fraud measure;
 - greater attention should also be paid to complementary technological options for the management of transit."
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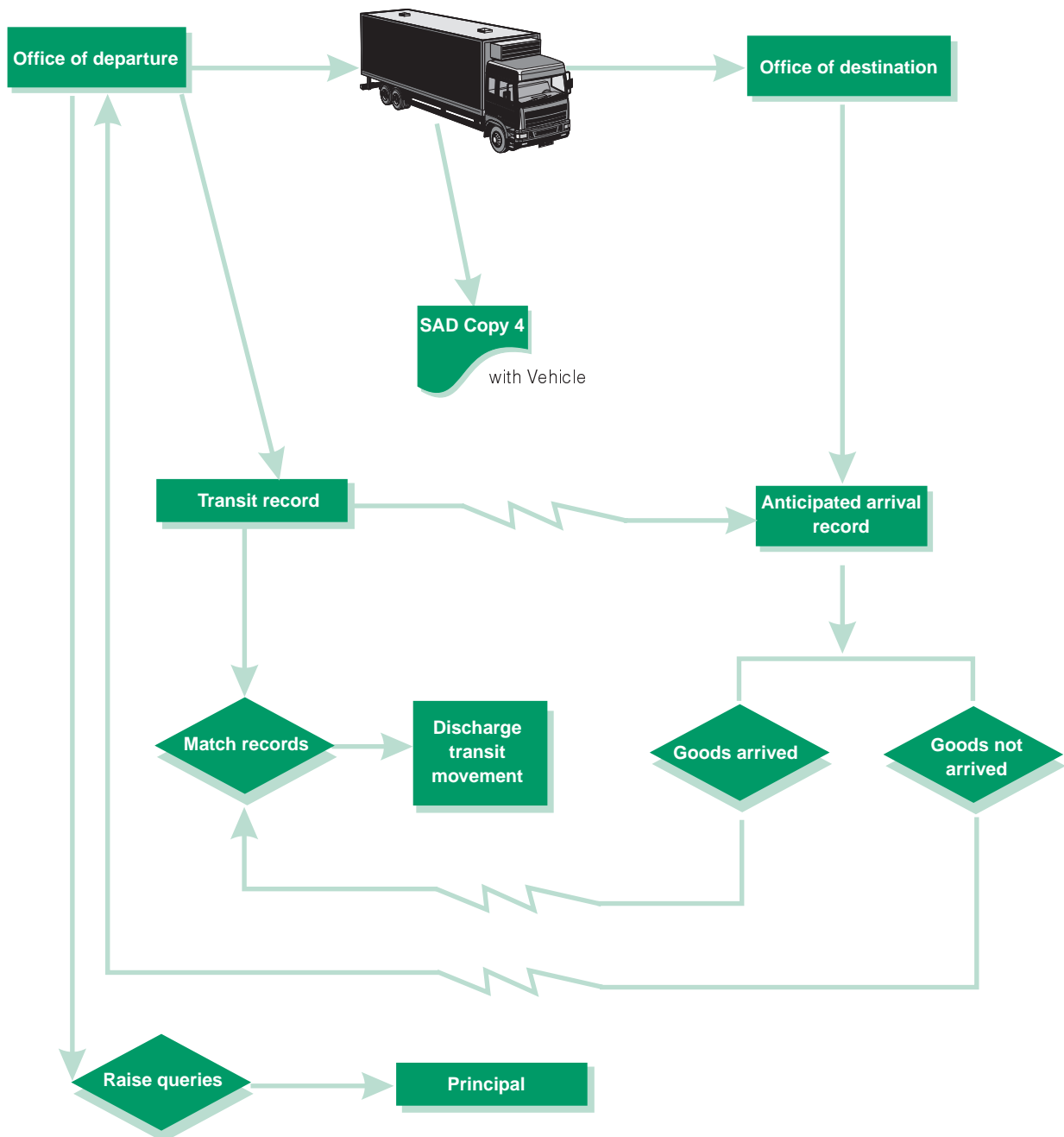
Background

5.1 Computerisation is seen by all parties as a key to reform of the Community transit system. It was one of the major recommendations of the European Parliament and the rapid introduction of the New Computerised Transit System (NCTS) was seen as essential in the Commission's action plan. It was suggested that such a system should improve deterrence and remove much of the scope for existing fraud. By eliminating the need for a large amount of the paper currently required for the operation of the system, it will permit a more timely matching of consignments sent with those delivered and, give early warnings of those apparently undelivered, as detailed in Figure 6. It should also prove more efficient than the current paper based system, and in addition, statistics from the system will enable customs investigation services to build up operational intelligence and will assist in the effective allocation of resources to examining transit movements and documentation.

5.2 Computerisation of the Community transit system was initially proposed by the European Commission in 1991 to:

- make the transit procedures more effective and efficient;
- provide the means for effective detection and prevention of fraud; and
- enhance the facilities available to users of the system both within the trade and for the customs authorities.

Figure 6 Schematic diagram of proposed computerised transit system



Source: National Audit Office

5.3 The Commission undertook a pilot project in 1991-92. This pilot project failed, primarily because it sought to enter the transaction twice - once at departure and once at destination, with too many resultant mismatches. A further feasibility study undertaken in September 1993 concluded that the project should continue, but in a revised form.

5.4 Under the revised computerisation project, each participating country will develop their own national transit system based on a common specification. These national systems will be linked. When a transit movement starts, details of that movement will be entered into the national computer system of the country of departure and then electronically transmitted to the office where the goods are expected to arrive. Thus each customs service will be able to compile lists of expected arrivals. Once goods have arrived, the office of departure will be notified of this through the system so they can discharge the movement.

5.5 The need for paper copies of the transit documents and their subsequent matching would thus be largely eliminated. This lack of paper documentation would also help to solve the problems of alteration of information on transit documents and the use of forged or stolen customs stamps. The system would provide enquiry procedures for transit movements which had not been discharged within the time allowed for the transit movement, thus enabling enquiries to be started early for the prompt detection of possible fraudulent activity. The statistics of the transit movements would be held on the national computer databases, which would also facilitate the collection of transit movement data for general intelligence and for the application of risk analysis techniques.

5.6 Following the European Court of Auditors report of 1994 and the Commission's report in March 1995 dealing with fraud in the transit procedure, the European Internal Market Council adopted Resolution C327 on 7 December 1995 relating to the computerisation of customs transit. The intention was to make the Commission's system the normal procedure but, although all Member States have expressed their full commitment to computerisation, it was not made legally binding upon them. The National Audit Office note that the overall success of the project and the achievement of value for money will be diminished should some Member States not participate in it.

Implementation

5.7 The European Commission fully support the rapid introduction of computerisation and have called upon national administrations to allocate resources for implementation. Full implementation of the revised computerised system was originally considered to be very much in the long term. Originally early 1998 was set as the expected date for the start of a fully operational system. The project was designed in the following phases:

Phase 0	Feasibility study	1993-1994
Phase 1	Development of system specifications	1995-1996
Phase 2	Construction and pilot implementation	1996-1997
Phase 3	Implementation and extension	1998-1999
Phase 4	Operation and maintenance	1999 onwards

5.8 In October 1996 the Commission forecast that the New Computerised Transit System would be fully up and running by 1999. By April 1997 the Commission's action plan indicated a trial phase taking place in mid-1998 and the operational phase beginning in late 1998, but both with only limited functions in a few countries, and at only some rather than all of the customs offices. The fully operational system would only be available by late 2000. At the time of this Report the central Community systems design stage (Phase 1) had not been fully completed. In the light of the delays in implementation of the various phases, the National Audit Office consider that this timetable is likely to suffer further slippage.

5.9 The European Parliament in February 1997 noted that although all Member States expressed full commitment to this project, some were unable to allocate the necessary resources. The European Parliament considered, therefore, the effect of only partial implementation and concluded that whilst the project was still feasible, criminals could well take advantage of any resulting weak links and incompatibilities. The National Audit Office note that even partial implementation of the new system by the major user Member States would go some way towards eliminating many of the paper transactions. Thus Member States would be able to apply resources more effectively to the remaining paper transactions and to those aspects of the system where problems with illegal diversion had been previously experienced.

Costs and benefits

5.10 The Commission estimated in a preliminary cost/benefit analysis in March 1995 that the net cost for the period 1995 to 2000 would be about ECU 8 million, but that by 2002 this would become a net benefit of ECU 17.5 million. They estimated that national investment costs exclusive of running costs would amount to some ECU 13 million up to the year 2000 and that ECU 9.5 million would be required for funding the central Community investment. They concluded, however, that these costs should be viewed in the context of likely impact on frauds over a similar period of some ECU 1,200 million. In addition they expect unquantified benefits from increased trade protection and increased intelligence on transit operations for the international customs network.

5.11 In February 1997, the European Parliament noted that the Commission had estimated the revised benefit over a five year period 1995 to 1999 as between ECU 5 and 10 billion. The National Audit Office note that these figures are highly conjectural and were pitched between an upper range of ECU 50 to 100 billion and a lower range of ECU 0.5 to 1 billion.

Progress in the United Kingdom

5.12 The UK fully supports the current computerisation project and is actively preparing for its implementation. HM Customs and Excise applied to be one of the five customs services involved in the initial implementation or pilot trials, but were not selected. The Commission selected Germany and the Netherlands as the two largest transit users, Spain and Italy as countries with control or diversion problems and Switzerland as a non-EC country.

5.13 Computerisation of the national transit system for the United Kingdom is considered by HM Customs and Excise to be in an embryonic stage with considerable development work still to be undertaken. HM Customs and Excise have established a draft national user requirement, based on their current understanding of the draft systems specification for the central Community system and their own basic requirements. They are awaiting the finalisation of the central design so that for the first phase the impacts can be properly assessed. The UK systems specification can then be finalised, and the system infrastructure can be developed and tested. HM Customs and Excise currently envisage the initial implementation stage for the New Computerised Transit System project being in mid-1999 at the earliest.

5.14 HM Customs and Excise have been assisting the Commission's computer contractors in the central systems development work. They have been commenting on the functional and business systems analysis, both through review of documents by outfield officers in a User Group and attendance at meetings of the Steering Committee and Transit Computerisation Working Party in Brussels.

5.15 HM Customs and Excise have spent some £240,000 in staff salary costs on the national transit systems development work up to December 1997. They have assessed other UK costs in the central systems design stage as £42,000. There are also plans to purchase a computer at the appropriate time.

Other applications

5.16 The European Parliament have also recommended that there should be a maximum exploitation of the potential offered by computerisation including complementary applications such as E-mail, optical and smart cards. The use of E-mail would be an interim measure, pending the full implementation of the New Computerised Transit System. The use of smart cards or optical cards could operate in combination with the new computer system. Although HM Customs and Excise have reservations about the use of E-mail on cost and security grounds, they are supportive of the potential offered by these measures.

Part 6: Streamlining administrative procedures

The European Parliament recommended specifically that:

- "the Commission must encourage customs services to exploit more fully the potential offered by existing information-sharing and control mechanisms such as the SCENT early-warning system for the control of sensitive goods and the Customs Information System;
 - common training programmes and transnational exchange schemes for national customs officers must be expanded and linked to career progression within national services. In this context, the Commission should examine the possibility of establishing a European Union Customs Academy, which would train national customs officers in a decentralised, but uniform manner."
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Problems

Failure to comply with transit procedures

6.1 The greatest single weakness of the Community transit system is the fact that it relies on the presentation and exchange of paper documents endorsed by an official stamp. Currently there are approximately 3000 customs offices in 23 countries acting as offices of departure or destination (or both). These share, albeit unevenly, the load of processing up to 18 million transit operations per year. Each operation involves three manual procedures: issuing the transit document and retaining copy 1, stamping and returning copy 5, and matching copy 5 with the original copy 1.

6.2 Under the Community administrative arrangements for transit, the customs office of destination is required to return copy 5 of the transit form within 10 days of the goods being presented to them. In practice this often does not happen, and delays occur. The European Parliament attempted to establish the time on average each Member State took to return the copy 5. The figures supplied by Member States led them to conclude that "customs services probably have very little idea of how long it takes in reality to return a form". They did however, obtain information from Germany (the largest transit country) specifying for each other Member State the percentages of cases where the copy 5 is returned within six weeks. The results are shown in Figure 7.

Transit document returns to the German customs service

Figure 7

Member State	Transit document copy returned within 6 weeks (per cent)
Luxembourg	99
Denmark	97
France	90
Ireland	89
UK	89
Netherlands	79
Portugal	79
Spain	72
Belgium	60
Austria	47
Finland	47
Sweden	45
Italy	26
Greece	3

Source: European Parliament Committee of Inquiry Report

There is a wide variance in the performance of the Member States in returning copies of the transit document to the German customs service.

6.3 Where copies 5 have not been returned within 10 weeks, the current Community administrative arrangements for transit require Member States to initiate inquiry procedures to establish whether any irregularities or infringements have occurred. The European Parliament found inquiry procedures to be slow and cumbersome with simple inquiries taking months to process. Moreover, they found the system had “deteriorated into a formalised paperchase for missing documents rather than an effective instrument for investigating fraud”. In evidence to the European Parliament, the trade were critical of some nation’s customs services, asserting that they did not fully comply with the transit legislation and rules.

Vulnerability to fraud

6.4 Most transit fraud falls into one of two categories:

- transit transactions are completed fraudulently; or
- transit transactions remain incomplete.

6.5 In the first category of fraud, a fake or stolen stamp covers up the failure to present goods at their destination and, unless further checks are carried out, means that a transit movement will be considered to have been properly conducted and therefore completed. The presence of an official stamp on copy 5 of

the transit document is taken as prima facie proof that the goods have been presented at destination and allows the office of departure to consider the transit movement complete.

6.6 In the second category the fraud usually relies on the inefficiency of the controls within the transit system. Goods can simply be placed on the black market in the confident expectation that by the time the fraud is discovered through the lengthy inquiry procedure, the perpetrator will have had sufficient time to make his profit and disappear. In some instances, the fraudster has time to repeat the fraud a number of times before anyone notices the first transaction was irregular.

6.7 There is such a large number of different customs stamps used to authenticate transit documents that it is difficult to check their authenticity. HM Customs and Excise do not know how many exist, but estimate there are likely to be many thousands. As well as all the different stamps which are used by the 3,000 customs offices within the Community, there are further stamps used by some authorised traders.

Limited use of an early warning system

6.8 The failure of customs' authorities to apply the Community transit procedures efficiently was identified in the mid-1990's. During 1994 the Commission took various measures in both legislative and operational areas to improve matters. One of these was the introduction of an early warning system. The purpose of the system is to provide assurance that goods which are considered most at risk from fraud (and known as sensitive goods) reach the office of destination. When sensitive goods start on a transit movement, the office of departure should inform the office of destination to which the goods have been declared to be going, that the goods are on their way. If the goods do not arrive within the expected time limit (customs give a deadline to the Principal by which the goods must reach their destination) then the office of destination can inform the office of departure and the inquiry procedure set in motion.

6.9 The early warning system utilises the customs network SCENT (Systems Customs Enforcement Network) which was designed for wider enforcement purposes. The European Parliament found that certain Member States made little use of early warning arrangements. Coordination of the arrangements for the early warning system in the United Kingdom is undertaken by HM Customs and Excise's National Investigation Service.

Impact on the United Kingdom

6.10 The United Kingdom has approximately 130 offices which act as offices of departure and destination. There are also around 350 companies authorised by HM Customs and Excise to self authenticate the transit form and send the copy 1 to customs. Figure 8 gives details of the number of transit movements in the United Kingdom since the creation of the Single Market. In 1997 there were approximately 261,000 movements commencing in the United Kingdom, and 201,000 finishing in the United Kingdom.

6.11 HM Customs and Excise start inquiry procedures if a copy 5 of the transit document has not been returned to them within about 12 weeks of the transit movement commencing. At present so many copies 5 are not returned from other Member States that the HM Customs and Excise have stated that it is impractical to investigate them all. Instead they sift out those which are low risk and pursue the rest (see Figure 8). The National Audit Office consider that the HM Customs and Excise practice of initiating the inquiry procedure after 12 weeks, rather than the 10 weeks recommended in the European Commission compendium of administrative arrangements, is reasonable on cost effectiveness grounds.

UK transit movements
and queries handled 1993
to 1997

Figure 8

Year	Transit movements commencing in the United Kingdom	Number of queries to other Member States	Transit movements finishing in the United Kingdom	Number of queries from other Member States
1993	248,882	38,325	188,515	4,873
1994	368,373	43,508	200,799	19,158
1995	342,902	29,435	177,186	19,240
1996	376,208	42,384	177,368	21,566
1997	261,481	34,655	201,311	16,940
Total	1,597,846	188,307 (11.8%)	945,179	81,777 (8.7%)

There is no direct relationship between the number of transit movements in a year and the number of queries. Over the five year period to 1997, however, HM Customs and Excise Central Community Transit Office has initiated inquiries on 1 in 8 movements to other Member States and received inquiries on 1 in 12 movements from other Member States.

Source: HM Customs and Excise - Central Community Transit Office

Proposed improvements

Organisation of customs' administration

6.12 To enable customs' authorities to run Community transit procedures more efficiently, the Commission have drafted legislation proposing that customs services might:

- reorganise offices responsible for returning copies 5;
- make one national office responsible for collating copies 1 and 5, and handling inquiries; and
- set realistic national targets for meeting Community-wide time limits.

6.13 HM Customs and Excise have their own central office, the Central Community Transit Office (the Central Office), which became operational on 1 January 1993 when the Single Market came into force. The Central Office is responsible for handling all copies 1 and 5 of the transit document, initiating queries and handling queries from other offices. It currently employs some 52 staff whose annual salary costs are about £775,000. Approximately £527,000 or 68 per cent relates to data processing, sorting and enquiries and the remainder relates to guarantees and freight compliance. There are additional unquantified local costs for transit at the customs offices where the transit movements are started or completed. However, the National Audit Office consider that these additional costs are likely to be only marginal as they relate primarily to checking of the guarantee arrangements. Most of the local office costs would persist if there were no transit regimes in operation, and they would indeed increase if duties and taxes had to be collected and refunded on every movement.

6.14 The benefits of having a central office include:

- better operational control of transit;
- easier introduction of changes and improvements;
- better management information about transit;
- investment in equipment that would not be justifiable at local offices; and
- increased staff expertise in transit matters.

6.15 HM Customs and Excise recognise, however, that a central office adds an additional process to the transit procedures. To reduce the time spent keying in information into their database about transit movements originating in the United Kingdom, they are in the process of introducing pre-numbered forms, which can be scanned into the database.

Principals' responsibilities for front-line operations

6.16 To assist in reducing the delays in discharging transit movements, the Commission have proposed in draft legislation that reliable Principals should be authorised to take charge of returning copies 5 of transit documents. Giving reliable, authorised Principals the responsibility for returning copies 5 would bring the Community transit system into line with other UK systems where responsible parties are required to make their own declarations. The main benefit of such an arrangement would be that the onus to return the copies 5 was placed on Principals, so that the grounds for making claims against Principals would be stronger where problems arose over their non-return. There would, however, be some increase in the risk of fraud which would need to be addressed through improved controls over Principals.

Administrative cooperation

6.17 The Commission have made recommendations for improving administrative cooperation, which include:

- improvements to the early warning system;
- setting up of a network of national transit coordinators and local office contacts;
- appointing a transit contact in every large transit office to be responsible for implementing transit management and control plans; and
- setting up a Transit Stamp Transmission System.

Early warning system

6.18 The Commission propose the expansion of the early warning system to cover all common transit countries; this is already in progress. They also propose a redefinition of the list of goods for which the system should be used, and to make its

use compulsory. Lastly they propose that communications on sensitive goods between the offices of departure and destination should be executed by the fastest means available.

6.19 HM Customs and Excise believe the early warning system is a useful anti-fraud tool and therefore they support the Commission's recommendations for improvements, though they believe any expansion of the system should be geared to assessment of risk.

National transit coordinators and local transit contacts

6.20 The Commission propose the appointment by each Member State of a national coordinator to, among other things, monitor the implementation of transit rules, and to draft national transit management and control plans. At the local level they propose that a contact in every large customs office should be responsible for implementing those plans, communicating directly with other customs administrations and with the trade.

6.21 Over the past year HM Customs and Excise have implemented a number of initiatives to improve the United Kingdom's operation of transit. These include:

- the publication of a national target in the HM Customs and Excise management plan which is supported by a Statement of Service for the Central Office setting out the services it will provide and the performance indicators against which these will be measured;
- the appointment of a national coordinator in September 1997; and
- the appointment of Community transit Liaison Officers to act as a channel for communications between the Central Office and the customs staff in local customs offices.

Transit Stamp Transmission system

6.22 The Transit Stamp Transmission system will comprise a central Community database of examples of Member State customs stamps, to which Member States will have access through computer links. The system aims to provide Member States with a mechanism for establishing the authenticity of customs stamps used on transit documents.

6.23 HM Customs and Excise have been advocating a central database of customs stamps and they expect to be linked to the system by the Spring of 1998. The system will only be fully effective once the database holds examples of all customs stamps that could be used on transit documents, is regularly updated, and is used by all Member States.

6.24 Since February 1996 in advance of the central system's availability, the HM Customs and Excise have been maintaining their own set of custom stamps examples. Because of practical problems in obtaining customs stamps, however, they have been able to obtain only approximately 2,500 examples. Where doubts arise about authenticity, the customs stamp on the transit documents is referred to the office of destination for verification.

Training customs officials

6.25 To increase the expertise with which transit is managed, the Commission are proposing to:

- hold seminars for customs officials;
- organise exchanges of customs officials between Member States;
- consider common core training courses at European level; and
- devise transit training modules for use in national training centres.

6.26 HM Customs and Excise support these proposals and have been participating in seminars and exchanges of customs officials since 1990. Most customs seminars and conferences cover transit, at least in part, and there have been specific transit seminars in Luxembourg (1996), Helsinki (1996), Le Havre (1997) and Prague (1997). HM Customs and Excise have specially targeted transit in recent exchange of officials with visits to France, Germany and Sweden. The Central Office have links with the Netherlands customs service on the detection of forged stamps. HM Customs and Excise have also created special training courses on transit for UK front-line customs staff and the Central Office has been given responsibility for providing technical expertise, advice and guidance to UK offices of departure/destination.

Transit handbook

6.27 To improve the management of transit the Commission propose the drafting of a handbook of instructions and information on transit for customs and operators throughout the Community. HM Customs and Excise support this action provided that the scope of the handbook does not unduly constrain national procedures. They are concerned that the instructions for customs might include, for example, prescriptive Community rules on the overall number of physical examinations of consignments. This could conflict with UK requirements for examinations based on HM Customs and Excise assessments of risks.

Part 7: Other European Parliament recommendations

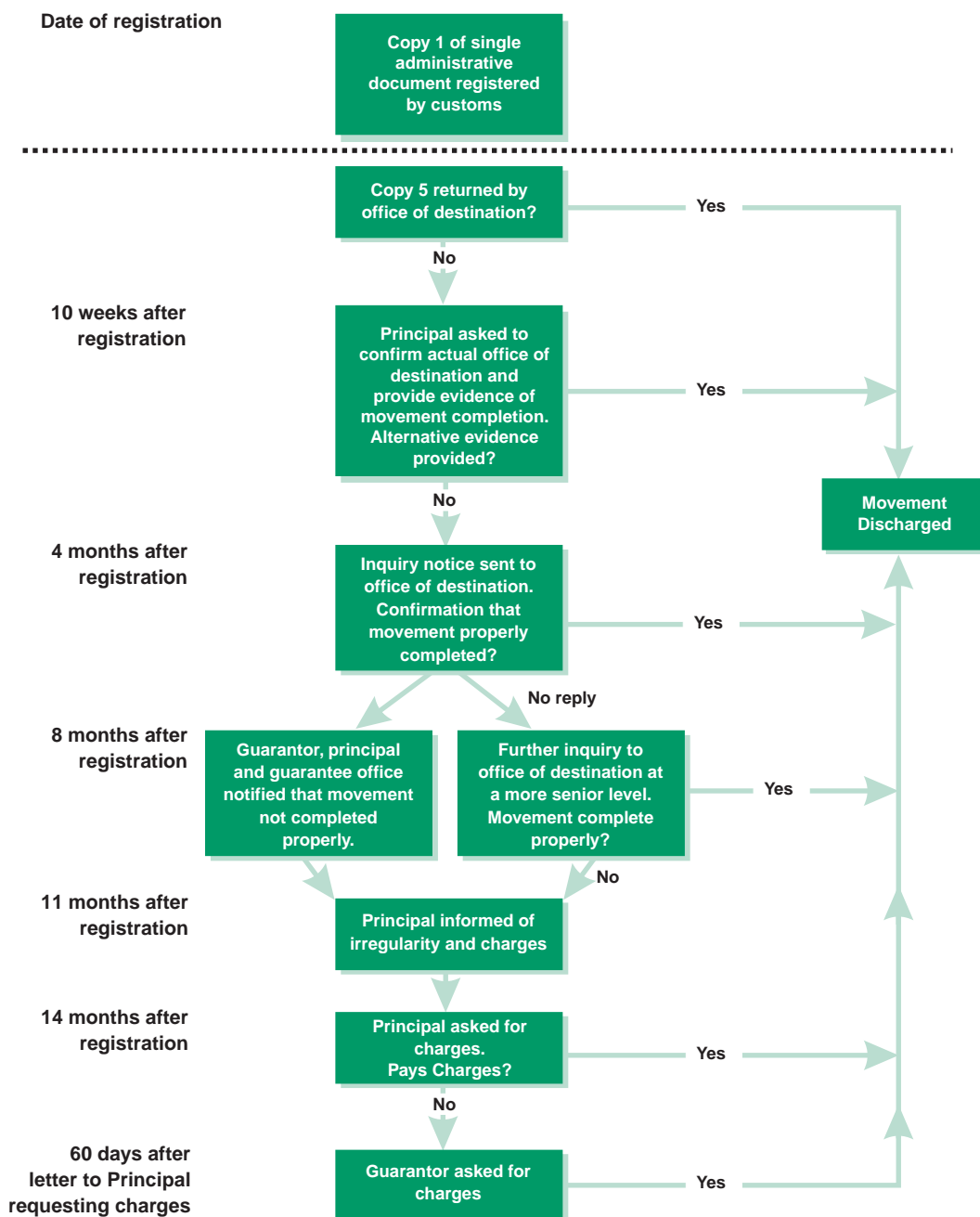
7.1 There are two further main recommendations made by the European Parliament. These are:

- “the Joint Committee on Common Transit bringing together 23 European countries should establish a working group to examine the ways in which the trade in cigarettes can be made more transparent, particularly in terms of the chain of ownership, as well as what sanctions should be taken against those involved in the illicit trade in cigarettes; and
- firm Community action is required with regard to the countries whose legislation contributes to the problems encountered in the transit system, in particular Switzerland, and the issue of ensuring adequate levels of control should feature in accession negotiations with the countries of Central and Eastern Europe and Cyprus.”

As these recommendations are considered by the Commission to require further input at the political level within the Community, they have not addressed them in their current action plan. The National Audit Office have also excluded them from the scope of this review.

Appendix 1

Inquiry procedures flowchart



Source: National Audit Office

Glossary and abbreviations

Subject	Abbreviation or Short Title	Definition
Central Community Transit Office	CCTO	The UK central office for transit documents.
Community Customs Code	CCC	The common customs code established in 1992 by Council Regulation 2913/92.
Community transit	CT	A transit system for moving goods across the Community free of duties and taxes.
Common Transit		An extension of the Community transit system to the EFTA and Visegrad countries.
Council of Ministers	Council	The EC's legislature comprising various national ministers depending upon the subject matter with dual roles of adopting legislative proposals from the Commission and representing and protecting national interests.
CT guarantee		A form of security to ensure the collection of the duties and other taxes, furnished by the CT Principal acting jointly and severally with an approved guarantor.
CT Principal		The person who requests permission to carry out a CT operation and is responsible to the competent authorities for the completion of the operation in accordance with the rules.
European Atomic Energy Community	EAEC	Established by the EURATOM Treaty in 1957 which was signed by the same six countries as the ECSC.
European Coal and Steel Community	ECSC	Established in 1951 by the Treaty of Paris to cover the pooling of production and consumption and signed by six countries: Belgium, France, West Germany, Italy, Luxembourg and Netherlands.
European Commission	Commission	The European civil service, but with some powers to frame legislation.
European Community	EC or Community	One or more of three European Communities (EAEC, ECSC, EEC) in the EU. Member States are currently 15: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden, UK.
European Council		Twice-yearly summit meeting of Heads of State and Foreign Affairs Ministers of Member States and the President of the Commission.

Subject	Abbreviation or Short Title	Definition
European Currency Unit	ECU	The common monetary or financial unit within the Community used mainly for accounting purposes at present.
European Economic Community	EEC	Established in 1957 by the Treaty of Rome which was signed by the same six countries as the ECSC and more commonly known as the Common Market.
European Free Trade Association	EFTA	Agreement dating from 1960 aimed at free trade for industrial goods between a group of member countries of whom several members including the UK have subsequently left to join the EC. Now comprises Switzerland, Norway, Iceland and the principality of Liechtenstein:
European Parliament	EP	An Assembly of 626 directly elected representatives from Member States with supervisory powers and the ability to appoint and dismiss the Commission.
European Union	EU	The term given to describe the union of the European Communities (EAEC, ECSC and EEC) and the intergovernmental arrangements on justice and home affairs and the intergovernmental arrangements on foreign and security policy.
Free circulation		Goods imported from a non-Community country are described as having been put into free circulation in the Community if all the import formalities have been complied with and any customs duties or charges have been paid and not repaid in whole or part. Goods originating in the Community are also in free circulation, unless an export refund has been claimed on them under the Common Agricultural Policy. The expression free circulation can also cover goods illegally entered into the Community which are indistinguishable from legally entered goods, except from their provenance.
General Agreement on Tariffs and Trade	GATT	A series of trade agreements since 1947 which have established strict procedures and tariffs for international trade. 96 countries are contracting parties covering over 80 per cent of world trade. Now known as the World Trade Organisation.
New Computerised Transit System	NCTS	The computerisation project for the CT system.
Office of departure		The customs office where a CT movement begins.

Subject	Abbreviation or Short Title	Definition
Office of destination		The customs office where the goods should be produced to complete a CT movement.
Office of guarantee		The customs office where a comprehensive or flat-rate guarantee is lodged.
Office of transit		The customs office at the point of exit from the customs territory of the Community when the goods are leaving the Community or at the point of entry when the goods have crossed the territory of a non-Community country.
Single Administration Document	SAD	The name for the Community model form of customs declaration - including Community transit declarations. Also called the Single Document.
Single Market		The Community as from 1 January 1993 under the Single European Act which effectively removed customs controls from internal borders between Member States.
System Customs Enforcement Network	SCENT	An information sharing system between the customs services and other law enforcement agencies in the EU.
Transports Internationaux Routiers	TIR	International transit convention of 1975 currently ratified by 61 countries including all the members of the Community.
Unité de Coordination de la Lutte Anti-Fraude	UCLAF	The Commission's anti-fraud investigation body.
Visegrad		Group of countries comprising Hungary, Poland, Slovakia and the Czech Republic.

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COM(96)477 Final	European Commission: Communication from the Commission - The Future of Transit Systems: Interim Report	October 1996
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