

CHAPTER 5

PREFERENCES

5.1 Introduction

Duty rates are contained in a book called "The **Tariff**". The Tariff sets out **full duty rates** and **preferential duty rates**.

Illustration 1

Goods are imported into the UK from Japan. The classification code of the goods has been determined and the rate shown in the Tariff is 12%. This is the full rate of duty that applies. The second but last column of the Tariff shows whether a reduced duty rate can be claimed for goods falling in this classification code. The **preferential rate depends on where the goods originate**.

For instance, if the goods originate in Pakistan they may receive a 9.6% duty rate, and if the goods originate in Bangladesh, they may receive a 0% rate. The reason that preferential rates are given is generally to **help countries with undeveloped economies grow**, by enabling them to export their products cheaper than the more developed countries.

5.2 Preference agreements

Other preferences might be given because certain countries have **reciprocal trading arrangements** with the EU. For instance, imports from **EFTA** countries, which include **Norway, Iceland, Switzerland and Liechtenstein**, may be imported into the EU free of duties. As the arrangements are reciprocal EU products can be imported in to the EFTA countries free of duties.

A new pan Euro-Mediterranean zone for preference purposes is currently being implemented. Once all the necessary legislation is in place, it will allow products to move between the EU and a number of other European, African and Asian countries under preference.

5.3 Generalised System of Preferences (GSP)

The largest preference regime is currently the **Generalised System of Preferences**, or **GSP**. It is an **EU wide scheme** that applies to imports of certain products, from certain 'developing' countries, which are known as '**beneficiary countries**'. Not all types of goods from beneficiary countries get preferential rates. If the country is developed in some industries, then a preference may not be available for those particular goods.

5.4 Claiming preference

In order to obtain a preferential rate of duty, the goods, must:

1. **originate** in the beneficiary country,
2. **travel direct** from that country to the EU; and
3. must be accompanied by the required **Certificate of Origin**.

We will now take each of these conditions in turn.

5.5 Originate in beneficiary country

The goods have to originate in the beneficiary country. What constitutes "originating"? Article 67 of the Implementing Regs provides us with a definition.

[Art 67
2454/93](#)

The products must either be **wholly obtained** in the beneficiary country, or **sufficiently worked or processed** there.

Illustration 2

The idea behind this rule is that you cannot produce goods in Japan, for instance and then import them into Bangladesh, do nothing to the goods whilst they are in Bangladesh and then ship them onwards to the EU, and try and claim a preferential rate of duty on the basis that they originate in Bangladesh!

Using the rules that we are going to look at in a minute, the goods would be deemed for preference purposes, to originate in Japan. As Japan is a developed country, the full duty rate would be payable when the goods are imported into the EU.

5.6 Wholly obtained

There is a list of what constitutes 'wholly obtained' in Article 68 of the Implementing Regs. To pick out a couple:

[Art 68
2454/93](#)

(1) (c), covers **live animals** born and raised in the country; and

(1) (e) includes products obtained by **hunting** or **fishing** conducted in the country.

Putting it simplistically, anything coming from the land, sea or air of that country is classed as wholly obtained. What if our products are not wholly obtained?

5.7 Sufficiently worked or processed

Sufficient working or processing is contained in Article 69 and this article refers us to Annex 15 of the Implementing Regs. Annex 15 is rather large and that is why it is not reproduced in the Tolley's Customs Duties Handbook. The origin rules are however reproduced in Public Notices, and they **depend on the commodity code** of the imported product.

[Art 69 & Annex
15
2454/93](#)

Illustration 3

Your supplier is based in a GSP beneficiary country. He is a manufacturer of teddy bears. The main stuffing, outer fur and clothing of the teddy bears all originate in that country and the teddy bear is manufactured there but the eyes and nose of the teddy bear are imported from Japan. Our teddy bear is made up of components that originate and components that do not. Where is the origin of the bear?

Teddy bears are classified in Chapter 95 which covers

'toys, games and sports requisites, parts and accessories thereof.'

The origin rule for the relevant classification code says

"manufacture in which all the non-originating materials used are classified in a heading other than that of the product, and the value of all the non originating materials used does not exceed 50% of the ex-works price of the product."

The teddy bears eyes and nose are classified in a different heading to the teddy bear itself and hopefully don't exceed 50% of the value of the teddy bear when sold! This is what '**ex-works price**' means- **the value as it leaves the factory gate**. So it is likely that the origin of the teddy bear is the GSP beneficiary country.

5.8 Simple processing

Even if the above origin rule means that the teddy bear appears to originate in a preference receiving country, there is a further condition that must be satisfied. Where the operations that have been carried out on the teddy bear are '**simple**', this will **not amount to 'sufficient working or processing'**.

Article 70 of the Implementing Regs gives a list of processes that would not amount to sufficient working. The list is very long, it goes through from a) to p). The following are simple processes:

[Art 70
2454/93](#)

- (c) **washing and cleaning;**
- (d) **ironing** or pressing of textiles; and
- (k) **simple placing in bottles.**

The manufacture of our teddy bear should amount to more than a simple operation; therefore, its origin should be in the beneficiary country.

5.9 Proposals to simplify rules of origin

The EU Commission is currently considering proposals to simplify all rules of origin and make other reforms to preference regimes. More information is available on their website <http://ec.europa.eu/taxation-customs> from document TAXUD/2046/2007-1.

5.10 Regional Groups

Some countries form regional groups and **products that originate in one country, which are subject to working or processing carried out in another country of the same group, will count as originating in the other country.**

Illustration 4

Material originating in Pakistan, which is exported to Bangladesh to be sewn into t-shirts counts as originating in Bangladesh. This is because these two countries are both members of the same group. You can see the regional groups listed in Article 72(3) of the Implementing Regs.

[Art 72\(3\)
2454/93](#)

Now, for the purposes of some preferences, Pakistan may not get such a good rate as Bangladesh, as it is more developed in certain industries, so which is the final country of origin, Pakistan or Bangladesh? Article 72a solves the problem.

[Art 72a
2454/93](#)

It says that the country of origin is where the **last working or processing was carried out, provided that the value added there is higher than the value of the product, originating in the other countries of the group.**

Therefore, provided that the value that the processing in Bangladesh has added to the product is greater than the value of the material from Pakistan, the t-shirts will originate in Bangladesh. On final proviso is that the processing carried out in Bangladesh can not be '**simple**' - remember we have already looked at the definition of simple back in Article 70.

As well as 'regional grouping', if products that originate in the EU are sent to Bangladesh to be 'sufficiently worked or processed', they also count as originating there for the purposes of preference. You'll find this in Article 67.

[Art 67
2454/93](#)

5.11 Direct transport rule

The second and third conditions we mentioned earlier were that the goods must be **transported directly** to the EU from the beneficiary country and the required **Certificate of Origin** needed to be presented with the goods.

The Direct Transport Rule is contained in Article 81(1) of the Implementing Regs. This is to stop manipulation of the rules.

[Art 81\(1\)
2454/93](#)

Illustration 5

Goods that originate in Bangladesh are exported to Japan, processed and then shipped onwards to the EU. Japan does not qualify for preference under GSP - so if the goods originate there the full rate of duty will be payable. Can we argue that the goods originate in Bangladesh to try and claim a preferential rate of duty?

Firstly, we would need to check the origin rules to see if the goods were 'sufficiently worked or processed enough' to count as originating in Bangladesh.

Secondly, we would need to check whether we satisfy the 'direct transport' rule. Article 78 of the Implementing Regs deals with this rule. It says that goods can only **pass through the territory of another country, provided** that they have **remained under the surveillance of the customs authorities** and have **undergone no processing** during their stay there. If these goods have been subject to processing in Japan, they do not satisfy the direct transport rule and we would not be able to claim a preferential rate of duty.

[Art 78
2454/93](#)

5.12 Certificate of origin

The final condition we need to satisfy is that a valid **Certificate of Origin** must be submitted with the import entry. For GSP preferences this is a **Form A**, which is stamped by the exporting authorities. See Annex 17 for an example. In place of a Form A, a **declaration** could be made on the **invoice** accompanying the goods, provided that certain conditions are satisfied. These conditions are detailed in Article 89 and cover **exporters that have been approved** to make invoice declarations, or shipments up to a **maximum value of 6,000 Euros**.

[Annex 17
2454/93](#)

[Art 89
2454/93](#)

For most other preference agreements a **Form EUR1**, as shown in Annex 21 is used, or again, approved exporters may be able to complete an **Invoice Declaration** in place of this form.

[Annex 21
2454/93](#)

GSP Forms A are valid for 10 months from the date of issue. You will see this in Article 90(b) and **EUR 1 Certificates** are generally valid for **4 or 5 months**.

[Art 90\(b\)
2454/93](#)

5.13 Problems

The final part of this chapter looks at the specific problems that some importers have had when claiming preference.

Illustration 6

You have been importing your products from a preference receiving country that receives a 0% rate of duty. Had you not claimed preference the full rate of duty was 12%. Customs then carry out an audit of your records and realise that you should not have claimed preference on those goods as the origin rules have not been met. However, you have got stamped certificates of origin for the goods, as the overseas authorities believed the rules were met.

Customs have the right to go back over a **three year period** to **retrospectively recover duty** from an importer. They can do this in accordance with Article 221(3) of the Code.

[Art 221\(3\)
2913/92](#)

You are being faced with paying hundreds of thousands of pounds of back duty to Customs. Is there any defence that you can raise so that you don't have to pay this amount?

5.14 Defences to back duty claims

This issue has been the subject of a number of Court decisions and as a result new legislation was enacted into the Code. This takes the form of Article 220(2) (b). This article applies where there has been an **error on the part of the customs authorities that could not reasonably have been detected** by the importer and the importer has **acted in good faith** and the importer has taken **due care** in importing the goods under the preferential regime. Customs will **not retrospectively recover the duty**. In our scenario an error has occurred by the exporting authorities, as they have incorrectly stamped the certificates of origin.

[Art 220\(2\)\(b\)
2913/92](#)

What does an importer have to do to fall within the category in Article 220 and not be faced with some large retrospective duty reclaims?

If the importer has:

- **understood the origin rules**
- actually **visited the exporters premises** to see the factories working and the goods being produced; and
- has **written confirmation from his supplier** that the rules have been met then it would be hard for the authorities to say that he has not taken due care and that the error could not have been reasonably detected. You will see that we refer to this article again in the chapter on administration and appeals.

5.15 Binding origin information (BOI) rulings

There are other ways that an importer can protect himself against back duty claims. One of these is to apply for a **binding origin information** ruling or **BOI**. These are covered in Article 12 of the Code. These **rulings are obtained from Customs** and provide the importer with certainty as to the origin of his imported goods. Once granted they are **valid for three years in all EU Member States**. This should stop Customs retrospectively going back and recovering duty, provided of course, that the importer gave Customs correct information on which the BOI was based in the first place!

[Art 12
2913/92](#)

Another advantage of a BOI is that if it **becomes invalid due to a change in legislation**, then usually the **importer can continue using it for three to six months** going forwards provided he has got **binding contracts concluded with his supplier** i.e. he has based the price of the goods from his supplier on the basis that he would receive a preferential duty rate.

5.16 Other ways of protecting against back duty claims

Another way that an importer might protect himself against large back duty claims is by taking out **insurance**.

He could also get a **clause included in the contracts with his suppliers providing that the supplier will indemnify him** if the origin rules are not met.

And the final fool proof way of ensuring that he will not be subject to any back duty claims is **not to claim the preferential rate** at all and pay the full rate. However, this is going to increase his costs, which he will then have to pass on to the end customer - so paying the full rate may not be an option for him. If he is in any doubt, he could pay the full rate and once satisfied that the goods do qualify for preference, he could **lodge a repayment claim** with Customs. You will see more on this in the chapter on administration and appeals.

Example 1

Fill in the blanks with the missing words.

To obtain preference, goods must in the beneficiary country, be from the beneficiary country and be accompanied by the requisite of

Simple processes are contained in Article of the Implementing Regulations.

Some countries form groups, whereby goods originating in one country of the group, which are subjected to working/processing in another country of the group, count as originating in the other country.

Example 2

Fill in the blanks with the missing words.

An importer can protect himself from back duty claims by:

1. Applying for a ruling, which is legally binding for 3 years.
2. By taking out
3. By including a in the contract with his supplier, to get re-imbursed if the goods don't originate in that country; and
4. By making sure that he the rules.

Answer 1

To obtain preference, goods must originate in the beneficiary country, be transported direct from the beneficiary country and be accompanied by the requisite certificate of origin.

Simple processes are contained in Article 70 of the Implementing Regulations.

Some countries form Regional groups, whereby goods originating in one country of the group, which are subjected to working or processing in another country of the group, count as originating in the other country.

Answer 2

An importer can protect himself from back duty claims by:

1. Applying for a binding origin information ruling, which is legally binding for 3 years.
2. By taking out insurance
3. By including a clause in the contract with his supplier, to get re-imbursed if the goods don't originate in that country; and
4. By making sure that he understands the origin rules.