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**FRAUD IN THE TRANSIT PROCEDURE, SOLUTIONS FORESEEN AND
PERSPECTIVES FOR THE FUTURE**

1. INTRODUCTION

This paper informs the Council and European Parliament of serious fraud in the transit procedures. Such fraud, which involves organised crime, is known to have had a financial impact for the Community and Member States of a minimum of 750 million ECU¹, during the period from 1990 to date. This amount does not take into account economic damage to business.

The measures proposed herein form an integral part of the Commission's Anti-Fraud Strategy Work Programme announced in 1994, which include specific action in the tightening of control procedures, and in the improvement and computerisation of transit procedures.

The paper describes the measures which have already been adopted and those which are proposed to solve the problems in the short term. It gives an overview of a long term solution to computerise the transit system.

The Council and the European Parliament are requested to support the Commission's initiatives in this area.

2. BACKGROUND

European trade has for long relied on transit systems that allow suspension of duties and other charges payable as well as non-fiscal measures for goods crossing more than one country under customs control, provided a guarantee is established to ensure the collection of duties and other charges payable in the event of irregularities.

The use of transit systems in the Community has always been promoted in particular because it is the only way to avoid congestion at the border. These systems enable the more intensive customs controls, which are necessary for specific customs procedures, to be concentrated at the office of destination where usually most information is available concerning the consignment and the consignee.

The main transit procedures used in the Community are: Community transit, common transit, which is an extension of Community transit to the EFTA countries under the Common Transit Convention of 1987, and the international transit regime by road as provided for in the TIR Convention of 1975.

The transit regimes have been designed to facilitate trade and are largely based on a general trust in the honesty of the majority of economic operators. They are the result of a search for a balance between, on the one hand, the needs of honest traders in their aims for competitiveness by reducing operating costs and, on the other hand, the requirements for protection of the internal economy by an effective control of international transactions.

¹320 Mecus own resources and 430 M.ecus VAT and excise

The transit system has developed over the years. It began as an internal Community procedure in 1969 to control movement of goods between Member States and movements to and from third countries. From its inception it was a trade facilitation measure as it superseded a succession of national transit procedures. After being initially extended to Switzerland and Austria, the system was extended in 1987 to all the EFTA countries by the 'Convention on a common transit procedure'. Already it could be considered as anticipating many of the advantages of the internal market. A major development affecting the transit system was the completion of the single market in 1993. This established the principle that all goods transported within the customs territory of the Community were deemed to be Community goods unless demonstrated otherwise. Thus all customs formalities and controls on such goods were eliminated and for these movements the transit procedure was no longer required.

Geo-political considerations arising from liberalisation of relations with Eastern and Central Europe has had an important impact on the development of trade with the countries in this area. These countries have turned their eyes towards the facilities offered by the Western European countries and have been increasingly demanding to participate in customs systems which promote and facilitate trade. Actions are being taken to extend the common transit system to Poland, Hungary, the Czech Republic and Slovak Republic. It is expected they will join the system in mid 1996. Other Eastern European countries are queuing up to join the Convention. However until these countries join the Common Transit Convention, the international TIR Convention will remain as the only transit procedure for the movement of goods between the Community and these countries.

3. BASIC OUTLINE OF TRANSIT SYSTEM

The Community transit procedure allows the movement, within the Community, of goods coming from or going to third countries under customs control with suspension of duties and other charges payable as well as measures resulting from Community policies. It is based on designating a person as a principal. His most important obligations are:

- the provision of a guarantee to ensure the collection of duties and other charges payable in the event of irregularities;
- the production of the goods intact at the customs office of destination within the prescribed time limit.

The procedure starts with the presentation of goods and the validation of a transit document at the office of departure. One copy is kept at this office to control the regularity of the operation. The goods move through the territory of the Community accompanied by the document and have to be produced at the customs office of destination within the prescribed time limit. The customs authorities at the office of destination carry out the necessary controls, notes the outcome on the document and returns a copy of such document to the office of departure. If everything is in order, the movement is discharged and the principal is released from his responsibilities.

In the case of an offence or irregularity committed during a transit operation the duties and other charges are recovered. The guarantee covering the transit operation will not be released until the duties and other charges have been paid. However, the guarantor shall be released from his obligations upon expiry of a period of twelve months from the date of registration of the T1 declaration where he has not been advised by the Customs authorities of the Member State of departure of the non-discharge of the T1 document.

4. PRINCIPAL ATTACKS ON THE SYSTEM

4.1 Introduction

It is not an exaggeration to say that the transit systems, for long a pillar of the customs union, are now in crisis.

4.2 Problems at operational level

The customs union being a single entity, its integrity is the affair of everyone. National administrations are responsible for the quality of administrative controls and the management of the system. The quality of these controls has fallen progressively over the last few years. This has resulted in an increasing number of complaints from economic operators concerning unacceptable delays in the system. These delays are typically caused by belated return of the return copy, leading to the accumulation of uncleared documents. Enquiry procedures regarding outstanding movements are not initiated at a sufficiently early stage, and are not pursued with sufficient priority and vigour. Legislation and administrative provisions are not always applied by Member States in such a way that good management is guaranteed. The consequence is that failure in any part of the system jeopardises the whole. These highlighted problems show that Member States' administrations have given lower priority to transit controls notably because on the one hand it has been considered as "someone else's problem" and on the other hand because in the completion of the single market Member States often had other priorities which resulted in a reallocation of resources to the detriment of transit.

Economic operators are responsible for the production of the goods and documentation intact at the Customs office of destination within the prescribed time limits. For sensitive goods they have to be particularly vigilant as regard the "clients" with whom they do business. Because of competitiveness this vigilance is not always applied.

The result is that these operational problems have created an ideal breeding ground for fraudulent activities.

4.3 Fraud

Since the opening up of the borders of Eastern and Central Europe to international trade the transit system has been targeted by major criminal networks for highly profitable fraudulent activities. Fraud has become a major and growing problem not only resulting in enormous revenue losses, but also in substantial economic damage due to the illicit competition from fraudulent goods and the evasion of Community policies, including sanitary legislation. In addition there is growing uncertainty for honest economic operators as they have to suffer the consequences of the impact of fraud and the effects of amended legislation under which, for example, the comprehensive guarantee for certain kinds of goods has been increased.

Fraud has now spilled over into the TIR system. A special carnet "Tobacco/Alcohol", which requires a higher guarantee than for normal carnets, was introduced last year. However, fraud for these products has increased to such an extent that insurance companies no longer wish to guarantee these carnets because the risks are too high. Therefore, the national associations and International Road Transport Union, which issue the TIR carnets, are now suspending the delivery of these special carnets, which places even greater pressure on the other transit systems.

4.4 Types of fraud

The fraudulent transit operations concern mainly goods which are subject to a high taxation (e.g. a single container load of cigarettes attracts duties and taxes of approximately 1 million ECU) or a high profitability due to the level of protection of Community policies for e.g. CAP products (meat, milk, sugar ...).

It should be noted that law-abiding economic operators are frequently being misused by major criminal networks which specialise in these frauds. The fraud in the transit procedure is mainly manifested by:

- non-presentation of consignments at the office of destination, but which are brought into free circulation in the Community without payment of duties and taxes and without application of any non-fiscal measures which might be applicable;

- the appearance that a consignment has been presented to the office of destination by forging the customs endorsement on the copy which is returned to the office of departure by the use of stolen or forged customs stamps.

The basic problem in this sector is that fraud is often only detected at a very late stage because of unacceptable delays in the system and because some of its mechanisms are no longer adapted to the present situation.

However, it is necessary to draw attention to the fact that in the area of own resources, the amounts notified by the Member States under the provisions of Council Regulation No 1552/89 of 29 May 1989 implementing the system of the Communities' own resources² corresponding to cases of fraud or irregularity remain at a very low level - about a third of the amount of known fraud. On the basis of these notifications, the amounts recovered are for that matter very low even if for some of them recovery is dependent on delays due to legal action. On this basis, according to the information supplied to the Commission, of more than 1000 cases notified under Regulation 1552/89 only 22 have been pursued by action in the courts.

4.5 Conclusion

Given the enlargement of the Community and the further extension of the common transit arrangements to more countries, the pressures indicated above can only increase. Moreover, despite the best efforts of the specialised investigation services of the Member States it has proved impossible to compensate for the weaknesses referred to above. The challenge for the European Union is how to reassert authority over the system, guarantee high quality customs controls and preserve the proper functioning of the internal market without losing the benefits of trade facilitation.

5. MEASURES TAKEN

During 1994 various measures have been taken in both the legislative and operational areas. They include :

- revised methods of handling the list of fraud-sensitive products in order to provide more flexibility in taking immediate action where necessary;
- provisions increasing the level of the comprehensive guarantee to cover the full amount of duties and other charges payable for a number of sensitive goods;
- the adjustment of the transport period in the light of the distance to be covered for the dispatch of the goods;
- increase in the actions co-ordinated by the Commission to deal with fraud cases (a strengthening of the co-operation between investigation services and an increased number of inquiry missions in third countries);
- the application of an early warning system for the exchange of information between the office of departure and the office of destination concerning consignments with sensitive goods;

²320 Mecus (own resources)

- in the TIR area, the introduction at international level of a special carnet "Tobacco/Alcohol" covered by a higher guarantee than for the normal carnets;
- strengthening of the contacts with the IRU (International Road Transport Union) to improve the management of the TIR regime and of the system of guarantees .

6. SOLUTIONS FORESEEN AND PERSPECTIVES FOR THE FUTURE

6.1 Introduction

Currently the system is operating with about 18 million transit declarations annually and on average about 1 million enquiries outstanding at any time of the year. The saturation point has been reached or is fast approaching in most customs services. Therefore, it is not credible to believe that a system, currently covering 18 countries and probably soon to be 22 or more, can continue to work by purely paper-based methods. However, over the years new technology and working methods have been developed. The Commission has for a long time been convinced that computerisation is the only solution. The main obstacle to previous attempts has been the resistance of certain Member States partly because of their budgetary reasons and partly because of other national priorities.

6.2 Long term solution

6.2.1 Transit Computerisation Project

The Commission services took the initiative to computerise the transit system and as a result of talks between the EU and EFTA countries a feasibility study was agreed in September 1993. As a result of this study it was agreed on 8 December 1994 to proceed with the project.

The aim of computerising transit is to make the transit procedure more effective and efficient, to provide the means for effective detection and prevention of fraud, and to enhance the facilities available to economic operators who use the transit procedure.

The proposed computerisation entails the data capture of consignment details at departure, ideally by direct links with economic operators, transmission of those details, over an international network and linked to the national computers systems at each end, to an office of destination in another country. The controls would be carried out on the basis of the electronic message, and the results of controls would be returned by the same route to the office of departure, thereby eliminating the need to return a paper copy of the transit document. The use of messages to communicate between offices would ensure integrity of departure information and of the outcome of the checks at the office of destination, thus solving the problem of alteration of information and of the use of forged stamps. The system would provide enquiry procedures for consignments which had not been discharged within the time allowed for their movement. In a computerised environment the customs authorities could detect cases of fraud at a very early stage and would therefore be able to take appropriate counter measures. Additionally, the computerised system will be used for a better management of the system of guarantees. The establishment of databases of transit movements would allow risk analysis techniques to be applied to particular consignments.

Because of the complexity of such a system, implementation is not expected to be finalised before early 1998.

Moreover, it should be clear that, besides computerisation, an increase of the number of physical controls at offices of destination will be necessary in order to prevent fraud by means of substitution of goods en route.

6.2.2 Cost/benefit analysis

A preliminary cost/benefit analysis indicates an operational net cost over the 5 years beginning in 1995 of about 8 million ECU. Over 7 years this becomes a net operational benefit of about 17.5 million ECU.

In order to implement a computerised transit system, investment will be required. The national investments costs (excluding running costs) amount to 13 million ECU over 5 years. An additional 9.5 million ECU is required at Community level to fund the central investment.

However, these amounts should be viewed in the light of the likely impact of computerisation on fraud. An estimate based on a conservative assumption, shows some 1,200 million ECU benefits over 5 years. Considerable additional but unquantifiable benefits could be expected to accrue from increased protection for those trading sectors which are currently undermined by fraudulent operations and from the strategic advantages which an international customs network would bring.

6.3 Short term solutions

6.3.1 Introduction

The Commission's aim is to provide a complete solution for the imperfections of the transit system by implementing the computerisation project. However, the earliest date for full application of the system is 1998. Until then all parties are, of necessity, to retain the paper-based transit system. However, the shortcomings in the present system are unacceptable for the intervening three year period and it is necessary to introduce short term improvements in order to improve the controls, while maintaining as far as possible an appropriate level of trade facilitation.

6.3.2 Measures proposed

Substantive measures proposed fall into two prime categories and include:

Improvement and strengthening of the transit legislation:

- The introduction of the necessary flexibility to forbid throughout the Union the use of the comprehensive guarantee for those sensitive goods which present high risks of fraud;
- the introduction of an expedited procedure for returning and discharging transit documents concerning sensitive products, possibly including special identification of these documents;
- prohibiting a change of office of destination for sensitive goods (or at least allowing a change only on fulfilment of conditions which would enable the transport operation to be monitored;)
- the drawing-up of binding itineraries;
- the reduction of the time-limits and stages provided for under the inquiry procedure.

The prevention and detection of fraud:

- the strengthening of the special Task Group set up by the Commission's Anti-Fraud Unit UCLAF charged, in co-operation with Member States, with taking all appropriate measures in the operational frameworks necessary to combat fraud in this sector;
- fuller involvement of economic operators in action to defeat fraud, (including clear legal provisions to create a shared financial responsibility for transporters);
- strengthening administrative and operational co-operation with countries neighbouring the European Union.

6.3.3 Other considerations

It should be clear that before extending the common transit procedure to applicant third countries it is essential these countries have a properly functioning administrative structure in place, to ensure that the system will not be undermined by criminal activities. This is a vital necessity for the Community as well as for the new partner countries whose economies could be substantially damaged by fraud in the transit procedures.

Also within the TIR regime there has been significant increase in fraudulent activities. Most of the cases concern tobacco and alcohol. For this reason a separate carnet has been introduced for which a higher guarantee than normal is required (Carnet TIR "Tobacco/Alcohol"). However, for these kinds of goods it has proved still to be inadequate. It is now proposed to increase the guarantee to a level equal to the full amount of the duties and other charges payable. Additionally, for this carnet it is proposed to introduce an accelerated inquiry procedure, a procedure for an accelerated return of the return copy and the introduction of a system for the exchange of information concerning fraud.

7. CONCLUSIONS

The measures discussed herein are wholly in line with the Commission's Anti-Fraud Strategy and fully reflect the importance placed on this initiative by the Commission and the concerns expressed by the Parliament and the Council.

Transit offers many advantages to a Community as economically complex as ours. We are unlikely to be able to offer operators the full benefits of an integrated internal market without such a regime. It is essential for the operation of the internal market and the EEA arrangements. It is also a vital vector for the integration of the countries of Eastern and Central Europe into EU and EEA trade flows. The economic advantages to European trading interests are undeniable.

There is no viable alternative to transit. To insist on the payment of duties and taxes and to apply systematic controls at the point of entry to the Community would result in congestion at the external borders especially at the road crossings in Central Europe and is therefore unpalatable and unthinkable. The existence of the transit systems remains indispensable. However, if present arrangements are fraud-ridden, slow, uncertain and burdensome, the system will lose its credibility. There is no choice, then, but to agree now to rapid and effective change.

The present system getting to the end of its operational life, computerisation offers major advantages. In particular it is the only credible protection against fraud and abuse. The costs of computerising the transit system would be largely offset by the savings. Furthermore a modest expenditure from the EU budget would guarantee business and revenue substantial benefits.

However, interim measures are essential to shore up the system until new arrangements are implemented. If rapidly and fully implemented, this would be sufficient to keep trade moving while ensuring satisfactory control.

Since these initiatives are of great importance at Community and Member State level, the Council and Parliament are requested to support the Commission's solutions foreseen and its perspectives for the future.

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