

TradeWatch



EY Global Trade

Issue 3 2023



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Welcome to Issue 3 2023 of *TradeWatch*



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Welcome to Issue 3, 2023 of *TradeWatch*, the global EY organization's global trade magazine.

As we approach the end of 2023, we continue to explore many of the themes that we have dealt with in previous issues of *TradeWatch* and in our thought leadership publications. It can be difficult to keep abreast of these fast-paced developments and their impact on your trade operations. But doing so is more important than ever. Dealing effectively with new compliance and reporting obligations is crucial to avoiding additional costs and delays in moving goods internationally. But it is also important to look ahead to anticipate the changes that will potentially affect your business in 2024 and beyond so that you can adapt your processes, procedures and even trade strategy accordingly.

Three megatrends affecting global trade

In past editions of *TradeWatch*, we have outlined how three global megatrends – disruption, sustainability, and transformation – are impacting trade globally. These trends feature in two articles available on [ey.com](https://www.ey.com) that we encourage you to read [How three global trends are shaping Indirect Tax](#) and [How disruption is shaping opportunities for global trade](#). These pieces identify how business leaders should respond to these trends and find opportunities to help their organizations thrive in turbulent times.

Supply chain disruption continues

Sadly, disruption from events such as the war in Ukraine continues. Trade functions must continue to keep abreast of these events and closely monitor

their effects on global supply chains and any sanctions that may be imposed, which are often introduced at short notice.

The United Kingdom (UK) leaving the European Union (EU) (Brexit) continues to affect trade between Great Britain, Northern Ireland, and the EU. In this edition of *TradeWatch*, we provide an update on the UK-EU Windsor Framework, taking stock of the current situation and looking ahead to measures expected next year and in 2025.

Sustainability and ESG – hot topics for trade

In this edition of *TradeWatch*, three articles in our Sustainability section focus on carbon border adjustment mechanisms (CBAMs). [Australia considers CBAM to address carbon leakage](#) looks at the possible future introduction of an Australian CBAM. While in the European Union (EU), CBAM is already in effect from 1 October 2023. The details of the EU CBAM and how businesses should respond are outlined in [EU: CBAM in force](#) and in [How tax departments should prepare for CBAM](#).

Carbon measures are not the whole environmental, social or governance (ESG) story for trade. Waste, pollution, and the need to increase circularity are dealt with in [EU: Commission and Council take steps as part of the circular economy action plan – new rules on textiles and batteries](#) and in [UK: Reducing waste](#). We also report on further US measures related to the implementation of the [Uyghur Forced Labor Prevention Act in action: updated guidance and trends](#).

Transformation

Digitalization is another disruptive force transforming society and the world of business – whether it be through new forms of payment or through new ways of delivering goods and services. In [EU: Proposed customs reform – a modern approach to e-commerce](#), we look at how the EU customs reforms are looking to align customs rules with existing VAT rules for e-commerce. In Colombia, we consider the impact of recent rulings that [crypto assets cannot be used as a means of payment for foreign trade operations](#). While in the UK, the [Electronic Trade Documents Act](#) will have far-reaching implications for customs declarations.

The changing trade function

The role of the trade function has changed in many organizations in response to these disruptive events and it continues to evolve. This is a topic that we have explored in depth recently in our report, [‘Refocusing the global trade functional organization – a global trade perspective’](#) and in [TradeWatch Issue 2 2023](#) in ‘Future-proofing the customs and trade function’. In this edition of *TradeWatch*, we consider specifically how the trade function should respond to the challenge posed by new obligations and priorities related to sustainability in [The role of customs and trade functions in the ESG era](#).

Customs reform

Customs authorities are being challenged to keep pace with how goods and services are being traded internationally in the digital age, leading international organizations to review and revise their regulations and guidelines.

In this issue of *TradeWatch*, we look at progress in reforms in international customs rules and regulations. While the [World Customs Organization harmonized classification reforms](#) are delayed, the EU is forging ahead with its reform of the [Union Customs Code](#).¹ And in Japan, there is a new definition of [Importer of Record](#).

Customs valuation

Customs valuation and the interplay with transfer pricing continues to be a hot topic around the world. We have dealt with this topic in recent issues of *TradeWatch*. In this issue, we feature the [Interplay between transfer pricing and customs valuation in Asia-Pacific](#). We provide insights into some of the different approaches and practices adopted by customs authorities in the region and outline possible strategies for businesses, including illustrations for select jurisdictions. We also look specifically at [Trends in Customs Valuation in Vietnam](#).

Trade facilitation

The effective use of free trade agreements (FTAs), special economic zones and trade facilitation measures is an essential part of managing trade operations as supply chains continue to transform.

[The LATAM advantage: A look at the region's thriving Free Trade Zones](#), focuses on some of the features and benefits of these special regimes in Latin America. Staying in Latin America, we also outline some key enhancements to [Authorized Economic Operator \(AEO\) program in Brazil](#).

Keep up to date with developments in trade

We hope you enjoy this edition of *TradeWatch*. We aim to reflect the key trends affecting international businesses and provide news and insights you can use to inform your trade strategy and improve your trade operations.

You can also keep up to date with developments in global trade by subscribing to EY Tax Alerts and to future editions of our *TradeWatch* and *TradeFlash* publications by visiting ey.com/global-trade.

If you would like more information on any of the topics covered in this issue or how they may impact your business, please reach out to the authors listed with the articles or any of the EY Global Trade professionals listed in the [Contacts](#) section of the magazine. We also welcome your feedback and suggestions for future editions. ■

1. EY has submitted a feedback paper to the European Commission in response to the call for feedback on the proposed EU Customs Reform, [European Commission website](#). [Find it here](#).

Harmonized System review cycle extended to 2028

The Harmonized Commodity Description and Coding System (Harmonized System or HS) is the international product classification nomenclature developed by the World Customs Organization (WCO) and used in over 200 jurisdictions as the basis for customs duties and the compilation of trade statistics. The HS is managed by the Harmonized System Committee (HSC), which meets regularly to provide guidance and resolve interpretive disputes. Typically, the HSC adopts updates to the HS every five years, with the most recent HS effective in 2022. However, in September 2023, the HSC approved the extension of the current review cycle from five years to six years – there will be no HS 2027 edition, and instead, the next HS edition will be issued in 2028.

The decision to extend the review cycle is largely due to a pause in activity during the COVID-19 pandemic. During the height of the pandemic, most in-person meetings for the HSC and HS Review Subcommittee (RSC), which analyzes potential changes required in the HS, were canceled. The HSC and RSC held virtual meetings, but the virtual meeting environment proved difficult for discussions needed to reach agreement on the content changes for the HS 2027 edition. The current extension appears to be a unique exception to the standard review cycle, and

it is not expected to create a precedent for routinely extending the review cycle timeline.

While 2027 is still more than three years away, many countries need significant lead time to implement changes to the HS. Having a new HS ready to implement worldwide in 2027 effectively requires the HSC to agree on content in early 2024. In fact, at the time the HSC decided to extend the review cycle, the RSC had not yet finalized major amendment recommendations for the HS 2027 edition. Absent the extension, the HS 2027 edition may have had only a limited number of amendments that were agreeable to all HSC members, or there may have been amendments based on rushed discussions without the normal time for consideration.

This extension also provides some additional time to align the current WCO strategic review of the overall health and effectiveness of the HS, which began in 2022, with the next HS edition. The HS is over 30 years old, and many changes have occurred in the global trade system in that time. Topics to be addressed in the WCO review include the overall complexity of HS classification, the effectiveness of HS supporting tools (e.g., explanatory notes), the HS's ability to adjust to changing policy needs in the international trade community and other similar long-term considerations. With the extended review



cycle for the next HS edition, it is possible that some of the recommendations resulting from the review could be implemented in the 2028 HS.

Considerations for businesses

Though HSC members are governments, in many instances recommendations for changes to the HS are initiated by, or influenced by, a business request to a government. While the lead time is long, a business facing inconsistent classification interpretations that would be benefitted by a change in HS nomenclature should consider opportunities to make changes effective in 2028. ■

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How disruption is shaping opportunities for global trade

In the face of continued geopolitical uncertainty, indirect tax and trade functions have an opportunity to show their real value.

[Read the article on ey.com.](#) ■



How trade functions are transforming the 'new normal'

A new perspective on recalibrating, refocusing and re-establishing companies' interest in their global trade function.

[Read the article on ey.com.](#) ■



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23 November 2023

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Refocusing on the global trade functional organization: A global trade perspective

5 October 2023

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UK: Understanding the true impact of the EU's Carbon Border Adjustment Mechanism (CBAM) for non-EU headquartered groups

5 October 2023

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Europe West: EU Carbon Border Adjustment Mechanism (CBAM): What effective compliance looks like

4 October 2023

Register [here](#) for the recording



Reform of the Union Customs Code

13 September 2023

Find the recordings for these timezones:

[APAC and EMEIA](#)
[EMEIA and Americas](#)



Reform of the Union Customs Code

13 September 2023

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CESA: EU Carbon Border Adjustment Mechanism goes live in October: Are you prepared for the reporting obligations?

6 September 2023

Find the recording [here](#)



Switzerland: EY Sustainability Tax webcast on CBAM

5 September 2023

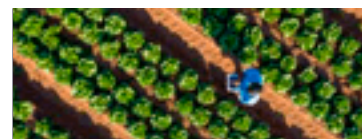
Find the recording [here](#)



How to prioritize governance in your organization's ESG strategy

29 July 2023

Find the recording [here](#)



Sustainability and the Tax impact on business: Africa focus

12 July 2023

Find the recording [here](#)

The LATAM advantage: A look at the region's thriving Free Trade Zones

Latin America (Latam) Special Economic Areas (SEAs) – known as Free Trade Zones (FTZs), among other names – are more dynamic than ever, with more than 700 zones generating around 1.1 million direct jobs across the region.¹ Although we will focus on some of the most significant players in this article – Brazil, Colombia, Costa Rica, Panama, Mexico and Peru – it is important to recognize that these zones are widespread, contributing to a substantial part of Latam's exports.

These selected countries potentially offer a compelling blend of tax incentives, compliance frameworks and untapped market opportunities. This article will cover each country's multifaceted appeal, revealing how they each leverage their SEAs for manufacturing and service sectors.

So, let's take a closer look at each of these countries to better understand the dynamic range of benefits and compliance requirements they offer.

Brazil

Brazil's Export Processing Zones (EPZs) are specialized free trade areas primarily focused on production and trading for foreign markets. EPZs are primary zones for controlling export customs clearance. Since the introduction of the first EPZ, 14 more zones have been established across Brazil, emphasizing the country's commitment to foreign trade and economic development.

Operating within an EPZ requires strict adherence to legal standards, including rules around export customs clearance and tax exemptions. They are monitored by the Brazilian Inland Revenue Service (IRS) with operators using specific software, providing full access to the authorities 24-7.



¹ Information obtained from the Association of Free Zones of the Americas (AZFA), accessed 4 October 2023. [Find it here.](#)

While EPZs eliminate the need for specific federal licenses and authorizations, businesses must still comply with regulatory standards, especially those concerning health and environmental protection. These compliance requirements help to ensure a quality and trustworthy business environment.

Companies operating in EPZs enjoy a wide range of financial benefits. Not only do they get tax exemptions on domestic acquisitions and exports, but they also benefit from specific exemptions from import tax and other indirect taxes.

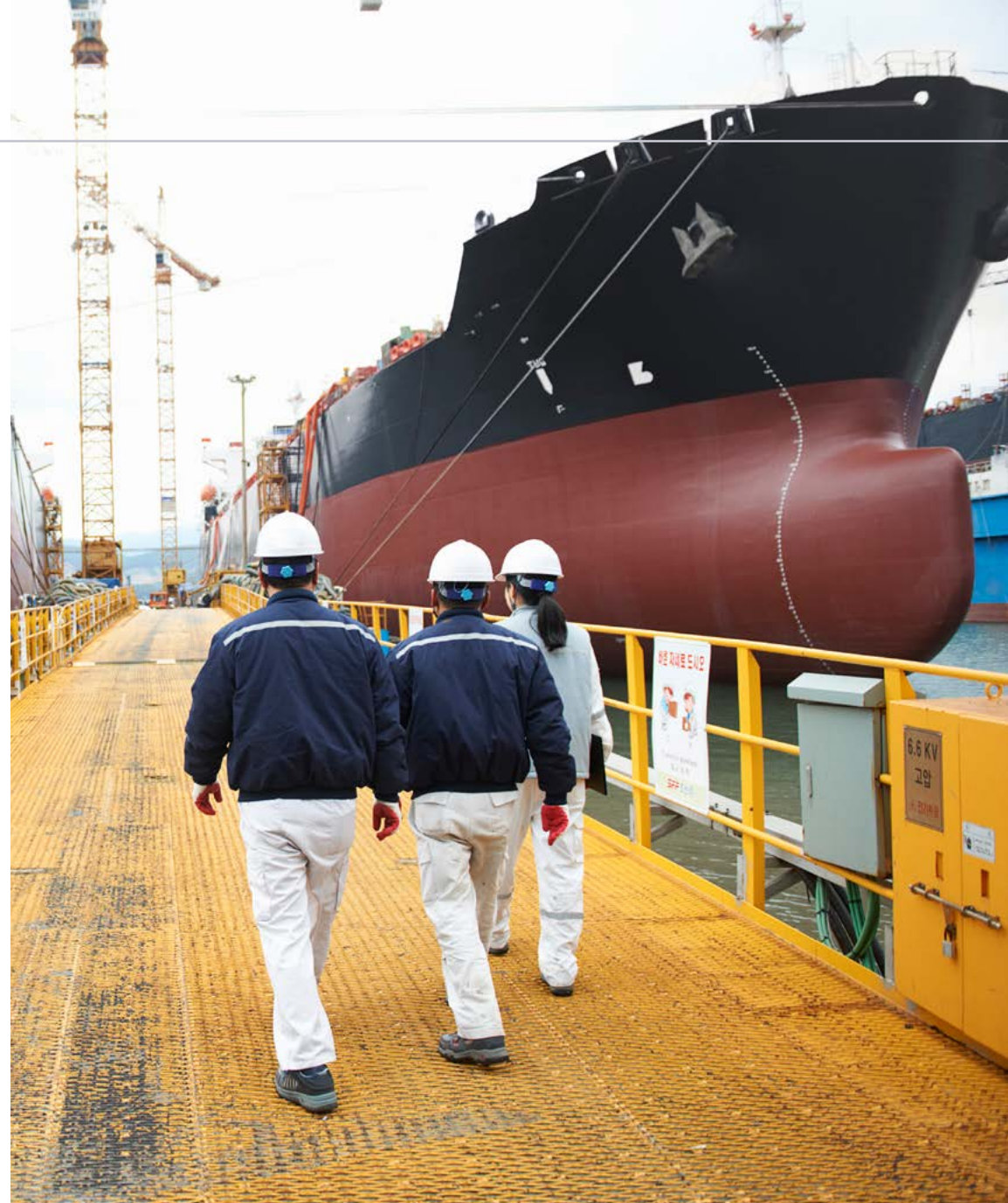
In addition to federal-level benefits, EPZs offer state-level tax advantages, including different tax treatments for ICMS (Tax on Circulation of Goods and Provision of Transportation and Communications Services). Furthermore, companies in EPZs can keep 100% of their export-generated currency overseas, offering significant financial flexibility and cost-reduction advantages; however, it is important to note that this last benefit is not guaranteed by law but by a resolution provided by the National Monetary Council.

Colombia

Colombia is home to 124 FTZs, divided into 42 multicompany permanent zones and 82 special single-company permanent zones. These zones are spread across 20 departments and host over 1,000 companies.² Notably, 90% of these companies are “small and medium-sized enterprises” (SMEs) engaged in industrial goods and services sectors. Multicompany zones facilitate various enterprises to operate under shared infrastructure, while special single-company zones are tailored for specific, large-scale business endeavors.

On the compliance front, Colombia’s FTZs operate under stringent regulations. Companies must adhere to comprehensive rules and procedures, ensuring that the zones remain reputable and well-organized.

From 2024, Colombia’s FTZs will offer a specialized tax benefit structure. A favorable 20% income tax rate will apply only to income from the export of goods or services, certain logistical services, port services, and offshore and refining activities. This focused tax benefit complements legal incentives, such as duty-free importation and exportation and value-added tax (VAT) exemptions, aiming to boost specific sectors and enhance overall business competitiveness.



² Data obtained from *Diario la Republica*, dated 28 April 2023, based on information provided by Angelica Peña, the manager of the Free Zone Users Chamber of the Andi. [Find it here.](#)

Costa Rica

Costa Rica's FTZ regime currently benefits more than 494 companies.³ This regime offers extensive benefits tailor-made for businesses, such as strategic service providers, park administrators, strategic manufacturing sectors, research and development, services, and trading companies. Activities such as mining and hydrocarbon exploration are excluded.

The compliance environment in Costa Rica's FTZs is designed to be both rigorous and supportive, aiming to build trust and quality. The authorities work closely with businesses to ensure regulations are met, fostering a smooth operational landscape.

The benefits granted to FTZs include duty exemptions on imported goods and the exception of other charges and taxes, such as VAT. There are also exemptions from real estate transfer taxes and municipal patents for several years, depending on the zone type. Companies are exempt from remittance taxes and all gross or net earnings, dividends, revenues or sales levies. Manufacturers can apply for tax credits if the gains are reinvested in fixed assets or training expenses. Companies also gain access to training and educational programs. The regime is limited to a period of several years, depending on the license type, but it can be extended, and companies may reapply if they meet the requirements.

Panama

Panama has 15 active FTZs,⁴ with six more in the pipeline, making it an attractive location for a variety of business sectors. Due to its logistics facilities, it is a preferred location for establishing distribution and production hubs for Latam and the US. Regulatory audits in these zones are designed to foster trust and ease compliance for foreign and domestic investors. The zones can be privately owned, be state-owned or have mixed ownership, and they can be established almost anywhere in the country.

The zones cater to a range of activities, from manufacturing and high-tech sectors to logistics, environmental services, health care, higher education and research. Key benefits include direct tax and import duty exemptions on materials, goods and services.

Recent approvals by the Panamanian Council of Ministers include the establishment of the new FTZ known as Tech Valley. This zone plans an initial investment of around Panamanian Balboa (PAB) 50 million (USD50 million) and aims to generate over 1,140 direct and 3,570 indirect jobs.⁵

Another significant development is the authorizing of the largest data center with an initial investment of PAB11.5 million (USD11.5 million).⁶ This center aims to host numerous companies and enhance Panama's strategy to become the digital hub of the region, offering cost-effective international traffic and low latency, thereby increasing Panama's competitive edge and connectivity.

Mexico

In Mexico, more than 6,000 companies across various industries take advantage of the unique Manufacturing, Maquila and Export Services Industries (IMMEX) program, which is not a traditional FTZ.⁷ Designed to support manufacturing activities and services, such as shared services centers, the program is open to all sectors, as long as a specific portion of the products manufactured or the services provided are ultimately exported. These companies can temporarily import raw materials duty-free, with some exceptions, with the expectation of adding value to them before exporting the final products or providing the services.

Compliance is a crucial aspect of the IMMEX program, requiring rigorous adherence to Mexican tax laws. Special audits may be applied to participants to ensure they meet the program's compliance standards. Moreover, companies must have a bond or VAT certification to utilize the program's offerings fully.

The benefits of participating in IMMEX extend beyond mere tax advantages. Companies can apply for reduced customs processing fees and import VAT credits, provided a bond or VAT certification exists. Additionally, temporarily imported products can, in some instances, be sold in the Mexican market. This flexibility allows companies to diversify import sources and capitalize on nearshore manufacturing benefits.

³ Data obtained from PROCOMER (the Foreign Trade Promoter of Costa Rica) website. [Find it here.](#)

⁴ "Zonas Francas," Republic of Panama's National Government website. [Find it here.](#)

⁵ "Panamá invertirá 78.5 mdd para nuevas zonas francas," *Forbes Central America*, 13 February 2023. [Find it here.](#)

⁶ Ibid.

⁷ Data is based on the public directories of companies with an IMMEX program, provided for online consultation by the Ministry of Economy in Mexico. [Find it here.](#)

Peru

Peru's Special Economic Zones (ZEEs) are emerging as significant players in Latam for businesses interested in the region's diversified industrial landscape. With nine ZEEs, four of which are operational, these zones provide multiple avenues for international trade and production.

Compliance is eased through a regulatory framework that offers unique and flexible tax and customs legislation.

Regarding tax benefits, businesses operating in Peru's ZEEs that are involved in allowed activities, such as maquila activities, logistics, warehousing, telecommunications, information technology and research, are entitled to various exemptions. These include complete exoneration from income tax, general sales tax, municipal promotion tax and selective consumption (excise) tax. Such benefits are significantly favorable compared to standard tax rates outside the ZEEs, which can be up to 29.5% for income tax and range between 2% and 50% for other taxes, depending on the type of goods.



On the customs front, Peru's ZEEs offer substantial advantages. Companies can import machinery, raw materials and supplies without paying import duties and taxes. Goods can be stored indefinitely within the ZEEs and directly exported without undergoing a nationalization customs regime. Furthermore, these goods can enter the national territory under international agreements and conventions.

Conclusion

In summary, Latam's SEAs do not merely provide tax incentives and reduced tariffs. They are dynamic, multifaceted hubs that accommodate diverse activities, from manufacturing and logistics to technology and services. Whether leveraging Brazil's benefits for renewable energy companies or taking advantage of Colombia's burgeoning business process outsourcing sector, these zones offer a holistic ecosystem for products and services.

Each SEA provides unique benefits, which may make them launchpads for businesses aiming to enter or expand within the Latam market. These zones are also evolving, adapting to modern business needs while offering avenues for traditional industries. With the international business landscape growing increasingly complex, Latam's SEAs provide a strategic advantage for companies seeking a balance of tax benefits, streamlined compliance and market opportunities. It is not just about cutting costs – it is about finding new ways to innovate, grow and thrive. ■

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Brazil: A step toward continuous improvement with enhancement of the Authorized Economic Operator program



Authorized Economic Operator (AEO) certification program is the recognition by customs authorities that the levels of control and compliance of a company performing foreign trade operations are sufficient to consider it to be a low-risk operator. As such, it confers certain simplifications and privileges that can greatly enhance the speed and efficiency of international movements of goods.

Originating from the World Customs Organization (WCO), the AEO certification program was adapted for Brazil with many similarities to auditing standards used in Europe in granting AEO status. This gives the applicant the opportunity to make a self-assessment of the structure of its business, the level of existing controls, an analysis of risks, and documentation of corrective measures and action plans.

The AEO program in Brazil is attractive to many businesses, due to the many tangible benefits available for certified companies, coupled with the Brazilian Customs authority's objective that the program succeeds. The Brazilian authorities have bought into the global objectives of identifying low-risk operators and increasing trade facilitation, while offering greater agility and predictability in international trade flows.

The legal basis governing the AEO program in Brazil has now undergone a further review process, which sought to align the WCO's guidelines with the most recent international commitments signed by Brazil.

Public consultation period

The Brazilian Federal Revenue Services (Brazilian IRS) launched a public consultation in May 2023 to gather companies' opinions and suggestions for the AEO program in Brazil and the reorganization of its criteria. As a result of this consultation, updates to the new legislation were published in July and August 2023.

The legislation primarily aims to simplify the procedures and terminologies used regarding international supply chain security, adapting the requirements to make them compatible with those of the WCO SAFE Framework of Standards (WCO SAFE) and the US' Customs Trade Partnership Against Terrorism (CTPAT) program, including the adoption of some new criteria.

The changes bring Brazil's AEO certification process closer to the WCO SAFE standards and updates. They also clarify and improve concepts and review the minimum percentage of direct operations required to qualify, since, according to the previous legislation, companies would only be eligible for AEO status if at least 90% of their international operations were directly made.¹ The new legislation also expands the list of companies eligible for AEO certification, by incorporating maritime agents. This expansion aims to reach new players to further strengthen the security of international supply chains.

While some of the legislative changes unrelated to the technical certification criteria have already been adopted, most of the technical enhancements will come into effect in August 2024. This will give existing certified companies and new applicants a one-year transition period to adapt to the new requirements, allowing for a more gradual transition, which will have a lower cost impact than if the new criteria went into effect sooner.

Main objectives of the new legislation and enhancements

The adjustments made to the legislation demonstrate a strong commitment by the Brazilian authorities to maintaining alignment with international standards and to continuously enhancing the uptake and international success of the AEO program. This action may contribute to the negotiation of mutual recognition agreements (MRAs) and expand to new proposals for partnerships with customs authorities in other countries, consequently allowing "Brazilian certified operators" to benefit from AEO facilitation measures in partner countries. ■

¹ Direct operations are operations performed by the company itself. Indirect operations are those performed by third parties, such as trading companies, or on behalf of a third party. The Brazilian IRS understood that AEO-certified companies could not be the buyer of another importer nor import or export on behalf of another company, to make sure that companies without AEO standards do not benefit from the certification through another's certificate.



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Colombia: Crypto assets cannot be used as a means of payment for foreign trade operations

Cryptocurrencies are challenging and reshaping financial norms around the globe, but Colombia has issued a clear decree: Crypto assets cannot be used as a means of payment for foreign trade operations.

This stance is deeply rooted in Colombia's history and how its foreign exchange regime, dating back to the 1930s, has continually adapted to navigate the challenges of a globalized world.

Foreign exchange regime in Colombia

The Colombian foreign exchange regime originated in the 1930s in response to the severe economic and monetary repercussions of the post-World War I period and the global Great Depression. The creation and evolution of the country's international exchange regime is particularly crucial because a medium-sized, open economy, such as Colombia's, is significantly influenced by various external factors and fluctuations in the international economy.

As a result, the Colombian legislature has needed to ensure an effective measurement, analysis and response to international movements and their consequences. Within this scope, Law 9 of 1991 established the general rules that the national government must follow to regulate international exchange. Both its explanatory statement and Article 2 of this law explicitly state that the purpose of the Colombian foreign exchange regime is to attain stable and balanced foreign trade. The regime aims to promote economic and social development through the internationalization of the economy, with the goal of enhancing its competitiveness. This is achieved by fostering and



encouraging foreign trade operations, simplifying the execution of international transactions (while still maintaining control and oversight mechanisms), promoting capital investment, and coordinating foreign exchange policies and regulations with other macroeconomic policies.

Since the enactment of this law, the Colombian foreign exchange regime has undergone substantial strengthening and modifications to address the emerging challenges and complexities of the globalized world. This evolution has been so significant that the Colombian Constitutional Court has affirmed that “within the scope of the foreign exchange regime, the intention is to achieve a political purpose which consists, basically, in the protection of the economic public order.”¹ As an example, the foreign exchange regime has served as a mechanism for preventing illegal activities, such as money laundering and the financing of terrorism.

Current state

Currently, the foreign exchange regime has embraced an informative and open approach to the international exchange market, allowing individuals to engage in a wide range of international transactions. However, based on the purposes of the regime in regulating and protecting the economy, a dual-nature foreign exchange regime has been established in Colombia. The regime that applies in any given situation depends on the nature of the exchange operation and whether it falls under a free exchange market where regulatory authorities

have minimal intervention or a regulated exchange market where a set of guidelines, procedures and inspections are mandatory.

The foreign exchange regime defines the following:

- ▶ The operations subject to its regulations.
- ▶ The competent authorities responsible for legislation in this area (i.e., the Congress of the Republic, the Central Bank and the Board of Directors of the Central Bank).
- ▶ Those responsible for overseeing compliance with the foreign exchange regime (i.e., the Superintendence of Corporations, the Superintendence of Finance and the National Tax and Customs Directorate).
- ▶ The individuals or entities qualified as intermediaries in the exchange market.
- ▶ The administrative procedures established for compliance with the foreign exchange regulations and the applicable sanctions.

Operations

Article 4 of External Resolution 1 of 2018 outlines the operations subject to mandatory channeling through the regulated foreign exchange market, which include:

- ▶ Import and export of goods.
- ▶ External borrowing operations conducted by residents in Colombia, along with the associated financial costs.
- ▶ Foreign capital investments in Colombia and the returns generated from them.

- ▶ Colombian capital investments abroad and the returns generated from them.
- ▶ Financial investments in securities issued and in assets located abroad, along with the returns generated from them, except when the investments are made using foreign currency from operations that should not be channeled through the foreign exchange market.
- ▶ Foreign currency guarantees and collateral.
- ▶ Derivatives trading.

This regime applies to operations in which Colombian residents and nonresidents engage in currency exchange, involving either foreign currencies or, in some cases, Colombian legal currency. Individuals are obliged to conduct these transactions through authorized intermediaries or compensation accounts. This ensures that the authorities have direct access to the terms and details of such transactions.

Intermediaries

Intermediaries of the exchange market are institutions authorized and supervised by the Financial Superintendence of Colombia through which exchange operations are channeled either on a mandatory or a voluntary basis. According to Annex 2 of the External Regulatory Directive DCIP-83 of the Department of International Exchange and Payments, the intermediaries of the exchange market are:

- ▶ Authorized banking institutions
- ▶ Authorized financial corporations

¹ Constitutional Court Plenary Session, Ruling C-010 of 23 January 2003. Presiding Judge Clara Ines Vargas Hernández

- ▶ Authorized financing companies
- ▶ Financiera de Desarrollo Nacional S. A. (FDN)
- ▶ Banco de Comercio Exterior de Colombia S. A. (Bancóldex)
- ▶ Authorized financial cooperatives
- ▶ Stock exchange brokers
- ▶ Foreign exchange brokers and special financial services companies (SICSFE)
- ▶ Companies specialized in electronic deposits and payments (SEDPE)

Compensation accounts

Compensation accounts refer to bank accounts held abroad that serve as conduits for conducting both operations subject to mandatory channeling into the exchange regime and those stemming from the fulfillment of obligations between residents (internal operations).

According to the provisions of Article 2.17.1.2 of Decree 1068 of 2015, residents who hold bank accounts in foreign currencies with financial entities abroad and are registered under the clearing mechanism of the Central Bank, as outlined in Section 8.2 of Chapter 8 of DCIP-83, are considered holders of compensation accounts.

In the case of autonomous patrimonies or collective investment funds, the compensation account is registered by the management company on behalf of the patrimony or collective investment fund, using the Tax Identification Number (NIT in Spanish) and the name of the autonomous patrimony or collective

investment fund. This registration includes the business purpose of the management company.

In the case of consortiums, temporary unions or partnerships, the compensation account is registered on behalf of one of the resident participants, indicating the names of the other resident participants on the registration form.

To facilitate control over these transactions, individuals are required to submit their foreign exchange declarations at the time of the transaction. This document is mandatory, regardless of whether the transaction is conducted through intermediaries of the exchange market or via a compensation account. It must be retained, along with its supportive documents, for five years.

Crypto assets as a form of payment

The rise of crypto assets has presented one of the most significant challenges to the foreign exchange regulations in recent times. Their capacity to facilitate transfers without relying on a centralized system for issuance, registration, clearing, settlement and payment contradicts the principles of Colombia's foreign exchange regime. Furthermore, Colombian legislation currently lacks specific regulation relating to crypto assets.

As a result, the concept of crypto assets has been addressed through the interpretation of jurisprudence and the guidance provided by the financial authorities. These authorities include the Technical Council of Accounting, the Central Bank, the Financial Superintendence, the Unit of Normative Planning and Financial Regulation

Studies, the Unit of Information and Financial Analysis, and the National Tax and Customs Directorate (DIAN). Their interpretation aligns with and adheres to international pronouncements and regulations related to this subject (specifically, the International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS)). They have concluded that crypto assets do not fully comply with the definitions stated in several international accounting and financial standards (including IAS 2, IAS 7, IAS 8, IAS 32, IFRS 9, IAS 38 and IAS 40).

The competent authorities (listed above) have determined that there is currently no appropriate asset category that can define crypto assets. For example, these assets do not meet the criteria for classification as money or money equivalents, financial instruments, noncash financial assets, investment properties or intangible assets. Consequently, since they do not fit into any of these definitions, the competent authorities have concluded that there is no obligation to accept them as a means of payment.



In lieu of payment and crypto assets

Under the foreign exchange regime, the authorized method for settling obligations is through payment in either legal or foreign currency. Exceptionally, an alternative method of payment is allowed known as “in lieu of payment.” However, it is important to note that this method cannot be agreed upon as the initial or preferred mode of payment.

According to the Central Bank, this method must always be associated with the notification and submission of transactional information to the competent authorities. This approach ensures that the authorities can verify that cross-border exchanges of goods and services, as well as their corresponding values, are accurately reflected in income and expense statements. Given the uncertainties surrounding the nature of crypto assets, an emerging alternative method for their use as a means of payment has been to treat them as being “in lieu of payment.”

The Supreme Court of Justice has interpreted this concept as an independent mechanism for settling obligations when both parties agree to provide a different asset than the one originally stipulated to satisfy the obligation. The primary intention of the parties is to discharge the initial obligation. According to the Financial Superintendence, one of the crucial elements of this method is the determination of the value or price. It is imperative that the value of the new asset corresponds to the value of the initial one.

However, determining the value poses a significant challenge when applying this concept to crypto assets. To ascertain the value of an asset, an active, recognized and traceable market is typically required.

In this context, the Central Bank has asserted that “in the crypto-assets market, there is a lack of certainty regarding the immediate availability of resources, the value at which crypto-assets can be exchanged, and the permanence of these assets in the market.”² This uncertainty arises from the existence of multiple active markets for the same crypto asset, each with varying prices, and the difficulty of accessing these markets. Consequently, certifying the value and converting the price to local or foreign currencies is deemed to be technically impossible.

In view of this impossibility, DIAN has determined that using crypto assets does not meet the requirements of the “in lieu of payment” method established in the foreign exchange regime. Therefore, the use of crypto assets as a means of payment is not feasible.

What's next?

As the use of crypto assets continues to grow, their implications become increasingly significant for foreign trade. However, the absence of a dedicated legal framework applicable to these assets results in uncertainty regarding their use in various economic sectors, including the foreign exchange regime.

This situation is creating gray areas that may spark substantial debates and discussion on the matter.

Hence, it is anticipated that the Congress of the Republic, in the exercise of its legislative authority, will undertake the regulation of this subject. Furthermore, both the Central Bank and the Technical Council of Public Accounting have expressed their anticipation for international entities to issue further pronouncements concerning crypto assets and to establish regulations in this regard.

Crypto assets are a reality in the modern world in which financial and exchange operations are conducted. Consequently, the development of a legal framework is necessary. Furthermore, the Colombian legislature may await international developments and regulations related to crypto assets to ensure that legislation is coherent and consistent. ■

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² Technical Concept SCD-000001230, Central Bank, 9 August 2023

Asia-Pacific: Interplay between transfer pricing and customs valuation

The interaction between transfer pricing and customs valuation can be challenging anywhere in the world but especially in the Asia-Pacific (APAC) region. Unlike in the EU, the implementation of the World Trade Organization (WTO) customs valuation rules is not harmonized across the various countries in the APAC region because they are independent customs jurisdictions. In addition, due to the generally high duty rates in the region, the financial impact of customs-valuation-related matters can be significant for businesses and customs authorities alike. This makes reviewing intercompany transactions and transfer pricing adjustments a key priority for customs authorities across the APAC region. This article aims to provide insights on the interplay between transfer pricing and customs valuation in the region. It also suggests strategies to mitigate disagreements with customs authorities, including illustrations for select jurisdictions.

Both transfer pricing and customs valuation prescribe rules regarding the acceptability of intercompany prices. The aim is to ensure related parties interact with each other as if they are not related and, therefore, comply with the arm's-length principle. However, certain differences exist between these sets of rules, specifically in how they are implemented. Transfer pricing generally focuses on the profitability of a legal entity, while customs valuation focuses on an acceptable price for each individual product and import transaction. The World Customs Organization (WCO) has said, despite these differences, transfer pricing documentation can be a valuable source of information for customs valuation purposes.¹ While several customs authorities agree on some degree of usefulness of transfer pricing documentation, the practical implementation across the APAC region can vary significantly. In addition, multinational enterprises (MNEs) should



recognize that transfer pricing documentation is seldom drafted with customs valuation in mind. This, in a best case, may not be very useful for defending a customs valuation challenge; in a worst case, this could lead to unintended consequences, such as having to provide additional elements to customs authorities to challenge customs values.

Acceptability of intercompany transaction prices

From a customs perspective, parties should demonstrate that their relationship has not influenced the price in a transaction. Most MNEs argue that this requirement is met if the importer earns a remuneration in line with a transfer pricing benchmark validated by an independent service provider. As customs authorities often point out in such a situation, simply providing transfer pricing documentation will not be sufficient. In practice, it is up to the importer to demonstrate that the intercompany prices are acceptable from a specific customs valuation perspective.

¹ For an example, see WCO Technical Committee on Customs Valuation (TCCV) Commentary 23.1, TCCV Case Studies 14.1 and 14.2, or the WCO Guide to Customs Valuation and Transfer Pricing (June 2015, updated in 2018)

Customs authorities across the APAC region regularly use import price databases to challenge the import prices as being too low. Complying with requests of customs authorities (i.e., higher import prices) may in turn result in scrutiny from tax authorities (i.e., higher import price results in a lower corporate income tax base in the importing market). According to the WCO, customs authorities may not use customs valuation databases to determine the customs value of imported goods as a substitute value for imported goods or as a mechanism to establish minimum values.² Nevertheless, it is likely that this will not be a successful argument. A first step in such cases is to determine whether the import prices in the database relate to products that are identical or sufficiently similar. This includes not just the product itself but also the other details of the sale (e.g., commercial level, quantities, timing). Alternatively, the importer will have to demonstrate that the intercompany prices, while potentially being lower than prices from an import price database, should still be acceptable from a customs valuation perspective. See the section “Customs valuation defense file” below for suggestions as to how to address this.

Retrospective transfer pricing adjustments

In all APAC jurisdictions, certain actions are required for retrospective transfer pricing adjustments. Failure to report transfer pricing adjustments may lead to additional duties and other import taxes, significant fines, and interest, once discovered by the customs authorities in an audit. As a starting point, the customs value becomes final once the import declaration is accepted by customs authorities, barring certain exceptions. As retrospective transfer pricing adjustments, per their definition, occur after the time of import, they create challenges from a customs valuation perspective. Some APAC jurisdictions have well-defined procedures, and some even have guidance available. However, for most jurisdictions, the treatment of retrospective transfer pricing adjustments is a gray area and requires case-by-case analysis.

One thing that customs authorities across the APAC region generally agree on is that if a transfer pricing adjustment results in an increase in the price of imported goods, then additional duties and other import taxes (if applicable) must be paid. However, in many jurisdictions, obtaining a refund in the case of a reduction in prices due to a transfer pricing adjustment is, in practice, not possible. Nevertheless, there are some APAC jurisdictions (e.g., Australia, Japan, New Zealand, Singapore, South Korea) where refunds can be obtained if certain procedures are followed. Often, proactive alignment with the customs authorities is required to qualify for refunds.

In certain jurisdictions, businesses can apply for rulings to get clarification on how to treat retrospective transfer pricing adjustments or other customs-valuation-related matters. This usually involves explaining the underlying transfer pricing model and providing legal agreements and other relevant documents. The ruling effectively is an agreement between parties on how potential transfer pricing adjustments should be treated for customs valuation purposes. This provides certainty for the importing business and helps to avoid audits and fines.

Australia illustration

Retrospective transfer pricing adjustments should be proactively reported to Australia Customs. If price changes are not notified, Australia Customs may impose penalties for a false and misleading statement, regardless of whether any duty is payable in connection with the imported goods. A voluntary disclosure can be submitted to obtain penalty protection. In addition, in the case of transfer pricing adjustments that increase the value of imported goods, the importer may be permitted to make a single additional payment for additional duties and import taxes based on a bulk amendment. However, to obtain a refund, all the relevant import entries will need to be amended. To avoid an uncertain outcome in the case of a voluntary disclosure and for ease of administrative formalities, importers can apply for a “Valuation Advice.” This is a private and binding agreement with Australia Customs regarding customs valuation matters, including, but not limited to, retrospective transfer pricing adjustment. This enhances certainty and predictability for Australian importers on customs valuations matters.

² ‘Guidelines on the development and use of a national database as a risk assessment tool’, *World Customs Organization website*. [Find it here](#).

China Mainland illustration

In recent years, managing retrospective transfer pricing adjustments has been getting increasingly difficult in the mainland China tax jurisdiction from a customs perspective. This includes reaching an agreement with China Customs to facilitate foreign exchange payments related to transfer pricing adjustments that increase the value of imported goods.

In May 2022, the first pilot scheme in Shenzhen, China, was introduced seeking alignment between Shenzhen customs and tax administrations on prices for related-party imports. The aim is to reduce potential scrutiny from a tax transfer pricing perspective and customs perspective as both administrations are proactively involved. Once both administrations reach an agreement, a memorandum (i.e., a Memorandum of Collaborative Management of Transfer Pricing of Related Party Imported Goods) will be signed. This pilot is currently in its early stage, and there is still uncertainty regarding certain aspects. For example, it is currently unclear whether foreign exchange payments arising out of transfer pricing adjustments would be facilitated by the memorandum. Also, there is no indication whether the pilot will be extended to other parts of China. While MNEs are interested in the program, they are hesitant to enrol in the pilot until additional details have been finalized. For the time being, businesses should consider retrospective transfer pricing adjustments in China on a case-by-case basis.

Japan illustration

Japan Customs is increasingly aware of the relevance of retrospective transfer pricing adjustments for customs valuation purposes. The agency is actively looking into this matter and asking targeted questions to importers. Retrospective transfer pricing adjustments should be proactively reported to Japan Customs to avoid penalties. The standard approach in these cases is to amend each impacted import declaration individually. However, it may be possible to negotiate a simplified method for declarations that share the same conditions (e.g., place of import, duty rates, customs year) to be combined into a single amended declaration. It may be possible to obtain a refund, subject to having robust documentation and/or having a prior agreement with Japan Customs.

Korea illustration

Businesses importing into Korea can submit a voluntary disclosure informing Korea Customs of retrospective transfer pricing adjustments. However, customs authorities have the discretion to not accept such disclosures. This may not immediately result in an audit, but there is a high likelihood that the customs authorities will investigate this further.

As part of the audit, Korea Customs tends to strictly examine transfer pricing adjustments. In addition to payment of additional duties, import taxes and penalties, the importer may lose the right to deduct import value-added tax (VAT) for any additional VAT assessed in the audit, resulting in an additional cost. The standard VAT rate is 10%.

The restrictions on the recoverability of the VAT assessed in customs audits appear to have been eased under revised VAT legislation in 2023. However, the authorities are still strictly applying the regulation in determining when import VAT on transfer pricing adjustments can be treated as deductible. To manage this risk, importers can apply for an Advance Customs Valuation Arrangement (ACVA). This provides protection against audits and penalties and facilitates the deductibility of import VAT.

New Zealand illustration

Importers in New Zealand are able to use the provisional value scheme (PVS) to manage retrospective transfer pricing adjustments. Under the PVS, importers can declare a provisional value for goods, then declare a final value later. This eliminates exposure to any penalties or other charges (assuming adherence to the respective compliance obligations). Post-importation adjustment disclosures are made by way of a reconciliation letter submitted within 12 months of the financial year-end to New Zealand Customs. To apply for PVS, importers will need to provide transfer pricing documentation and other relevant information to New Zealand Customs.

Thailand illustration

In some jurisdictions, obtaining a customs valuation ruling may not be the answer. For example, in Thailand, while there is an administrative process to obtain legally binding customs valuation rulings, this often does not provide a workable solution. Thai Customs is generally more inclined to consider and issue a nonbinding “consultation letter.” In practice, this can usually be relied upon to support taxpayers’ valuation position and assist with challenges at the port level or during customs audits.

In the case of retrospective transfer pricing adjustments, a voluntary disclosure is possible if the adjustment leads to a duty shortage. A voluntary disclosure helps reassure Thai Customs that there is no duty-evasion intent in relation to the price adjustment, for the case to be settled without penalties. Nevertheless, interest surcharges will still apply.

Taiwan illustration

Taiwan has a so-called one-time transfer pricing adjustment mechanism to facilitate one retrospective transfer pricing adjustment per financial year. At the time of the import, certain elements should be included in the import declaration. This includes, for example, information indicating that the customs value may be subject to retrospective transfer pricing adjustments. Customs duties, excises and other import taxes are then paid based on the initial customs value. Within one month following the end of the year, a package should be submitted to Taiwan Customs containing details of the transfer pricing adjustment. In case the importer cannot provide the necessary information within the one-month period, they should proactively reach out to Taiwan Customs to discuss how to proceed. Depending on the type of transfer pricing adjustment, either an additional payment will have to be made or a refund can potentially be requested, subject to meeting the relevant criteria.

Customs valuation defense file

Given the challenges surrounding intercompany prices and retrospective transfer pricing adjustments in the APAC region, several MNEs have instituted “customs valuation defense files.” In the case of an audit, it is often difficult to swiftly provide a high-quality and consistent response taking into account all relevant considerations and data sources. As previously mentioned, simply handing over transfer pricing documentation is usually not sufficient as this does not specifically address the acceptability of import prices from a customs valuation perspective. A customs valuation defense file can explain the customs valuation logic regarding various matters, such as intercompany pricing, transfer pricing adjustments, royalties and value-added services fees. This allows the importer to provide a timely, consistent and high-quality response to customs authorities. It also allows creating and maintaining contemporaneous documentation (e.g., customs-specific benchmarks), which often may not be possible to do after the fact, especially when disputes arise in post-clearance audits years after the relevant import transactions. This may help to manage disagreements with customs authorities, avoid unnecessary additional duty payments and fines, and limit delays at the port. In addition, by carefully reviewing the customs valuation position, a business may identify potential risks or business opportunities.

Prospective transfer pricing adjustments

MNEs are increasingly looking into prospective transfer pricing adjustments to avoid various customs valuation challenges on account of retrospective transfer pricing adjustments. If an MNE uses prospective transfer pricing adjustments, it needs to actively monitor the profitability of the importing entity. In case profitability is not in line with the benchmark, it will adjust the price of the imported goods going forward.

The aim is to avoid retrospective transfer pricing adjustments at the end of the year or at least to reduce the amount of the adjustment. At first glance, this seems like a good solution from both a transfer pricing and a customs valuation perspective. However, prospective transfer pricing adjustments do not come without their (customs) challenges.

Customs authorities in the APAC region actively compare the prices of imported goods both to the prices of other importers and the historical prices of the importer itself. Significant price fluctuations, either upward or downward, can raise a red flag. What is considered significant will differ per jurisdiction and is usually not public knowledge.



For a reduction of the price of the imported goods, customs authorities can simply continue to determine the customs value based on the previous (higher) price, thereby preventing any reduction in customs duties payable. However, for a significant increase in price of the imported goods, the customs authorities may take the position that the customs value of the previous imports was too low. This could result in retroactively increasing the price of the previously imported products (sometimes covering the imports of multiple years), resulting in additional customs duties. In addition, they may claim that the previous import declarations were incorrect, potentially resulting in additional fines and interest. Therefore, a careful implementation of prospective transfer pricing adjustments is key in the APAC region.

Action for businesses

The interplay between transfer pricing and customs valuation is a dilemma for most MNEs importing goods in the APAC region. Due to its inherent complexity, combined with varied practices in the different jurisdictions, it needs to be navigated carefully. A solution that works in one country may not work in another. Engage in proactive customs planning to avoid noncompliance and incurring additional duties and other import taxes, fines, interest, etc. Potential solutions to consider include rulings, voluntary disclosures, a customs valuation defense file and implementing prospective transfer pricing adjustments. ■

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Japan: New definition of Importer of Record



On 30 June 2023, Japan Customs released a revised Basic Circular to the Customs Law¹ relating to who can act as an Importer of Record (IoR) in Japan. The changes that came into effect from 1 October 2023 provide clarity on who may be the IoR for goods imported into Japan not pursuant to an import transaction or a buy/sell transaction (e.g., when a company moves its own inventory into Japan).

Due to the rapid increase in imports of goods conducted by e-commerce traders, Japan Customs has found widespread underpayments of import taxes on such imports and has faced difficulty in collecting additional duties and import consumption tax on these imports.² The Council on Customs, Tariff, Foreign Exchange and Other Transactions (Customs Committee), which is a consultative body within the Ministry of Finance, was tasked in June 2022 with discussing how to treat import declarations by e-commerce traders.³ As a result, the Basic Circular was amended.

Who can act as the IoR in Japan?

Before the revision, Basic Circular 6-1 to the Customs Law stipulated that the IoR should be the person who intends to import the goods, which, in principle, should be the person who appears on any invoices or bills of lading as the consignee. This implied that the IoR could be anyone who acts as the consignee for the shipment even when such person did not have an adequate understanding of the goods being imported. The Customs Committee highlighted many examples of such cases in which the IoR did not have full understanding of the imported goods,⁴ which ultimately led to incorrect or fraudulent declarations. It used these examples as reasons for why the Basic Circular needed to be amended to provide more clarity on the definition of IoR.

¹ Basic Circular 6-1 to Customs Law and Basic Circular 67-3-3-2 to Customs Law.

² This is mentioned in the final report issued by the Customs Committee: "Regarding the cargo handled by Fulfillment Service provider, there have been cases of non-residents using the names of domestic residents without their consent, a practice commonly known as impersonation, to import goods. Furthermore, instances have arisen where imports are declared at unfairly low prices, even though no actual transaction has occurred at the time of import, leading to the evasion of customs duties and other taxes." [Find it here.](#)

³ Further background information is provided in our article 'Japan: 2023 tax reform changes to the customs law,' *TradeWatch* Issue 1 2023, page 24. [Find it here.](#)

⁴ This is mentioned in the discussion paper of the 31 October 2022 Customs Committee meeting, pages 18 to 22. [Find it here.](#)

As a result, the new definition of “a person who intends to import the goods” has been clarified in the revised Basic Circular under Article 67-3-3-2 as follows:

- ▶ Where goods are imported pursuant to an import transaction under the Customs Tariff Law, the importer shall be the consignee stated on the commercial invoice.
- ▶ Where goods are not imported pursuant to an import transaction, the importer shall be either:
 - ▶ The person who has the authority at the time of importation to dispose of the imported goods after the goods are released for free circulation in Japan or
 - ▶ Any other persons who perform the act which constitutes the purpose of importation. Examples of the act which constitutes the purpose of importation are:
 - ▶ Importing goods that are leased goods
 - ▶ Importing goods to conduct toll manufacturing services
 - ▶ Importing goods to provide sales agent or commissionaire services
 - ▶ Importing goods to conduct repair services of damaged goods
 - ▶ Importing goods to conduct disposal services of goods as waste

Impact of this revised Basic Circular

While the reason for this revision in the definition of IoR was the increase in imports by e-commerce traders, the way the Basic Circular was amended does not limit its application to e-commerce traders alone. As a result, the revised circular could have a much broader application for other importers as well.

Specifically, if an importer is not purchasing or does not own the imported goods at the time of importation, and it is not providing certain services related to the imported goods that constitute having a purpose to import the goods, the importer may no longer qualify as an IoR for customs purposes.

Japan Customs may still allow companies to act as IoRs, provided they have a legitimate reason for why they need to import goods into Japan. However, given that the revised Circular is so new and lacking in past precedents, it would be advisable for companies to carefully review their IoR position if they do not fit the definition provided in the revised Circular and, where necessary, seek clarification from Japan Customs as to their position. ■



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Vietnam: Draft proposal to abolish some on-the-spot export-import transactions

As of 29 May 2023, new laws apply to on-the-spot (OTS) export-import transactions. The changes arise from an Official Letter 2587/TCHQ-GSQL issued by the Vietnam General Department of Customs (the GDC) to Vietnam Ministry of Finance (the MoF).¹ Based on its internal review of relevant laws and regulations, the GDC provided feedback on and proposed some regulatory amendments to the execution of OTS transactions in Vietnam.

OTS transactions

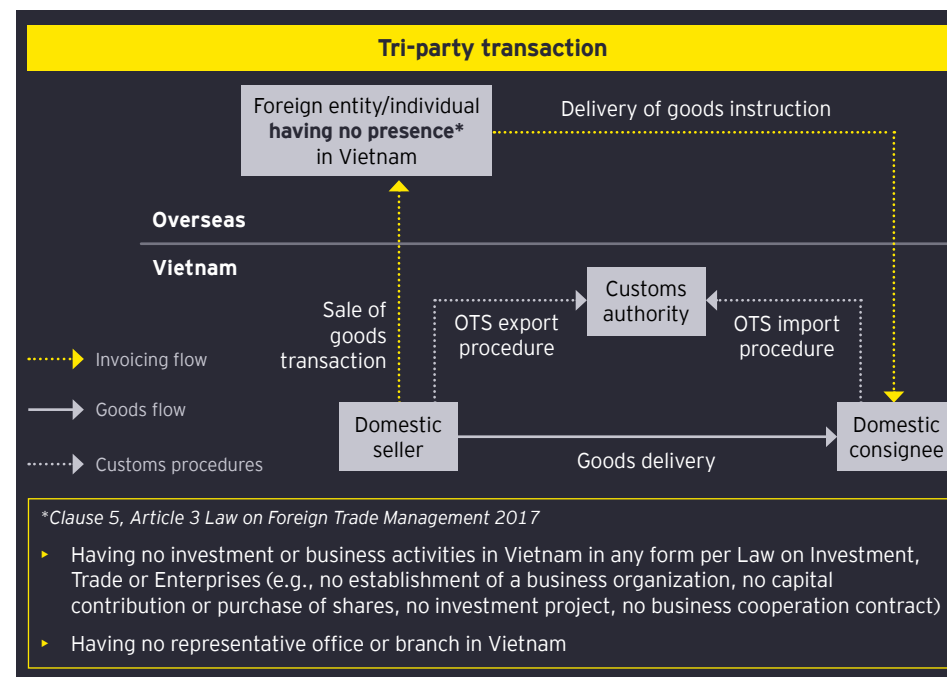
OTS transactions are sales of goods from sellers in Vietnam to overseas buyers, but the goods do not physically leave the country and are delivered to another party in Vietnam, who purchase them from the overseas buyers. The goods are treated as exports by the sellers in Vietnam, which are subject to 0% export duty (except for natural resources) and 0% value-added tax (VAT). They are then re-imported by the other party in Vietnam. The importation is subject to import duty, special consumption tax (if any) and import VAT, which is calculated on an ad valorem basis.

The proposal

The GDC has submitted a proposal to the MoF and other competent authorities to abolish tri-party transactions (point c, clause 1, Article 35 of Decree No. 08/2015/ND-CP), which provides guidance on the implementation of the Customs Law related to these transactions.



For example, under the proposal, the below OTS tri-party transaction would be abolished.



¹ Official Letter 2587/TCHQ-GSQL 2023 commenting on amendments and supplements to Article 35 of Decree 08/2015/ND-CP. [Find it here.](#)

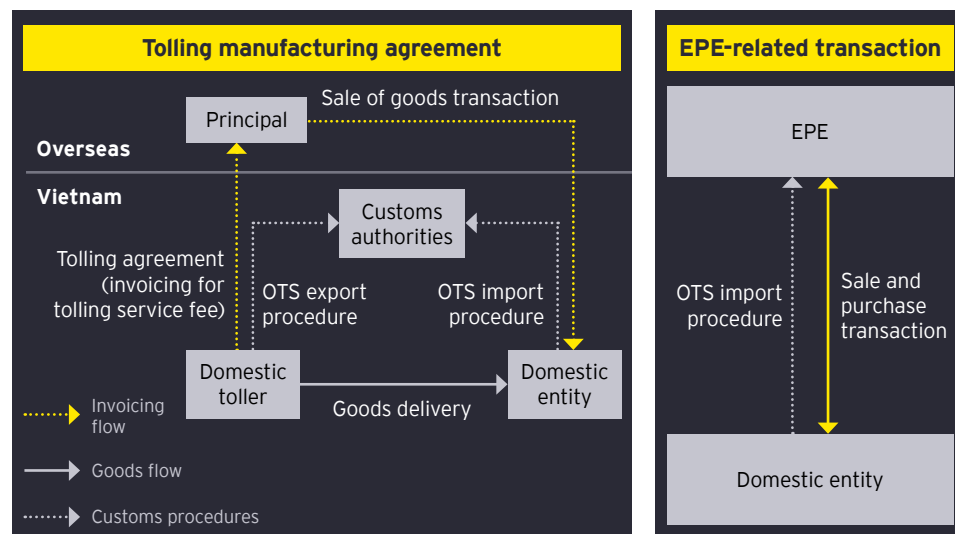
The MoF has reviewed the GDC's proposal and seems agreeable to the suggested abolition. In its recent Official Letter No. 9133/BTC-TCHQ dated 25 August 2023² to the Vietnam Government Office, the MoF provided its assessment on the matter, including potential impacts on business and tax budget collection, as well as setting out some recommended alternative transaction structures for businesses to consider adopting as a replacement for their current OTS transactions after the abolition is approved.

To support businesses and to avoid sudden supply chain disruption, the MoF has proposed a transition period of one year before the abolition becomes permanent, provided that the foreign entity can strictly satisfy the condition of having “no presence in Vietnam.”

Remaining OTS transactions unaffected by the change

The two remaining OTS transactions – toll manufacturing agreements and export processing enterprise (EPE)-related transactions – are not set to be abolished.

An EPE is a company set up and located in Vietnam, but its main business activity is to manufacture for export, and so it is treated as being in a non-tariff zone, therefore, it is exempted from almost all customs duties and VAT.



Alternative options

As mentioned, the MoF suggested some alternative options for businesses operating in Vietnam to consider if the proposed abolition is approved. Those alternatives include:

- ▶ Treating the sale or purchase transaction in the same way as a transaction between domestic entities
- ▶ Using a bonded warehouse
- ▶ Converting domestic entities into EPEs
- ▶ Notwithstanding these suggestions, the MoF has not yet issued any concrete guidance on these alternatives, which may create some confusion for businesses.

Common trends and practices

- ▶ Businesses should review the MoF's proposed abolition and suggested alternative arrangements to explore their possible options for business continuity and to avoid supply chain disruption.
- ▶ In considering any new arrangements, in addition to the supply chain feasibility, businesses should also assess the potential new tax, customs duty and customs procedure implications, in particular:
 - ▶ If a “bonded warehouse” is used, would new or additional customs procedures apply for the first domestic seller? Who would bear the cost of such warehousing? How long can goods be stored in such a warehouse?
 - ▶ If the sale between the foreign entity and the domestic buyer or consignee is treated as a domestic sale, is there an obligation for the foreign entity to register for VAT and pay VAT in Vietnam?
 - ▶ Given that the cost structure of the transaction may change, there is a potential need to revisit transfer pricing for the transactions to ensure they are at arm's length and comply with transfer pricing regulations if the transactions involve related parties.

² Official Letter 9133/BTC-TCHQ 2023 draft Decree amending Decree 08/2015/ND-CP. [Find it here.](#)

- ▶ To convert a domestic entity into to an EPE, there are likely to be many administrative procedures, potential consequences and possible risks that should be analyzed, such as the possibility for VAT refund of existing VAT credits and the possibility of using subcontractors for the business in the future.
- ▶ There may be some other nontax considerations to assess, such as the possibility of collecting foreign currencies by the first domestic seller under any alternative options.
- ▶ In addition, for previous periods, businesses should do an internal review of their qualification for OTS tri-party transaction status. In particular, it is crucial to supply evidence to the authorities that the foreign entity has “no presence in Vietnam” upon audit or request.
- ▶ Businesses should continuously monitor the progress of this policy change to be able to respond with appropriate actions and decisions. ■

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Vietnam: Trends in customs valuation for imported goods

Vietnam generally follows the World Trade Organization (WTO) Valuation Agreement¹ framework. As in that framework, Vietnam's domestic regulations provide the following six methods for customs valuation:

- ▶ Transaction value
- ▶ Transaction value of imported identical goods
- ▶ Transaction value of imported similar goods
- ▶ Deductive value
- ▶ Computed value
- ▶ Fallback method

In this article, we do not present the details and rules for each of these methods. Rather, we will review the latest practices and customs valuation trends as applied by Vietnam's customs authorities, who may interpret and implement certain aspects of the valuation rules differently from the WTO agreement. Customs inquiries about valuation may happen at any the stage of an importation, including in the process of a customs valuation consultation, through questioning by the customs authority, or in the course of a regular or special customs audit.

Trend 1: Using the export price with other countries or the domestic selling price in export countries

The Vietnamese regulations prohibit the customs authorities from using these prices for the purposes of imposing a customs value on imported goods. However, these prices may be used (especially if used by the importer) by way of comparison to see whether these prices are approximately the same as the importer's import price that is being questioned by the customs authorities.

This comparison is especially helpful if the importer does not have any other documents or justification for its import price, such as when the importer and the foreign exporter or seller have a special relationship and the importer has no way to justify that this special relationship has not influenced the transaction price.

For the comparison to be accepted, the importer would need to convince the customs authorities why this is an effective method to follow. This would also depend on the specific situation of each company (e.g., whether it is difficult to find identical or similar goods on the market, whether the exporter or seller is willing to disclose such information).



¹ "Trade Guide: WTO Customs Valuation Agreement," *International Trade Administration website*, accessed 4 October 2023. [Find it here](#).

It is also important to stress that this comparison is a way to help an importer to justify its transaction price; it cannot be used to impose a customs value. If this comparison is not accepted, the customs authorities will still follow the six valuation methods (listed above) to impose a customs value for duty collection purposes.

Trend 2: Detailed review and assessment of ordering processes and sales contracts to determine whether a special relationship has influenced the transaction value

The customs authorities verifying whether the relationship between parties has affected the transaction is not a new topic. The WTO rule stipulates that if a transaction is conducted between unrelated parties, then the customs authorities may accept the transaction value. That said, there is no detailed guideline in the Vietnamese regulations as to how or what documents the customs authorities will look at to determine this (other than the use of value of identical or similar goods, or the use of the deductive value).

In practice, we have seen the tax authorities tend to focus on the ordering process of the importer and the importer's compliance with what has been agreed in its contract with the seller. For example, if the order is automatically made through an internal system (which is very common for related parties within the same multinational group) without any back-and-forth negotiation, the customs authorities may question the relationship. In this case they could deem the transaction not equivalent to a sale between unrelated parties. Therefore, for the

importer to prove that the transaction value has not been influenced, it may need to improve the ordering process or document it better, depending on each individual case.

Another criterion for examination may be whether the importer and seller comply with what they have committed to in their sales contract. For example, if the importer promises to make a payment by a deadline but fails to do it without any consequences or penalty, the customs authorities may deem the contract just a formality with no substance, such that the special relationship between two parties has influenced the transaction price.

Trend 3: Reviewing intercompany service agreements

The customs authorities may now request to review relevant intercompany service agreements (other than goods sales contracts) between the importer and the foreign seller, or between related parties in the same group, to identify whether there may be "additions" to the customs value, if they are directly related to the imported goods.

For importers, this trend implies the need for strong collaboration between global and local customs and tax functions within the group to review intercompany agreements together to ensure consistency.

Royalty payments are an area where attention is needed. It is well known that such payments are usually subject to withholding tax. However, not all companies are aware that such payments should be added to the customs value and are thus subject to

customs duty as well, if they are directly related to imported goods and subject to certain conditions as prescribed by law. The situation may be exacerbated if such royalties are provided for under a service agreement and the agreement only provides for a lump-sum fee rather than separating out the payments for royalties and services respectively. In this case, the risk is that the customs authorities may require that the entire lump-sum amount be added to the customs value for the purposes of duty calculation.

Trend 4: Detailed review of insurance fees and international freight

The customs authorities may compare the insurance fee or international freight charge for a particular import shipment with similar import shipments – maybe in the same industry or maybe in different industries – to identify anomalies.

For example, if customs finds that the insurance fee for a luxury goods shipment is much lower than that for a normal goods shipment, they may ask questions and even send a verification request to the insurance company. The same may happen for international freight charges.

It is crucial that the importer ensures the accuracy of its declarations and is able to provide strong commercial justification for the values declared. There have been cases in which, upon verification by the customs authorities, it has been found that payments for insurance and international freight were paid overseas and re-charged to the local importer through intercompany service agreements, but the local importer was not fully aware of this



fact. As a result, it failed to declare these dutiable amounts for customs purposes. This type of omission is a serious violation of the customs regulations and may result in disqualification for the use of the transaction value method by the importer.

Trend 5: Transfer pricing adjustments (i.e., the Vietnam importer makes additional payments for imported goods)

There has been little regulatory progress on the matter of how to treat transfer pricing adjustments for customs valuation purposes involving an increase in the price. The matter has been unofficially discussed between companies and the customs authorities, but no formal guidance has been issued so far. In practice, a few companies have declared and paid customs duties on such price adjustments although the process is not straightforward.

Notwithstanding the lack of guidance, Vietnam importers should voluntarily disclose any relevant pricing adjustments to the local customs authorities and document any such disclosure, as doing so could be a mitigating factor for the waiver of any penalties for underpayments that may be imposed at a later date.

Businesses operating in Vietnam should monitor the progress of this hot topic.

Trend 6: The use of the deductive value (deduction method)

The deduction method of customs valuation is applied more commonly now than in the past, both to test whether a transaction value is acceptable where there is a special relationship between the parties and to impose a customs value on imported goods.

Although there is guidance under the Vietnamese regulations on the use of this method, issues remain with its application in practice:

- ▶ What profit ratio may be deducted? The answer to this question may depend on each customs audit team. Some teams may simply agree to the ratio mentioned in the importer's transfer pricing documentation, but some may challenge that amount and may apply a different ratio (e.g., the auditors may refer to a profit ratio as announced in annual statistics).
- ▶ What expenses may be deducted? There are also some uncertainties on this issue. Some authorities may agree to deduct all expenses, but some may not agree to deduct any expenses

that the importer treats as nondeductible for corporate income tax purposes, while others may not agree to deduct indirect expenses (e.g., general expenses that cannot be directly linked to the goods, financial expenses, ad hoc bonuses to distributors). This type of question often requires detailed discussion and consultation with the customs authorities on a case-by-case basis to find a resolution.

- ▶ What local selling price should be used? The local selling price may be the price used for the largest volume of goods sold, but it may also be the price of each item of goods sold. In addition, if a price is discounted, the customs authorities may also consider the legal validity of that price (i.e., whether the importer has complied with other legal procedures to sell the goods at that lower price). If it has not, the authorities may use a standard or normal price before making any deduction.

The process of using this deduction method is typically time-consuming and requires a great deal of consultation with the customs authorities. Importers involved in such a process need to be patient and do their best to present the necessary evidence to support their position. ■

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EU: Proposed customs reform – a modern approach to e-commerce



The European Commission (Commission) announced its long-term plans for the EU Customs Union on 17 May 2023.¹ The Commission envisions implementing a fully revised Union Customs Code (UCC) by 2028. In addition to this general overhaul of the system, specific rules for e-commerce are proposed.²

While time will tell whether it will be possible for the Commission to implement all the measures in the whole package, adopting the proposed rules for e-commerce would lead to a significant alignment between value-added tax (VAT) and customs rules and practice for these shipments. Also, the desired implementation time frame is shorter than for the whole package, starting in 2028.

In this article, we provide a brief overview to explain and classify the proposed e-commerce rules with some suggested action for affected businesses.

The 'deemed supplier'

In 2021, a new concept, the “deemed supplier” was introduced into the EU’s VAT Directive to deal with e-commerce. The concept targets electronic interfaces, such as online marketplaces or platforms. It creates a fiction that puts the platform into the supply chain from a VAT perspective – even if the legal contracts are concluded otherwise.

¹ “EU: Customs legislation reform,” *TradeWatch* Issue 2 2023, page 24. [Find it here.](#)

² EY has submitted a feedback paper to the European Commission in response to the call for feedback on the proposed EU Customs Reform, *European Commission website*. [Find it here.](#)

It works as follows: When a third-country supplier sells goods to a private customer (B2C) in the EU, in VAT terms, the supplier supplies the goods to the platform, and the platform supplies the same goods to the customer. Hence, a fictitious supply chain for VAT purposes is created. In brief, the first transaction between the supplier and platform does not attract VAT. In contrast, the platform is responsible for the VAT on the transaction to the customer.

After two years of experience with this concept in the VAT world, the Commission proposes to extend it to the customs world. Furthermore, the proposed amendments also extend the scope of the fiction in the VAT Directive, as it currently only applies for consignments with an intrinsic value not exceeding EUR150.

Currently the deeming fiction only applies to distance sales of goods (coming from a third country to an EU customer) and supplies of goods within the EU by a taxable person not established in the Union. In the Commission's proposals regarding the future of VAT, the so-called VAT in the Digital Age (ViDA) proposals,³ among other things, the Commission proposes a deeming fiction also for a specific set of services, namely the supply of short-term accommodation and passenger transportation.

The role of 'importer'

The role of "importer" currently does not exist in the UCC. According to the Commission's proposals, an importer will be defined as any person who has the power to determine and has determined that

goods from a third country are to be brought into the customs territory of the Union. The importer will be responsible for paying the applicable duties and taxes and for ensuring compliance with the various procedural and legislative requirements.

The deemed importer

In addition, the Commission proposes creating the role of the "deemed importer" in the customs world. This is a corresponding concept to the deemed supplier for e-commerce in the VAT world.

The deemed importer builds on the VAT rules. Traders will be defined as deemed importers if they are involved in the distance sale of goods where the VAT supply chain fiction applies, and the person involved uses the Import One Stop Shop (IOSS). Furthermore, the deemed importer – or someone on their behalf – will lodge the customs declaration if the IOSS is used.

Currently, a deemed importer needs an indirect representative if it is not established within the customs territory of the Union. The same holds from the VAT perspective, whereby an intermediary is needed if the supplier has no EU establishment.

These proposals aim to align the customs and VAT rules for e-commerce. In both cases, online platforms become key actors in the chain and assume responsibilities for taxes and duties, thus preventing tax evasion and providing a level playing field for EU businesses. The Commission believes this is a modern approach to dealing with e-commerce transactions.

Simplified tariff regime

With online platforms in the driver's seat for VAT and customs duties, they could face enormous challenges. To manage these challenges, the Commission proposes the introduction of a new simplified tariff treatment for distance sales.

Currently, distance sales up to EUR150 are regarded as goods of "negligible" value and are admitted free of import duties. This provision, according to the Commission proposals, will be abolished. According to the Commission, with several other sources agreeing, this provision causes an imbalance in the market and has led to abuses, such as imports being undervalued to avoid customs formalities and payments.

A five-tier bucket system for distance sales is proposed. The buckets will have 0%, 5%, 8%, 12% and 17% customs rates. For distance sales, goods may be put in one of the five buckets, and the respective customs rate is then applied to the customs value of the goods.

In effect, this bucket-system is intended to replace the exemption system for low-value goods. Other jurisdictions already employ such a system to simplify the tariff treatment for distance sales. The simplified system will be fully optional. Only upon request of the importer will customs duty be charged according to the proposed system.

The simplified tariff treatment will not apply to goods subject to harmonized excise duties or subject to anti-dumping, anti-subsidy and safeguard measures.

³ "VAT in the Digital Age," European Commission website, 8 December 2022.
[Find it here.](#)



Certain products are further excluded from the scope of the treatment, due to their nature (e.g., iron and steel products, complete industrial plants, goods imported or exported under special circumstances).

Proposed amendments to the VAT Directive

Finally, the Commission proposes changes directly to the VAT Directive, expanding the scope of the deemed supplier mechanism. This treatment currently applies to taxable persons who facilitate, through the use of an electronic interface, distance sales of goods imported from third territories or third countries in consignments of an intrinsic value not exceeding EUR150. In the future, under the Commission's proposals, it will apply regardless of a value threshold. Through this, the EUR150 "customs threshold" will also be removed from the VAT rules.

This deletion must also be seen in the context of the VAT threshold of EUR22, which was abolished effective 1 July 2021. Since then, no low-value exemption for VAT exists within the EU. The abolishment of low-value thresholds can also be regarded as an international trend. Australia, for example, deleted its Goods and Services Tax threshold as of 1 July 2018.⁴ With the now intended abolition of the EUR150 threshold in the deemed supplier fiction, imports will become fully "thresholdless" for both VAT and customs duty purposes.

⁴ "Goods and services tax (GST) when you sell to Australia," *Australian tax authority website*. [Find it here](#).

Actions for businesses

Although these changes are taking place over years, their impact will be significant. Therefore, affected business should begin to examine their likely impact and consider appropriate actions, especially the following aspects:

- ▶ Evaluate the impact of the changes on the business.
- ▶ Evaluate which responsibilities and duties remain with the actual seller or whether these responsibilities will shift to a platform or a marketplace.
- ▶ Consider the impact on customers, pricing, any contractual relationships, and terms and conditions.
- ▶ Implement processes to fulfil any new obligation. ■

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UAE: Navigating the GCC Common Customs Law – complying with the new tax landscape



GCC customs legislation

The Member States of the Cooperation Council for the Arab States of the Gulf (Gulf Cooperation Council or GCC) are: the Kingdom of Bahrain, the Kingdom of Saudi Arabia, the State of Kuwait, the State of Qatar, the Sultanate of Oman and the United Arab Emirates (UAE). They form a customs union known as the GCC Customs Union. Accordingly, the GCC Member States adopted the GCC Common Customs Law¹ in 1999 that unifies customs regulations and procedures across the GCC Customs Union.

UAE Importer of record

The conditions for a company to import goods into the UAE include, but are not limited to, the following:

- ▶ Articles 50, 52, 63 and 110 of the GCC Common Customs Law provide that the Importer of Record (IoR) should be the owner of the goods at the time of import and should be allowed to import within the relevant territory as per its trade license.

- ▶ In turn, the UAE Imports and Exports Processes guide² states that the IoR needs to have a valid trade license issued by a UAE license-issuing authority to import goods into the UAE in its own name. The UAE solely provides trade licenses to locally incorporated companies and local branches (i.e., a local legal presence – entity or branch – is required to have a trade license).
- ▶ The UAE Imports and Exports Processes guide also state that the company should be registered with the Customs Department (i.e., it should have its own customs code to act as the IoR; this code is not provided to foreign companies without a legal presence in the UAE).

The main takeaway is that a foreign entity cannot import goods into the UAE in its own name. Only local entities or branches that own the goods at the time of import can act as the IoR and import the goods into the UAE.

Common practices leading to non-compliance

Foreign groups that have been importing goods under another licensed entity's name into the UAE may not be aware of these rules. The following are some of the deviations observed in the imports process:

¹ "Common Customs Law of the GCC States," *Secretariat General of the Gulf Cooperation Council*. [Find it here](#).

² Imports and Exports Processes issued by the UAE Ministry of Economy Foreign Trade Affairs, published by Motivate [motivatepublishing.com](https://www.motivatepublishing.com)

► **Importing goods into the UAE in the name of a customs broker for reselling them in the UAE:**

The foreign owner of the goods issues an invoice to the customs broker solely for customs purposes (no transfer of ownership) before the customs broker imports goods into the UAE under its own name. The foreign company remains the owner of the goods throughout the import process; however, the customs broker is the owner of the goods according to the customs records and, therefore, can act as the IoR without the customs authorities being aware of the actual transaction.

- **Consignment stocks:** The foreign owner of the goods issues a pro forma invoice to its UAE business partner solely for customs purposes (no transfer of ownership) before the business partner imports goods into the UAE under its own name. The foreign company remains the owner of the goods throughout the import process; however, the business partner is the owner of the goods according to the customs records. The goods are stored in the business partner's warehouse in the UAE until a UAE customer places an order. Placing the order triggers a flash title sale by the foreign company to the business partner for goods located in the UAE, followed by a sale by the business partner to the UAE customer.

The common element in these scenarios is the use of a customs invoice to fictionally transfer the ownership of the goods from the foreign company to the customs broker or local business partner solely for customs purposes, while the ownership legally and contractually remains with the foreign company.

The risks associated with such scenarios lie in the artificial transfer of ownership. The customs broker or business partner acting as the IoR becomes liable for customs purposes without being the owner of the goods. In parallel to this, a non-UAE company owns stocks in the UAE and sells goods located in the UAE, triggering a potential VAT liability. Further this transaction would be made by the foreign entity without a valid trade license to stock and sell goods in the UAE.

Impact of the implementation of corporate tax in the UAE

Corporate tax (CT) applies to UAE legal entities and branches for financial years starting on or after 1 June 2023. CT implementation changes the noncompliance risk profile of companies operating under the transactional models set out earlier.

In the above-mentioned practices, the customs invoice artificially transferred ownership of the goods from the foreign entity to the UAE customs broker or business partner, without actual title transfer or consideration paid for the supply of goods. This customs invoice becomes an issue when dealing with CT:

- The customs broker or local business partner does not record the customs invoice (purchase of goods) for accounting purposes. A guiding principle for accounting purposes is that the accounting entries should reflect the economic reality of the underlying transactions; however, it is unclear how to record this invoice, as the transaction is fictional (no transfer of ownership), and the invoice is only used for customs purposes. This discrepancy potentially

creates reputational damage for the business and serious consequences should the Federal Tax Authority regard such accounting processes as unsatisfactory.

- As the foreign entity has ownership of the goods once imported, the tax authority might consider the pro forma invoice as duly raised (as the customs broker or local business partner acting as IoR should be the owner of the goods at the time of import) and complete the fictional arrangement with a resale of the goods from the customs broker or local business partner to the foreign company. This invoice would be considered by the tax authority when calculating the tax base of the entity in the UAE for CT purposes.

In the context of increased synergies between administrative bodies in the UAE, the cooperation between the tax authorities and customs authorities would easily highlight the arrangement in place where the pro forma invoice should be considered for customs purposes but be disregarded for CT and VAT purposes. The use of such pro forma invoices not in accordance with the rules, therefore, proves risky and unsustainable.

Implications for businesses: adapting customs practices to the new tax landscape

In the light of the new tax legislation and the increasing complexity of the UAE tax landscape, businesses may want to redesign their operating models.

Regulatory and tax rules applicable in the UAE, and more broadly in GCC countries, are different from those in other regions in the world, for example, a

local presence is generally required to do business in, and import goods into, GCC countries. This principle has recently been modified in some areas in UAE, with more leeway given to international groups targeting the region (such as Federal Decree-Law No. 26 of 2020 amending the provisions of Federal Law No. 2 of 2015 on Commercial Companies, which annuls the requirement for commercial companies to have a major Emirati shareholder or agent). However, the customs legislation has not followed this trend. The IoR should still be a local entity and it should own the goods at the time of import.

Such specificities need to be considered by international companies when designing regional operating models. In the context of increased regionalization, adopting operating models in the GCC that are used in other regions may not be viable or efficient. It is crucial that processes and procedures adopted in the UAE comply with the GCC customs regulations.

Regional operating models should be reviewed to ensure that the arrangements used comply with all regulatory tax rules in the UAE. ■

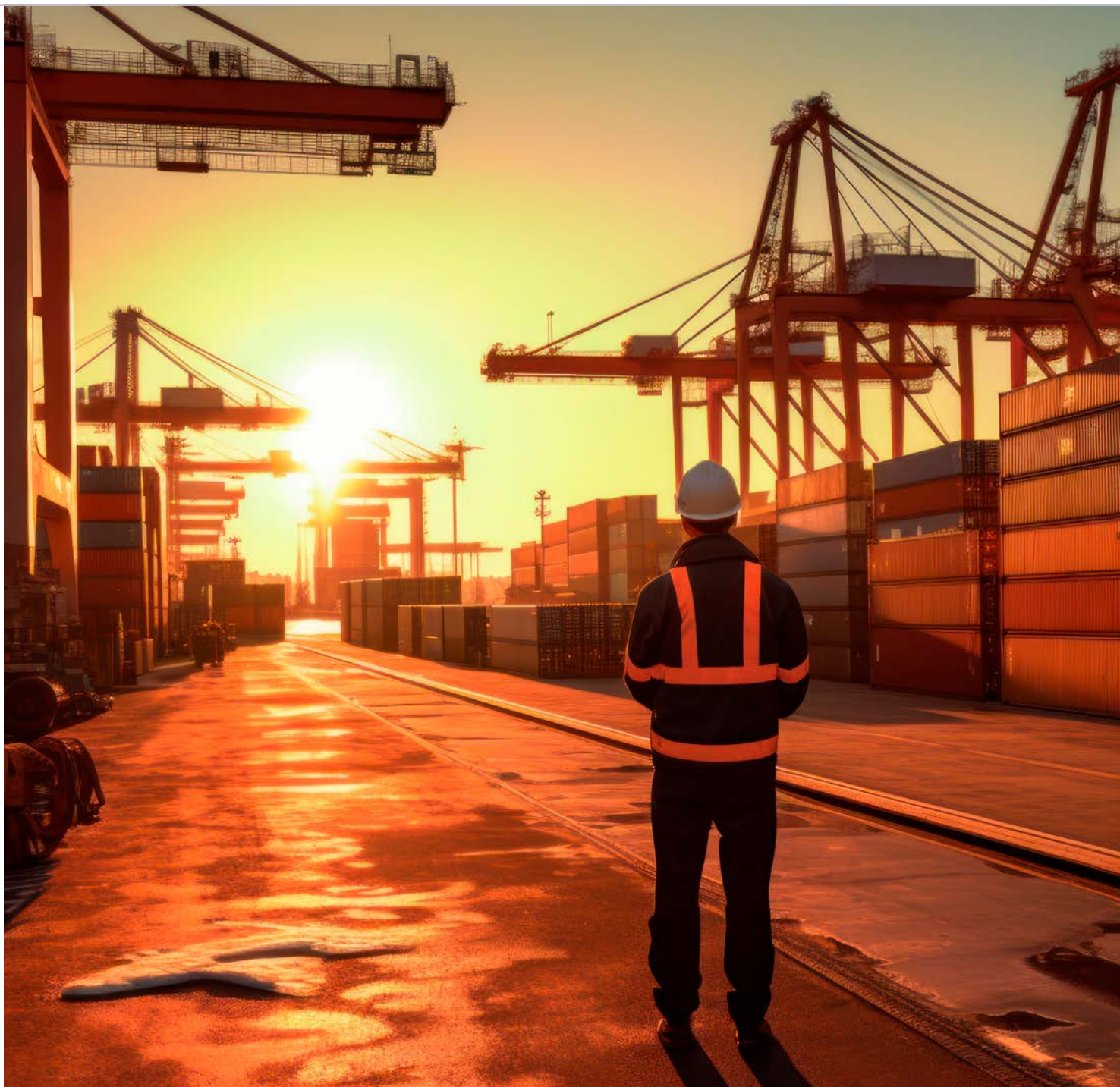
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UK: An overview of the Electronic Trade Documents Act

On 20 July 2023, the Electronic Trade Documents Act (ETDA or the Act) 2023 entered into force in the UK, giving certain electronic documents used in trade and trade finance the same legal footing as their hardcopy counterparts. In legalizing electronic documentary transferability, the Act sets a global precedent – providing the evidence base necessary

to prove how the digitization of trade supports international and domestic businesses, which benefit from reduced operational costs and more operational efficiencies, increased trade flow transparency and security, reduced manual-processing errors, and greater resilience against economic shocks like COVID-19 and the war in Ukraine.

What's in the Act?

The UK's ETDA enables businesses, under specific conditions, to convert their hardcopy trade documents into electronic trade documents and for electronic trade documents to be converted into paper-based documents.

In removing the age-old requirement for trade transactions to be documented through paper-based documentation, it is estimated that British businesses trading internationally will receive a GBP1.14 billion boost over the next 10 years and be better equipped to engage with international suppliers, customers and trade service providers.¹

Applicable trade and transport documents reflected in the ETDA include:

- ▶ Bills of exchange
- ▶ Promissory notes
- ▶ Bills of lading
- ▶ Ship's delivery orders
- ▶ Warehouse receipts
- ▶ Mate's receipts
- ▶ Marine insurance policies
- ▶ Cargo insurance certificates

While applicable only in the UK, the ETDA has been drafted to be nonrestrictive in operation, providing businesses with the choice to continue using hardcopy trade documentation or transitioning, at their own pace, to digital trade documentation.

¹ "UK economy to receive £1 billion boost through innovative trade digitalisation act," UK government website, 20 July 2023. [Find it here.](#)



How will the ETDA reform the traditional approach to trade and transport documents?

A typical trade transaction involves the movement of goods and services across borders and between numerous trade stakeholders, requiring linkages between freight, insurance, finance and customs capabilities. For example, a trade transaction that uses trade finance often requires over 100 pages of paper – normally comprising 10–20 separate trade documents. Where a trade transaction involves sea freight, it is not uncommon to see an additional 50 pages included and movement between as many as 30 different trade service providers.

Despite the rapid expansion of international trade, the fundamental processes and supporting laws still rely on practices developed over 100 years ago. For example, as goods make their way from the end of the production line to their final destination, they are accompanied by multiple documents that entitle a holder to claim the performance of obligations reflected in the document, including the ability to transfer the right to claim performance of an obligation when the document is transferred (physically) and possession by a new holder is achieved. It is the process of physically transferring a document that marks the transfer of an obligation, which may include delivering goods or paying a sum of money, as opposed to simply acknowledging existence.

Prior to the ETDA, the UK laws governing these processes were structured on the concept that documents must be physically held or “possessed.” For example, the Bills of Exchange Act 1882² (which applies to promissory notes and bills of exchange) references “bearers,” “holders” and “delivery,” and defines the terms in regard to maintaining and transferring physical possession.

Progress toward the digitization of trade processes

Progress toward digital trade documentation began in 2006 with the United Nations Commission on International Trade Law (UNCITRAL) and its work on the Model Law on Electronic Transferable Records (MLETR). In the UK, the Act was codeveloped by the Law Commission for England and Wales and the UK government, with the active support of the business community.

How will it work in practice?

The ETDA applies equally across England, Wales, Scotland and Northern Ireland, with an additional clause applicable to Scotland only. In operation, the Act requires digital documents to meet certain criteria, ensuring a replication of the key features of paper trade documents. As the Act encompasses a number of different trade and transport documents, the drafters have defined criteria that must be satisfied for documents to be considered “possessable” under the Act.

Key criteria include:

- ▶ Ensuring only one person, or parties acting jointly, can exercise exclusive control over a document at any time
- ▶ Removing any previous holder’s ability to exercise control over a document once it has been transferred

To support these criteria, documents must be transferrable through a “reliable system” to ensure that certain features of an electronic document can replicate the features of its paper-based equivalent. In operation, this means systems capable of:

- ▶ Containing the same trade information as its paper equivalent
- ▶ Remaining distinguishable from any copies or duplicates
- ▶ Ensuring protection against unauthorized alterations
- ▶ Remaining access-restricted to ensure exclusive control can be exercised
- ▶ Ensuring those who possess exclusive control can demonstrate their right to control
- ▶ Divesting exclusive control of the document upon an authorized transfer

² “Bills of Exchange Act, 1882,” *UK government website*, accessed 2 October 2023. [Find it here.](#)

Benefits of digitizing trade processes

The International Chamber of Commerce (ICC) has estimated the digitization of trade documents could generate GBP25 billion in new economic growth by 2024, and free up GBP224 billion in efficiency savings.³

The World Economic Forum (WEF) has found that digitizing trade documents could potentially reduce global carbon emissions from logistics by as much as 12%⁴ by reducing the estimated 28.5 billion paper trade documents printed and flown around the world daily.⁵

Next steps

Work has already started on developing industry-agreed standards required to support adoption, create market certainty for platform providers and participants, and define what constitutes a “reliable system.”

International interoperability will remain crucial for the long-term success of the ETDA. The development and deployment of MLETR-compliant solutions will support trade participants sharing documents and data between parties to a trade transaction outside of the UK. The route to increased interoperability

is ensuring that the ETDA has a cascading effect, providing operational insights to regulators to develop their own MLETR-compliant laws around electronic transferrable records.

For businesses looking to explore the benefits of the ETDA, they should focus efforts on identifying the most appropriate documents within their trade and transportation operations that could be transitioned to an electronic format. The process will involve working closely with their shipping and logistics suppliers to identify and agree efficiency and transparency benefits – and save on hard-copy paper. ■

- 3 “G7 | Creating a modern digital trade ecosystem,” *UK International Chamber of Commerce website*. [Find it here](#).
- 4 “Paperless Trading: How does it impact the trade system?” *World Economic Forum website*, October 2017, [Find it here](#).
- 5 “Digital assets: electronic trade documents. A consultation paper,” *UK Law Commission website*, 30 April 2021, [Find it here](#).

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Update on the UK-EU Windsor Framework



On 27 February 2023, negotiations between the UK and EU concluded with the Windsor Framework, amending the text and provisions of the original Northern Ireland Protocol, which was agreed as part of the UK's exit from the EU.¹

The changes under the Windsor Framework include easements for goods traded from Great Britain to Northern Ireland, simplifications to the application of EU value-added tax (VAT) rules for certain goods for consumption in Northern Ireland, and new governance mechanisms. However, much of the detailed guidance is still to be published ahead of the new measures being phased in.

In this article, we take stock of the current situation and look ahead.

Further guidance provided

The Windsor Framework has resulted in the implementation of a comprehensive set of solutions that tackle the issues people and entities encountered when moving goods to and from Northern Ireland since the UK's Withdrawal Agreement from the EU. This includes the introduction of new green and red lanes that signify a revamped goods checking system and special arrangements relating to labeling requirements for medicines and certain products under the Northern Ireland Retail Movement Scheme.

The implementation of the Windsor Framework is intended to take place in a staged manner from 2023 through 2025.

Green lanes

- ▶ Per the latest guidance on the UK Internal Market Scheme,² the full effect of the new "green lane" for moving goods from Great Britain to Northern Ireland will begin in September 2024. This new checking system for qualifying traders

¹ "UK and EU amend Northern Ireland Protocol with Windsor Framework," *EY website*, 4 March 2023. [Find it here.](#)

² "Apply for authorisation for the UK Internal Market Scheme if you bring goods into Northern Ireland," *UK tax authority website*, 9 June 2023. [Find it here.](#)

builds on the current trusted trader scheme and aims to considerably reduce the required customs procedures and checks for goods. Imports made using the green lane will need to be labeled “Not for EU” to negate the possibility of entering the EU single market.

- ▶ Traders that cannot access the green lane benefits will be compensated through a new tariff reimbursement scheme, if the trader can demonstrate that its goods did not ultimately enter the EU. This new scheme is in an expansion of current customs duty waivers.

Northern Ireland Retail Movement Scheme

- ▶ Traders can now register for the Northern Ireland Retail Movement Scheme (NIRMS),³ which went into effect on 1 October 2023. NIRMS replaced the former Scheme for Temporary Agrifood Movements into Northern Ireland (STAMNI), meaning that all traders selling or facilitating the movement of retail food and drink into Northern Ireland can register, including retailers selling finished goods to end customers, wholesale suppliers and those providing goods to the public sector.

As EU animal and plant health requirements and UK public health and consumer protection standards will apply for all included products (e.g., for fisheries, organics), relevant traders can make use of the scheme to avoid costly certification and assurance processes, while also meeting UK public health rules. Affected goods will move into Northern Ireland based on a single general certificate. NIRMS is seen as an expansion to STAMNI, as it encompasses a much wider range of traders.

Sanitary and phytosanitary controls

- ▶ In addition to NIRMS, there was a further change on 1 October 2023 for plant health labeling, called the Northern Ireland plant health label (NIPHL)⁴ scheme. The purpose of this scheme is to ensure that adequate checks for diseases and pests are carried out on relevant goods and that they may be traced.

Under this scheme, traders can move covered goods (including plants and seeds, seed potatoes, and used agricultural machinery and vehicles) without a phytosanitary certificate.

Goods moved with a valid NIPHL must follow certain procedures, including that the movement must be between an authorized professional operator in Great Britain and a registered professional operator in Northern Ireland, and the goods may not enter the Republic of Ireland or other EU countries.



³ “Northern Ireland Retail Movement Scheme,” *UK tax authority website*, 1 September 2023. [Find it here.](#)

⁴ “Moving plants from Great Britain to Northern Ireland,” *UK tax authority website*, 22 September 2023. [Find it here.](#)

Medicines authorizations and packaging

- ▶ The Windsor Framework lays out how marketing authorization for medicines⁵ is to be covered between the UK and EU. Beginning in January 2025, medicines may only be lawfully placed in the Northern Ireland market with a valid authorization from the UK, ending the application of any EU rules. Traders of medicines in Northern Ireland will be licensed by the Medicines and Healthcare products Regulatory Agency (MHRA), allowing for the same packaging and labeling across the rest of Great Britain.

Any new products falling under the scope of these changes must be labeled clearly with “UK only” to be allowed onto the UK market (including Northern Ireland). Products with this labeling will not be available on the market in the Republic of Ireland and the rest of the EU. All other EU serialization and barcodes based on the EU Falsified Medicines Directive will no longer be required. A single deadline for these new packaging changes has been set out by the MHRA for 31 December 2024. After this point, manufacturers of medicines may no longer use legacy EU packaging standards.

Subsidy control

- ▶ The Windsor Framework introduces a new subsidy control agreement, which relates to the practical application of Article 10 (i.e., the scope and application of EU State aid rules in Northern Ireland, the assessment of subsidies that constitute State aid, and the management of the application of the Framework in relation to agri-fish measures and services). It is intended to help public authorities to make a risk assessment before granting a subsidy, either individually or via a scheme, to determine whether it falls within the scope of the Framework. The guidance to this new mechanism⁶ shows how this may be done to enable public authorities to grant subsidies with greater confidence.

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Stormont Brake

- ▶ The Windsor Framework also included a new democratic governance safeguard for Northern Ireland that can be enabled if EU rules “significantly” change or new ones are introduced for regulation relating to trade and agriculture. This mechanism, called the Stormont Brake (the Brake), was included in the Framework as a response to concerns about a democratic deficit in Northern Ireland. The Brake allows the Northern Ireland Assembly to object to such changes if it passes a petition of concern threshold.

Increasing UK-EU regulatory divergence

The UK-EU relationship continues to evolve, and the Windsor Framework requires both sides to meet regularly to monitor implementation across the different areas of the Framework.

However, the regulatory regime in both the UK and the EU also continues to evolve – with significant divergence in trade regimes envisioned over the coming years. The most pressing example is the EU Carbon Border Adjustment Mechanism (CBAM), which entered into force on 1 October 2023.

The CBAM regime introduces a new reporting requirement (and eventual cost obligation) for companies importing iron and steel, aluminum, fertilizer, concrete, hydrogen, and electricity into the EU. As Northern Ireland is already part of the island of Ireland electricity market, east-west electricity trade will likely need to submit CBAM declarations, as will goods traded from Great Britain to Northern Ireland that are “at risk” of entering the EU. This would require the EU to add CBAM to the Windsor Framework’s annexes and may constitute the first test of the Stormont Brake.

UK businesses should remain vigilant to regulatory divergence between the UK and EU, which may impact their operations. ■

⁵ “Windsor Framework medicines announcement,” *UK tax authority website*, 9 June 2023. [Find it here.](#)

⁶ “Guidance on the scope and application of Article 10 of the Windsor Framework,” *UK tax authority website*, 9 June 2023. [Find it here.](#)

How tax departments should prepare for CBAM

Tax functions need to plan for the challenges CBAM will create and identify the potential opportunities it offers.

[Read the article on ey.com.](#) ■



Sustainability

The role of customs and trade functions in the ESG era

In a previous edition of *TradeWatch*, we discussed the need for businesses to future-proof their customs and trade functions,¹ with one of the key drivers being the need to react and adapt to new regulations.

For the customs and trade functions, emerging legislation in the sustainability space and changing expectations of corporate social responsibility raise vital questions about where its role sits within the corporate response to these priorities – and whether there is potential for the trade function to play a bigger part in shaping the sustainable future of the business.

While the short answer is that the trade function has an important role to play in this evolving business priority, the long answer, as always, is somewhat more complicated. In this article, we explore a few common issues we have seen businesses facing in dealing with this challenge and share examples of effective responses by trade functions to these considerations.

Background

Increasingly, we are seeing businesses transforming to become more sustainable, not just because it is the right thing to do and stakeholders now expect it, but also because a groundswell of regulation is pushing them in that direction.

These new regulations include at-border regulations, such as the EU's Carbon Border Adjustment Mechanism (EU CBAM)² and broader Plastic Packaging Taxes (PPTs)³; supply chain due diligence requirements, such as the EU's Anti-Deforestation Regulation (EUDR)⁴ and Corporate Sustainability Due Diligence Directive (CSDDD)⁵; disclosure obligations, such as the EU's Corporate Sustainability Reporting Directive (CSRD)⁶; and activity impacting regulatory policy, such as the EU's waste export ban.⁷

These regulations can be overwhelming for the business to handle – and the materiality of their impacts can vary significantly. Overall, there are a few common themes.

New reporting activities: These can take various forms, whether in the form of public disclosures (e.g., under CSRD) or reporting obligations to the authorities (e.g., EU CBAM). Businesses need to report more information about their operational footprint than ever before.

Additional supply chain visibility priorities: Many new regulations and standards require an unprecedented level of oversight on the business' operational footprint, such as the EUDR requiring geolocation of the production site for forestry products.



1 "Future-proofing" the customs and trade function," *TradeWatch* Issue 2 2023, page 5. [Find it here.](#)

2 "Carbon Border Adjustment Mechanism," *European Commission website*, last updated 1 October 2023. [Find it here.](#)

3 "Plastic Packaging Tax: steps to take," *UK government website*, last updated 31 March 2023. [Find it here.](#)

4 "Deforestation-free products," *European Commission website*. [Find it here.](#)

5 "Corporate sustainability due diligence," *European Commission website*. [Find it here.](#)

6 "Corporate sustainability reporting," *European Commission website*. [Find it here.](#)

7 "Plastic waste shipments," *European Commission website*. [Find it here.](#)

Changes to operating model and footprint: It is increasingly conceivable that business will make decisions to change their financial models and operational footprints in response to these demands – and some of them already have. This could be driven by cost pressure (e.g., from the imposition of the EU CBAM); regulatory pressure (e.g., activity bans); or by new demands from customers, employees and investors. These pressures may lead businesses to adopt new trade routes, new manufacturing locations and new commercial activities.

Who is responsible for sustainability?

Customs and trade functions can easily see the important role they have to play related to sustainability considering this evolving environment. However, in many cases, responsibilities for dealing with sustainability matters are not formalized, and this lack of clarity can be particularly crucial when new regulations strike.

Trade functions are not typically positioned to answer the question, “How do we run sustainability as a business?” However, this question is crucial in maximizing the value the function can add to the business and to ensuring business continuity. Based on our experience of working with companies globally, we have identified four key questions for trade functions to ask to better define their role in the sustainability space.

Four key trade function sustainability questions for businesses

1. How should the business be monitoring new barriers to trade and other regulations?

Sustainability regulations are evolving at an accelerating rate, presenting a real challenge for businesses with international trading footprints to keep up.

In June 2023, the environmental group edie reported⁸ that environmental, social and governance (ESG) regulations globally have increased by 155% in the past decade, with 1,255 ESG regulations introduced worldwide since 2011. Trade functions are now monitoring the soon-to-take-effect EUDR and requirements such as those presented by the EU Batteries Directive, which, later this decade, will establish firm obligations for businesses placing goods on the EU market.⁹

Meanwhile in the green tax space, the [EY Green Tax Tracker](#) identifies over 3,000 environmental taxes now in application across the 61 jurisdictions represented in the tracker.

Businesses are asking themselves how best to keep abreast of these regimes as they are asymmetrically implemented across jurisdictions, and in corporations with international footprints, that task can be a significant one.

Identifying and responding to these regimes is not necessarily the core responsibility of the trade function. However, given a trade function's top priority is usually to ensure the smooth movement of goods across borders, it is only natural for it to share a concern with the wider business for tracking these new policies, as noncompliance can impact not just market access but also the cost base and reputation of the business.

Key considerations for effectively monitoring relevant developments include:

- ▶ The policy elements and geographies to be monitored
- ▶ The stakeholders undertaking the monitoring activity
- ▶ The technology or other tools needed to deliver monitoring of new policy developments

2. Who should be responsible for compliance activities for green taxes and new due diligence requirements?

In many cases, the data and operational requirements presented by new ESG regulations require cross-functional collaboration. This has knock-on impact for clarity about internal roles and responsibilities.

Given the trade function's own compliance obligations, it is natural for it to have certain data at its fingertips that also happens to be required for compliance with these ESG regimes. For example, being an Authorized Economic Operator (AEO) requires the business to audit and monitor its own import and export footprint.

⁸ “ESG regulations have increased 155% in the last decade,” edie, 20 June 2023. [Find it here.](#)

⁹ “EU: Commission and Council take steps as part of the Circular Economy Action Plan with new rules on textiles and batteries,” [page 55](#) in this edition.

It is, therefore, almost inevitable for the trade function to be involved in some capacity in responding to these new ESG regulations. However, data fields used by the trade function are rarely the complete picture, making it impossible for it to be solely responsible for these reports.

The EU CBAM regime, which entered force on 1 October 2023, presents a strong example. Trade compliance data is a core tenet of the corporate response to the EU CBAM, as reporting obligations now apply to EU imports of certain products, defined by customs classification. However, responses to the regime also require an interface with suppliers to access “embedded emissions” data on the carbon content of imported products. Consequently, sustainability, supply chain and trade functions all need to be involved in the response.¹⁰

In practice, as we have seen in many cases, it can be challenging for various functions to come together and agree on a set of responsibilities, with the risk that important actions may “slip between the cracks” between functions.

This functional challenge extends beyond fiscal measures, with new regimes, such as the CSDDD, requiring new levels of transparency over the supply chain. Trade functions are not typically managing this regime, but, again, trade data can be critical to CSDDD reporting.

While many ESG regimes will continue to be owned elsewhere in the business, trade functions need to understand what compliance activities they have responsibility for. And, where they do not have responsibility, they need to identify what support they may be asked to provide to the responsible parties and through what processes.

3. Is there an interface between existing trade function trade priorities and new data needs?

Alongside the ESG regulations mentioned in this article that use international trade data for compliance purposes and thus require trade function cooperation, we are also seeing examples of broader trade function priorities intersecting with new imperatives presented by sustainability regulations.



As an example, some of the new regulations under discussion demand transparency from businesses over the product makeup and manufacturing footprint of imported products (e.g., the UK's PPT and the EU CBAM). These demands align with the data collection requirements and priorities for proof of both preferential and non-preferential origin. These existing customs priorities already put obligations on the business to break down the Bill of Materials to review product makeup and to begin to understand the identity of specific installations for manufacturing and other upstream activities.

Meanwhile, some of the wider activities undertaken to respond to ESG regulations are enhancing the business case for some customs and trade function initiatives, such as:

- ▶ **Customs classification:** While customs classification is already a priority for many trade functions, regimes such as the EU CBAM apply to goods based on their customs classification. Consequently, the importance of customs classification is heightened, as it defines exposure to the regime. We are seeing this interplay beginning to inspire businesses to test the robustness of their product classifications.

¹⁰ See our “EU: CBAM in force” article on [page 51](#) of this issue.

- ▶ **Broker rationalization:** Increasingly, customs and trade functions look to access international trade data to assist with sustainability priorities, and in many cases this data can be accessed from customs brokers. However, where a company operates with a distributed brokerage environment, this can require a high volume of data requests and a suboptimal data environment. Rationalizing the number of customs brokers the business uses can mitigate this challenge.

Consequently, for proactive customs and trade functions, understanding the demands placed upon the business by evolving ESG regulations can present great opportunity and accelerators, enabling a trade function leader to articulate at a higher and more impactful level within the corporate structure the added value that may be made possible by improvements and investment in the trade function.

4. How do international trade priorities interface with corporate sustainability transformation priorities?

In many cases (and certainly in best-in-class trade functions), international trade data is already used for business-level visibility over the corporate footprint and to help with matters such as assessing the landed cost of certain product lines, as trade functions have strong technical and operational knowledge of a business's movements of goods.

Businesses may look to reorganize their product lines, manufacturing footprints and supply chain profiles to respond to sustainability priorities (e.g., changing providers to move from using from traditional steel to green steel). They need to understand the implications of different footprint options for their wider operations and their cost profile and opportunities. International trade considerations should be critical to this analysis.

For example, consider a company that buys steel for its manufacturing activities in the EU. Based on the emissions profile of the steel used currently and the carbon price already paid, the company decides it wants to start buying steel from South Korea rather than from its current supplier in Brazil. What might that decision mean for its wider trade footprint? Some questions that the business should be asking in this case include:

- ▶ What evidence do we need to reduce the duty liability for the new steel imports made via the EU-South Korea free trade agreement (FTA)?
- ▶ What does this new purchase flow mean for the regional value content in our EU-manufactured goods for export?
- ▶ If trade compliance is looking after the EU CBAM response, what documentation do we need to capitalize on the Korean emissions trading scheme carbon price already paid to avoid double paying the carbon price under CBAM?

The trade function can add real value in this scenario, both through providing the necessary data and sharing its expertise for strategic decisions on supply flows, procurement and the organization's wider footprint – not just by keeping goods moving but by helping to shape and optimize a more sustainable business footprint.

Understanding the success factors for sustainable trade functions

Based on these four questions, what attributes may a business want to focus on to ensure that the trade function is set up for success in this space?

Clarity over roles and responsibility

We often see businesses falling down on compliance with new ESG regimes (e.g., PPTs) when no responsibility is allocated and certain activities slip between the cracks among different functions.

Some high-performing businesses are developing detailed RACI (responsible, accountable, consulted and informed) matrices and process flows for new sustainability regulations and taxes to ensure their response is clearly planned.

Even if the business does not have a detailed process in place, at a minimum, a responsible and empowered stakeholder or champion should be identified for monitoring new sustainability regulations and for compliance with each of them. Such a champion (or champions) could sit in sustainability, tax, supply chain, the trade function or elsewhere in the business.

An upskilled and engaged team

At the heart of success for everything is people. In addition to the challenge around clearly defined responsibilities and obligations, we see many clients facing a lack of readily available talent in the market. This is especially true with sustainability skills, which are increasingly in demand as businesses respond to the groundswell of new regulations facing them.

In light of this, we are seeing many customs and trade specialists branching out into some aspects of sustainability. This seems a natural progression as, for decades, the customs and trade functions have been playing a role in policy interpretation and business partnership.

Consequently, rather than hiring new people, the talent solution may very well be providing learning and training on the job for existing personnel. If this approach is supported by the wider business, putting the right upskilling approach in place is key, and we are beginning to see enterprise-wide sustainability learning programs implemented in many organizations. This approach can include the trade function but often extends far beyond it.

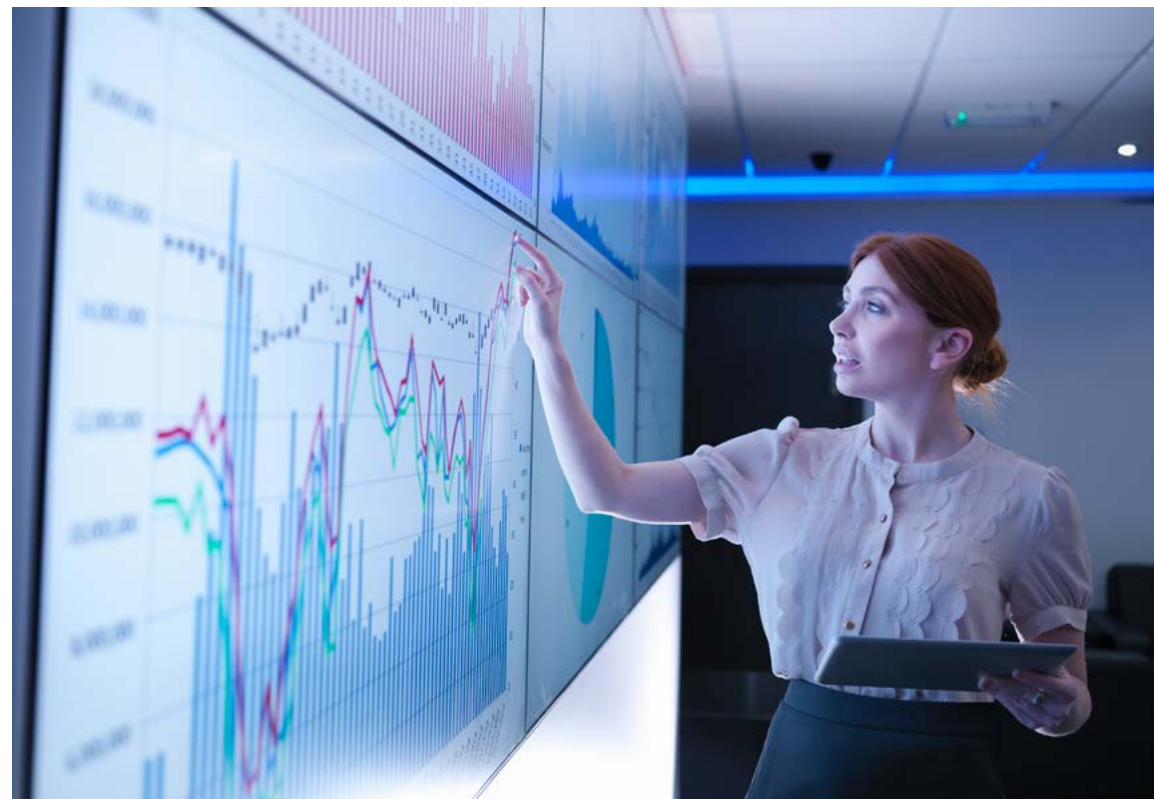
The right technology

Responsible, upskilled stakeholders cannot deliver without the right tools, and increasingly pressures to align international trade data and sustainability data are requiring businesses to look at investing in new technology or developing bespoke solutions in-house.

In this digital age, leaders of every corporate function are exploring better automated ways of working, underpinned by technology solutions. Different departments are pursuing and evaluating different technology solutions, which can bring challenges, such as inefficiencies of data acquisition processes and the need for constant customization and reconfiguration as new technology solutions are introduced.

As all of these stakeholders look to get the right technology in place to respond to new sustainability demands, having a uniform technology strategy and approach across sustainability, finance, supply chain and trade will be key. Coordination is vital to ensure that the selected solutions are fit for purpose and provide the right data interfaces for compliance with the cross-functional data

demands imposed by the new ESG regulatory environment. No doubt there will be increasing instances where management needs to make investment decisions based on what is deemed to be a priority. However, many of these objectives go hand in hand, and the right technology and responsible governance can bring a considerable amount of synergy across various functions' objectives. ■



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Australia considers CBAM to address carbon leakage

The Australian government has announced a review of policy options to address carbon leakage, including the feasibility of an Australian Carbon Border Adjustment Mechanism (CBAM). As the urgency to address climate change intensifies globally, Australia has commenced the Carbon Leakage Review, which aims to assess the carbon leakage risk, consider policy options for addressing leakage and then conduct a feasibility assessment of a possible Australian CBAM, following the EU's lead.¹ In a marked change from the previous government, Australia's Minister for Climate Change and Energy, the Hon. Chris Bowen, has made clear that efforts to combat carbon leakage by regulating supply chains is "a key consideration in the development of climate policy."²

This new provision stems from Australia's reforms to its Safeguard Mechanism, which commenced at the start of the financial year on 1 July 2023 and sets limits on emissions at Australia's largest industrial facilities. The proposed introduction of an Australian CBAM aims to level the playing field for domestic producers that are subject to carbon pricing and the Safeguard Mechanism and face competition from foreign producers' imported products that are not subject to the same rules. A CBAM could do this by applying a "carbon tariff" at the border on imports of certain commodities, such as steel and cement (including clinker and lime), from countries with weaker emissions reduction policies.



1 Further background information on the EU CBAM can be found in our article "EU: CBAM in force" in this edition of *TradeWatch*, [page 51](#), and in our alerts [European Parliament approves EU Emission Trading System reform and new EU Carbon Border Adjustment Mechanism](#), *EY website*, 20 April 2023; and [Final regulations published for new EU Carbon Border Adjustment Mechanism \(CBAM\) and EU Emission Trading System revisions; CBAM transition period begins 1 October 2023](#), *EY website*, 22 May 2023.

2 Hon Chris Bowen, "Speech to Australian Business Economists," *Australia Department of Climate Change, Energy, the Environment and Water website*, 15 August 2023. [Find it here.](#)

The EU's CBAM has gained attention for its attempt to address this carbon leakage challenge, wherein industries shift production to countries with less-stringent climate policies, undermining global emissions reduction efforts. The EU CBAM imposes a levy on industries with significant emissions, such as cement, iron and steel, aluminum, fertilizer, and electricity. The goods in the CBAM's scope are identified based on the Harmonized System for Tariff Classification, a standardized global framework for categorizing traded goods, and are correlated with what importers would have paid under the EU's emissions trading scheme.

The EU's experience offers valuable lessons for Australia. The EU's CBAM has faced concerns and criticism from trading partners (e.g., China, South Africa, Brazil, India) that view it as a discriminatory trade barrier, and it could face a challenge at the World Trade Organization (WTO). The Australian review will, therefore, likely focus on finding the appropriate balance between the country's national net-zero ambitions, its trading relationships, consistency with international trade rules and possible interoperability with other CBAM schemes.

The government's Carbon Leakage Review of additional policy options will be led by Frank Jotzo, a professor of environmental economics and climate change economics at the Australian National University. Jotzo will be supported by a team within the Department of Climate Change, Energy, the Environment and Water, and representatives from other Australian government agencies. The review team will consult extensively with two rounds of public consultation, including calls for written

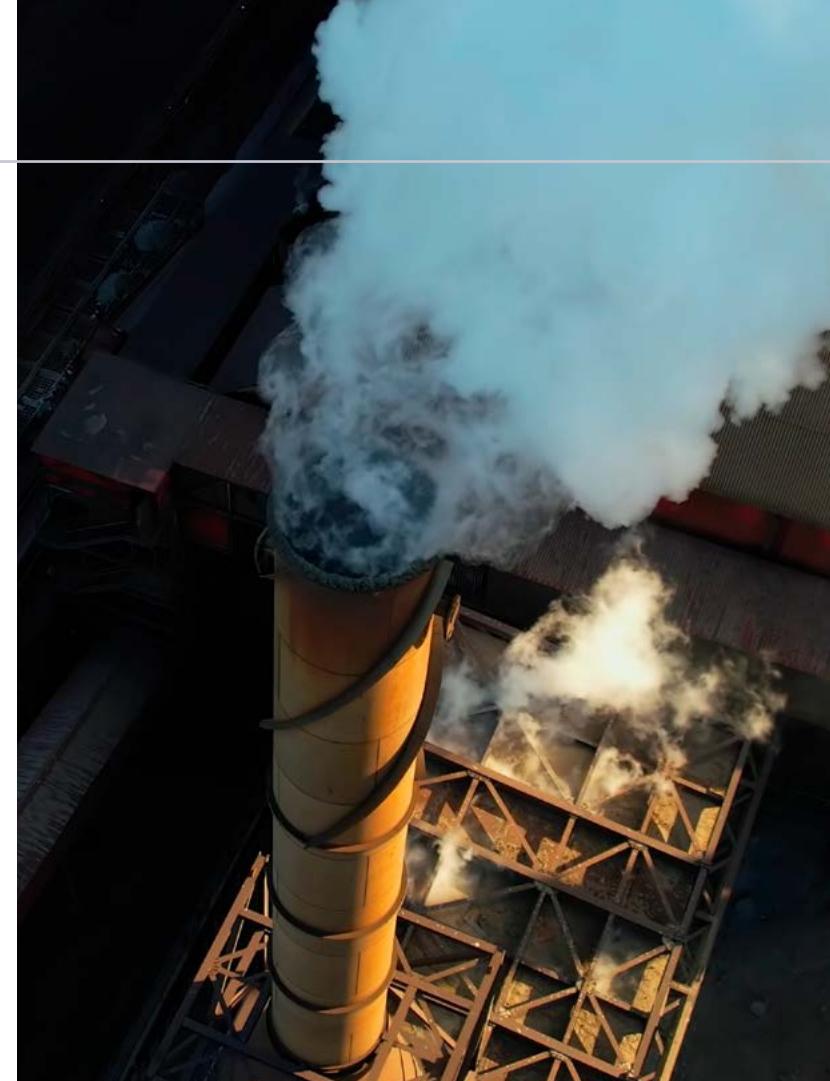
submissions. Key stakeholders include industry, peak business groups, experts and researchers, commonwealth and state and territory government agencies, international trading partners, relevant international bodies, and the broader community.

The final review report is due to be finalized by 30 September 2024, and detailed design of any agreed policy options will then be developed and could be implemented in the government's Net Zero 2050 plan.

Actions for businesses

To prepare for the potential implementation of a CBAM or similar carbon tariff, Australian businesses should consider:

- ▶ Undertaking an assessment of exposure and impacts by identifying the goods and sectors that could be affected by the tariff and estimating the potential financial impact on their operations
- ▶ Implementing further emission tracking and reporting to verify the carbon emissions associated with their products
- ▶ Prioritizing carbon reduction and diversification strategies to reduce reliance on high-emission products
- ▶ Evaluating existing trade relationships, proactively initiating dialogue to address concerns and exploring ways to minimize tensions
- ▶ Engaging and collaborating with businesses, industry associations and government bodies to help shape a harmonized approach to carbon pricing and trade ■



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EU: CBAM in force

On 1 October 2023, the world's first legal instrument for a CBAM became effective in the EU. This is an important landmark in development of carbon pricing measures – and not only for businesses based in the EU. The EU measure impacts a wide range of businesses globally. It may also influence the approach to carbon pricing instruments currently considered in other jurisdictions, including Australia and the UK, where local CBAMs are in the initial stages of legislative development.

Key dates for the EU CBAM

- ▶ The EU CBAM instrument started with a transitional period, which lasts until 31 December 2025. It requires importers (customs declarants and indirect representatives) to keep records about CBAM data and report embedded emissions in goods subject to CBAM.
- ▶ From 1 January 2026, the final implementation of CBAM will require importers to hold a new authorization (as an authorized CBAM declarant) to declare goods for release for free circulation in the EU. The authorization can be applied for from 31 December 2024.
- ▶ From 1 January 2026, importers will be required to purchase CBAM certificates on an ongoing basis to cover the emissions embedded in imported CBAM-covered goods.



- ▶ The CBAM charges are phased in from 2026 until 2034, with a progressive amount of CBAM certificates due as the measure progresses.
- ▶ This CBAM phase-in period mirrors the phase-out of so-called free allowances for CO2 certificates, which EU manufacturers will continue to receive in the next few years, and it will provide for a level playing field between EU goods and imports from outside the EU.

Impact of CBAM charges

Depending on the emission intensity of imported goods, and the volume an importer brings into the EU, CBAM charges may become a material cost, making them a real strategic or competitive advantage or disadvantage for businesses. Businesses investing in low- or zero-carbon manufacture will earn a competitive edge for their

investment, as their carbon pricing will be lower than for competitors that have not invested (with charges applying by way of the EU Emissions Trading System for EU manufactured goods and CBAM for non-EU manufactured goods being imported to the EU).

Who is affected by CBAM?

Businesses in many sectors can be affected by CBAM. CBAM in its current version covers products such as:

- ▶ Kaolin and other kaolinic clays, calcined
- ▶ Cement, aluminous cement, cement clinkers, etc.
- ▶ Fertilizers (e.g., ammonia, nitric acid, sulphonitric acids)
- ▶ Agglomerated iron ores and concentrates

- ▶ Comprehensive coverage of iron and steel products (except some ferroalloys, scrap, etc.)
- ▶ Iron and steel products, including downstream products, such as screws, bolts, nuts, coach screws, screw hooks, rivets, cotters, cotter pins, washers (including spring washers) and similar articles
- ▶ Aluminum structures and parts of structures
- ▶ Certain aluminum reservoirs, tanks, vats and containers
- ▶ Stranded wire, cables, plaited bands and the like, made of aluminum, not electrically insulated
- ▶ Other articles of aluminum
- ▶ Hydrogen
- ▶ Electrical energy

A wider net, in which many businesses may be caught

Responsibility for CBAM extends not only to the “heavy importers” of the products listed above. Even businesses that import small amounts of them may be caught by these provisions. This is because CBAM only has a de minimis limit for consignments up to EUR150. Hence, most business-to-business import shipments of CBAM-covered goods will be relevant.

In particular, it is crucial to consider that CBAM not only covers raw materials or semifinished products but also some downstream products, such as basic metal parts and connection tools, including screws, bolts and nuts. That means that each business sourcing these common goods (e.g., spare parts and components for machines, electronics) from outside the EU can become liable under the CBAM regulations. Therefore, it is important for businesses to actively validate whether they are excluded from CBAM (as it is so easy to become covered).

These provisions may even extend further in the next few years. Given the importance of sustainability, it seems likely that policies will be introduced to bring all imported products into the CBAM net that would be subject to carbon pricing in the EU, if they were produced in the EU. If so, these rules may cover an extended range of metal products, polymers (plastics), mineral oil products, diverse chemicals, paper and pulp, ceramics, and others. Therefore, the strategic impact of CBAM is likely to grow over the coming years and that will impact even more businesses.

Who is responsible within the organization?

For most businesses, the CBAM journey starts with the fundamental question: Who is responsible for CBAM? And there is no simple answer.

CBAM is neither a customs duty, nor a tax.¹ Hence, some tax and trade professionals may argue that someone else within the organization should own CBAM. In practice, this responsibility often falls to the sustainability department, supply chain or procurement. However, this may not always be the best solution.²

CBAM is a measure closely connected to trade and cross-border movements of goods. Therefore, it is heavily connected to customs and not just to customs import data (which is needed for accurate CBAM reporting). The CBAM regulations are full of legal clauses taken from customs regulations or that make reference to them. Therefore, effective compliance requires a deep understanding of customs principles. This is an argument for the trade function within the organization to have a strong role in dealing with this measure.

Other possible contenders for responsibility are the tax, trade or finance functions within the organization. One possible argument for CBAM responsibility residing with them is the fact that tax and trade professionals have the necessary experience and knowledge to deal with these types of legal regulations and to comply with their conditions. Also, traditionally, these departments are experienced in reporting to the authorities, which is also often cited as a reason for giving them the task. If no other department takes responsibility for CBAM, by default it may simply end up with these functions.

None of these decisions is right or wrong. Each decision about where governance should reside has its advantages and disadvantages. Of course, factors such as resources, experience and corporate structure are also vital to consider in making any decision about who should own the topic. In practice, the best solution is likely to involve multiple stakeholders across the organization. The important thing is that a decision about who has ultimate responsibility must be made, and it should be made consciously, not by default. CBAM is now a reality

1 The EU's Carbon Border Adjustment Mechanism (CBAM) is our landmark tool to put a fair price on the carbon emitted during the production of carbon intensive goods that are entering the EU, and to encourage cleaner industrial production in non-EU countries. The gradual introduction of the CBAM is aligned with the phase-out of the allocation of free allowances under the EU Emissions Trading System (ETS) to support the decarbonisation of EU industry.", *European Commission website*. [Find it here](#).

2 "The role of customs and trade functions in the ESG era" in this edition of *TradeWatch*, [page 44](#).

and affected businesses must decide who is going to take ownership of it and prepare the organization for CBAM reporting and the impact of CBAM costs.

Dealing with CBAM

Once responsibility has been assigned, the initial steps for a business to approach CBAM are generally:

- ▶ Screening the product portfolio for CBAM-covered goods
- ▶ Identifying the affected entities
- ▶ Screening the affected customs service providers and suppliers

Our experience in helping organizations to deal with the new regulations is that the whole project may become far more complex than initially expected. Some of the issues that may cause challenges include:

- ▶ **Customs classification:** For some products (especially metal products) customs classification can become truly complex as, depending on details of the product's characteristics, different products performing the same function can have different customs classification and may or may not be covered by the CBAM.
- ▶ **Indirect procurement:** Aside from the import of products or traded materials, businesses often have imports of "indirect procurement," such as purchases made by the IT or marketing departments or import of samples and the like. These goods may not be easily visible in standard reports, and they may arise in entities that would not be readily considered as subject to the CBAM.

▶ Customs service providers and suppliers:

Non-EU businesses often use logistic service providers and customs representatives to act in the capacity of an indirect customs representative to import cleared goods for the non-EU principal. However, these EU service providers are likely to take on considerable additional obligations under CBAM. In that case, they may want to change their current arrangements and service agreements to avoid becoming obliged to act on behalf of their non-EU clients under CBAM and running additional risks.

Scenario planning for additional costs

Most businesses are also interested in the cost implications of CBAM from 2026 onward. These scenario simulations can cover multiple dimensions. Businesses will want to understand the direct CBAM impact coming from their own imports. They will also want to understand the indirect CBAM impact if another upstream party imports the goods, pays for CBAM and will potentially include the cost when making intra-EU sales to the customer.

Changes in the portfolio and volumes of procured goods may also be considered. Finally, improvements in emissions intensity, changes in carbon costs paid in the country of origin and the EU carbon price (the price of the CBAM certificates) may be considered in the modeling.

Often, the results of an initial indicative modeling are needed to convince other stakeholders in a clients' organization that CBAM can become business critical. This may be a necessary step in receiving support and resources to drive comprehensive CBAM preparation.



The data challenge

CBAM reporting appears to be a challenging data exercise for most importers. In full, the CBAM report has more than 200 data elements (although, not all are initially mandatory). It comprises data that should come from customs declarations, data from enterprise resource planning systems and emissions data. Key preparatory steps include finding the right data sources (i.e., identifying the relevant systems and data owners), identifying how to extract the data from systems, and determining the availability and quality of the available data.

If data is available and is of a good quality, governance organization and processes are needed to extract and transport it from different sources and owners to a central function designated to prepare and submit the CBAM report to the authorities (i.e., the EU Commission).

Different reporting solution options are likely to apply. For example, the reporting may be organized locally (at the level of single entities), through an internal shared service center arranging the reports for a group of entities or by integration of an external service provider. Outsourcing or co-sourcing these tasks may be an option. Service providers (including EY firms) may offer CBAM reporting as a managed service or provide a dedicated IT solution to efficiently connect data providers and streamline the CBAM reporting workflow.

Reporting emissions data

Another specific data challenge for businesses is the reporting of emissions data. Three methods for emissions determination are defined by law:

1. As a standard, the EU method requires determining emissions from source streams based on so-called “activity data,” which means determining emissions from emission sources by means of continuous measurement.
2. As a simplification, until the end of 2024, emissions data may also be determined by way of methods used under monitoring, reporting and verification systems (MRV) or other methods (e.g., if a carbon pricing scheme is applicable where the installation is located, the data is based on an emissions monitoring scheme applicable to the installation that can also include verification by an accredited verifier or data determined based on compulsory emission monitoring schemes).

3. If a CBAM-obliged importer does not own data determined in accordance with the above methods, standard values, which will be published by the EU Commission, can be used for a simplified calculation of embedded emissions. However, the use of this simplified method will only be available for the first three reports, until mid-2024.

The EU Commission has provided a template for the documentation and sharing of emissions information, which is a comprehensive guideline detailing the standards for CBAM emission determination. However, the rules are complex and may overburden many manufacturers. Also, in some scenarios, suppliers may not be prepared to provide details about the manufacturer and embedded emissions for commercial reasons, which may place importers in a difficult situation, as they will not have the data required.

Non-EU manufacturers that sell into the EU market should familiarize themselves with the EU rules for CBAM embedded emissions determination and pursue ways of providing this information. While EU importers sourcing from third-party suppliers need to consider how they will enable their suppliers to provide the data they will need, collaboration will be crucial throughout the supply chain.

CBAM penalties²

Working toward accurate CBAM compliance is also important to mitigate the risk of incurring penalties for noncompliance or false reporting. For the CBAM transitional period, the regulations specify a penalty from EUR10 to EUR50 for each unreported ton of emissions. When setting the penalty amount, authorities may consider the extent of unreported information, the quantity of unreported imported goods and the unreported emissions relating to those goods. The CBAM declarant’s readiness to correct the situation and their historic behavior will also be considered. Higher penalties may be applied if more than two incomplete or incorrect reports are submitted in a row or the duration of the failure to report exceeds six months. Some EU Member States establish local penalty regimes in addition, which, in some cases, contain much harder sanctioning. ■

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² Further information can be found in our alert “EU | Compliance obligations for EU CBAM,” EY website, 16 October 2023. [Find it here.](#)

EU: Commission and Council take steps as part of the Circular Economy Action Plan with new rules on textiles and batteries

Sustainability continues to be a hot topic around the world as governments take action to reduce carbon emissions, waste and pollution – not only introducing new taxes and levies but also offering incentives to businesses to improve their environmental footprint.

The EU Commission and Council have announced proposals aimed at improving sustainability for the textiles industry and for batteries. Developments include new waste targets and extended producer responsibility (EPR) requirements in these areas. Businesses should review these developments, make use of available research and development (R&D) incentives and grants, and consider how their supply chains may need to be reworked in accordance with new requirements.

Overview

As part of its journey toward a more circular economy, in July 2023 the EU Commission and Council made further announcements to previous

environmental proposals to ensure that producers of textiles and batteries move toward more sustainable production, consumption and disposal of their products in the EU. These packages were released alongside a package of measures for a sustainable use of key natural resources and reflects Europe's continued commitment to the European Green Deal. These measures are part of the Circular Economy Action Plan (CEAP), a key pillar of the European Green Deal,¹ which is setting Europe on the path to climate neutrality by 2050.

Textiles

From the perspective of European consumption, textiles are the fourth-largest source of environmental and climate pressure – after food, housing and mobility – as established by the European Environmental Agency.² Estimates show that the carbon footprint of the textiles sector is 442kg CO₂-eq per person a year.³ At the same time, almost 90% of this climate footprint occurs outside the EU.⁴

¹ "The European Green Deal," *European Commission website*. [Find it here](#).

² "EU exports of used textiles in Europe's circular economy," *European Environment Agency website*, 27 February 2023. [Find it here](#).

³ "Circular Economy Perspectives in the EU Textile sector," *European Commission website*, 16 June 2021. [Find it here](#).

⁴ "Circular Economy in the Textile Sector," *European Union website*, January 2019. [Find it here](#).



Specific rules have been proposed to introduce EPR requirements for textile producers across the EU. EPR is an environmental policy measure that extends a producer's responsibility to the full lifecycle of a product, which could include not only waste, recycling and return of products but also product design. Although numerous legislative stages remain before enactment, companies that could fall within the scope of these measures should note that the impact will be significant and will largely influence day-to-day operations.

Circular economy for textiles

Given the high impact of textiles on the environment and climate change, the full lifecycle of textile products has been under high scrutiny by the EU.⁵ The release of the "EU strategy for sustainable and circular textiles" on 30 March 2022 marked the policymakers' vision for more sustainable management of textile waste. On 5 July 2023, new EU rules were proposed, aimed at:

- ▶ Introducing a mandatory and harmonized EPR for textiles across EU Member States
- ▶ Promoting R&D of innovative technologies for the circularity of the textiles sector, such as fiber-to-fiber recycling

⁵ "EU strategy for sustainable and circular textiles," *European Commission website*, 30 March 2022. [Find it here](#).

⁶ "Council adopts new regulation on batteries and waste batteries," *Council of the EU press release*, 10 July 2023. [Find it here](#).

⁷ "Circular economy: New law on more sustainable, circular and safe batteries enters into force," *European Commission website*, 17 August 2023. [Find it here](#).

⁸ "Critical Raw Materials Resilience: Charting a Path towards greater Security and Sustainability," *European Commission website*. [Find it here](#).

⁹ Including the [EU Waste Framework Directive \(2008/98/EC\)](#), and [Regulation \(EU\) 2019/1020](#).

- ▶ Preventing the practice of illegal exports of textile waste disguised as being for reuse

The above measures will support the new rules requiring the separate collection of textile waste, which will become mandatory in the EU in 2025.

Potential implications – textiles

Steps in the regulatory process still need to be completed. However, companies either headquartered in the EU or present in the EU at some point in their supply chain should consider taking actions such as:

- ▶ Mapping responsibility for the EPR costs and obligations if products are only partly composed of textiles and preparing for new reporting obligations
- ▶ Reviewing supply chains and considering impacts such as durability, reparability and recyclability of textiles; carbon impact of textile processes (e.g., production or transportation) and/or water usage; human rights and labor considerations; and qualification for textile waste under the new waste shipment regulation
- ▶ Making use of available R&D incentives, grants and funding to finance sustainable textiles transformation
- ▶ Understanding and modeling other potential operational costs, in addition to EPR, such as for production costs, new shipping or waste costs, and carbon-related costs
- ▶ Considering recycle or repair programs to champion circularity and reduce operational costs

For companies active in the textiles sector, it will be important to continue to monitor developments in this regulatory space. Early understanding of their potential impact from a legal, business, operational, tax and transfer pricing perspective is crucial for adopting appropriate strategic measures.

Batteries

On 10 July 2023, the EU Council adopted a new regulation on batteries and waste batteries⁶ that will replace the existing legal framework (dating to 2006) by introducing more stringent requirements. The new legislation became directly applicable across the EU on 17 August 2023.⁷

The environmental impact of over consumption is not the only reason why the EU is focusing on circularity in this sector. Equally important are technical solutions based on raw materials used in batteries, which play a key role in the development of zero-emission mobility solutions and the storage of renewable energy. Research shows that for batteries for electric vehicles and energy storage, the EU will need almost 60 times more lithium and 15 times more cobalt by 2050, compared with the current supply of these materials to the EU.⁸

New regulation: strengthening sustainability rules for batteries and waste batteries

The new regulation will repeal the existing batteries and waste batteries directive (2006/66/EC) and amend other related legal acts.⁹ Key updates include:

- ▶ A broader and more detailed EPR regime
- ▶ Labeling and information requirements to apply by 2026
- ▶ An obligation to set up an electronic “battery passport” and a QR code by 2027 (operators are also required to verify the source of raw materials used for batteries placed on the market – subject to a small and medium-sized enterprises exemption from the due diligence rules)
- ▶ An obligation to ensure that portable batteries incorporated into appliances are removable and replaceable by the end user by 2027
- ▶ Waste collection targets and separate lithium collection targets for waste batteries
- ▶ Mandatory minimum levels of recycled content (initially set at 6% for nickel, 6% for lithium, 16% for cobalt, 85% for lead) and maintaining recycled-content documentation
- ▶ A recycling efficiency target for waste batteries

EU Member States are required to establish rules on penalties applicable to infringements of the new battery and battery-waste regulation.

Potential implications – batteries

Primarily, it is important to remember that an EU regulation is a binding legislative act that must be directly applied in its entirety across the EU. Therefore, this measure will become immediately relevant to all companies headquartered in the EU and companies with an element of their supply chain in the EU. The new regulation will automatically replace previously applied national frameworks. However, it can be expected that some EU Member States may introduce additional obligations on a national level.

Affected businesses should consider and evaluate:

- ▶ Additional compliance and reporting obligations and the associated costs
- ▶ Increased regulatory focus on EPR systems
- ▶ The need to redesign products if batteries are neither removable nor replaceable by the end user or if the components are not compliant with the regulation's requirements
- ▶ Available R&D incentives, grants and funding to finance supply chain transformation, especially to meet new requirements
- ▶ The cost efficiency of a recycle or repair program
- ▶ The company's new carbon footprint, resulting from any changes to the supply chain

It will be important for companies to reassess their obligations and their supply chain in light of the new rules to meet targets and comply on time. ■



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UK: Reducing waste

In recent years, customer and shareholder demands have rapidly shifted – consumers expect companies to play a key role in delivering a sustainable future, and shareholders base investment decisions on environmental, social and governance (ESG) criteria. In the UK, like many other countries globally, tax and regulatory developments reflect this shift. In recent years, the government has responded with policy measures focused on emissions reduction, transparency and reporting, and incentives and government funding for sustainable advancements. In addition to these measures, resource preservation is a key factor and one of the biggest challenges that we face globally.

EPR and PPT

Extended producer responsibility (EPR) and Plastic Packaging Tax (PPT) are two measures focused on controlling the level of packaging that is not recycled or reusable. The EPR regulations will apply to all UK organizations that import or supply packaging. EPR recognizes that the traditional “take-make-dispose” linear economic model is unsustainable, as it leads to resource depletion, pollution and the accumulation of waste. The aim of this legislation is to give companies financial incentives to reduce the amount of packaging they supply and improve recyclability.

This new environmental policy has created a range of challenges for businesses, particularly those heavily reliant on packaging, as in-scope businesses are required to re-evaluate their packaging materials, supply chains and production processes to comply with the data and reporting requirements. Businesses should also take the opportunity to assess their plastic and packaging reduction strategy to ensure that they understand the impact of both packaging measures (PPT and EPR) on their current business model.

Latest updates

The Department for Environment, Food & Rural Affairs (DEFRA) has extended the reporting and packaging fees deadlines associated with EPR. DEFRA confirmed that it will use the additional year to continue to discuss the scheme's design with industry and reduce the costs of implementation wherever possible:

Packaging fees

Fees associated with EPR have been deferred to October 2025. However, organizations must report their first packaging data report for 2023 by 31 May 2024, at the latest.

Reporting under EPR

The first reporting period for EPR is 1 January 2023 to 30 June 2023. Small organizations should submit the report for this period by 1 April 2024, and large organizations should have submitted their data by 1 October 2023. DEFRA confirmed that these deadlines are laid out in the regulations; however, no enforcement action will be taken if this data is submitted by 31 May 2024.

Four key actions for organizations to consider

Businesses should consider taking the following four actions now to prepare:

1. **Understand when to report your EPR data.** Reports should be submitted for two periods (1 January 2023–30 June 2023 and 1 July 2023–31 December 2023) on 31 May 2024. Each report must be reported separately.
2. **Closely monitor developments** with EPR and other packaging regimes across the EU as other jurisdictions prepare to launch their own EPR regimes.
3. **Communicate with your packaging suppliers** to understand whether they have undertaken any preparations for the implementation of the regime, including understanding whether monitoring systems are used and whether required information for EPR reporting is available.

4. **Assess the data requirements** needed to submit quarterly EPR reports, mapping them against existing data availability to identify gaps. Where data gaps exist, implement mechanisms to close them. This will likely involve a wide range of stakeholders to examine the internal systems, processes and controls to capture the necessary data.

The EPR extension relieves the time pressure on companies to close data gaps identified in their packaging data. However, for a significant number of businesses, there are still large amounts of packaging data and backend processes not yet in place that are required to meet the requirements of the regime. The more businesses submit their data on time, the sooner businesses will have visibility of the fees associated with EPR, allowing for earlier assessment and forecasting of the financial impact. ■



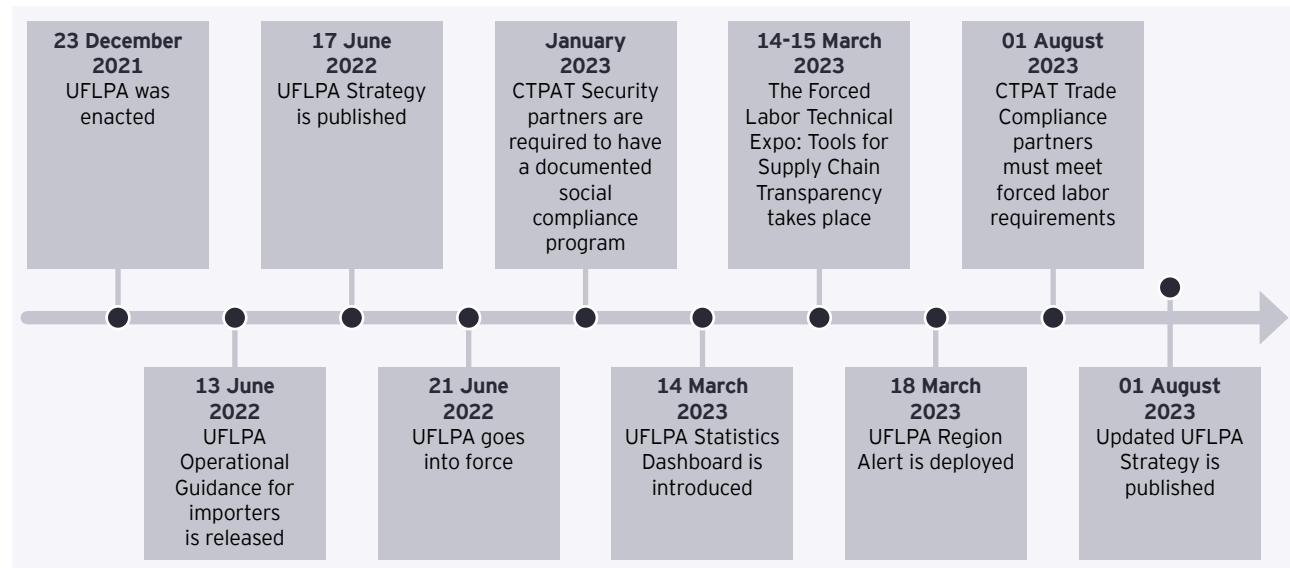
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US: Uyghur Forced Labor Prevention Act in action: updated guidance and trends



The Uyghur Forced Labor Prevention Act (UFLPA) took effect on 21 June 2022. The UFLPA establishes a rebuttable presumption that goods made in whole or in part in China's Xinjiang Uyghur Autonomous Region (XUAR) or goods produced by certain named entities (i.e., on the UFLPA Entity List) are made with labor practices set out in the Act and are prohibited from importation into the US. To rebut this presumption when goods are detained, importers must demonstrate by "clear and convincing" evidence to US Customs and Border Protection (CBP) that the detained goods are not the product of such labor practices.¹ This article focuses on updated guidance in the year since UFLPA implementation and trends since enforcement began.

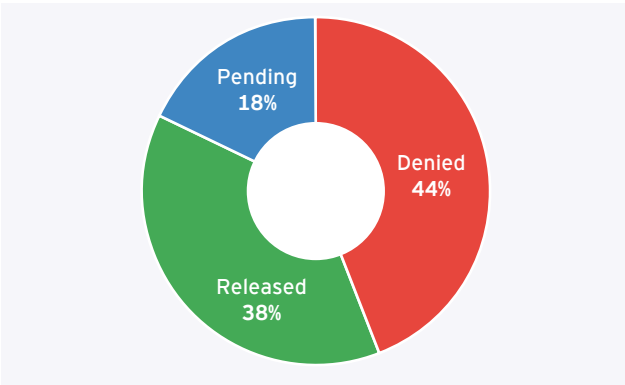


¹ "US: Uyghur Forced Labor Prevention Act goes into force," *TradeWatch*, Issue 3, 2022, page 31. [Find it here.](#)

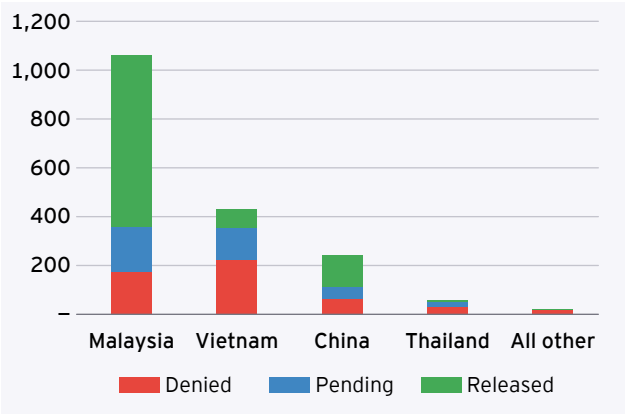
Enforcement to date

At the time of preparing this article, CBP has detained 5,346 shipments worth over USD1.8 billion dollars.² The majority of shipments detained, 2,325 shipments valued at USD510 million, were denied entry into the US, while 2,033 shipments valued at USD985 million were released, and the remaining are pending resolution. The industry most impacted by detentions and denied shipments is the electronics industry, followed by industrial and manufacturing materials, then apparel, footwear and textiles. Most detained shipments were not of Chinese origin – the highest-value detained shipments were Malaysian-origin goods. Vietnamese-origin goods were the highest-value shipments denied entry.³

Results of detailed shipments from June 2022 to September 2023



Shipment value (USD million) by country of origin



UFLPA Region Alert

In March 2023, CBP introduced the UFLPA Region Alert enhancement to the Automated Commercial Environment (ACE).⁴ The UFLPA Region Alert provides notifications to importers (and representatives) when goods are at risk of being detained due to connection to XUAR. The update also changed the postal code field to be mandatory. Users now receive error messages if the postal code provided is not a valid postal code in China and a warning message when a XUAR postal code is provided.

Additional requirements imposed on US trading partners

After the implementation of UFLPA, CBP made revisions to the voluntary Customs Trade Partnership Against Terrorism (CTPAT) Security⁵ and CTPAT Trade Compliance programs. These revisions introduced new requirements pertaining to the

restrictions and prohibition of importing goods believed to be manufactured, in whole or in part, using forced labor.⁶ The CTPAT requirements apply to CTPAT participants only, but the conditions have generated challenges for importers seeking to comply with the various requirements.

CTPAT Security

As of January 2023, CTPAT Security participants are required to have a documented social compliance program that addresses how the company verifies that forced or child labor is not found in its supply chain. CBP previously encouraged a documented social compliance program, but this requirement is now mandatory. This change can be found in section 3.9 of the Minimum Security Criteria.⁷

CTPAT Trade Compliance

The CTPAT Trade Compliance program replaced the Importer Self-Assessment (ISA) Program as an enhanced component of the CTPAT Security

2 See "UFLPA Statistics Dashboard," US Customs and Border Protection, Forced Labor Division. [Find it here](#). Statistical information is subject to change due to corrections or additional information. Data is current as of 12 September 2023.

3 Ibid.

4 "Trade User Information Notice: Uyghur Forced Labor Prevention Act Region Alert," US Customs and Border Protection, last updated 26 January 2023. [Find it here](#).

5 Customs Trade Partnership Against Terrorism (CTPAT) is a US policy that is one layer in U.S. Customs and Border Protection's (CBP) multi-layered cargo enforcement strategy, *US CBP website*. [Find it here](#).

6 It is the policy of the United States – (1) to strengthen the prohibition against the importation of goods made with forced labor, including the effective enforcement of section 307 of the Tariff Act of 1930 (19 U.S.C. 1307), which prohibits the importation of all "goods, wares, articles, and merchandise mined, produced or manufactured wholly or in part in any foreign country by * * * forced labor." *US Congress website*. [Find it here](#).

7 CTPAT Minimum Security Criteria are based on the corresponding industry and role of participant. "CTPAT Minimum Security Criteria," US Customs and Border Protection, [Find it here](#).

program. The new obligations on the issue of targeting the use of forced labor in supply chains are outlined in the CTPAT Trade Compliance Handbook.⁸ Participants were required to meet the specified requirements by 1 August 2023, including:

- ▶ Conduct risk-based analysis that outlines the supply chain in its entirety.
- ▶ Develop, upload to the CTPAT online portal and publish publicly a code of conduct statement indicating the company's position against this issue in any part of its supply chains.
- ▶ Provide evidence of the implementation of a social compliance program.
- ▶ Provide training to suppliers, as well as proof of the training upon request, on the social compliance program requirements that identify the specific risks and help identify and prevent this issue.
- ▶ Establish remediation plans in the event that the issue is identified in the supply chains.
- ▶ Share best practices with the CTPAT Trade Compliance program to help mitigate the issue's risk.

Strategy annual update

The US Department of Homeland Security (DHS), as Chair of the Forced Labor Enforcement Task Force (FLETF), published the Strategy to Prevent the Importation of Goods Mined, Produced, or Manufactured with Forced Labor in the People's Republic of China (UFLPA Strategy) on 21 June 2022 with specific guidance to importers. The FLETF is required to publish annual updates to the UFLPA Strategy, which it did for 2023 on 1 August. The updates to the UFLPA Strategy⁹ include:

- ▶ Updates to the UFLPA Entity List and related plans
- ▶ Updates on the additional resources necessary to ensure no goods made with forced labor enter at US ports
- ▶ Updates on coordination and collaboration with appropriate nongovernmental organizations (NGO) and private-sector entities

While the updated UFLPA Strategy remained largely the same, with no formal changes to the list of high-risk sectors, the addition of certain entities to the UFLPA Entity List certainly expands the overall scope of UFLPA (discussed later in this article). Moreover, the updated UFLPA Strategy states the importance of continuously monitoring potential high-risk areas identified by NGOs, including red dates and other agricultural products, vinyl

products and downstream products, aluminum and downstream products, steel and downstream products, lead-acid and lithium-ion batteries, copper and downstream products, electronics, and tires and other automobile components.¹⁰

UFLPA Entity List

The UFLPA Entity List included 20 entities when it was first made available in June 2022.¹¹ In June 2023, two additional entities were added in the list,¹² followed by the addition of two more entities in August 2023.¹³ On 27 September 2023, three textile entities were added to the UFLPA Entity List.¹⁴

Initially, the UFLPA Strategy described the following as high-risk sectors: (1) apparel, (2) cotton and cotton products, (3) silica-based products (including polysilicon) and (4) tomatoes and downstream products.¹⁵

Notably, the two additions in August 2023 are not companies in industries targeted on the initial list and subsequent revisions. One of the added entities is a producer of lead-acid batteries, and the other entity is involved in the production of plant-based products.

The addition of these entities illustrates the widening scope of the UFLPA Entity List and demonstrates an expansion of enforcement efforts.

8 "Customs Trade Partnership Against Terrorism Trade Compliance Handbook," Version 4, September 2023. [Find it here.](#)

9 "2023 Updates to the Strategy to Prevent the Importation of Goods Mined, Produced, or Manufactured with Forced Labor in the People's Republic of China," US Department of Homeland Security website, 26 July 2023. [Find it here.](#)

10 Ibid.

11 "Notice on the Addition of Entities to the Uyghur Forced Labor Prevention Act Entity List," 4 August 2022. [Find it here.](#)

12 "Notice Regarding the Uyghur Forced Labor Prevention Act Entity List," 12 June 2023. [Find it here.](#)

13 "Notice Regarding the Uyghur Forced Labor Prevention Act Entity List," 2 August 2023. [Find it here.](#)

14 "Notice Regarding the Uyghur Forced Labor Prevention Act Entity List," 27 September 2023. [Find it here.](#)

15 "Strategy to Prevent the Importation of Goods Mined, Produced, or Manufactured with Forced Labor in the People's Republic of China," US Department of Homeland Security website, 17 June 2022. [Find it here.](#)

Technology

CBP is actively engaging with industry groups to identify technology innovations to support supply chain mapping and product testing relating to UFLPA. CBP has reportedly allocated resources to assess technology capabilities for UFLPA compliance and anticipates concluding this analysis in the near future.

On 14-15 March 2023, CBP held the Forced Labor Technical Expo: Tools for Supply Chain Transparency. The event was open to the importing community, public and private companies, and other federal agencies to demonstrate and present their technological capabilities. While CBP has not publicly supported technology capabilities or companies providing specific technology capabilities, it has signed contracts with companies that provide services related to directives under UFLPA.

Influence outside the US

Several countries have proposed or passed legislation targeting modern slavery and forced labor in the supply chain. Notable examples include:

- ▶ Australian Commonwealth Modern Slavery Act
- ▶ California Transparency in Supply Chains Act
- ▶ Canada Modern Slavery Act (Bill S-211, An Act to enact the Fighting Against Forced Labour and Child Labour in Supply Chains Act and to amend the Customs Tariff)

- ▶ EU Corporate Sustainability Due Diligence Directive
- ▶ EU proposal for a ban on goods made using forced labor
- ▶ EU Regulation on deforestation-free products¹⁶
- ▶ French Corporate Duty of Vigilance Act
- ▶ Germany Supply Chain Due Diligence Act
- ▶ Mexico Forced Labor Regulation (implementing obligations set forth in the United States-Mexico-Canada Agreement)
- ▶ Norwegian Transparency Act
- ▶ UK Modern Slavery Act 2015

Obligations and compliance vary among jurisdictions, but most rely on standards set by international organizations, such as the International Labour Organization and the United Nations Global Compact.

Concluding remarks

After a year since enforcement began, US importers and stakeholders have been able to adapt to the changes brought by UFLPA and its many challenges and complexities. US importers and stakeholders are now able to focus on refining supply chain due diligence in this regard and promote responsible sourcing initiatives, including:

- ▶ Proactive engagement with stakeholders to foster transparency and compliance
- ▶ Thorough mapping and due diligence of their own supply chain
- ▶ Robust monitoring mechanisms to identify and address risks
- ▶ Further improving on current processes implemented as a result of UFLPA enforcement
- ▶ Seeking technology solutions to support compliance
- ▶ Supporting compliance with other legislation targeting this issue in supply chains
- ▶ Monitoring changes and updates to current regulations on this topic ■

¹⁶ This regulation also forces EU importers to ensure that labor rights and human rights protected under international law have been complied with in the relevant country of production.

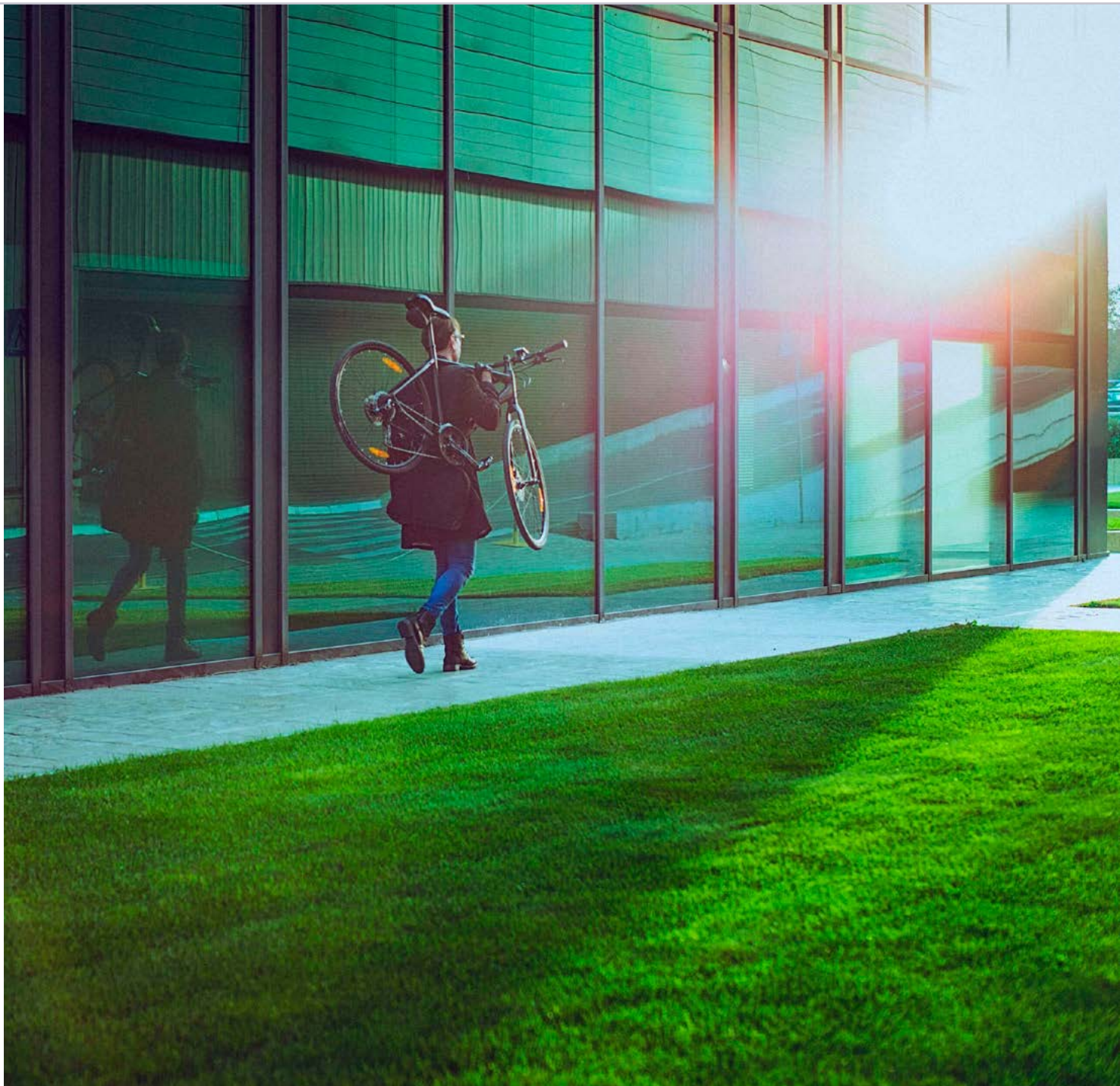
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Tax alerts

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Americas

Argentina

- ▶ Argentina applies tax on purchases of foreign currency in new transactions, provides preferential foreign-exchange rate to certain exported goods (26 July 2023)

Aruba

- ▶ Aruba Fiscal Plan 2023 – Part II Tax changes (02 August 2023)

Brazil

- ▶ Brazil's Complimentary Law number 199 simplifies tax obligations (16 August 2023)
- ▶ Brazil Senate considers VAT reform plan (10 August 2023)

Canada

- ▶ Canada publishes trade compliance verification list update, July 2023 (03 August 2023)

Costa Rica

- ▶ Costa Rica's Tax Authority issues resolution on services related to exports exempt from VAT (08 August 2023)

Dominican Republic

- ▶ Dominican Republic establishes special transitional treatment for audit, management and recovery of tax debt (18 August 2023)

El Salvador

- ▶ Salvadoran Congress approves brief tax amnesty program (10 November 2023)
- ▶ El Salvador's Congress approves bills to reform International Services Law and Free Trade Zones Law (22 August 2023)
- ▶ El Salvador's Congress receives bills to amend International Services Law and the Law for Industrial and Commercial Free Zones (04 August 2023)

Global

- ▶ OECD releases tax report to G20 Finance Ministers and seventh annual progress report of the Inclusive Framework (07 November 2023)
- ▶ EY Global Tax Controversy Flash Newsletter (Issue 63) – Free trade agreements provide opportunities for global businesses – but may increase controversy risk (10 October 2023)
- ▶ Global Tax Policy and Controversy Watch (20 July 2023)

Mexico

- ▶ Mexico offers tax incentives to taxpayers in key sectors of the export industry (13 October 2023)

Uruguay

- ▶ Uruguay's Government enacts law for accountability for 2022, making some changes to tax regulations (15 November 2023)

Asia-Pacific

Australia

- ▶ Australia considers CBAM to address carbon leakage
(21 August 2023)

Global

- ▶ OECD releases tax report to G20 Finance Ministers and seventh annual progress report of the Inclusive Framework
(07 November 2023)
- ▶ EY Global Tax Controversy Flash Newsletter (Issue 63)
– Free trade agreements provide opportunities for global businesses – but may increase controversy risk
(10 October 2023)
- ▶ Global Tax Policy and Controversy Watch
(20 July 2023)



Europe, Middle East, India and Africa

Bulgaria

- New energy contribution for transfers of natural gas of Russian origin
(31 October 2023)

East African Community

- East African Community implements tariff changes for the Financial Year 2023/24
(26 July 2023)

European Union

- EU Council adopts new renewable energy rules and rules for promotion of sustainable aviation fuels under Fit for 55
(01 November 2023)
- EU – Compliance obligations for EU CBAM
(16 October 2023)
- European Commission adopts final Implementing Regulation for transitional phase of CBAM
(18 August 2023)
- EU Commission and Council take steps as part of the circular economy action plan – new rules on textiles and batteries
(21 July 2023)

France

- France submits new e-invoicing timetable to Parliament
(25 October 2023)
- France postpones electronic invoicing initially scheduled for 1 July 2024
(02 August 2023)

Germany

- Germany to lower reporting thresholds for energy and electricity tax subsidies
(27 October 2023)

Ghana

- Ghana issues Budget Statement and Economic Policy for the 2024 Financial Year
(27 November 2023)

Global

- OECD releases tax report to G20 Finance Ministers and seventh annual progress report of the Inclusive Framework
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- EY Global Tax Controversy Flash Newsletter (Issue 63) – Free trade agreements provide opportunities for global businesses – but may increase controversy risk
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- Global Tax Policy and Controversy Watch
(20 July 2023)

Italy

- Italy's new Enabling Law for Tax Reform foreshadows positive changes to cooperative compliance program
(28 September 2023)
- Italy approves framework for major tax reform, including BEPS Pillar Two principles
(25 August 2023)

Ireland

- Budget 2024 – The EY Perspective
(06 October 2023)

Kenya

- Kenya Revenue Authority unveils guidelines for customs clearance at port of entry for passengers
(22 November 2023)
- Kenya High Court ruling provides clarity on what constitutes manufactured tobacco
(10 November 2023)
- Kenya enacts tax changes under Finance Act, 2023
(20 July 2023)

Poland

- Polish Government seeks annulment of CBAM regulation in European Court of Justice
(15 August 2023)

Saudi Arabia

- Saudi Arabia announces ninth wave of Phase 2 e-invoicing integration
(21 November 2023)
- Saudi Arabia approves new operating procedures of the General Secretariat of Zakat, Tax and Customs Committees
(20 November 2023)
- Saudi Arabia further extends tax amnesty initiative until 31 December 2023
(31 July 2023)

South Africa

- South Africa's 2023 draft Tax proposals
(02 August 2023)

Turkey

- Türkiye removes right to deduct import VAT calculated due to certain trade policy measures
(01 December 2023)
- Türkiye increases additional customs duty rates on textile industry
(26 October 2023)

United Kingdom

- UK announces tax measures for growth in Autumn Statement 2023
(22 November 2023)

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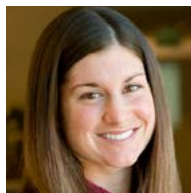
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