Review of Precedents in Appealing against Decisions of Customs Authorities

Disputes between importers and customs authorities are complex cases. The implementation of electronic declaring and a risk management control system, as well as a change in the approach of customs control led to an increase in customs audits of participants of foreign economic activity, and, consequently, to an increase in the number of customs disputes.

Additional charges during the customs audits come down mainly to the following two factors: adjustment of the customs value of goods and change in the classification code of the goods. In this article, we will analyse the above grounds for additional charges and the current precedents of appealing against decisions of the customs authority.

Customs Value

The accuracy of the declared customs value is verified by the customs authority both at the stage of customs clearance and after the goods are released. Therefore, even at the stage of customs clearance, the declaration of goods passes through a risk management control system to assess the probability of the goods value underestimation. If the customs authority "detects" such an underevaluation, then it requires the importer to provide an indefinite list of documents, including:

- commercial details of the delivered goods, including accounting documents;
- information on the physical characteristics, quality, goods market recognition and their impact on pricing;
- data on sales of similar goods to other counterparties to confirm fair prices;
- price list;
- export declaration of the country of departure, often in the original.

To save costs of storing goods in a warehouse and not to violate obligations to counterparties, as well as not to waste time collecting a large number of documents during a short time-frame, importers are forced to agree for adjustment of the customs value (increasing). The customs authorities then use the fact of such “forced consent” of the importer to the increased customs value of the goods as an “affirmative” argument for the “legality” of the customs authority actions. Sure, this creates negative precedents for importers.

However, even the submission of a full package of documents does not guarantee the importer that the customs authority will consider the provided information and admit the value of goods as proven according to the first method of the customs value determination (based on the value of the transaction with imported goods). Practice shows that in most cases, the customs authority adjusts the customs value of imported goods based on its own information on prices.

A similar situation exists in case of a desk audit[1] of the importer after the customs clearance of the goods. If the importer fails to provide all or a part of the documents and information requested by the customs authority in a timely manner, the customs authorities independently adjusts the customs value of the goods based on their own available information. The customs authority receives such information from the integrated data warehouse ('IDW'), which, together with the customs value index ('CVI'), are used to change the value of goods and the subsequent calculation of the amount of customs payments. In fact, the IDW is a collection of data on all goods that have passed the customs clearance and are used to determine the customs value

[1] Desk Customs Audit is an audit of documents and information contained in the customs declarations. Such an audit is conducted without visiting the audited person (Article 417 of the Code on Customs Regulation in the Republic of Kazakhstan dated 26 December 2017).

using the second method (based on the transaction price with identical goods) and the third method (based on the transaction price with homogeneous goods).

In practice, we often face an arbitrary abuse of powers by the customs authorities, since representatives of the customs authority clearly cannot be in the position of not knowing the customs legislation and misapply it. For instance, as follows from the analysis of many audit acts, the customs authority, when assessing the applicability of methods for determining the customs value of goods, ignores the first five methods and adjusts the customs value according to the last (reserve) sixth method. According to the Customs Code, the sixth method shall be only applied when the consistent application of the previous five methods is impossible. In this case, the customs authority justify the legitimacy of their actions by arguing that it is impossible to define the cost of goods according to the previous five methods due to the lack or absence of the required data and information. However, it does not actually provide in audit acts for any justification for the impossibility of applying the previous five methods. Therefore, such a “response” allows the customs authority to use the reserve method, which is actually the”spare” method, which is reflected in its name, and therefore, it should be used only in exceptional cases.

Despite this so-called 'incompetence' of local customs authorities, when appealing additional charges related to an increase in a customs value to a higher state authority, the latter still often makes decisions on complaints in favour of an importer. We attribute such a positive change both to an increase in the level of customs knowledge among importers, the work of customs consultants, and to the introduction in 2017 of the institution of the Appeals Commission under the Ministry of Finance of the Republic of Kazakhstan. Based on the performance of the Appeals Commission for 2018, the results of about 38% of audits conducted by the state authority were completely or partially cancelled.

Nevertheless, we are of the opinion that the percentage of cancelled audits could be much higher according to our practice, many notices are revoked independently by the territorial customs authority before the actual consideration of the complaint by the Appeals Commission.

As one of our cases, we were representing a large manufacturer of metal structures in appealing the notice of the desk audit results to the Ministry of Finance. The territorial customs authority revealed a discrepancy between the data on the customs value of goods and the index of customs value of the customs authority. The customs authority considered the documents provided by the Company to substantiate the customs value of goods to be insufficient, then changed the method of determining the value from the first (according to the transaction price of imported goods) to the sixth (reserve) method and made an additional charge of customs duties, taxes and penalties in a large amount. As a result of a complaint filed to the Ministry of Finance and providing sufficient reasoning to justify the Company's position, the notice of the audit results was independently withdrawn by the territorial customs authority.

Another case of charging customs payments and taxes refers to a change in the rate of customs duty within one group of goods. When conducting a desk customs audit, the Company was requested to provide documents - drawings that were the subject of import. At the time of the audit, the drawings were already handed over to the counterparty as part of the contract execution and, therefore, could not be provided to the customs authority. The auditors, in turn, came to the conclusion that the information specified in the goods declaration was not confirmed, and relying on the Customs Code applied the highest rate of customs duties within one commodity group. When appealing against additional charges, we proved the illegality of claiming drawings, which in essence were the goods imported, the illegality of changing the classification code of the goods, the inapplicability of the method for determining customs value and charges due to the failure to provide the drawings. In this case, following the appeal results, the territorial customs authority independently cancelled the previously issued notice.

Thus, the accrual of the customs payments based on the results of the customs audit does not mean at all that such accruals are legal and justified. As a rule, a thorough analysis of documents and legal framework, correct legal argumentation always makes it possible to appeal against accruals by customs authorities.

Goods Classification

Additional charges associated with a change in the commodity code of the nomenclature of foreign economic activity (HS code) are no less significant. In such cases, the customs authorities of Kazakhstan are guided by the decisions and explanations of the Eurasian Economic Commission regarding the classification of certain types of goods, as well as Russia practice.

Over the past five years, there has been a series of additional charges related to changing the HS code; the most notable of them are: classification of parts of shoes, baby diapers, precision seed drills, Vitrum mixtures of vitamins and minerals. Changes in the codes for such goods affected the activities of a large number of importers throughout the country.

However, judicial practice in such cases is different. As a rule, courts rarely rule in favour of importers. Single court decisions made in favour of an importer are not a guarantee that subsequent precedent on the identical dispute will not be contradictory.

In this case, litigation on the classification of baby diapers is indicative. The essence of the dispute is that the main function of diapers is the ability to absorb and retain moisture. For these purposes, manufacturers use an absorbent layer consisting of cellulose and sorbent as part of the product. Therefore, the proper classification of the product requires to understand which substance in the product plays the main role - cellulose or sorbent. Thereat, analysing judicial practice, we can see that the court decisions are often polar opposite. In one case, the courts support an importer and believe that the main property (moisture absorption) is provided by cellulose paper pulp due to its porous structure. In another case, the court considers that the main property is provided by a sorbent - granular filler, and supports the decision of the customs authorities to change the goods classification code.

The same contradiction arises in court decisions on the classification of seed drills - either by the code for “precision seed drills” or by the code as “other seed drills”. In one case, the courts do not accept the opinion of the customs expertise of the documents for the goods because the expertise is carried out without examining the goods themselves, and, guided by GOST, they take the position of the importer when challenging the classification decision. Other court decisions are made in favour of the customs authorities precisely on the basis of the conclusion of the customs expertise of only documents.

We would like to separately note that despite the fact that customs legislation states the principle of uniform application of the product nomenclature of foreign economic activity, we can see a different approach to the classification of goods by territorial customs authorities. Importers, when importing goods, often check the HS codes with the database of preliminary classification decisions. However, the presence in the decision database of an already issued code for a particular product does not give any guarantee that the same HS code will be accepted for similar goods imported by another importer. Importers of Vitrum faced this problem. When arguing for the legitimacy of the goods classification, the importers referred to the current practice on classification from a single database of decisions of the customs authority. The courts, however, did not take such arguments into account, given that importers did not receive preliminary classification decisions and, therefore, could not appeal to decisions received by other importers, despite they import identical goods.

Summarising the practice of appealing against decisions of customs authorities, we notice that the situation in general starts changing. The chance of importers of appealing against decisions of a customs authority to a higher state authority has been significantly increased. With regard to judicial practice, it is too early to talk about the quantitative and qualitative results of this category of cases, since it is not always clear from the decisions wording as to what the courts are guided by when making a decision not in favour of an importer. We hope that with the further development of courts, the number of positive decisions in such cases will increase.

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