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The transition from CCC to UCC with regard to royalties and license fees, and necessary consequences for the VAT-Directive

by

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List of abbreviations

AG	Advocate General
CCC	Community Customs Code
CCCIP	Implementing Provisions of the Community Customs Code
CJEU	Court of Justice of the European Union
EC	European Community
EU	European Union
GATT	General Agreement on Tariffs and Trade
GATT 47	GATT dated on 30 October 1947
GATT 94	GATT dated on 14 April 1994
MCC	Modernised Customs Code
MCCIP	Implementing Provisions of the Modernised Customs Code
MS	Member State of the European Union
No	Number
OECD	Organisation for Economic Co-operation and Development
OJ	Official Journal
VAT-D	Value Added Tax Directive
Para	Paragraph
Paras	Paragraphs
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
UCC	Union Customs Code
UCCIA	Implementing Act of the Union Customs Code
WCO	World Customs Organization
WTO	World Trade Organization

Abstract

The importation of goods into the territory of the European Union is liable to customs duties. In order to calculate this duty, the customs value constitutes the fundamental basis. The customs value is the transaction value, which has to be adjusted, inter alia, by royalties and license fees. As the Union Customs Code will replace the Community Customs Code with effect from 1 May 2016, the present thesis focuses on the new treatment of royalty payments for customs purposes and its legal consequences.

In a first step, a comparison between the Community Customs Code and the Union Customs Code reveals that importers will have to face a significant increase in the customs liability of royalty payments.

Secondly, with the European Union being a member of the World Trade Organization, it is investigated whether the topic-related provisions of the Union Customs Code comply with the provisions of the General Agreement on Tariffs and Trade. A survey of the advisory opinions and commentaries of the World Customs Organization indicates that the European customs law will follow the interpretation of the World Customs Organization to a great extent.

Due to the fact that the taxable amount for import value added tax purposes corresponds with the customs value, the validity of this rule under the Union Customs Code is explored: an examination of the case law on the direct linkage between a supply and its consideration proves this rule as being justified.

On the basis of these findings, then, the thesis discloses the considerable problem of double taxation of royalties and license fees in the case of taxable persons being exempt from the value added tax, as the royalty payment for the imported goods establishes a second taxable transaction, namely the supply of a service. Therefore, it is submitted to exclude the supply of services rendered in relation to the importation of goods from the taxable amount for import value added tax purposes.

1 Introduction

1.1 Background

One of the most fundamental achievements of the European Union (EU) is the establishment of the internal market based on Article 3 (3) of the Treaty on European Union (TEU). An essential part in the creation of the internal market constitutes the free movement of goods due to Article 26 (2) of the Treaty on the Functioning of the European Union (TFEU), which is, inter alia, ensured through the implementation of the customs union according to Article 28 (1) of the TFEU. With regard to that, it is the Community Customs Code[1] (CCC) that "[…] *made the* [internal] *market a reality in relation to customs*"[2]. Indeed, there would be no EU without an economically successful union.[3]

Apart from that, the CCC is not merely a result of the EU legislation but is also influenced by international agreements, which are forming an integral part of European law.[4] Such an international agreement constitutes the Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade, which concerns the valuation of goods. It is this convention that has an effect on both the customs value due to Article 29 (1) of the CCC and the taxable amount with regard to the import value added tax (VAT) due to Article 85 of the current VAT-Directive[5] (VAT-D).

The transaction value based on Article 29 (1) of the CCC is decisive for the assessment of the customs value and has to be adjusted by expenses set out in Article 32 of the CCC. Article 32 (1) (c) of the CCC applies to royalties and license fees and has experienced a specific consideration because "[…] *there is no part of the Code where so much is left to interpretation and implementation, and so little can be derived from a literal reading of the words used*"[6].

The same degree of attention must be given to today's highly competitive environment which changed the demands on the customs legislation.[7] The result of that is the implementation of the Union Customs Code[8] (UCC),

[1] Council Regulation (EEC) No 2913/92 of 12 October 1992 establishing the Community Customs Code, OJ L 302, 19 October 1992, p.1.

[2] Opinion of the Economic and Social Committee on the ´Proposal for a European Parliament and Council Regulation (EC) amending Council Regulation (EEC) 2913/92 establishing the Community Customs Code, OJ 96/C 174/04, 17 June 1996, para 1.1.

[3] T. Lyons, *EC Customs Law*, Oxford, Oxford University Press, 2nd Edition, 2008, p. 1.

[4] Joined Cases C-447/05 and C-448/05 *Thomson Multimedia* ECLI:EU:C:2006:158, para 30.

[5] Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, OJ L 347/1, 11 December 2006.

[6] S. Sherman and H. Glashoff, *Customs Valuation - Commentary on the GATT Customs Valuation Code*, Paris, ICC Publishing, 1988, p. 123.

[7] Council Resolution of 25 October 1996 on the simplification and rationalization of the Community's customs regulations and procedures, OJ 96/C 332/01, 7 November 1996.

[8] Regulation (EU) No 952/2013 of the European Parliament and of the Council of 9 October 2013 laying down the Union Customs Code (recast), OJ L 269/1, 10 October 2013.

which has replaced the Modernised Customs Code[9] (MCC) and is to be applied from 1 May 2016.[10] Consequently, the UCC deserves a particular regard as "[t]*he present Community Customs Code* […] *is out of date*"[11].

1.2 Purpose

The application of the UCC from the 1 May 2016 includes a lot of changes that are important to consider, indeed. The question asked in this thesis is how royalties and license fees are treated under the UCC. Moreover, is this treatment in line with the provisions of the General Agreement on Tariffs and Trade (GATT) and does it require a modification of the current VAT-D with regard to import VAT?

1.3 Method and material

In order to realise the investigation mentioned in Chapter 1.2 different techniques have been applied, namely the legal dogmatic method and the literature review. Furthermore, both descriptive and analytical writing methods have been conducted within the progress of this paper. Concerning the materials, the acquisition of the information during the writing period was challenging as, for example, it has been difficult to find literature that does not merely explain the customs code in general but provides for more detailed information with regard to the treatment of royalties and license fees. As a consequence, in some places, the scope of references is very limited in the thesis.

As there is only a small amount of literature available in this particular field, the present thesis delivers new insights into the customs treatment of royalty payments.

1.4 Delimitation

Besides the transaction value due to Article 29 of the CCC, there are different provisions in connection with the calculation of the customs value, i.e. the so called 'secondary methods' based on Article 30 of the CCC (Article 74 of the UCC). With regard to that, the thesis focuses on the conditions of the

[9] Regulation (EC) No 450/2008 of the European Parliament and of the Council of 23 April 2008 laying down the Community Customs Code (Modernised Customs Code), OJ L 145/1, 4 June 2008.

[10] European Commission, ´The Union Customs Code: a recast of the Modernised Customs Code`, http://ec.europa.eu/taxation_customs/customs/customs_code/union_customs_code/index_en.htm, 2015, (accessed 11 May 2015).

[11] Proposal for a Regulation of the European Parliament and of the Council laying down the Community Customs Code (Modernized Customs Code), COM(2005) 608 final, 30 November 2005, p. 2.

transaction value according to Article 29 (1) and (3) (a) of the CCC (Article 70 (1) and (2) of the UCC).

Concerning the required adjustments laid down in Article 32 of the CCC, the provision of interest is Article 32 (1) (c) of the CCC (Article 71 (1) (c) of the UCC), namely royalties and license fees.

Last but not least, the scope investigated in the field of VAT is restricted to Article 85 and 86 as well as to 143-145 of the VAT-D.

1.5 Outline

The subsequent chapter gives an overview of the relevant provisions of the CCC and focuses, in particular, on Article 29 (1) and (3) (a) of the CCC with regard to the definition of the concept 'transaction value'. As Chapter 2 also introduces the adjustments to be made to the transaction value, Chapter 3 goes into more detail with regard to the treatment of royalties and license fees for customs purposes and presents a summary of the status quo in 3.5. The upcoming change based on the UCC of the knowledge gained in Chapter 3 is shown in Chapter 4. Chapter 5 introduces the relevant provisions of the GATT and investigates whether the topic related articles of the UCC are in line with the intention of the GATT. Furthermore, Chapter 6 examines whether the customs value is in contradiction with the nature of the VAT and, therefore, the provisions of the VAT-D concerning import VAT have to be changed. A final conclusion is drawn in Chapter 7.

2 The relevant provisions of the CCC

Title II Chapter 3 of the CCC concerns the customs valuation. Following the order of the articles, it is the concept of the 'transaction value' that has to be considered first.

2.1 The transaction value

Article 29 (1) of the CCC defines the customs value as the following:

> The *customs value* of imported goods shall be the *transaction value*, that is, the *price actually paid or payable* for the goods when *sold for export* to the customs territory of the Community adjusted, where necessary in accordance with Articles 32 and 33.

Consequently, the terms 'price actually paid or payable' (the price) and 'sold for export' have to be further examined.

2.1.1 The price actually paid or payable

An explanation of the price can be found in Article 29 (3) (a) of the CCC, which states that the price has to be understood as the totality of payments in relation to the imported goods made by the buyer to the seller or for his benefit. It should be noted that the interpretative note of Annex 23 to the Implementing Provisions of the CCC (CCCIP)[12] concerning Article 29 (1) of the CCC specifies that the price refers to the imported goods and that, therefore, the flow of dividends or other payments remitted by the buyer to the seller do not relate to the imported goods.

In addition to the totality of payments, the price also includes all payments made or to be made as a condition of sale[13] of the imported goods by the buyer to the seller or to a third party to satisfy an obligation of the seller.[14] At this point, it has to be mentioned that if the price has not been paid at the time of valuation, the price negotiated between the buyer and the seller shall be taken as the basis for the customs value according to Article 144 (1) of the CCCIP.

With regard to the payment, Article 29 (3) (a) of the CCC does not necessarily demand the payment to take the form of a transfer of money and, moreover, offers another possibility of payment, namely the letter of credit or negotiable instrument. In addition, this article enables the payments to take both forms – direct and indirect. An example for an indirect payment can be found in the agreement of a debt, whether in whole or in part, between the buyer and the seller based on Annex 23 to the CCCIP concerning Article 29 (3) (a) of the CCC.

Activities, such as marketing activities, undertaken by the buyer on his own account do not establish an indirect payment, even though they constitute a benefit for the seller or have been the result of an agreement between the buyer and the seller.[15]

In order to reduce the price actually paid or payable to its essential nature, it can be defined as the price negotiated between the buyer and the seller[16] or "[i]*n other words, the buyer and seller themselves determine the customs value of imported goods*"[17]. This approach has been confirmed by the Court of Justice of the European Union (CJEU) as it can be derived from its statement in the Case C-65/85 *Hauptzollamt-Ericus*:

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[12] Commission Regulation (EEC) No 2454/93 of 2 July 1993 laying down provisions for the implementation of Council Regulation (EEC) No 2913/92 establishing the Community Customs Code, OJ L 253, 11 October 1993, p. 1.

[13] The term ´condition of sale` in connection to the price will not be further examined in this thesis.

[14] Article 29 (3) (a) CCC.

[15] Article 29 (3) (b) CCC.

[16] Please be aware of the conditions laid down in Articles 29 (1) (a) to (d) CCC and Article 29 (2) CCC.

[17] B. J. O'Shea and S. Rosenow, *A Handbook on the WTO Customs Valuation Agreement*, Cambridge, World Trade Organization, 2010, p. 27, Available from: E-Book Library, (accessed 13 May 2015).

> "*The customs value must* […] *be calculated on the basis of conditions on which the individual sale was made, even if they do not accord with trade practice or may appear unusual for the type of contract in question*".[18]

With regard to the determination of the transaction value it is not only important to be aware of the price actually paid or payable but also to know which sale is relevant for the calculation. That is why the concept ´sale for export` is further investigated in chapter 2.1.2.

2.1.2 Sale for export

Due to Article 29 (1) of the CCC the transaction value is the price actually paid or payable for the goods *when sold for export to the customs territory of the Community*.

Based on the first sentence of Article 147 (1) of the CCCIP an adequate indication for goods to be sold for export to the customs territory of the Community[19] constitutes the fact that the goods, which are subject of a sale, are declared for free circulation[20]. Consequently, the introduction of goods into the customs territory can be regarded as sufficient proof that the goods were sold for export to the European Community (EC).[21] It has to be mentioned that this approach is applicable to situations where goods are sold only once (one sale).[22]

In principle, the approach of the 'one sale' can also be adapted for circumstances where goods are sold more than once before their actual importation takes place.[23] The second sentence of Article 147 (1) of the CCCIP states that in such situations only the last sale, which led to the introduction of the goods into the customs territory of the Community, before the entry for free circulation of the goods shall constitute the relevant sale. In order to increase clarification, the sale at interest in a successive sale situation is the last sale that occurs in the commercial chain before the introduction of the goods into the customs territory of the Community.[24]

A derogation from the 'last sale' can be found in the third sentence of Article 147 (1) of the CCCIP, which provides for the possibility to refer to an

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[18] Case C-65/85 *Hauptzollamt Hamburg-Ericus v Van Houten* ECLI:EU:C:1986:53, para 13.

[19] Please note that it is referred to the EU as the Community during the examination of the CCC's provisions.

[20] The release for free circulation shall confer non-Community goods the customs status of Community goods due to Article 79 (1) CCC.

[21] Commentary No 7 of the Customs Code Committee (Customs Valuation Section) on the application of Article 147 of Commission Regulation (EEC) No 2454/93 of 2 July 1993, para 3.1, in Compendium of Customs Valuation texts of the Customs Code Committee, TAXUD/800/2002-EN, September 2008 (hereinafter as Commentary No 7 of the Customs Code Committee).

[22] Ibid, para 3.1.

[23] Ibid, para 3.2.1.

[24] Ibid, para 3.2.1.

earlier sale instead of the last sale. In particular, the declarant can ask the customs authority to accept the price of a sale prior to the last sale, provided that the declarant can demonstrate that there are specific and relevant circumstances, which led to an export of the goods to the customs territory of the Community.[25]

Such elements of proof are:

- that the goods are manufactured according to EC specifications, or are identified as having no other use or destination;

- that the goods in question were manufactured or produced specifically for a buyer in the EC;

- that specific goods are ordered from an intermediary who purchases the goods from a manufacturer and the goods are shipped directly to the EC from that manufacturer.[26]

With regard to situations involving more than one sale, it has to be mentioned that "[…] *where, in successive sales of goods, more than one price actually paid or payable fulfils the requirements* [of Article 29 of the CCC] […] *any of those prices may be chosen by the importer for the purposes of determining the transaction value*".[27]

Last but not least, the term 'sold for export' concerns the goods and not the seller, which means that the seller is not required to be established outside the territory of the Community.[28] What is necessary is that the buyer has an establishment in the customs territory of the Community[29] and that the sale relates to an international transfer of goods[30].

What should be kept in mind is that the wording 'sold for export' refers to the (last) sale of the goods that leads to an introduction into the Community's customs territory, bearing in mind the possibility to refer to an earlier sale in the case of successive sales.

Article 29 (1) of the CCC states that the transaction value *shall be adjusted where necessary in accordance with Articles 32 and 33*. With regard to the purpose of this thesis, Chapter 2.2 introduces the adjustments to be made in accordance with Article 32 of the CCC.

[25] Commentary No 7 of the Customs Code Committee, para 3.2.2.
[26] Ibid, para 4.
[27] Case C-11/89 *Unifert Handels GmbH* ECLI:EU:C:1990:237, para 21.
[28] Ibid, para 11.
[29] Case C-111/79 *S.A. Caterpillar Overseas* ECLI:EU:C:1980:78, para 14.
[30] B. J. O'Shea and S. Rosenow, *A Handbook on the WTO Customs Valuation Agreement*, Cambridge, World Trade Organization, 2010, p. 39, Available from: E-Book Library, (accessed 13 May 2015).

2.2 Adjustments to the price paid or payable

Adjustments to the transaction value are to be made in order to prevent the undervaluation of the imported goods and, thereby, to protect the Community's customs revenues.[31] In connection to that, Article 32 (1) of the CCC[32] provides for the following adjustments:

(a) commissions other than buying commissions, brokerage, the cost of containers which are treated as being one with the imported goods as well as the cost of packing;

(b) the value of goods and services supplied by the buyer free of charge or at a reduced cost to the seller for the production and sale for export of the goods, for example:

  (i) materials incorporated in the imported goods, or

  (ii) tools, dies, moulds and similar items used in the production of the imported goods;

(c) royalties and licence fees related to the imported goods, which the buyer has to pay directly or indirectly as a condition of sale;

(d) the value of any part of the proceeds of any subsequent resale, disposal or use of the imported goods that accrues to the seller;

(e) transport and insurance costs of the imported goods as well as loading and handling charges.

In favour of the topic of this thesis, the subsequent chapter concerns the treatment of royalties and license fees due to Article 32 (1) (c) of the CCC, whose importance has already been mentioned above.

3 Royalties and license fees

The transaction value has to be adjusted by *royalties and licence fees*, which are *related to the goods being valued* that the buyer must pay, either directly or indirectly, as a *condition of sale* of the goods being valued, provided that such royalties and fees are not already included in the price actually paid or payable in accordance with Article 32 (1) (c) of the CCC.

Therefore, first, a definition of royalties and license fees is given in Chapter 3.1 and, second, the concepts of the 'condition of sale' as well as 'related to the goods being valued' are explained in Chapter 3.2 and 3.3.

[31] T. Lyons, *EC Customs Law*, Oxford, Oxford University Press, 2nd Edition, 2008, p. 296.

[32] Please be aware of further conditions for the adjustments set out in Article 32 (2) to (5) of the CCC.

Furthermore, Chapter 3.4 concerns the specific treatment of royalty payments with regard to trademarks before a conclusion will be drawn in Chapter 3.5.

3.1 The definition of royalties and license fees

In determining the meaning of 'royalties and license fees' mentioned in Article 32 (1) (c) of the CCC, a first indication can be found in the Annex 23 to the CCCIP concerning the article at issue. It is this interpretative note that defines that the term 'royalties and licence fees' includes inter alia, payments in respect to patents, trademarks and copyrights.

Further information is given by Article 157 (1) of the CCCIP, which specifies that payments for 'royalties and license' fees have to be considered as payments for the use of rights relating to:

- the manufacture of imported goods (in particular, patents, designs, models and manufacturing know-how), or

- the sale for exportation of imported goods (in particular, trademarks and registered designs), or

- the use or resale of imported goods (in particular, copyright, manufacturing processes inseparably embodied in the imported goods).

With regard to a general definition, Commentary Number 3 of the Customs Code Committee on the incidence of royalties and license fees in customs value refers to Article 12 (2) of the Organisation for Economic Co-operation and Development (OECD) Model Double Taxation Convention on Income and Capital (1977).[33] According to this article 'royalties and license fees' are:

> "[…] *payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial, or scientific experience*".

Due to the fact that the wording 'information concerning industrial, commercial, or scientific experience' relates to the term 'know-how',[34] it is helpful to take a look at the definition of this term in order to increase the understanding of royalties and license fees. 'Know-how', as generally understood, is the outcome of previous experience, which leads to a

[33] Commentary No 3 of the Customs Code Committee (customs valuation section) on the incidence of royalties and licence fees in customs value, para 3, in Compendium of Customs Valuation texts of the Customs Code Committee, TAXUD/800/2002-EN, September 2008 (hereinafter as Commentary No 3 of the Customs Code Committee).

[34] Ibid, para 3.

knowledge in an industrial, commercial or scientific area that is valuable in the operation of a business and, consequently, whose nondisclosure results in an economic benefit.[35]

What can be derived from the foregoing is that 'royalties and license fees' concern the right relating to intangibles (inter alia, patents, trademarks, copyrights, and know-how) and are protected as they involve economic benefits for the inventor. This conclusion can be compared with definition given by the OECD that states that, in general, "[…] *royalties in respect of licenses to use patents and similar property and similar payments are income to the recipient from a letting*"[36].

As Article 157 (2) of the CCCIP puts emphasise on the requirements for royalties and license fees to be added to the transaction value set out in Article 32 (1) (c) of the CCC, namely that they are related to the goods being valued and constitute a condition of sale of these goods, the subsequent chapters give a theoretical background with regard to these specifications.

3.2 'Related to the goods being valued'

The first condition referred to in Article 32 (1) (c) of the CCC and Article 157 (2) of the CCCIP requires that the royalties and license fees are related to the goods being valued in order to be adjusted to the transaction value.

An appropriate introduction for this topic constitutes the Commentary No 3 of the Customs Code Committee, which states that, in determining whether royalties and license fees are related to the imported goods, the fundamental question is why they are paid.[37] More specific, what (right) does the buyer receive for his payment?[38]

In order to ascertain the meaning of the wording 'related to the goods', Article 158 (1) of the CCCIP determines that, with regard to goods as ingredients or components of other goods manufactured in the Community, an adjustment to the transaction value shall only be made when the royalty or license fee relates to the imported goods. Moreover, an appropriate apportionment of the royalty payments has to be made, if the royalties and license fees are partly connected to imported goods and partly to other ingredients or components as well as to post-importation activities or services.[39] These provisions do not deliver any distinct definition of 'related to the goods' but what can be derived from that is the indication that the royalty payments only become dutiable inasmuch as they are made in favour of the imported goods.

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[35] OECD, *Model Tax Convention on Income and Capital*, OECD Publishing, 2012, p. C(12)-7, Available from: E-Book Library, (accessed 13 May 2015).
[36] Ibid, p. R(16)-26.
[37] Commentary No 3 of the Customs Code Committee, para 11.
[38] Ibid, para 11.
[39] Article 158 (3) CCCIP.

Even though the imported goods are unassembled or are the subject of minor processing before resale, i.e. diluting or packing, a royalty or license fee still relates to the imported goods due to Article 158 (2) of the CCCIP. This results in the finding that "[…] *intellectual property is considered to be incorporated in the good already prior the minor processing*"[40].

In addition, one should pay attention to the fact whether the royalties and license fees relate to the imported goods or to another product or service as, for example, Article 32 (5) (a) of the CCC states that royalty payments for the right to reproduce imported goods in the Community must not be added to the transaction value.[41]

Furthermore, if the amount of the royalties and license fees paid or payable refers to the price of the imported goods, Article 161 (1) of the CCCIP states that it can be assumed that they relate to the goods being valued. At this point, it has to be mentioned that where the amount of the royalties and license fees paid or payable do not refer to the price of the imported goods, the payments may nevertheless relate to the goods being valued according to Article 161 (2) of the CCCIP.

When examining the relation between royalty payments and imported goods, a reference has to be made to the Case C-1/77 *Robert Bosch*, which dealt with the question whether royalties and license fees for a patented process embodied in a machine have to be added to the transaction value.[42] With regard to that, the CJEU stated that, basically, it is necessary to consider the intrinsic value of the goods and to put less emphasise on the process.[43] A different result can be achieved in the case where the good and the process are so closely linked with each other that they have to be considered as embodied in one and the same article.[44] More specific, a patented process can be regarded as embodied in the imported goods and, consequently, the royalty or license fee payment relate to the imported goods, if the process "[…] *constitutes the only economically viable use of the goods and* […] *is only put into effect by the use of those goods*"[45]. In contradiction to the condition of sale (see Chapter 3.3), payments are 'related to the goods' if they are necessary in order to use the imported goods.

In conclusion, one can relate back to the beginning of this chapter where it has been said that the essential key for determining whether a royalty or license fee relates to an imported good can be found in the motivation for the payment. In other words, royalties and license fees are related to the imported goods, if they are necessary for further usage of the goods.

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[40] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 9.

[41] Ibid, p. 6.

[42] Case C-1/77 *Robert Bosch GmbH* ECLI:EU:C:1977:130, para 1.

[43] Ibid, para 4.

[44] Ibid, para 5.

[45] Ibid, para 5.

Even though the royalties and license fees are related to the goods being valued, they are not adjusted to the transaction value until the second requirement is fulfilled, namely the condition of sale, which is further investigated in Chapter 3.3.

3.3 'Condition of sale'

To begin with, the concept 'condition of sale' relates to the key issue whether the seller would agree to sell his goods without receiving the royalty payments[46] or "[i]*n other words, the key question is whether the seller would or could sell the tangible to the buyer in case the latter is not purchasing the right to use the intangible*"[47].

In a situation where the buyer purchases machinery from the seller but also needs to pay license fees for a patented process in order to receive the goods, the concept at issue leads to the result that the royalty payments will be adjusted to the transaction value.[48]

It has to be mentioned that the 'condition of sale' can be explicit or implicit and that, generally, it can be derived from the sale agreement whether the sale of the goods are dependent on royalty payments.[49] However, it must not necessarily be stipulated in that way.[50]

With regard to situations where the buyer imports goods from the seller and renders royalty payments to a third person, Article 13 of the Commentary No 3 of the Customs Code Committee states that the payments may nevertheless be regarded as a condition of sale, if the requirements of Article 160 of the CCCIP are fulfilled.[51] Due to this provision, the condition of sale demands that the seller or a person related to him requires the buyer to make the royalty payment. In order to determine whether a person has to be regarded as being related to the seller, Article 143 (1) of the CCCIP provides that persons shall be deemed to be related if:

(a) they are officers or directors of one another's businesses;

(b) they are legally recognized partners in business;

(c) they are employer and employee;

(d) any person directly or indirectly owns, controls or holds 5 % or more of the outstanding voting stock or shares of both of them;

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[46] Commentary No 3 of the Customs Code Committee, para 12.

[47] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 6.

[48] Ibid, pp. 6-7.

[49] See footnote 46, para 12.

[50] Ibid, para 12.

[51] Ibid, para 13.

(e) one of them directly or indirectly controls the other;

(f) both of them are directly or indirectly controlled by a third person;

(g) together they directly or indirectly control a third person; or

(h) they are members of the same family[52].

The provision that deserves a particular interest constitutes Article 143 (1) (e) according to Commentary Number 11 of the Customs Code Committee.[53] Based on Annex 23 to the CCCIP concerning Article 143 (1) (e), a person controls another person, if the first has the legal or operational authority to give directives to the latter. Commentary No 11 of the Customs Code Committee states that in order to ascertain whether a 'control' is established, inter alia, the following elements have to be analysed:

- the licensor selects the manufacturer and specifies it for the buyer;

- there is a direct contract of manufacture between the licensor and the seller;

- the licensor exercises actual control either directly or indirectly over the manufacture (as regards centres of production and /or methods of production);

- the licensor exercises actual direct or indirect control over the logistics and the dispatch of the goods to the buyer;

- the licensor nominates / restricts who the producer can sell their goods to.[54]

In the case that different indicators put together lead to the conclusion that the monitoring of the licensor goes beyond what can be regarded as a purely quality control, the fulfilment of the concept 'condition of sale' is established.[55] In other words, the licensor restricts the seller or buyer in such a way as not being completely free to decide what to do with goods. It has to be mentioned that, in individual cases, there might be other indicators and that some indicators are more important than others, which could in themselves establish a condition of sale.[56]

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[52] Several examples for 'members of the same family' are set out in Article 143 (1) (h) of the CCCIP.

[53] Commentary No 11 of the Customs Code Committee (customs valuation section) on the application of Article 32 (1) (c) CC in relation to royalties and licence fees paid to a third party according to Article 160 of Reg. (EEC) n° 2454/93, para 1, in Compendium of Customs Valuation texts of the Customs Code Committee, TAXUD/800/2002-EN, September 2008 (hereinafter as Commentary No 11 of the Customs Code Committee).

[54] Ibid, see further elements under para 1.

[55] Ibid, para 1.

[56] Ibid, para 1.

Furthermore, Commentary No 3 of the Customs Code Committee extends the scope of the concept at issue to multinational groups where the seller or a related person requires the buyer to make the royalty payment.[57]

With regard to everything mentioned above, it seems to be not surprising that royalties and license fees paid for the right to distribute or resell the imported goods do not have to be adjusted to the transaction value, if the royalty payments are not a condition of sale for export to the Community of the goods in accordance to Article 32 (5) (b) of the CCC.

Last but not least, it has to be mentioned that, basically, when a payment falls under the definition of royalties and license fees, the payment has to be examined solely with regard to Article 32 (1) (c) of the CCC.[58] That there are also exceptions to this approach can be shown by the outcome of the Case C-116/89 *BayWa AG*. In the circumstances of the case, BayWa bought goods from a company X, established in the Community, and sold them to another company Y, located outside the territory of the Community. After processing the goods, BayWa bought the goods from company Y and sold them within the Community. When selling the processed goods, BayWa had to pay license fees to company X.[59] Company X and Y are not related persons.

With regard to that, the CJEU decided that the license fees had to be adjusted to the transaction value due to Artice 32 (1) (b) (i) of the CCC,[60] even though Advocate General (AG) Lenz argued that they cannot be regarded as being comprised in the goods purchased from X.[61] Consequently, this judgement demonstrates that "[…] *for cases where goods subject to license fees are supplied directly or indirectly by the importer for use in the production by the foreign seller is that the importer cannot rely on the specific rules on royalties and license fees*"[62]. At this point it has to be mentioned that royalty payments for design work could also be dutiable based on Article 32 (1) (b) (iv) of the CCC.[63]

Taking all this into consideration, the conclusion can be drawn that the 'condition of sale' has a broad area of application explained, inter alia, by "[…] *legal relationships and control factors*"[64]. In particular, the determination of related persons has a very wide scope[65], which can be seen through the several situations set out in Article 143 (1) of the CCCIP. More specific, this is the case in situations involving a third party where the

[57] Commentary No 3 of the Customs Code Committee, para 13.
[58] Ibid, para 20.
[59] Case C-116/89 *BayWa AG* ECLI:EU:C:1991:104, para 3.
[60] Ibid, para 18.
[61] Ibid, Opinion of AG Lenz ECLI:EU:C:1990:178, para 40.
[62] M. Lux et al., ´The Customs Treatment of Royalties and License Fees with Regard to Imported Goods`, *Global Trade and Customs Journal*, Volume 7, Issue 4, Kluwer Law International, 2012, p. 120 at 138.
[63] Ibid, p. 133.
[64] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 13.
[65] T. Lyons, *EC Customs Law*, Oxford, Oxford University Press, 2nd Edition, 2008, p. 302.

combination of different control indicators go beyond what can be considered as a purely quality control, which is difficult to determine as there is no clear interpretation or approach to follow.[66] Finally, the circumstances of the individual case are decisive[67], bearing in mind that the Case *BayWa AG* has demonstrated that, sometimes, royalties and license fees can be adjusted under another provision and, consequently, the importer cannot always rely on the conditions set out in Article 32 (1) (c) of the CCC.

In the definition of royalties and license fees, trademarks constitute an essential part as it has already been mentioned above. In addition, the CCCIP contains a separate article for the handling of payments for trademarks for valuation purposes. That is why it seems to be reasonable to consider royalties and license fees with regard to trademarks in Chapter 3.4.

3.4 Royalties and license fees with regard to trademarks

Trademarks are used to improve the attractiveness of a product in a certain market and, thereby, to increase its market value.[68] The above mentioned criteria, namely that the payments are related to the goods and are paid as a condition of sale, are also decisive for the customs liability of royalties and license fees paid for the usage of a trademark.[69] That leads to the finding that "[i]*n case the seller and the licensor are the same party, the likelihood increases that the royalty payment for the use of the trademark is made a condition of sale*"[70].

Article 159 of the CCCIP provides the following conditions to be fulfilled in order to adjust to the transaction value the royalties and license fees paid in connection with trademarks:

- the royalty or licence fee refers to goods which are resold in the same state or which are subject only to minor processing after importation,

- the goods are marketed under the trade mark, affixed before or after importation, for which the royalty or licence fee is paid, and

- the buyer is not free to obtain such goods from other suppliers unrelated to the seller.

[66] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 13.
[67] Ibid, p. 13.
[68] Ibid, p. 7.
[69] Ibid, p. 7.
[70] Ibid, p. 7.

Please note that the first and second conditions refer to the requirement that the royalty payments are related to the goods.[71] Furthermore, even in situations concerning payments for trademarks, minor processing does not preclude the payments from being related to the goods.[72] In addition, it has to be mentioned that the provision refers 'only' to minor processing. Consequently, in the case of more than what can be regarded as minor processing, the royalty payments cannot be considered as being related to the goods.[73]

A general explanation why trademarks are related to the goods may be found in the fact that trademarks can be affixed to the goods prior to importation, if they are subject to a trademark license.[74]

The third condition relates to the criterion that the payments are made as a condition of sale, which is based on the concept 'freedom of source' in the matter of trademarks.[75] With regard to that, "[…] *the EU legislator has – specifically for trade mark royalty and license fee payments – narrowed down the condition of sale. There is no condition of sale in case the buyer has the right to source from suppliers unrelated to the seller*"[76].

In conclusion, royalty payments with regard to a trademark are dutiable, if they are paid for the usage of a trademark and the imported goods at issue have not experienced a major processing. With regard to the condition of sale, the "[…] *EU Customs Law already back in 1983 did foresee the "freedom of source"-concept resulting in many trademark related royalties being excluded from the customs value*"[77].

After having illustrated the basic information concerning the treatment of royalties and license fees for customs purposes, Chapter 3.5 gives a conclusion with regard to the concept of their customs treatment in accordance with the CCC.

3.5 Conclusion

As it has already been mentioned above, payments for the usage of, inter alia, patents, trademarks, and copyrights may be dutiable for customs purposes. The customs liability depends on the fulfilment of two conditions, namely that the payments are related to the imported goods and that they are made as a condition of sale. Whereas the first requirement concerns the purpose of the

[71] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 11.
[72] Ibid, p. 11.
[73] Ibid, p. 11.
[74] M. Lux et al., ´The Customs Treatment of Royalties and License Fees with Regard to Imported Goods`, *Global Trade and Customs Journal*, Volume 7, Issue 4, Kluwer Law International, 2012, p. 120 at 133.
[75] See footnote 71, p. 11.
[76] Ibid, p. 11.
[77] Ibid, p. 13.

payment, the latter depends on the criteria of legal relationships and control factors. These conditions are also valid in connection with payments for trademarks, although there are different elements to consider, i.e. the freedom of source concept.

Furthermore, the possibility for royalties and license fees to become dutiable based on other provisions than Article 32 (1) (c) of the CCC leads to an enlargement of the area of their customs liability. Even though royalty payments experience a broad scope of application from a customs point of view, there are some exceptions to consider, i.e. Article 32 (5) of the CCC.

Finally, it is the license agreement and the arrangement of the business relations that are decisive for the customs liability of royalties and license fees.

4 The Union Customs Code

Considering the relevant provision of the CCC that states that royalties and license fees have to be added to the transaction value if they are related to the imported goods and have to be paid as a condition of sale, Article 71 (1) (c) of the UCC provides for exactly the same wording as it is written in Article 32 (1) (c) of the CCC.

Even though not similar to the same extent, Article 32 (5) of the CCC finds its expression in the Articles 72 (d) and (g) of the UCC. This has the consequence that also in accordance with the provisions of the UCC, first, royalty payments for the right to reproduce the imported goods in the Union[78] and, second, royalties and license fees paid for the right to distribute or to resell the imported goods[79] do not have to be adjusted the transaction value.

As it has already been referred to the exclusion of royalty payments for, inter alia, technical assistance for the goods after their importation, Article 72 (b) of the UCC does not derogate from that limitation.[80]

A different situation can be found with regard to the implementing provisions. The topic-related articles of the CCCIP have been reduced as it can be derived from the latest document published by the European Commission, namely the consolidated draft of the implementing act concerning the UCC (UCCIA)[81].

Article IA-II-3-10 of the UCCIA states the following in connection with the customs liability of royalties and license fees:

[78] In this context, the Union has to be understood as the EU.

[79] Please note that such payments must not be made as a condition of sale based on Article 72 (g) of the UCC.

[80] Please note that the UCC does not demand such payments to be shown separately.

[81] Consolidated preliminary draft of the Union Customs Code Implementing Act, TAXUD/UCC-IA/2014-4, European Commission, 4 March 2015.

1. For the purposes of point (c) of Article 71(1) of the Code, royalties and licence fees refers to payment for the use of rights relating to, inter alia, know-how, trademarks, copyright, patents, designs and models.

2. Royalties and licence fees are related to the imported goods where in particular, the rights transferred under the licence or royalties agreement are embodied in the goods. The method of calculation of the amount of the royalty or licence fee is not the decisive factor.

   However, where the method of calculation of the amount of a royalty or licence fee derives from the price of the imported goods, it may be assumed in the absence of evidence to the contrary that the payment of that royalty or licence fee is related to the goods to be valued.

3. If royalties or licence fees relate partly to the imported goods and partly to other ingredients or component parts added to the goods after their importation, or to post-importation activities or services, an appropriate apportionment may be made only on the basis of objective and quantifiable data.

4. Payments made by the buyer for the right to distribute or resell the imported goods are not part of the customs value if such payments are not a condition of the sale of the goods for export to the customs territory of the Union.

5. Royalties and licence fees are considered to be paid as a condition of sale for the imported goods when any of the following conditions is met:

   (a) the seller or person related to the seller requires the buyer to make this payment;

   (b) the payment by the buyer is made to satisfy an obligation of the seller, in accordance with contractual obligations;

   (c) the goods cannot be sold to, or purchased by the buyer without payment of the royalties or license fees to a licensor.

6. The country in which the recipient of the royalty or licence payment is established is not a material consideration.

The first paragraph of the above mentioned article concerns the definition of royalties and license fees. It goes without a saying that this provision gives a rather short definition in comparison to Article 157 (1) of the CCCIP in connection with Annex 23 to the CCCIP concerning Article 32 (1) (c). However, it can be assumed that the meaning of royalties and license fees remain the same. Nevertheless, it cannot be excluded that the scope of the meaning has been expanded as it leaves more space for interpretation.

Furthermore, as the provisions of Article 157 (1) of the CCCIP have not been adopted in the latest draft of the UCCIA, further evidence has been given for broadening the customs liability of royalties and license fees. Consequently, it is likely that the customs liability of, inter alia, royalty payments relating to the manufacture of imported goods will still be established under the UCC.[82]

With regard to royalty payments rendered for the right to distribute or to resell imported goods in the Union, it is questionable why the fourth paragraph has been included in the UCCIA as Article 72 (g) of the UCC contains the same ruling and refers explicitly to Article 71 (1) (c) that concerns royalties and license fees.

Last but not least, the sixth paragraph reflects Article 162 of the CCCIP in the preliminary version of the UCCIA.

As the second, third, and the fifth paragraph of the implementing acts concern the terms 'related to the goods' and 'condition of sale', an investigation on the their new meaning is rendered in the following. With regard to that, first, Chapter 4.1 concerns royalty payments related to the goods and, second, Chapter 4.2 examines the term 'condition of sale'.

4.1 'Related to the goods being valued'

To begin with, the provisions of Article 158 of the CCCIP, which defines to what an extent royalty payments have to be regarded as being related to the goods, cannot be found in the previous drafts of the implementing acts.[83] This approach has been partly corrected as is it can be seen through the latest draft of Article IA-II-3-10. A new paragraph has been introduced, namely paragraph three, which reflects Article 158 (3) of the CCCIP that determines that an appropriate apportionment of the royalty payments has to be made, if royalties and license fees are partly connected to the imported goods and partly to other ingredients or components as well as to post-importation activities or services. Whereas Article 158 (3) of the CCCIP demands that an appropriate apportionment *shall* be made only on the basis of objective and quantifiable data, the latest draft of paragraph three provides for the word *may*. The consequence of this derogation may be disclosed in the future but what can be expected is that an apportionment of the royalty payments will not be mandatory under the UCC.[84]
With regard to the determination of when royalty payments are related to the imported goods, Article IA-II-3-10 (2) of the UCCIA has been introduced. Whereas Article 158 of the CCCIP defines payments as being related to the goods by describing certain situations, i.e. with regard to imported goods as

[82] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 15.

[83] See, for example, Article IA-II-3-10 of the consolidated preliminary draft of the UCCIA, TAXUD/UCC-IA/2014-1, European Commission, 13 January 2014.

[84] Please note that the last part of the sentence of Article 158 (3) of the CCCIP has been cancelled as the current draft of the UCCIA does not contain an Annex.

ingredients or components of goods manufactured in the Community, the first sentence of the article in question determines that royalties and licence fees are related to the imported goods where, in particular, the rights transferred under the licence or royalty agreement are *embodied* in the goods. At this point, a reference has to be made again to the Case C-1/77 *Robert Bosch*, in which the CJEU has defined the meaning of 'embodied in the goods' with regard to patented processes. Due to its decision, 'embodied' shall mean that the goods and the protected right are so closely linked with each other[85] that the protected right "[…] *constitutes the only economically viable use of the goods and* […] *is only put into effect by the use of those goods*"[86]. As a consequence, the presumption that the CJEU has already given a definition of 'embodied', as it has been implemented in the UCCIA, seems to be obvious.

With regard to the treatment of royalty payments for trademarks, the provisions of Article 159 of the CCCIP have been cancelled, which leads to the conclusion that trademarks will not enjoy special conditions anymore. Instead, trademarks will experience the same treatment as royalty payments for others intangibles set out in Article IA-II-3-10 (1) of the UCCIA concerning the relation of the payments to the goods being valued. As a result of that, more payments for the right to use a trademark will be regarded as being related to the goods.

Article 161 of the CCCIP provided for the possibility of payments being related to the imported goods due the calculation method of the amount payable or paid. With regard to that, Article 161 (1) of the CCCIP has been adopted in the third sentence of Article IA-II-3-10 (2) of the UCCIA, whereas Article 161 (2) of the CCCIP has been abolished. It has to be mentioned that a new provision has been introduced by the UCCIA, which can be found in the second sentence of Article IA-II-3-10 (2). It is this provision that determines that the calculation method of the amount of the royalty payment is not the decisive factor. By mentioning that the calculation method is not the decisive factor, it can be assumed that this provision is only another way to express the second paragraph of Article 161 of the CCCIP, which states that where the amount of the payment is calculated regardless of the price of the imported goods, the payment may still be regarded as being related to the goods. In so far, there is "[n]*o change in comparison to the current CCCIP (article 161)*"[87].

In conclusion, the intention of the word 'may' in the third paragraph is unclear and demands an explanation. Furthermore, the introduction of the wording 'embodied in the goods' will presumably involve a new series of case law as long as no further commentary is given by the EU Customs Code Committee. A starting point for the case law may have been established by the Case C-1/77 *Robert Bosch*. In the same manner, further clearance with regard to

[85] Case C-1/77 Robert Bosch GmbH [1977] ECLI:EU:C:1977:130, para 5.

[86] Ibid, para 5.

[87] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 16.

the situations set out in Article 158 of the CCCIP, i.e. minor vs. significant processing, is desirable.[88] In addition, payments for the use of trademarks will not enjoy a special customs treatment under the UCC, which has the consequence that more payments for the use of trademarks will establish a customs liability.

4.2 'Condition of sale'

The fifth paragraph of Article IA-II-3-10 of the UCCIA sets out three different requirements with regard to the condition of sale. As the introducing sentence of the fifth paragraph provides that royalties and license fees are to be considered as being paid as a condition of sale for the imported goods when *any* of the conditions set out in the letters a) to c) are met, the condition of sale is established, if one of those requirements is satisfied.

Letter a) of the provision at issue determines that the condition of sale is met, if the seller or a person related to the seller requires the buyer to make the royalty payment. With reference to the provisions of the CCCIP, Article IA-II-3-10 (5) (a) of the UCCIA reflects Article 160 of the CCCIP. This leads to the result that also under the UCC third parties situations will be captured. Further guidelines of the Customs Code Committee will disclose whether the rules provided for in the Commentaries No 3 and 11 of the Customs Code Committee remain valid for the determination of related parties in connection with royalty payments under the new Customs Code.
Concerning the determination of whether the seller and the licensor have to be regarded as related persons, Article IA-II-3-01 of the UCCIA is basically similar to Article 143 of the CCCIP, which contains a list of situations where persons can be seen as being related with each other. The only derogation from Article 143 of the CCCIP can be found in Article IA-II-3-01 of the UCCIA, as it does not foresee an enumeration for relationships that establish a membership of the same family. It is not likely that meaning of 'members of the same family' will differ under the UCC from the CCC.

The second rule, more specific letter b) of the provision at issue, establishes the condition of sale, if the royalty payment by the buyer is made in order to satisfy an obligation of the seller in accordance with contractual obligations. This provision is new with regard to the CCCIP and also covers third party situations. An example for the new ruling can be found where the seller and the licensor have arranged a license agreement but it is the buyer who has to make the payment to the licensor in order to satisfy the seller's obligation.[89] It has to be mentioned that the payment by the buyer constitutes an indirect payment and will be, consequently, adjusted to the transaction value.[90]

[88] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 15.
[89] Ibid, p. 16.
[90] Ibid, p. 17.

Until now, no further explanation of the wording 'contractual obligations' has been given.[91] With regard to that, several Member States expressed their concerns during the meeting of the Customs Code Committee held on 24 February 2011 because this wording could not be seen as a proof of an establishment of the condition of sale.[92] It goes without a saying that an introduction of a new wording leads to an uncertainty in the application of the law but what can be expected is that 'contractual obligation' covers, particularly, license agreements and is applicable to several third party situations (inter alia, buyer-licensor as well as seller-licensor)[93] as "[…] *it is clear that the EU legislator is determined to increase the scope of taxation of intangibles*"[94].

Letter c) of the provision at issue demands that the condition of sale is met, if the goods cannot be sold to, or purchased by the buyer without payment of the royalties or license fees to a licensor. In order to clarify the meaning of this provision it seems to be reasonable to refer to a previous draft of the implementing provisions concerning the MCC (MCCIP), which can be regarded as the precursor of the UCCIA and provided for the condition set out under letter c) to be met in the following cases:

- the seller is required by contract to pay royalties or license fees to the licensor and the buyer pays the licensor to satisfy an obligation of the seller; and/or

- the seller may refuse to sell, or cancel the sale of the goods, if the buyer does not pay royalties or license fees to the licensor.[95]

These provisions have been cancelled as several Member States expressed their concerns during the meeting of the Customs Code Committee held on

[91] Compare the summaries of the conclusions reached during the meetings of the Customs Code Committee (Valuation Section) held on 30 September 2011 (TAXUD/B4/MN/D(2011)1287373), 2 December 2011 (TAXUD/B4/MN/D(2012)94162), 9 March 2012 (TAXUD/B4/MN/D(2012)1112108), 1 October 2012 (TAXUD/B4/MN/1740133), 17 and 18 January 2013 (taxud.b.4(2013)3337666), 14 October 2013 (TAXUD/B4/440961/2014), 13 and 14 March 2014 (TAXUD/B4/Ares(2014)3468766), and 10 October 2014 (TAXUD B4/MN/aga(2015)694388). Due to the agenda of the 18 meeting of the Customs Code Committee, 'contractual obligations' have not been a subject of discussions during the meeting held on 5 and 6 March 2015 (Taxud B4/MN/aga(2015)699964).

[92] Summary of the conclusions reached during the meeting held on 24 February 2011, Customs Code Committee, TAXUD/B4/(2011)266601, 11 March 2011, p. 10.

[93] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 17; Please note that, although Mr. De Rybel investigated Article 230-11 of the MCCIP, references to Mr. De Rybel's article are justified as Article 230-11 of the UCCIA is to a large extent identical with Article IA-II-3-10 of the UCCIA.

[94] Ibid, p. 15.

[95] Article 230-11 (4) (c) of the consolidated preliminary draft of the MCCIP, TAXUD/MCCIP/2010/100-2, European Commission, 25 January 2011.

the 22 November 2010, i.e. that the first point should be moved under letter b).[96]
It can be assumed that the cancellation of both indents implies that the intention of letter c) is to cover situations where the licensor has the power to interfere in the sale of the goods[97] and, thereby, to expand the customs liability of royalties and license fees. As this provision does not explicitly demands a relation to the licensor, the possibility might have been given for royalty payments to become dutiable without the buyer or seller being related to the licensor.[98] Consequently, the ruling of letter c) can be regarded as a catch all clause.[99]

As it has already been mentioned above, the provisions that provided for a special treatment of royalty payments rendered for the usage of trademarks have been cancelled. As a result of that, the concept 'freedom of source' has been abolished. Due to the fact that trademarks will experience the same treatment like other intangibles, it is highly likely that the customs liability for payments for the usage of trademarks will be increased significantly.

To draw a conclusion, paragraph five of the provision at issue contains new rulings which leads to the assumption that the scope of the condition of sale will be enlarged notably. In particular, this concerns the treatment of royalty payments for the usage of trademarks. Further explanation of the wording 'contractual obligations' and of the scope of letter c) are desirable. With regard to that and also to the uncertainties mentioned in Chapter 4.1, a guideline for the customs valuation under the UCC can be expected.[100] However, further actions of the Customs Code Committee and of the EU Commission have to be awaited.

5 Is the treatment of royalties and license fees under the UCC in line with the provisions of the GATT?

First of all, the binding effect of the GATT for the European customs law originates in the Agreement Establishing the World Trade Organization (WTO), which includes also the provisions of the GATT dated on 14 April 1994 (GATT 94), which in turn refers to the articles of the GATT dated on 30 October 1947 (GATT 47).[101] As the EU is a contracting party[102] and

[96] Summary of conclusions reached during the meeting held on 22 November 2010, Customs Code Committee, TAXUD/302113/2011, 11 March 2011, p. 6.
[97] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 20.
[98] Ibid, p. 18.
[99] Ibid, p. 18.
[100] See the summaries of the conclusions reached during the meetings of the Customs Code Committee held on 1 October 2012, TAXUD/B4/MN/1740133, pp. 3-4, and on 17 and 18 January 2013, taxud.b.4(2013)3337666, p. 4.
[101] See Article 2 (2) of the Agreement Establishing the WTO and Article 1 (a) of the GATT 94.
[102] WTO, ´Members and Observers`,

Article 2 (2) of the Agreement Establishing the WTO makes the agreement and its associated legal instruments obligatory for the members of the WTO, the provisions of the GATT have to be considered when estimating the validity of the UCC.

The starting point in the WTO customs law concerning the determination of the customs value constitutes Article VII of the GATT 47, which establishes the 'actual value'. It is the Agreement on Implementation of Article VII of the GATT that specifies it to the 'transaction value' in Article 1 and, finally, demands in its Article 8 (1) (c) that royalties and license fees have to be adjusted to the transaction value[103], if they are not already included.

In the following, the validity of the treatment of royalties and license fees under the UCC is examined with regard to the concept 'related to the goods being valued' and 'condition of sale', as the latest commentary of the World Customs Organization (WCO)[104] refers to them as the two main questions in determining the customs liability of royalty payments.

5.1 'Related to the goods being valued'

To begin with, neither Article VII of the GATT 47 nor the Agreement on Implementation of Article VII of the GATT contain explanations concerning the actual meaning of 'related to the goods being valued'. During the study of the advisory opinions of the WCO, it becomes clear that the WCO rather tends to define that requirement by using different case examples.[105] However, there are some advisory opinions that try to specify when royalty payments are related to the goods being valued. For example, the advisory opinion 4.3 defines this condition to be fulfilled, if the payment is for a process 'embodied' in the good and constitutes its only valuable use of the good.[106] Subsequent advisory opinions have changed this approach in so far as the payments have to be in favour of intangibles 'incorporated' in the imported goods.[107] In addition, the latest commentary of the WCO follows that approach as it states the following:

"*The most common circumstances in which a royalty or licence fee may be considered to relate to the goods being valued is when the imported goods*

https://www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm, 2015, (accessed 11 May 2015).

[103] When considering Article 8 (1) (c) of the Agreement on Implementation of Article VII of the GATT, it becomes obvious that this provisions has been copied and pasted into Article 32 (1) (c) of the CCC and Article 71 (1) (c) of the UCC respectively.

[104] Commentary 25.1, WCO Technical Committee on Customs Valuation, 2011.

[105] Advisory opinions 4.1 (2 October 1981), 4.2 (23 March 1982), 4.3 (2 October 1981), 4.4 (23rd March 1982), 4.5 (23 March 1982), 4.6 (11 March 1983), 4.7 (8 October 1993), 4.8 (8 October 1993), 4.9 (8 October 1993), 4.10 (8 October 1993), 4.11 (8 October 1993), 4.12 (8 October 1993), 4.13 (8 October 1993), and 4.15 (April 2013), WCO Technical Committee on Customs Valuation.

[106] Advisory opinion 4.3, 2 October 1981, WCO Technical Committee on Customs Valuation.

[107] Advisory opinions 4.4 (23 March 1982) and 4.12 (8 October 1993), WCO Technical Committee on Customs Valuation.

incorporate the intellectual property and/or are manufactured using the intellectual property covered by the licence"[108].

From my point of view, besides the substitution of 'incorporated' for 'embodied', the fundamental idea behind the term did not change, namely that the intangible is essential in the use of the imported good.[109] In other words, without the payment of the royalty or license fee, the goods cannot be used for further purposes.

The term 'incorporated' concerns all tangibles as, for example, advisory opinions 4.4 and 4.12 concern regular royalty and license fee payments. In general, it seems that the WTO customs law does not foresee a special treatment for trademarks.[110] That is why I have to disagree with Mr. De Rybel, who wrote that "[…] *it seems that that the* [UCCIA] *rules, based on the WTO Commentary, may no longer envisage royalties paid for trademarks which are only embodied in the goods*"[111].

As Article IA-II-3-10 (2) of the UCCIA refers to the rights transferred that are embodied in the goods, the assumption can be made that "[t]*his new interpretation of 'related to the goods' is now being embedded in the* [UCCIA], *fully in line with the WTO Commentary 25.1*"[112] and, consequently, with the GATT. It has to be mentioned that the future will show whether this assumption proves to be correct.

5.2 'Condition of sale'

Neither Article VII of the GATT 47 nor the WTO Agreement on Customs Valuation contain explanations concerning the definition of the 'condition of sale'.[113] Consequently, the interpretation of the 'condition of sale' can be derived from an investigation of the advisory opinions and commentaries of the WCO. As a result of that, it becomes clear that the key question is: "[…] *could the buyer purchase the imported goods without paying the royalty*"[114]?

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[108] Commentary 25.1, WCO Technical Committee on Customs Valuation, 2011.

[109] B. J. O'Shea and S. Rosenow, *A Handbook on the WTO Customs Valuation Agreement*, Cambridge, World Trade Organization, 2010, p. 55, Available from: E-Book Library, (accessed 13 May 2015).

[110] Compare the provisions of the GATT 47 and of the Agreement on Implementation of Article VII of the GATT as well as the advisory opinions and commentaries of the WCO Technical Committee on Customs Valuation.

[111] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 15.

[112] Ibid, p. 15.

[113] Only the Interpretative Note to Article 8 of the WTO Agreement on Customs Valuation concerning paragraph 1 (c), second passage, states that payments for the right to distribute or resell the imported goods must not be added to the transaction value, if such payments are not made as a condition of sale. Compare Article 72 (g) of the UCC and Article IA-II-3-10 (4) of the UCCIA.

[114] B. J. O'Shea and S. Rosenow, *A Handbook on the WTO Customs Valuation Agreement*, Cambridge, World Trade Organization, 2010, p. 57, Available from: E-Book Library, (accessed 13 May 2015)..

It has to be mentioned that the same underlying question can be found in the EU customs law (as discussed above, see Chapter 3.3).

As it has already been mentioned above, Article 71 (1) (c) of the UCC has been copy pasted from Article 8 (1) (c) of the WTO Agreement on Customs Valuation. That means that:

> "[…] *the payment of a royalty or license fee to a third party will only be a condition of sale if the seller was obligated to the third party to pay the royalty or license fee and if the importing purchaser effects such payment for the benefit of the seller*"[115].

With regard to situations including a third party, a reference has to be made to the advisory opinions 4.3 and 4.8 of the WCO. In these opinions, the WCO expressed its view not to treat royalty payments as being made as a condition of sale because the seller and the licensor are not related with each other based on separate agreements (importer-seller and importer-licensor).

The advisory opinion 4.15 introduced the influence and control approach[116], which has been confirmed by commentary 25.1 of the WCO. In its commentary, the WCO determined that in order to ascertain whether the condition of sale has been met, inter alia, "[…] *the sales agreement can be terminated as a consequence of breaching the royalty or licence agreement because the buyer does not pay the royalty or licence fee to the licensor*"[117]. That means that the main attention lies on the fact whether the licensor has the power to stop the supply of the goods but based on a linkage between the license and the sale agreement.[118] Thereby, the approach mentioned in the advisory opinions 4.3 and 4.8 has been extended.[119]

Whereas the commentary 25.1 still has a connection to contractual arrangements, the provisions under the UCC seem not to demand such a requirement when considering Article IA-II-3-10 (5) (c) of the UCCIA. As a consequence of that, the UCC seems to go one step further than the WTO Customs Valuation Agreement.[120] At this point, it has to be mentioned that the advisory opinions and commentaries of the WCO do not have a binding effect on the customs administrations and do not constitute an element of international valuation law.[121] Even though the customs liability of royalties

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[115] S. Sherman and H. Glashoff, *Customs Valuation - Commentary on the GATT Customs Valuation Code*, Paris, ICC Publishing, 1988, p. 125.

[116] D. Cannistra and M. A. Rodríguez Cuadro, ´The Dutiability of Royalty Payments: The Impact of the World Customs Organization's Advisory Opinion 4.15`, *Global Trade and Customs Journal,* Volume 9, Issue 2, Kluwer Law International, 2014, p. 61 at 62.

[117] Article 9 (c) of the Commentary 25.1, WCO Technical Committee on Customs Valuation, 2011.

[118] B. De Rybel, ´Dutiability of Royalty payments and License fees – Extending the concept of ´´condition of sale`` in the EU`, Post Master Thesis, Erasmus University Rotterdam, 2011, p. 20.

[119] Ibid, p. 20.

[120] Ibid, p. 20.

[121] WCO, ´Customs Valuation Compendium`, http://www.wcoomd.org/en/topics/valuation/instruments-and-tools/val_customs_compendium.aspx, 2015, (accessed 11 May 2015).

and license fees will be significantly increased, the treatment under the UCC has to be considered as being closer to the economic reality[122] from my point of view.

6 Are changes of the VAT-Directive necessary?

The importation of goods is a subject to VAT based on Article 2 (1) (d) of the VAT-D. The VAT-D defines the 'importation of goods' as the entry into the Community of goods, which are not in free circulation within the meaning of Article 24 of the Treaty of the European Community (now Article 29 of the TFEU).[123] In order to estimate the taxable amount for the importation of goods, Article 85 of the VAT-D determines that the taxable amount for import VAT purposes shall comply with the customs value of the CCC, which will be replaced by the UCC from 1 May 2016.
Therefore, first, the validity of Article 85 of the VAT-D with regard to the new treatment of royalties and license fees under the UCC is examined in Chapter 6.1, and, second, as the taxable amount for import VAT purposes includes royalty payments, double taxation of royalties and license fees under the provisions of the VAT-D is examined in Chapter 6.2.

6.1 The validity of Article 85 of the VAT-D under the UCC regime

To begin with, Article 73 of the VAT-D determines that, in respect of the supply of goods or services, the taxable amount includes everything which constitutes consideration obtained or to be obtained by the supplier, in return for the supply, from the customer or a third party. With regard to import VAT, Article 85 of the VAT-D states that the taxable amount shall be the customs value. As it has already been mentioned before, royalty payments have to be added to the transaction value under certain circumstances and are, consequently, included in the taxable amount for import VAT purposes.
It has to be mentioned that Article 144 of the VAT-D, basically, exempts the supply of services in connection with the importation of goods but that the exemption is only valid for services in the meaning of Article 86 (1) (b) of the VAT-D, namely incidental expenses, such as commission, packing, transport, and insurance costs incurred up to the first place of destination within the Community. Article 46 of the EU Regulation 282/2011 makes it clear:

[122] Case C-653/11 *Paul Newey* ECLI:EU:C:2013:409, paras 48-49. Even though this case concerns abusive practices in the field of VAT, I support the approach to consider the economic reality when it comes to taxation.
[123] Article 30 VAT-D.

"*The exemption provided for in Article 144 of Directive 2006/112/EC shall apply to transport services connected with the importation of moveable property carried out as part of a change of residence*"[124].

Hence, royalties and license fees paid in connection with the importation of goods are not excluded from the taxable amount for import VAT purposes.

For the purpose of the thesis, let us divide the import into two taxable transactions. First, the supply (importation) of goods within the meaning of Article 14 (1) of the VAT-D, and, second, the supply of services (royalties and license fees) based on Article 24 (1) of the VAT-D. With regard to the taxable amount for import VAT purposes, the fundamental question of this chapter is whether the royalties and license fees paid can be considered as a consideration for the supply (importation) of the goods.

The starting point for determining a taxable relation between the supply and its consideration can be found in the Case C-154/80 *Coöperatieve Aardappelenbewaarplaats*[125], which determines that "[…] *there must* […] *be a direct link between the* [supply] *provided and the consideration received*"[126] in order for a transaction to become taxable. Furthermore, the consideration must be capable of being expressed in money and has to constitute a subjective value different from a value assessed according to objective criteria.[127] Moreover, the Case C-16/93 *Tolsma* introduced the approach that a direct link can only be established "[…] *if there is a legal relationship between the provider of the* [supply] *and the recipient pursuant to which there is reciprocal performance*"[128]. That this approach is not in itself satisfactory can be seen through the outcome in the Case C-102/86 *Apple and Pear Development Council* where the growers had to pay a specific amount to the organisation in order to enable the organisation to pay for its expenses.[129] The CJEU held that "[…] *no relationship exists between the level of the benefits which individual growers obtain from the* [supplies] *provided by the Development Council and the amount of the mandatory charges which they are obliged to pay*"[130] as there is the possibility that only certain growers receive specific supplies[131]. In other words, there must be the possibility to exclude the persons who are not paying from receiving the supply.[132]

Furthermore, there also cases concerning the direct link with regard to other circumstances, i.e. the consideration in vouchers as it can be found in the Case C-230/87 *Naturally Yours* and Case C-288/94 *Argos Distributors* or the

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[124] Council Implementing Regulation (EU) No 282/2011 of 15 March 2011 laying down implementing measures for Directive 2006/112/EC on the common system of value added tax (recast), OJ L 77/1, 23 March 2011.

[125] D. Butler, ´The usefulness of the 'direct link' test in determining consideration for VAT purposes`, *EC Tax Review*, 2004-3, p. 92 at 92.

[126] Case C-154/80 *Coöperatieve Aardappelenbewaarplaats* ECLI:EU:C:1981:38, para 12.

[127] Ibid, para 13.

[128] Case C-16/93 *R. J. Tolsma* ECLI:EU:C:1994:80, para 14.

[129] Case C-102/86 *Apple and Pear Development Council* ECLI:EU:C:1988:120, para 5.

[130] Ibid, para 15.

[131] Ibid, para 14.

[132] See footnote 125, p. 92 at 93.

consideration for gambling as it can be seen in the Case C-38/93 *Glawe Spiel* and Case C-440/12 *Metropol Spielstätten*. What all of these cases have in common is that they define consideration as the sum actually received for the supply[133] or, in other words, as the amount the supplier can actually keep for himself[134]. In connection with that, a direct link between the supply and its consideration can be determined by an analysis of the destination of the customer's payment.[135]

As it has already been mentioned before, the VAT-D defines consideration as everything that the supplier receives from the customer or a third party. In connection with the case law set out above, it can be derived that the direct link between the supply and its consideration can be determined by an analysis of the destination of the customer's payment and the existence of a legal relationship between the supplier and the customer that excludes non-paying persons. With regard to the term 'consideration', it can be assumed that it constitutes everything what reaches the supplier's authority of dispose.

These considerations should also be valid for the determination of the taxable amount for import VAT purposes. Even though the definitions of 'importation of goods' and its taxable amount are distinct from the determinations for the supplies of goods and services[136], import VAT still constitutes a value added tax[137] and does not simply loses its character because it concerns the importation of goods. Therefore, it should comply with the fundamental characteristics of VAT, namely that there must be a direct link between a supply and its consideration.
In order to connect the direct link for VAT purposes with EU customs law, the essential transaction underlying an importation constitutes the trade of goods[138]. That means that royalty payments become dutiable, if they are necessary for the initiation of the import of the goods as the key issue is whether the seller would or could sell the goods without the payments of royalties and license fees being made (condition of sale).
That is why the validity of Article 85 of the VAT-D can be considered as being established, in so far as the royalties and license fees have been paid as a condition of sale to the supplier or to a person related to him, in order to being able to import the goods.
The same result can be found in the application of Article IA-II-3-10 (5) (c) of the UCCIA. If the buyer of the goods does not pay the royalty and license fees and the licensor is able to interfere in the sale of the goods, the royalty

[133] Case C-230/87 *Naturally Yours Cosmetics Limited* ECLI:EU:C:1988:508, para 16; and Case C-288/94 *Argos Distributors Ltd* ECLI:EU:C:1996:398, para 23.
[134] Case C-38/93 *H. J. Glawe Spiel- und Unterhaltungsgeräte Aufstellungsgesellschaft mbH&Co. KG* ECLI:EU:C:1994:188, para 13; and Case C-440/12 *Metropol Spielstätten Unternehmergesellschaft (haftungsbeschränkt)* ECLI:EU:C:2013:687, para 44.
[135] Case C-38/93 *Glawe Spiel*, para 11.
[136] Compare, for example, Articles 14 (1), 24 (1), 30, 73, and 85 VAT-D.
[137] Case C-15/81 *Gaston Schul Douane Expediteur BV* ECLI:EU:C:1982:135, para 21. There, the CJEU states that the import VAT is not a charge having an effect equivalent to customs duties.
[138] M. Lux et al., ´What a Customs Lawyer Should Know about EU Value Added Tax (VAT) Law`, *Global Trade and Customs Journal*, Volume 7, Issue 10, Kluwer Law International, 2012, p. 406 at 408.

payment has to be considered as being made as a condition of sale. This approach, again, reflects the economic reality.

To draw a conclusion, the validity of Article 85 of the VAT-D for import VAT purposes has been proved. However, as the actual intention of Article IA-II-3-10 (5) (c) of the UCCIA remains unclear, further guidance from the Customs Code Committee is desirable.

As it has already been mentioned above, royalties and license fees are not excluded from the import VAT. Therefore, Chapter 6.2 examines the VAT-D with regard to the issue of double taxation.

6.2 Double taxation of royalty payments

There is a common sense that double taxation for VAT purposes can be defined as "[…] *the imposition of* [a general] *tax* [on consumption] *on the same supply by two different states, irrespective of whether* [that] *tax is levied from the same or different taxpayers*"[139]. This definition can be expanded to situations where only one jurisdiction taxes the same transaction twice, which will be shown in the following. For the purpose of this thesis, double taxation shall not merely mean that VAT is levied twice on a single transaction but also that the possibility for an input VAT deduction or refund[140] is excluded. This assumption is based on my (German) definition of a tax as a payment of money, which does not constitute a consideration for a specific supply and is levied from a public authority in order to gain revenues.[141]

The subject of double taxation in the field of VAT has not received much attention[142] as "[c]*ases of effective double taxation, that is, the concurrent levying of indirect taxes on the same subject matter by two different States, seem comparatively rare*"[143]. Another reason for this lack of interest may be given by the fact that taxable persons can deduct the input VAT.[144] Even though that cases of double taxation might be rare, they are nevertheless existing, i.e. with regard to royalty payments, as it will be shown in the following.

In a situation including a seller, a buyer and a licensor[145], two taxable transaction are established in the case of an importation of goods and royalty payments. The first taxable transaction constitutes the supply of a service in

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[139] See, for example, T. Ecker, *A VAT/GST Model Convention – Tax Treaties as Solution for Value Added Tax and Goods and Services Tax Double Taxation*, Amsterdam, IBFD, 2013, p. 37; and B. J. M. Terra, *The Place of Supply in European VAT*, London, Kluwer Law International, 1998, p. 2.

[140] See, for example, Article 168, 170 and 171 VAT-D.

[141] Article 3 (1) of the German General Tax Code.

[142] B. J. M. Terra, *The Place of Supply in European VAT*, London, Kluwer Law International, 1998, p. 2.

[143] OECD, Note by the Swiss Delegation on Double Taxation with Respect to Indirect Taxes, TFD/FC/174, 22 September 1964, p. 1.

[144] See footnote 142, p. 2.

[145] All parties have to be regarded as taxable persons due to 9 (1) VAT-D.

accordance with Article 24 (1) of the VAT-D, which takes the form of a royalty payment rendered to the licensor. The second taxable transaction establishes the importation of goods[146] by the buyer from the seller.
As Article 59 (a) of the VAT-D[147] concerns services rendered to non-taxable persons established outside the EU, the place of the supply of the royalty rights has to be determined in accordance with Article 44 of the VAT-D and is, consequently, where the recipient of the service is established. The place of the importation of the goods is where the goods enter the EU based on Article 60 of the VAT-D.[148] Therefore, two taxable transactions in the territory of the EU are given.
As it has already been mentioned above, the taxable amount for the supply of the service constitutes the consideration, which is the royalty payment. It has also already been mentioned that the taxable amount for import VAT purposes refers to the customs value which, under certain circumstances, includes royalty payments. For the case that the buyer and the licensor are related persons, the royalty payment is regarded as being paid as a condition of sale and is, consequently, included in the customs value and in the taxable amount for the import VAT.
This is where the double taxation of royalties and license fees begins. The person liable for the payment of the VAT for the supply of the service and the importation of the goods is the buyer.[149] A deduction of the import VAT and a deduction, respectively refund, of the reverse charge VAT is possible with regard to the Articles 168 (e), 170 (b) and 171a of the VAT-D. The problem leading to double taxation of royalties can be found in the exclusion of taxable persons being exempted from VAT. Due to the fact that they are not carrying out transactions which are actually taxed, Article 168 (e) of the VAT-D denies a deduction. Such taxable persons are also not allowed to deduct the reverse charge VAT based on Article 171a as it refers to the conditions laid down in Article 168 of the VAT-D.[150] A refund of the VAT due to Article 170 (b) of the VAT-D is also excluded as Article 6 of the Council Directive 2008/9/EC[151] foresees the right for a refund solely for taxable persons carrying out transactions giving the right to deduct input VAT. This has been further supported by the CJEU, which stated in the Case C-4/94 *BLP* that "[…] *where a taxable person supplies services to another taxable person who uses them for an exempt transaction, the latter person is not entitled to deduct the input VAT paid*"[152]. The reason for this treatment can be found in the purpose of the deduction system which is to relieve the taxable persons

[146] Article 30 VAT-D.
[147] As amended by Council Directive 2008/8/EC of 12 February 2008 amending Directive 2006/112/EC as regards the place of supply of services, OJ L 44/11, 20 February 2008.
[148] Please note the possibility to derogate from this approach with reference to Article 61 VAT-D.
[149] Articles 196 and 201 VAT-D.
[150] Please note that Article 169 (b) of the VAT-D also does not enable a deduction for taxable persons, which are exempt from VAT.
[151] Council Directive 2008/9/EC of 12 February 2008 laying down detailed rules for the refund of value added tax, provided for in Directive 2006/112/EC, to taxable persons not established in the Member State of refund but established in another Member State, OJ L 44/23, 20 February 2008
[152] Case C-4/94 *BLP Group plc* ECLI:EU:C:1995:107, para 28.

entirely from the VAT burden, provided that this person carries out transactions that are subject to VAT.[153]

It has to be mentioned that there are discussions whether the import VAT constitutes a frontier duty or a domestic tax, which is distinct from the first one.[154] With regard to that, the CJEU made it clear that the import VAT is not a frontier duty.[155] Even though Article 145 (2) of the VAT-D contains the possibility for MSs to adapt rules in order to prevent double taxation within the EU, it does not make it mandatory for all MSs and, consequently, the risk of a double taxation of royalties and license fees is existing in the VAT-D. This problem has already been addressed by Professor Terra in the year 1998,[156] but the EU legislator has not provided for a solution, since.

It has also been submitted by Professor Terra that, furthermore, this problem violates the provisions of Article 3 of the GATT 47.[157] For example, Article 3 (1) of this agreement states that the contracting parties should not tax the importation of goods in a way as to protect domestic production. Consequently, the double taxation of royalties and license fees clearly discourages VAT exempt companies or organisations from purchasing goods from another contracting party and, thereby, protects the domestic production. The binding effect of the provisions of the GATT has already been examined in Chapter 5.

Even though the situation of exempt organisations entering into license agreements seems not to be very common, the possibility of double taxation exists and, therefore, the provisions of the VAT-D have to be changed. It is unclear why the EU legislator has limited the scope of Article 144 of the VAT-D only to incidental expenses, such as commission, packing, transport and insurance costs. An explanation for that may be given by the pursuit of a harmonisation between customs and VAT. However, the harmonisation of customs and VAT cannot take precedence over double taxation. Furthermore, this violates Article 3 of the GATT 47, which "[…] *provisions* […] *have the effect of binding the Community*"[158]. As a result of that, the EU legislator has to come up with a solution for this situation. A possible answer to that problem could be to expand the scope of Article 144 of the VAT-D and, thereby, to ensure that all services in connection with the importation of goods are exempt. By doing that, the taxable amount for import VAT purposes would be reduced to its key issue, namely the trade of the goods.

The content of the VAT-D is up to the EU legislator but something has to be done, as Article 3 (5) of the TEU determines that one of the EU's maxim is to contribute to a free and fair trade in its relations with the wider world.

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[153] Case C-408/98 *Abbey National plc* ECLI:EU:C:2001:110 , para 24.

[154] M. Fabio, *Customs Law of the European Union*, Alphen aan den Rijn, Kluwer Law International, 2011, p. 4-24.

[155] Case C-15/81 *Gaston Schul Douane Expediteur* BV ECLI:EU:C:1982:135, para 21.

[156] B. J. M. Terra, *The Place of Supply in European VAT*, London, Kluwer Law International, 1998, p. 159.

[157] Ibid, p. 159.

[158] Joined Cases 21/72 to 24/72 *International Fruit Company NV* ECLI:EU:C:1972:115, para 18.

7 Conclusion

"*The dutiability of royalties and license fees is one of the most controversial topics that has arisen since the Customs Valuation Agreement* [has] *adopted* [the] *transaction value as the primary basis for the calculation of customs duties and import taxes.*"[159] With regard to that, Chapter 4 has shown that this statement will probably also remain valid for the future, as, for example, the meaning of the term 'embodied' in Article IA-II-3-10 (2) and the intention of Article IA-II-3-10 (5) (c) of the UCCIA are not clear. As a consequence, further guidance of the Community Customs Committee is desirable.

Chapter 5 has revealed that it can be expected from the provisions of the UCC and UCCIA that the treatment of royalties and license fees under the new EU customs law will be to a great extent in line with the advisory opinions and commentary of the WCO. Even though the customs liability of royalty payments will be increased significantly, this step has to be appreciated in the interest of a taxation of the economic reality.

With regard to Import VAT, the validity of Article 85 of the VAT-D, concerning the taxable amount, has been proved in Chapter 6. This leads to the problem of double taxation of royalties and license fees in the case of taxable persons carrying out exempt transactions. Since Professor Terra has already addressed this problematic situation in 1998, the EU legislator is called to finally present a solution. Even though the inclusion for import VAT purposes of royalty payments meeting the condition of sale requirement is justified and further supported by means of a harmonisation of customs and VAT, the VAT-D has to be changed. A possible solution would be to extend the scope of Article 144 of the VAT-D to the effect that all services related to the importation of the goods are excluded from the import VAT liability.

[159] D. Cannistra and M. A. Rodríguez Cuadros, ´The Dutiability of Royalty Payments: The Impact of the World Customs Organization's Advisory Opinion 4.15`, *Global Trade and Customs Journal*, Volume 9, Issue 2, Kluwer Law International, 2014, p. 61 at 61.

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