

IV

(Notices)

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COURT OF AUDITORS

SPECIAL REPORT No 11/2006

on the Community transit system, together with the Commission's replies

(submitted pursuant to Article 248(4), second subparagraph, EC)

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LIST OF ACRONYMS AND ABBREVIATIONS

DG BUDG	Budget Directorate-General
DG TAXUD	Taxation and Customs Union Directorate-General
EC	European Communities
EEC	European Economic Community
EU	European Union
EWS	Early warning system
MCC	Minimum common core
NCTS	New computerised transit system
OJ	Official Journal of the European Union
OLAF	European Antifraud Office

SUMMARY

I. Between 1990 and 1994 the transit system was affected by fraudulent activities which caused an estimated revenue loss of 320 million ecus to the Community budget. Computerisation of transit procedures, the reform of the legal base, and enhanced physical checks based on common risk analysis were recommended by the European Parliament, by the Council, and by the European Court of Auditors.

II. In response to these recommendations, the Commission presented an 'Action plan for transit in Europe' in 1997. In 2001 it put in place a revised legal framework and until the end of 2005 coordinated the implementation of a new computerised transit system (NCTS), designed to exchange electronic messages between the customs offices of all the Member States.

III. The Court examined the application of the new legislation and the implementation of NCTS in 11 Member States, focusing on clearance of transits, collection of any customs duties on them and fraud prevention. The main findings were as follows:

- (a) the Commission successfully coordinated implementation of NCTS and has provided efficient back-up;
- (b) in the Member States audited, application of the revised legal provisions on procedure simplifications, enquiries and recoveries in cases of non-completion of transits, was often unsatisfactory;
- (c) Member States applied the legal provisions on accounting for duties on non-completed transits in disparate ways, which led to delays in making the duties available to the Community budget;
- (d) as of the end of 2005, the Commission's services had still not carried out any inspections in the Member States focusing on transit in order to evaluate whether application of the new legal framework was effective;
- (e) rudimentary risk management and few physical checks on goods in transit were identified in most of the Member States visited;
- (f) information available to the Commission regarding fraud in transit was neither reliable nor complete enough for it to be possible to determine whether the legal reform and the NCTS project have successfully reduced fraud in transit.

IV. A lack of data on fraud and deficient risk management in the Member States call for coordinated action at European level. The Commission should have access to detailed NCTS information for risk analysis purposes and on the basis of best practice should be able to promote strategies for targeted physical checks on goods in transit.

INTRODUCTION

Definitions and risks

1. Customs transit simplifies customs formalities and facilitates the movement of goods throughout the territory of the Community, by temporarily suspending the duties and other charges on goods imported into the Community until they reach their final destination. Actual customs formalities are shifted from the border to the place of final destination.

2. Community transit applies to:

- (a) movements of non-Community goods and, in certain specific cases, Community goods (external Community transit);
- (b) movements of Community goods between two points in the Community customs territory via a third country, where such possibility is provided for in an international agreement (internal Community transit).

3. The main risk of Community transit is that non-Community goods are unlawfully removed from customs supervision and diverted to the domestic market without payment of customs duties and other taxes, especially value added tax and excise duties.

4. Given the suspensive and temporary nature of a transit, customs authorities tend to regard control of transits as low priority. In order to cover the financial risks, transits are usually secured by a guarantee assuring the payment of duties, taxes and other charges. The guarantee can be either an individual guarantee covering a single transit operation or a comprehensive guarantee covering a number of transit operations ⁽¹⁾.

Remedial action following the problems of the 1990s

5. In the early 1990s, increasing fraud in transit was reported. Estimates of losses to the Community budget between 1990 and 1994 ⁽²⁾ amounted to 320 million ecus, before taking account of subsequent clawback from Member States, with even bigger losses of national taxes. At the time, the Council ⁽³⁾ and

the European Parliament Temporary Committee of Inquiry into the Community Transit System ⁽⁴⁾ recognised computerisation and legal reform of Community transit as key elements for fighting fraud, a view which was supported by the Court in its Annual Report for 1994 ⁽⁵⁾.

6. Until the system was computerised, Community transit declarations were made out on paper. The originals of the declarations were kept at the office of departure and the copies accompanied the consignment through to the customs office of destination. The latter then had to return a document to the office of departure as notification that the consignment had arrived and had to indicate whether or not any irregularities had been detected. The procedure was slow and involved many risks.

7. The Commission therefore presented the 'Action plan for transit in Europe' ⁽⁶⁾, in 1997, together with a list of measures aiming to manage the risks of the transit system and to reduce its vulnerability to fraud. The measures were concerned with the implementation of computerised transit, streamlining of the transit procedure, a reinforcement of control activities at all levels, and lastly, enhanced cooperation between different customs administrations and between customs and traders. At the same time it initiated a revision of the transit legislation.

8. In 1999, the legal basis for the NCTS (new computerised transit system) project was adopted. NCTS aimed to replace the existing paper-based Community transit procedure by a computer-based exchange of electronic messages between the customs offices involved, and at a later stage, between traders and customs.

9. In the fight against transit fraud, NCTS was to serve a double purpose, as it would:

- (a) prevent traditional forms of fraud, e.g. the use of forged stamps or falsified documents;
- (b) detect in real time the non-arrival of goods at the destination customs office and, in this case, trigger the immediate start of enquiry proceedings.

⁽¹⁾ Council Regulation (EEC) No 2913/92 of 12 October 1992 establishing the Community Customs Code, Article 94(2) (OJ L 302, 19.10.1992, p. 1).

⁽²⁾ See COM(95)108 final. There are no estimates for subsequent periods.

⁽³⁾ Decision No 210/97/EC of the European Parliament and of the Council of 19 December 1996 adopting an action programme for customs in the Community (Customs 2000) (OJ L 33, 4.2.1997, p. 24).

⁽⁴⁾ Final Report (PE 220.895/fin), 20.2.1997.

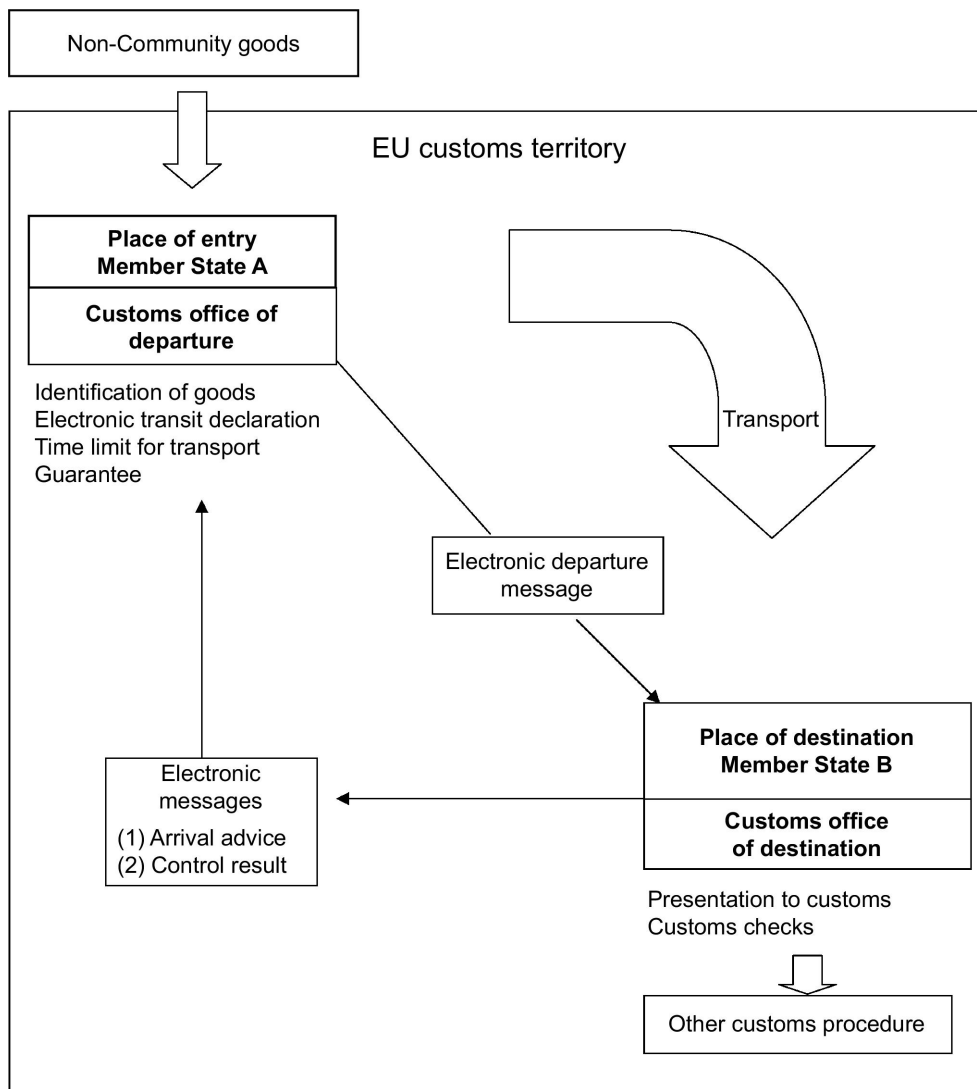
⁽⁵⁾ Annual report concerning the financial year 1994 together with the institutions' replies (OJ C 303, 14.11.1995, p. 1).

⁽⁶⁾ COM(97) 188 final of 10 June 1997.

10. Diagram 1 shows a standard NCTS transit procedure.

Diagram 1

A standard NCTS transit procedure (external Community transit)



11. In 2001, in parallel with the computerisation, the Commission presented a reform of the legal base for the transit system (7) introducing new provisions which aimed, *inter alia*, to:

(a) distinguish more clearly between standard and simplified transit procedures (different methods of customs supervision in the latter case) and better define reliability criteria for participating traders;

(b) base the guarantee system on trader reliability and the risks of the goods involved, whilst introducing the concept of goods involving greater risk of fraud (sensitive goods) (8);

(c) harmonise enquiry and recovery proceedings after non-completed transits and shorten the deadlines for the start of such proceedings.

(7) Mainly Commission Regulation (EC) No 2787/2000 of 15 December 2000 amending 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 330, 27.12.2000, p.1).

(8) Annex 44c to 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, 11.10.1993, p. 1). It applies to items such as live animals, cigarettes and certain alcoholic beverages.

12. NCTS was implemented in several phases. The 'core business' ⁽⁹⁾ was achieved by 30 June 2003 in EU-15 and the Commission then continued to provide assistance to the implementation of NCTS in the accession countries. The subsequent phases included computerised handling of guarantees and enquiries and were completed in January 2006.

13. Since 1 July 2005 Community transit declarations must, as a general rule, be lodged electronically ⁽¹⁰⁾. Commission statistics show a rise in the number of NCTS transit movements, from around 5,5 million in 2004 to more than 7,5 million in 2005.

AUDIT SCOPE AND APPROACH

Main audit objectives

14. The objective of the Court's audit was to obtain assurance that the Member States were applying the revised legal provisions correctly and that the new procedures for transit had been well coordinated by the Commission and correctly implemented by the Member States in a way which protected the EU's financial interests effectively.

15. A second objective was to analyse the implementation of the measures recommended by the European Parliament, the Council and the Court, and more specifically, the measures envisaged in the Commission's action plan. The emphasis here was on review of the new system's vulnerability to fraud and how this is followed up by the Commission services.

Audit approach

16. A questionnaire was sent to all Member States to collect recent transit-related data. Between May 2005 and January 2006 audit visits were performed in 11 Member States which account for almost 80 % of NCTS transits ⁽¹¹⁾.

17. These audits covered:

- (a) the general management and IT aspects of NCTS in the Member States visited;
- (b) authorisation of transit procedure simplifications (authorised consignors/consignees, use of comprehensive guarantees);
- (c) enquiry and recovery proceedings after non-completed transits.

⁽⁹⁾ Core business: computerisation of the Community transit procedure for which the single administrative document was used.

⁽¹⁰⁾ Council Regulation (EC) No 837/2005 of 23 May 2005 amending Commission Regulation (EEC) No 2454/93 laying down provisions for the implementation of Council Regulation (EEC) No 2913/92 establishing the Community Customs Code (OJ L 139, 2.6.2005, p. 1).

⁽¹¹⁾ Belgium, Germany, Spain, France, Italy, Latvia, Hungary, the Netherlands, Poland, Slovenia and Sweden.

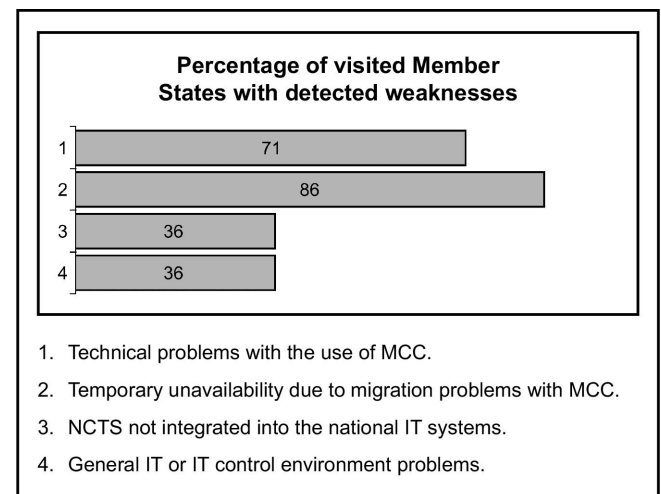
A total of 620 files and 26 transit declarations were examined during the audit.

18. The role of the Commission services was also analysed, especially the coordination and management work done by Taxation and Customs Union Directorate-General (DG TAXUD), the control activities carried out by Budget Directorate-General (DG BUDG) in relation to transit, and OLAF involvement in preventing and fighting fraud.

AUDIT FINDINGS

19. *Annex I* gives an overview of the main weaknesses observed in the countries visited.

Implementation of the new computerised transit system



Appropriate Commission coordination

20. The Commission has coordinated the implementation of the NCTS project in the Member States and put considerable effort into establishing assistance and monitoring tools. The Commission also developed the standard NCTS application MCC (Minimum Common Core), and is responsible for its maintenance. MCC is used by 15 Member States, the other 10 Member States having chosen to develop their own national transit applications.

21. Work has largely been outsourced using the standard tendering procedures. In 2005 the Commission's internal audit service reviewed the organisation, planning and management of the NCTS project and found them very satisfactory. On the other hand, it criticised the fact that no operational agreement existed between the Commission and the Member States regarding the management of critical situations affecting availability and continuity of NCTS.

22. Transit computerisation is required by the legislation, as a general aim of Community Customs Policy ⁽¹²⁾. Commission services have therefore emphasised their role as coordinator of the NCTS project whereas the actual monitoring of NCTS implementation is Member States' responsibility.

23. As part of their coordination activities Commission services have made regular visits to Member States to provide assistance and technical support.

Deficiencies due to the IT environment in the Member States

24. Tests and checking performed by the Commission have not been able to prevent some IT control environment problems.

25. Five of the Member States visited, four of them using MCC, experienced serious compatibility problems when trying to integrate NCTS into their existing national IT environment, e.g. in order to check that every completed transit is followed by another customs procedure, or to use existing risk profiles. Four of them eventually preferred to maintain NCTS as a stand-alone system and did not interface it with their national customs IT systems.

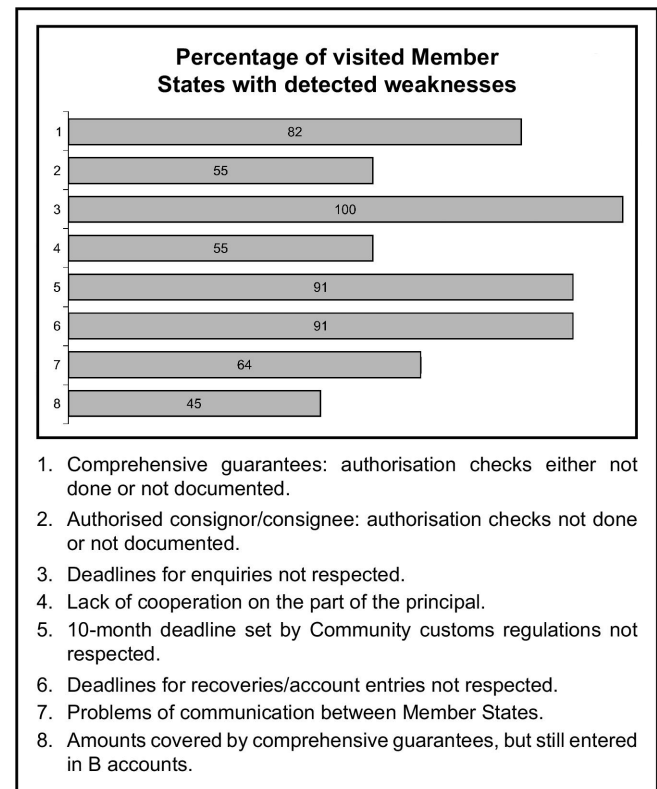
Commission control activities after the legal reform

26. DG TAXUD ensures that Community customs law is uniformly applied by national administrations. DG BUDG carries out regular inspections on traditional own resources, during which compliance with the applicable customs provisions is also checked. DG BUDG also cooperates closely with DG TAXUD on customs policy questions arising from these inspections.

27. Traditional own resources inspections specifically focusing on transit were not made between 2001 and 2005, as the Commission had decided to await the full implementation of NCTS before embarking upon any extensive examination. Nevertheless, the implementation of the core business element of NCTS was operational in June 2003 (see paragraph 12) and the major elements of the legal reform were effective in 2001. Transit is the main subject in DG BUDG's 2006 inspection programme.

⁽¹²⁾ For example Decision No 210/97/EC and Decision No 105/2000/EC of the European Parliament and of the Council of 17 December 1999 (OJ L 13, 19.1.2000, p. 1).

Weaknesses in the application of the new legal provisions



Variations in Member States' application of the revised legal provisions

28. Following the reform of the legal base (see paragraph 11), the Commission specified details of the transit procedures in a handbook agreed by national administrations and available in 19 Community languages, called the Transit Manual ⁽¹³⁾.

29. Member States were still not applying the revised legal provisions correctly: cases of divergence from the provisions in force (some of a formal nature) were found in 392 of the 620 files reviewed during the audit.

Procedure simplifications

30. Economic operators in the European Union most commonly use comprehensive guarantees and the status of authorised consignor/consignee as simplifications of transit procedures. Article 373 of the provisions implementing the Community Customs Code specifies the general conditions governing persons applying for these simplifications (see *Annex II*).

⁽¹³⁾ The Transit Manual was announced in the action plan and developed by DG TAXUD. It consists of detailed provisions for all aspects of the transit procedure, as laid down in Community customs law and dates from the 1 May 2004.

31. Using a comprehensive guarantee makes it possible to cover numerous transit operations with one instrument. The guarantee is applicable up to an average amount of customs duties and charges (the reference amount), which must be reviewed annually by the customs office concerned ⁽¹⁴⁾.

32. Having the status of an authorised consignor with comprehensive guarantee status allows transit operations to be started without the goods being presented at customs. Similarly, an authorised consignee can end a transit procedure without presenting the goods to customs.

33. If a trader wants to benefit from a reduction of the guarantee or a guarantee waiver or wants to transport sensitive goods under the transit system, the reliability criteria applicable are stricter. *Box 1* sets out the criteria which applicants for comprehensive guarantees covering normal and sensitive goods have to meet ⁽¹⁵⁾. Criteria for reduction of comprehensive guarantee or guarantee waiver

34. Apart from the annual review of the reference amount, customs authorities are not obliged to carry out controls after authorisation. The holder of an authorisation is, however, obliged to indicate actively any factor arising which may influence its continuation or content ⁽¹⁶⁾.

Box 1

Criteria for reduction of comprehensive guarantee or guarantee waiver

Criterion	% of guaranteed amount	Normal goods				Sensitive goods			
		100 %	50 %	30 %	Waiver	100 %	50 %	30 %	No waiver allowed
1. Good financial standing	— (**)		✓	✓	✓	✓	✓	✓	
2. Sufficient experience (years) (*)			1	2	3	1	2	3	
3. Very close cooperation with the competent authorities			—	✓	✓	✓ (***)	✓	✓	
4. Control of transport operations			—	—	✓	✓ (***)	✓	✓	
5. Good financial standing, sufficient to fulfil the commitments of the principal			—	—	✓	—	—	✓	

(*) Periods reduced by one year when the principal uses IT techniques to lodge the transit declaration.

(**) No additional conditions.

(***) Either criterion 3 or criterion 4 must be met.

35. In six Member States, Customs could not deliver all the evidence to show that the conditions required for authorised consignor/consignee status had been checked prior to the authorisation. In five of them, Customs had not carried out verifications after authorisation to check whether the beneficiary still met the requirements.

36. As regards the use of comprehensive guarantees, the situation gave cause for concern: in nine Member States, Customs did not have sufficient records proving that the beneficiaries met the required conditions when the authorisation was granted. In four Member States Customs accepted traders' calculations of reference amounts, instead of carrying out the prescribed annual review. In one Member State, traders continued to benefit from guarantee waivers or comprehensive guarantees with reduced

amounts, even when customs authorities had started enforced recovery proceedings against them.

Enquiry proceedings

37. If a transit is not completed by the deadline, enquiries have to be started by the departure country in order to determine whether the transit ended correctly and whether a customs debt has been incurred. The revised provisions implementing the Community Customs Code introduced a considerable shortening of the deadlines for notification of the principal ⁽¹⁷⁾ and for the start of enquiries when computerised procedures are used.

⁽¹⁵⁾ Articles 380 and 381 of Regulation (EEC) No 2454/93, as amended.

⁽¹⁶⁾ Article 377 of Regulation (EEC) No 2454/93, as amended.

⁽¹⁷⁾ The principal is the holder of the transit procedure, Article 96 of amended Regulation (EEC) No 2913/92.

⁽¹⁴⁾ Article 379(2) of Regulation (EEC) No 2454/93, as amended.

38. Notification to the principal and the start of enquiry proceedings now ⁽¹⁸⁾ have to be carried out simultaneously, immediately after the deadline for presentation at destination has expired, if the customs office of destination has not sent the arrival message ⁽¹⁹⁾. This requirement was not respected in any of the Member States visited.

39. In general, national rules have a tolerance of two weeks before enquiry proceedings are started.

40. However, 10 of the 11 Member States visited did not respect their own rules and started enquiries with delays well in excess of two weeks. In some Member States traders did not cooperate properly with Customs, which resulted in delays in clearance which in turn could potentially lead to late recovery of duties.

41. In its annual report on the financial year 1994 the Court pointed out that the recovery procedures should be strengthened by focusing on the principal's obligations and recommended a stronger and more harmonised penalty system.

42. Until the introduction of computerised enquiry handling, the departure country of the transit sent a paper enquiry notice (TC 20) to the country of destination, asking for the specific information needed ⁽²⁰⁾. The customs authorities of the Member State of destination were then required to respond to these enquiry notices without delay ⁽²¹⁾. In nine of the Member States audited, customs authorities reacted late to enquiry notices, or did not communicate the necessary information. In seven of these Member States investigation activities started with delays of several months, as the information forwarded often left unclear whether duties had ultimately been collected. These deficiencies led to late collection of duties.

43. Most Member States visited expected that the introduction of the NCTS enquiry handling module ⁽²²⁾ would solve such problems of communication. This could not be assessed by the Court's audit, as the module had only recently been implemented.

⁽¹⁸⁾ Articles 365(1a) and 366(1) of amended Regulation (EEC) No 2454/93.

⁽¹⁹⁾ Article 366 of Regulation (EEC) No 2454/93, as amended.

⁽²⁰⁾ Specific rules for carrying out the enquiry procedure on paper (e.g. communication between Member States, forms to be used, administrative bodies in each Member State) are specified in part IV of the transit manual.

⁽²¹⁾ Article 366(3) and (4) of amended Regulation (EEC) No 2454/93.

⁽²²⁾ The enquiry handling module of the NCTS project (Phase 3.2.2) was practically implemented in the beginning of 2006 in all Member States. It replaces the paper-based enquiry procedure.

Recovery proceedings

44. Finalised enquiries usually provide the information needed to establish the existence of a customs debt and determine which country has to collect the duties. In case of doubt the revised customs law lays down that the debt must be considered as incurred in the country of departure or entry at the latest 10 months after the goods were placed under a transit procedure ⁽²³⁾.

45. The previous legal provisions dealing with the recovery procedure had already caused application problems in two Member States. The Commission took action against these countries in the European Court of Justice and won the cases ⁽²⁴⁾.

46. Member States interpreted and applied the new provisions in different ways. In ten of the eleven Member States visited, the 10-month deadline was generally not respected, often with considerable delays. In two Member States, Customs awaited the elapse of the 10-month period, although the necessary conditions for the establishment of the debt had been fulfilled long before this deadline. In one of the EU-10, 18 months after accession, almost no recovery action had started for any such cases at the customs offices visited.

47. Community regulations do not specify a precise time limit for the start of recovery proceedings in countries of destination of a transit. However, as soon as customs authorities learn that a customs debt has been incurred in their country following a non-completed transit and they can determine the debtor and the amount of duties, they have a maximum of two weeks to enter the debt in the accounts ⁽²⁵⁾.

48. In the Member States visited such cases were rarely handled speedily, so delaying collection of own resources. In three Member States, consignees of goods had themselves informed the customs authorities and asked for duties to be collected, but the authorities started recoveries only after delays of several months.

49. As already highlighted by the Court in its Annual Report on the financial year 1994 and its Special Report No 8/99 on securities and guarantees ⁽²⁶⁾, Member States reported that the value and commodity code were not always mandatory information on transit declarations under Community regulations and that this often caused delays in recoveries. In two Member States, however, customs authorities required traders to provide such information before starting a transit.

⁽²³⁾ Article 450a of amended Regulation (EEC) No 2454/93 and Article 215(1) third indent of amended Regulation (EEC) No 2913/92.

⁽²⁴⁾ Cases C-460/01 and C-104/02, Judgments of 14 April 2005 (OJ C 132, 28.5.2005, pp. 1 and 2).

⁽²⁵⁾ Article 218(3) and Article 219 of Regulation (EEC) No 2913/92, as amended.

⁽²⁶⁾ Special Report No 8/99 on securities and guarantees provided for in the Community Customs Code to protect the collection of traditional own resources, together with the Commission's replies (OJ C 70, 10.3.2000, p. 1).

Delays in accounting for duties after non-completed transits

50. As with all customs debts discovered after the event the Community Customs Code ⁽²⁷⁾ stipulates that where debts are due on non-completed transit movements these must be entered in the accounts within two days of the date on which the amount of duty and the debtor become known. This time limit may be extended to 14 days in certain cases provided for in the Customs Code ⁽²⁸⁾.

51. In 10 of the 11 Member States visited it was noted that account entries had been made late, after the 14-day deadline. The delays were due to inadequate enquiry procedures. In five Member States account entries were affected by other delays, because of the complexity of recovery procedures. Of the 194 recovery files checked during the audit, 110 were found to have late entries in the accounts.

52. Member States must keep detailed accounts according to the own resources regulation ⁽²⁹⁾. They must aggregate the data arising from individual account entries in the A account, and make the total amounts of duty established, less collection costs, available to the Commission in the second month following the month in which the entitlement was established. As an exception, duty that remains unpaid and unsecured, or is secured but under appeal, need not be made available until it is actually collected. If Member States exercise this option, the duty concerned shall instead be entered in a separate account (the B account) ⁽³⁰⁾.

53. Member States follow different practices for accounting for own resources owed for recoveries after non-completed transits. In one Member State duties on non-completed transits covered by an individual guarantee were entered in the B accounts. Three Member States considered that the actual amount covered by comprehensive guarantees is unknown at the moment when the recovery note is issued and that therefore no amount can be entered in the A account. These Member States entered the full amount of the duties in the B account, i.e. they treated these amounts as if no guarantee had been provided. The same practice was found at customs offices in two further Member States.

⁽²⁷⁾ Article 218(3) of Regulation (EEC) No 2913/92, as amended.

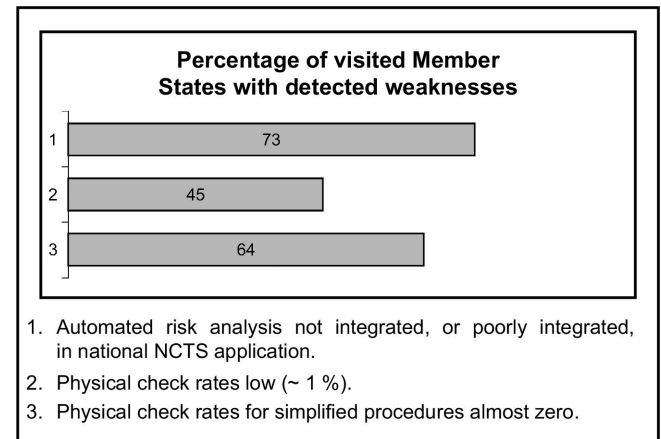
⁽²⁸⁾ Article 219(1) of Regulation (EEC) No 2913/92, as amended.

⁽²⁹⁾ Council Regulation (EC, Euratom) No 1150/2000 of 22 May 2000 implementing Decision 94/728/EC, Euratom on the system of the Communities' own resources (OJ L 130, 31.5.2000, p. 1), as amended.

⁽³⁰⁾ Article 6 of amended Regulation (EC, Euratom) No 1150/2000.

54. In order to eliminate divergent interpretations the Commission stipulated that secured duties be entered in the A account, and others in the B account. In the case of comprehensive guarantees Member States did not always follow the Commission's interpretation. As a consequence, the Commission started proceedings before the European Court of Justice concerning the proper accounting treatment of secured duties.

Necessity of stepping up the fight against fraud and enhancing risk management



Limited data reliability and completeness

55. NCTS impedes certain forms of fraud, such as the use of forged or false stamps or guarantee certificates, and allows the enquiry process to be speeded up in cases where transits are not completed. However, computerisation cannot prevent misdescription or intentional false declarations that seek to abuse the system.

56. An assessment of the effectiveness of the reform of the transit system, in terms of reducing transit fraud, would require reliable and complete data on fraud at EU level. The audit showed, however, that the reliability and completeness of the available main sources of data on fraud and irregularities in transit at EU level cannot be assured.

NCTS data

57. The Commission carries out continuous analysis of non-completed NCTS transit movements. The data available showed a reduction by half between 2004 (2,5 %) and 2005 (1,2 %). However, this analysis of NCTS transits ignores those taking place on the territory of a single Member State ⁽³¹⁾, although such transits account for a considerable number of all NCTS movements.

⁽³¹⁾ Except for Austria and Finland.

OWNRES data

58. The OWNRES database contains data on cases of fraud and irregularities relating to own resources and involving amounts in excess of 10 000 euro communicated to the Commission (DG BUDG) by Member States under the own resources regulation ⁽³²⁾.

59. Despite the Commission's efforts to improve the quality of the OWNRES data, it is still not adequate. Nevertheless the OWNRES data are the only source used in the recent Commission annual reports on the fight against fraud and show, in contrast to other sources, an increase in the number and value of cases of fraud and irregularities reported for the transit area between 2001 (year of the legal reform) and 2005. Further measures will be necessary to establish a reliable source of information for analysis of fraud in the various Community customs procedures.

Early warning system (EWS)

60. The early warning system (EWS) was introduced in 1992 using the concept of sensitive goods (see paragraph 11). The practical operation of the EWS is similar to NCTS: the office of departure sends a prior arrival notification of transits referring to sensitive goods to the office of destination and the office(s) of transit, as appropriate, and to OLAF.

61. According to OLAF the percentage of non-arrival communications as notified by Member States in the years 2004 and 2005 was 20 times lower than in the first quarter of 1998 alone.

62. However, because of the introduction of NCTS and the similarity of the information to be put onto the two systems, Member States apparently consider that NCTS is sufficient and have stopped inputting data to the EWS. OLAF, however, has no access to the data contained in NCTS transit declarations. A revision of the administrative arrangements was adopted in January 2006 in order to provide OLAF with access to data concerning movements of sensitive goods from 2007 onwards.

Shortcomings in risk management and analysis of fraud-related aspects

63. A proper balance between trade facilitation and effective protection of the Community's financial interests calls for appropriate risk management and risk-based checking of transits.

⁽³²⁾ Article 6(5) of amended Regulation (EC, Euratom) No 1150/2000.

64. The Court found that transit risk analysis was still rudimentary in many Member States. Only one country applied random selection by the IT system in order to maintain an uncertainty factor for all traders. Only three of the eleven Member States visited applied automated risk analysis integrated into NCTS with specific risk profiles for transit. Customs authorities in these three Member States considered the fact that the commodity code was not compulsory for transit declarations was a serious obstacle to the implementation of effective checks on transits. The Court's Special Report No 8/99 pointed out that checks by Community customs authorities were hampered by the absence of provisions requiring information on the nature and value of goods to be included in the single administrative document.

65. Identification of risks and checks on goods still depend on the personal initiative of individual customs officers. Most of the Member States visited considered checks on transit consignments as low priority, partly because of the scarcity of information on transit declarations. In five Member States the Court found particularly low rates of physical checks on transit consignments (around 1 %), while almost no checks were made on authorised consignors/consignees in seven of the eleven Member States visited.

66. NCTS provides the Commission with statistical data on the number and status of transits and the countries involved, but not with goods or trader-related data that might allow more refined analysis. Moreover, the Commission services have not so far carried out analyses of transit fraud patterns, undertaken intelligence activities in the same area, nor yet developed transit-specific risk analysis tools.

CONCLUSIONS AND RECOMMENDATIONS

67. The Commission has put in place the key elements of the action plan for transit and in particular has computerised the transit procedure and concluded a reform of the legal base (effective in 2001).

68. The Court's audit work on Community transit has confirmed the good quality of NCTS implementation, even though some technical problems still persist. It has also identified certain shortcomings in the application of legal provisions on transit and related provisions on traditional own resources. At both Community and national level, deficiencies were also found in the measures designed to counteract fraud in transit.

Implementation of NCTS

69. The Commission has successfully coordinated the implementation of the NCTS project in the Member States. However the IT environment in some Member States has not allowed the system to operate optimally (see paragraphs 20 to 25).

The Commission should:

- (a) consider establishing an operational agreement with Member States for the management of NCTS, namely for critical situations affecting business continuity;
- (b) in addition to acting as coordinator, enhance monitoring activities, especially as regards the IT control environment affecting NCTS in the Member States.

Application of the new legal provisions

70. As of the end of 2005, the Commission had not carried out any specific inspection activity on transit in order to assess whether the legal reform concluded in 2001 was being implemented effectively (see paragraphs 26 and 27).

71. Member States often did not apply the revised provisions correctly. The Community customs regulations provide that transit procedure simplifications may only be authorised for reliable traders who meet specific criteria. The audit detected a lack of checks on compliance with these criteria — this could potentially harm the Community's financial interests (see paragraphs 30 to 36). The enquiry procedure was found to be cumbersome and Member States had neither applied the regulations in force, nor shown the necessary diligence once an enquiry had been launched. Implementation of the new NCTS procedures is too recent for their impact to be measured (see paragraphs 37 to 43). Lastly, recovery proceedings were often started late, with the result that traditional own resources were not collected or made available at the proper time (see paragraphs 44 to 49).

72. The late entering of non-completed transits in the traditional own resources accounts was linked to variations in the accounting procedures applied or, quite simply, to incorrect application of the regulations, particularly as regards guarantees (see paragraphs 50 to 54).

The Commission should consider the shortcomings detected by the Court's audit when it drafts implementing rules on authorised economic operator status ⁽³³⁾.

As regards enquiry procedures, the Commission should:

- (a) ensure that computerised handling of enquiry procedures does indeed lead to faster settlement of non-completed transits, as well as improving communication between Member States. It should also take remedial action, if that is necessary;

- (b) propose the application of sanctions against traders who obstruct enquiry proceedings.

As regards recovery procedures, the Commission should:

- (a) develop inspections in Member States and target them on recovery proceedings after non-completed transits;
- (b) clarify the interpretation of the legal provisions on recoveries in relation to transit and propose an amendment of customs law so as to shorten the ten-month time limit and facilitate recoveries after non-completed transits by making indication of necessary particulars such as commodity code and goods value mandatory on transit declarations.

Lastly, in the case of the guarantee system, the Commission should:

- (a) continue its efforts to obtain correct and consistent application of the rules for the treatment of duties covered by guarantees;
- (b) reinforce inspections in Member States in order to ensure that legal provisions are correctly and uniformly applied.

Fight against fraud and risk management

73. The sources of information available to the Commission regarding transit fraud are still not reliable enough to allow an assessment of the part played by the legal reform and the NCTS project in terms of fraud reduction and analysis of the cases presumed to follow it (see paragraphs 55 to 62).

74. Commission services have not yet carried out analyses of transit fraud patterns nor developed transit-specific risk analysis tools. Systematic risk management for transit is rudimentary or non-existent in many Member States and only a few of them have risk profiles integrated into NCTS. The number of physical checks on transit consignments is very low in some Member States, and in some they are non-existent (see paragraphs 63 to 66).

The Commission should take measures to improve the reliability of sources of information on fraud, and should make better use of them by developing risk management strategies.

The Commission should consider promoting a reasonable rate of targeted physical checks on transit consignments and should also consider the possibility of building automated risk profiles specifically for transit, as part of the development of the common risk management framework ⁽³⁴⁾.

⁽³³⁾ Article 1(2) of Regulation (EC) No 648/2005 of the European Parliament and of the Council of 13 April 2005 amending Council Regulation (EEC) No 2913/92 of 12 October 1992 establishing the Community Customs Code (OJ L 117, 4.5.2005, p. 13).

⁽³⁴⁾ Article 1(3) and Article 2 of Regulation (EC) No 648/2005.

This report was adopted by the Court of Auditors in Luxembourg at its meeting of 14 December 2006.

For the Court of Auditors
Hubert WEBER
President

ANNEX I

OVERVIEW OF OBSERVATIONS FOR THE 11 MEMBER STATES VISITED

	DE	ES	FR	IT	BE (*)	LV (*)	HU (*)	NL (*)	PL (*)	SI (*)	SE (*)
Implementation of NCTS											
Technical problems with the use of MCC					X	X		X		X	X
Temporary unavailability due to migration problems with MCC					X	X	X	X		X	X
NCTS not integrated into the national IT systems			X			X		X			X
General IT or IT control environment problems			X	X	X				X		
Application of legal provisions and legal reform											
Comprehensive guarantees: authorisation checks either not done or not documented	X	X	X	X	X		X		X	X	X
Authorised consignor/consignee: authorisation checks either not done or not documented	X	X	X				X			X	X
Deadlines for starting enquiries not respected	X	X	X	X	X	X	X	X	X	X	X
Lack of cooperation by the principal	X		X	X		X	X			X	
10 month deadline not respected	X	X	X	X	X	X	X		X	X	X
Deadlines for recoveries/account entries not respected	X	X	X	X	X	X	X		X	X	X
Problems of communication between Member States	X	X	X	X		X				X	X
Amounts covered by comprehensive guarantees, but still entered in B accounts	X	X	X		X		X				
Fight against fraud and risk management											
Automated risk analysis not integrated, or poorly integrated, into the national NCTS application	X				X	X	X	X	X	X	X
Physical check rates low (~ 1 %)		X	X		X	X					X
Physical check rates for simplified procedures almost zero	X	X	X	X	X	X					X

(*) Country using MCC.

ANNEX II

Box 2: Article 373 of the Provisions for the implementation of the Community Customs Code

1. The authorisations referred to in Article 372(1) shall be granted only to persons who:
 - (a) are established in the Community, with the proviso that authorisation to use a comprehensive guarantee may be granted only to persons established in the Member State where the guarantee is furnished,
 - (b) regularly use the Community transit arrangements, or whose customs authorities know that they can meet the obligations under the arrangements or, in connection with the simplification referred to in Article 372(1)(f), regularly receive goods that have been entered for the Community transit procedure, and
 - (c) have not committed any serious or repeated offences against customs or tax legislation.
2. To ensure the proper management of the simplifications, authorisations shall be granted only where:
 - (a) the customs authorities are able to supervise the procedure and carry out controls without an administrative effort disproportionate to the requirements of the person concerned, and
 - (b) the persons concerned keep records which enable the customs authorities to carry out effective controls.

THE COMMISSION'S REPLIES

SUMMARY

I.-II. The Commission strengthened customs transit by introducing a modern and robust computerised system throughout the Community.

III.

- (b) According to provisional findings from the Commission's recent inspections, the application of certain simplifications has already improved in some Member States. As regards enquiries and recoveries the Commission is examining ways to streamline the procedure.
- (c) The follow-up of undischarged operations has been examined during inspections of Member States' B accounts. Where administrative delays resulted in traditional own resources being made available late Member States were or are being requested to make further investigations and to pay interest on the delays found. Should they not comply then infringement procedures will follow.
- (d) Based upon its risk analysis, the Commission decided to defer any wide-ranging inspections of transit until the NCTS system was fully implemented, to allow conclusions to be drawn about its effectiveness throughout the full range of its capabilities.
- (e) The adoption and implementation of Regulation (EC) No 648/2005 will oblige Member States to use risk analysis for targeting customs controls.
- (f) The Commission obtains information on suspected fraudulent activity from a variety of sources. Overall, the indications are that transit fraud has declined.

IV. The Commission is taking the necessary steps to have access to NCTS data which will provide an overview of the consolidated traffic routings of sensitive goods in transit and also enable strategic and operational analysis to be carried out for such goods.

AUDIT FINDINGS

20. As regards the coexistence of MCC (minimum common core) and national applications, the latter also had to be based on the agreed functional and technical specifications which are common to all Member States.

21. An operational agreement with Member States was adopted in July 2006.

24. The Member States are responsible for the operation of their national transit application systems and the Commission has no mandate and no resources to perform IT audits of the national systems. However, the Commission spent considerable effort in providing support to and co-ordinating the development projects of the National Administrations (NAs) and is now reviewing periodically the quality of services provided by the NAs.

25. In the beginning of the NCTS project several Member States not wishing to develop a national transit application requested the Commission to produce a standard one. MCC as supplied by the Commission is a stand alone application. Member States were thus free to choose between developing a NCTS

application for themselves with consequent advantages for integrating that with their existing systems or using the MCC stand alone application supplied by the Commission. During its 2006 inspections of transit the Commission is examining whether Member States have suitable procedures in place to control goods moving from transit into other customs regimes and also goods moving from another regime into transit. The systems used by Member States may be effective, even if they are not fully integrated.

27. The legal reform of transit was progressive, starting in 1994. The Commission featured transit in its inspection programmes for 1996, 1997 and 2000. Thereafter in view of its limited resources for inspections the Commission decided to defer further extensive inspections until it would be able to gauge whether NCTS was actually delivering the expected benefits. Some specific aspects of transit were however pursued usually as part of other themes.

29. The Commission will examine the Court's findings in detail, together with those from its own inspections, and draw Member States' attention to areas of non-compliance which need to be remedied. Where divergences from the legal requirements have led to losses to the Community budget Member States have been or will be required to make the own resources available and pay interest.

35. The Commission too has identified instances of incomplete records of pre-authorisation checks in these Member States and has stressed the potential financial consequences that could arise from not fully complying with Community legislation.

36. The Member States concerned will be reminded of the importance of documenting pre-approval checks and reviews. The fact that enforced recovery might be started against an economic operator does not automatically mean that facilitations granted should be withdrawn. Member States need to judge each case on its merits. Should an incorrectly granted reduced guarantee or guarantee waiver lead to an identified loss to the Community budget the Member State concerned will be required to make the own resources concerned available together with interest on any delay involved.

38. The Commission similarly has found, in its inspections, that enquiries rarely begin immediately. An expert group on the end and discharge of transit operations including the enquiry and recovery procedures has been set up to report by the end of 2006. Any resultant proposals for change will be pursued during 2007.

41. Should principals not cooperate, administrations already have the means to deny or withdraw transit simplifications such as the comprehensive guarantee or a reduction granted in the reference amount. With the reform, customs were specifically given the possibility of initiating recovery, independently of the degree of cooperation of the principal. Further sanctions and penalties currently fall under the competence of Member States although the Commission proposal for a Modernised Customs Code ⁽¹⁾ provides for a framework of convergence.

42. The paper based enquiry procedure suffered from delays. The electronic NCTS 'enquiry handling' module introduced in January 2006 was designed to remedy this. Findings from current inspections indicate it is doing so. In any event the law sets down a time limit by which the office of departure must take action to establish the debt. The Commission will follow up those cases identified by the Court where economic operators have themselves notified the receipt of goods and prompt action to ensure the goods were declared for another customs regime did not apparently follow.

43. The Commission's own inspections are still ongoing but the indications are that cases entering the enquiry procedure are being resolved more quickly.

45. The European Court of Justice (ECJ) gave judgment in a number of cases dealing with the precise effect of various provisions for dealing with undischarged movements (including those

under the TIR convention) in October 2006. In the three judgments which have implications for current legislation the ECJ confirmed the Commission position ⁽²⁾.

46. The Commission too has often found that despite the clear legal provisions Member States have belatedly established debts on undischarged transit operations. Action has been taken to get the own resources involved made available and interest has been charged on delays. Where the delays have appeared systematic Member States have been required to make further investigations to identify any further instances. The Commission will be taking action on the cases the Court has identified in the three Member States.

48. The cases raised by the Court which have an effect on traditional own resources will be followed up with the Member States concerned.

49. The commodity code in transit declarations is mandatory for sensitive goods (see Court's footnote 9) and in certain other cases ⁽³⁾. When value and commodity code are not in a transit declaration for an operation the necessary information to calculate the customs debt is usually obtained as part of the enquiry procedure. Should this not happen the customs debt is normally calculated on the basis of the highest tariff.

51. The Commission will follow up the Court's findings with Member States.

53.-54. The law on how the secured portion of debts should be accounted for is clear — it must be entered in the A account unless a written appeal which might change the amount of the debt has been received before it falls due to be made available. If these latter circumstances apply it may instead be entered in the B account. Despite this clarity and all Member States having been advised of the correct practice the Commission is aware that some customs offices have been treating guaranteed debts incorrectly and that in three Member States they were systematically entered in the B account. Recent judgments of the European Court of Justice against two of these Member States ⁽⁴⁾ have confirmed that this was not in accordance with the law. Action is now underway to make sure that all Member States are aware of the Court judgments and to collect any amounts of traditional own resources not made available plus interest on any delays involved.

⁽²⁾ Cases C-105/02, C-377/03 and C-275/04, judgments of 5 October 2006.

⁽³⁾ Whenever the transit declaration is made by the same person at the same time as, or following, a customs declaration which includes the commodity code and whenever Community legislation so requires.

⁽⁴⁾ C-105/02, C-377/03.

⁽¹⁾ COM(2005) 608 final of 30 November 2005.

56. The reliability and completeness of data at EU level depend on the correct application by Member States of the legal requirements and procedures for reporting fraud and irregularities, as specified by Regulations (EC) No 515/97 and (EC) No 1150/2000. The OWNRES data does not necessarily reflect the trend in transit frauds and irregularities, when compared to data from other available sources and indicators (mutual assistance communications, customs information system, EWS). For instance, since 2001 OLAF has dealt with very few cases of transit fraud. This decreasing trend is also evidenced by the declining number of mutual assistance (MA) messages for transit fraud issued by the Office (from an average of 35 % of the total yearly number of MA messages issued at the beginning of the 1990's, down to less than 3 % since 2001) and the absence of operational cases related directly to transit movements in the Customs Information System (CIS). To date, only one CIS case out of 620 concerns transit.

57. The Commission considers it important to analyse the situation of open movements. It concentrates this analysis on the international ones as this was the only independent data available from the common gateway.

59. As stated in recent Commission annual reports on the fight against fraud, the OWNRES data is not considered to reflect the real trend in transit fraud. The data conflicts with other available indicators (EWS, mutual assistance communications, CIS), see also the reply to paragraph 56. The Commission notified the budgetary authority in 2004 that OWNRES was not a reliable source of information as the data Member States were recording was neither complete nor up-to-date. Member States have been urged to improve their performance and have been taking action. There have been major improvements in reporting with the latest results showing OWNRES and B account data currently being 90 % comparable. The Commission will continue to monitor Member States' performance.

64. With the adoption and implementation of Regulation (EC) No 648/2005 a clear legal basis for customs controls based on risk analysis will become a reality and a legal obligation for the Member States (Article 13 of Regulation (EEC) No 2913/92 as amended by Regulation (EC) No 648/2005). It is more efficient to work with clear and well tailored profiles and common criteria and priority areas of controls rather than to introduce from the beginning minimum rates of controls that might lead to a diversion of resources from sensitive consignments to non-sensitive ones just to meet the minimum control rate. Nevertheless, the Commission does not exclude that based on experience it might further develop the legislation.

As regards the commodity code, please see the Commission's reply to paragraph 49.

65. The Commission is currently proposing that the selection of consignments for control should include a random element. In addition common priority control areas — to be subject

to increased levels of customs controls during a particular period based on risk analysis using common criteria — are to be agreed with the Member States under the committee procedure. The Court's concerns and recommendations will be raised in the Code Committee.

66. Currently the Commission has no access to the data, it can only see the envelope of the message, not the content. However, the Commission is taking the necessary steps to have access to NCTS data which will provide an overview of the consolidated traffic routings of sensitive goods in transit and also enable strategic and operational analysis to be carried out for such goods.

CONCLUSIONS AND RECOMMENDATIONS

68. The Commission will follow up the technical problems and shortcomings identified by the Court on a case by case basis, particularly when financial consequences are to be drawn, and will monitor the situation as well as encourage administrations to apply the provisions correctly.

To this end it will make sure that the legal provisions are clear and unambiguous and if necessary propose modifications. It will give further detailed guidance on how certain provisions should be applied by means of administrative arrangements, such as the Transit Manual. Should doubts persist the Commission will offer a platform to clarify these.

Ultimately the Commission will consider infringement procedures against Member States in duly justified cases of non or incorrect application of Community legislation.

Please also see reply to paragraph 66.

69.

- (a) As recommended by the Court a detailed operational agreement has already been adopted in July 2006 to cover critical situations affecting the availability and continuity of NCTS.
- (b) Monitoring of the operation of NCTS has been enhanced and will be further improved during 2007, please see also reply to paragraph 24.

70. The Commission decided to defer any wide-ranging inspections of transit until all aspects of the NCTS system were fully implemented to allow conclusions to be drawn about its effectiveness.

71. The Commission too has found some Member States unable to show after the event that all the necessary checks on a business' suitability for being granted simplified procedures had been made. However, the potential damage to the Community budget is limited: were incorrectly granted guarantees to prove insufficient then the Member State concerned would be liable for its own resources lost and where appropriate for interest too.

The previous paper-based enquiry procedure suffered from too many cases which appeared undischarged because of transmission delays and other problems inherent to the procedure. NCTS is tackling the overload. Furthermore a review by an expert group is in progress (see reply to paragraph 38).

Where during its routine inspections or as a result of Court activity the Commission finds delays in making traditional own resources available Member States are required to pay any own resources due plus where appropriate interest on delays. Where there is evidence that the failure was systematic then Member States are required to investigate all such instances and to make the necessary financial corrections.

72. Where appropriate the Commission has taken action to ensure that Member States compensate the Community budget for any amounts of own resources which should have been made available but were not because Member States did not take timely action on apparently undischarged transit movements.

The Commission has taken account of shortcomings found in various areas when drafting the implementing rules for authorised economic operator (AEO) status. Further account will be taken when producing the AEO guidelines. Article 14q of the Implementing Provisions to Regulation (EC) No 648/2005 foresees that, once the status of AEO has been granted, the customs authorities shall monitor AEO compliance with the conditions and criteria set. Furthermore, continuation of the status shall be reassessed by the customs authority which granted it whenever the relevant Community legislation changes or when that authority has reasonable indication that the relevant conditions are no longer met.

As regards enquiry procedures:

- (a) The Commission can confirm that computerisation of the enquiry procedure is already contributing to the speedier handling of enquiries. Remedial action will be taken where necessary and a separate review of the enquiry procedure is underway as stated in reply to paragraph 71. One of the Commission's objectives is to shorten the time limits following the introduction of NCTS.
- (b) With the reform, customs were specifically given the possibility of initiating recovery, independently of the degree of cooperation of the principal. Sanctions and penalties currently fall under the competence of Member States although the Commission proposal for a modernised customs code provides for a framework of convergence (see paragraph 41).

As regards recovery procedures:

- (a) This recommendation is implemented by the 2006 inspection programme the main theme of which was transit. The overall objective for those inspections included checking that Member States' procedures for following-up any undischarged operations comply with the relevant regulations and that Own Resources have been properly calculated, established and accounted for.
- (b) The Commission has examined the question of making the commodity code and goods value mandatory in all transit declarations (i.e. in addition to the cases referred to under point 49). Since in transit the declarant is often not the exporter nor the importer particular attention has to be given to the additional cost for the operator to provide this type of information and to offset this against the limited number of recoveries that are initiated by customs. On balance, the Commission is of the opinion that, for the purpose of transit, this type of information need not be required for all transit declarations and that, provided that customs diligently carries out the enquiry procedure, the appropriate amount of duty will be recovered. See also reply to paragraph 72(a).

As regards the guarantee system:

- (a) The Commission will continue to monitor Member States' procedures.
- (b) The Commission will continue to select the themes for its compliance inspections in Member States by risk analysis. Prior to 2006 transit was a candidate for inspection but was not selected for examination because we wished to await fuller implementation of NCTS. For 2007 the Commission considers it is likely that there will be further inspection activity concerning transit.

73. The Commission obtains information on suspected fraudulent activity from a variety of sources. Overall, the indications are that transit fraud has declined.

74. With the adoption and implementation of Regulation 648/2005 a clear basis for customs controls based on risk analysis will become a reality and a legal obligation for the Member States (Article 13 of Regulation (EEC) No 2913/92 as amended by Regulation (EC) No 648/2005).

The RIF (Risk Information Form), a central component in the development of a common risk management framework required by Council Regulation (EC) No 648/2005 which facilitates the exchange of risk information among Member States on customs control issues including transit is already in operation.