OPINION OF ADVOCATE GENERAL TESAURO

delivered on 23 February 1995 *

1. The present proceedings are concerned with the customs rules on inward processing arrangements, in particular the provisions governing the discharge of those arrangements by placing of the goods under the system of processing under customs control.

More specifically, the preliminary questions concern the interpretation of Article 18(2)(d) and the first paragraph of Article 18(3) of Council Regulation (EEC) No 1999/85 of 16 July 1985 on inward processing relief arrangements [1] (hereinafter 'the basic regulation'), which makes the transfer of goods from inward processing arrangements to the system of processing under customs control subject to the grant of an authorization by the competent authorities. The Bundesfinanzhof asks the Court to define the scope of that authorization in order to enable it to decide whether, under the Community legislation, it should, or may, be subjected to quantitative limits.

2. The main proceedings are between Temic Telefunken Microelectronic GmbH (hereinafter 'Temic'), a German company which imports and manufactures electronic components, and the Hauptzollamt (Principal Customs Office), Heilbronn, the competent German customs authority (hereinafter 'the Hauptzollamt'). In January 1991 the Hauptzollamt had granted to Temic an authorization for inward processing, under the suspension system, of unmeasured integrated circuits from the Far East. The processing of those products by Temic consists in testing ('measuring') them, after which the usable circuits are identified and separated from those which are defective. The usable circuits (hereinafter 'A goods') are for the most part intended for re-export from the customs territory of the Community. For the unusable circuits (hereinafter 'B goods'), Temic had sought and obtained, in August 1991, authorization for them to be placed under the system of processing under customs control, for the purpose of recovering the precious metals they contained. The second authorization, however, was granted by the Hauptzollamt only for a quantity of B goods proportional to the quantity of A goods actually re-exported. And it was against that limitation that Temic commenced legal proceedings, claiming that it was entitled to an authorization without any quantitative limits.

The legislative background

3. The situation with which the main proceedings are concerned, which arose before

* Original language: Italian.

1 — OJ 1985 L 188, p. 1.

the entry into force of the Community customs code, [2] is covered by the basic regulation, supplemented by Council Regulation (EEC) No 3677/86, [3] of 24 November 1986 laying down certain provisions for the implementation of the basic regulation (hereinafter 'the supplementary regulation') and Commission Regulation (EEC) No 2228/91 [4] of 26 June 1991, which lays down other provisions applicable to the basic regulation (hereinafter 'the implementing regulation').

Pursuant to Article 1(2) of the basic regulation, the inward processing arrangements make it possible, after the relevant authorization has been obtained, for the following goods to be used in the customs territory of the Community in one or more processing operations: (a) non-Community goods intended for re-export outside the Community in the form of compensating products, such goods not being subject to import duties (the suspension system); (b) goods released for free circulation with refund or remission of the import duties levied on such goods if they are re-exported outside the Community in the form of compensating products (drawback system).

4. Article 1(3)(i) of the basic regulation defines compensating products as all products resulting from processing operations, whilst Article 1(2) and (3) of the supplementary regulation and Article 1(2) and (3) of the implementing regulation state that compensating products comprise 'main' products, for the production of which use of the inward processing arrangements was authorized, and 'secondary' products, being products other than main products which 'are a necessary by-product of the processing operation'.

The processing operations, as defined in Article 1(3)(h) of the basic regulation, are the working, processing and repair of goods, including the use of certain goods which allow or facilitate the production of compensating products and are used up in the process. Moreover, according to Article 6(3)(b) of the basic regulation, and Article 26(1)(b) of the implementing regulation, processing operations may also involve 'the usual handling operations to which goods may be subject in pursuance of Community provisions on customs warehousing and free zones'. Those provisions [5] include under the heading

2 — Council Regulation (EEC) No 2913/92 of 12 October 1992 establishing a Community customs code (OJ 1992 L 302, p. 1).

3 — OJ 1986 L 351, p. 1.

4 — OJ 1991 L 210, p. 1.

5 — See in particular Article 18(1) of Council Regulation (EEC) No 2503/88 of 25 July 1988 on customs warehouses (OJ 1988 L 225, p. 1); Article 34(1) and Annex IV of Commission Regulation (EEC) No 2561/90 of 30 July 1990 laying down provisions for the implementation of Council Regulation (EEC) No 2503/88 and customs warehouses (OJ 1990 L 246, p. 1); Article 8(a) of Council Regulation (EEC) No 2504/88 of 25 July 1988 on free zones and free warehouses (OJ 1988 L 225, p. 8); and Article 20(1) of Commission Regulation No 2562/90 of 30 July 1990 laying down provisions for the implementation of Council Regulation (EEC) No 2508/88 on free zones and free warehouses (OJ 1990 L 246, p. 33).

of inward processing 'any operation carried out manually or otherwise on goods entered for the arrangements with a view to preserving them, improving their presentation or merchantable quality or preparing them for distribution or resale.'

5. Article 18 of the basic regulation governs final discharge of inward processing relief arrangements. In addition to the re-export of compensating products (Article 18(1)), provision is made for other cases of discharge, including the placing of compensating products under the system of processing under customs control (Article 18(2d)). Discharge on that basis is subject to authorization from the customs authority, which 'shall grant this authorization where circumstances so warrant' (Article 18(3)).

Article 20 of the basic regulation lays down the principle that, where a customs debt is incurred, its amount is to be determined on the basis of the taxation elements appropriate to the import goods at the time of the declaration of placing the goods under inward processing relief arrangements. However, that principle is subject to certain exceptions, including the following: application of the duties payable ('appropriate to them') on the compensating products released for free circulation which appear on the list adopted in accordance with a special procedure, [6] but only 'to the extent that they correspond proportionally to the exported part of the compensating products not included in that list' (Article 21 (1)(a), first indent); [7] (b) application of customs duties calculated in accordance with the rules of the system for compensating products which are subject to a different customs procedure (Article 21(1)(b)). [8]

6. Also relevant, in so far as they apply to goods transferred to the system of processing under customs control, are certain provisions of the regulations which established that system. [9] In particular, it should be noted that, under the rules on processing under customs control, it is possible, after obtaining the appropriate authorization, to

6 — The list was adopted under the special procedure provided for in Article 31(2) and (3) of the basic regulation, and appears in Annex VI to the supplementary regulation; it is clear from the list as presently drafted, and from the scheme of the provision, that the products concerned are essentially secondary compensating products.

7 — The holder of the authorization is nevertheless entitled to request taxation of those products under Article 20 where the provisions of that article would be more advantageous.

8 — In the present case, the relevant regulations are those mentioned in footnote 6.

9 — In particular, Council Regulation (EEC) No 2763/83 on arrangements permitting goods to be processed under customs control before being put into free circulation (OJ 1983 L 272, p. 1) and Commission Regulation (EEC) No 3548/84 of 17 December 1984 laying down certain provisions for the application of Regulation (EEC) No 2763/83 on arrangements permitting goods to be processed under customs control before being put into free circulation (OJ 1984 L 331, p. 5).

process non-Community goods without paying customs duties within the Community customs territory; the goods obtained from the processing may then be released into free circulation and subjected to the duties appropriate to them.

It is therefore necessary to establish whether a quantitative limit such as that imposed on Temic is compulsory, according to the proper construction of the Community legislation described above, or, in the alternative, whether it is lawful. It is, I think, appropriate to deal with the three questions at the same time.

The preliminary questions

7. The preliminary questions submitted by the Bundesfinanzhof are all intended to establish whether the authorization issued in August 1991 by the Hauptzollamt to Temic for placing of B goods under the system of processing under customs control was lawfully limited in proportion to the quantity of A goods re-exported.

More specifically, the national court asks the Court of Justice to state: (a) whether Article 18(2)(d) and the first paragraph of Article 18(3) of the basic regulation must be interpreted as meaning that discharge of the arrangements by an authorization for processing under customs control may be made subject to quantitative limits; (b) whether the concept of 'circumstances' warranting the issue of the authorization Article 18(3) must be interpreted as meaning that it is compulsory to limit the said authorization in proportion to the quantity of products re-exported (in accordance with Article 21(1)(a), first indent, of the basic regulation); and (c) whether such a limitation is permitted, even if not compulsory.

8. The inward processing system was established essentially in order to avoid any imbalances which might affect undertakings exporting products from the Community as a result of the application of customs duties and other commercial policy measures to raw materials from non-member countries. The system allows temporary importation of goods intended to be processed and then re-exported, with a remission or refund of customs duties.

The system in question is therefore designed, and ordinarily used, for the purpose of processing within the Community raw materials which are then re-exported (or forwarded to another authorized customs location) in the form of main compensating products. The latter products usually have added commercial value and, after processing, have reached a subsequent (and sometimes final) stage in the production process. The added value is a direct consequence of the physical treatment which the products receive in the course of

processing. The processing usually gives rise to residual materials — rejects, waste — of limited commercial value; in fact, they constitute secondary compensating products, which it is permitted *inter alia* to release for free circulation against payment of the duties applicable to the products when classified as residues, which almost always proves more advantageous than re-export.

The typical case envisaged, therefore, is use of the system for processing of a raw material, by means of operations (working, transformation, repair, handling and so forth) which make it into a product of greater commercial value (main compensating product) and at the same time give rise to waste materials (secondary compensating products). However, both the first and the second types of product are usually contained in the raw material at the previous stage of processing. [10]

9. However, the present case does not appear to fall within the circumstances just described. Here, there seems to be no doubt that the product intended for processing is an electronic component already assembled in the country of origin. The processing consists of testing (described in the order for reference as 'measuring') which involves no change to, or physical processing of, the product. The testing only makes it possible to identify the components which are (already) operational (A goods) and those which are (already) unusable (B goods). Residual materials do not arise from that operation, nor can the B goods strictly be regarded as such, in that they do not derive from processing, even though the processing enables them to be identified.

However, the fact that Temic's integrated circuits were placed under inward processing arrangements is not disputed by either of the parties and is confirmed by the Commission. The testing carried out on the goods is therefore to be regarded as constituting processing, on the basis of a truly broad interpretation of the provisions referred to by Article 6(3)(b) of the basic regulation and Article 25(1)(b) of the implementing regulation, cited above: 'usual handling' or 'any operation' carried out on goods 'preparing them for distribution or resale'.

If, therefore, testing constitutes processing, the result of that operation is the identification of two categories of products: usable products (A goods), which represent the main compensating product; and unusable products (B goods), representing the secondary compensating product.

10 — See, for example, the list of secondary compensating products contained in Annex VI to the supplementary regulation, cited above, which contains 138 items.

10. Against that background, we come to the essential issue in the case, namely the scope of the authorization referred to in Article 18 of the basic regulation.

That provision, in providing as a possible alternative way of discharging the inward processing arrangements, for, *inter alia*, placing of the compensating products under the system of processing under customs control, requires that in such cases an appropriate authorization be granted by the competent authority. Also, under that provision, the authorizations are to be granted 'where circumstances so warrant'.

11. It is common ground that the provision imposes no obligation on the customs authority to grant the authorization in question only for a quantity of goods proportional to the quantity of goods re-exported. Still less does the provision explicitly entitle the authority to do so.

The all too broad formulation of the last sentence of paragraph 3 ('shall grant this authorization where circumstances so warrant') relates to the conditions for issue of the authorization, but neither requires nor expressly allows it to be limited quantitatively by reference to any particular criterion. The authorization therefore appears, at least where the relevant conditions are fulfilled, to constitute an unconditional measure.

12. The preliminary problem therefore arises of establishing, in the absence of an express provision, what those conditions are. In other words, it is necessary to ask of what conditions the competent authority must verify fulfilment before granting the authorization.

I think it is reasonable in that connection to say that the circumstances are the same as those which must exist for goods to qualify in general for the system of processing under customs control, as indicated in Article 4 of Regulation No 2763/83. [11] The conditions are of a personal and substantive nature, being intended to ensure that application of the system does not lead to an unjustified advantage for the holder of the authorization at the expense of Community producers of competing goods and of the finances of the Community. There is no reason to conclude that those conditions should not necessarily exist, as a pre-condition for eligibility, even where the goods for which the benefit of the system is sought have previously been subject to inward processing arrangements.

However, where those conditions are fulfilled, it seems to me that the authorization must be granted. Indeed, it would be unthinkable for the authority with responsibility for granting authorization to enjoy a discretion. Otherwise applicants would be exposed to the risk of differences of treatment which would be incompatible with the purposes and functioning of the system and

11 — Cited above, note 6.

with one or more fundamental principles of Community law.

13. Having regard to the principle whereby the authorization is granted when the preconditions are fulfilled, but is withheld when they are not, I find it difficult to imagine that the authority requested to issue the authorization could have any right to impose quantitative limits on it.

It does not seem to me that such a power can be inferred from an interpretation of the basic regulation, in particular a purportedly systematic interpretation to the effect that Article 18 must be read in conjunction with Article 21(a). Whilst it may be true that those provisions embody the concept of compulsory proportionality between re-exported compensating products and compensating products remaining within the customs territory, it is also true that the concept applies to an entirely different matter (which, moreover, accounts for the way in which it is drafted): namely, quantification of the customs debt incurred when the compensating products (what is more, secondary products) are released for free circulation in the customs territory.

Moreover, Article 21 of the basic regulation itself expressly provides, in paragraph (b), that when the compensating products are placed, after processing, under another customs procedure, they are subject to import duties calculated in accordance with the rules applicable to the customs procedure in question. It is therefore clear that the rules on duties applicable to processing under customs control are different: they take account of the operation which the product has undergone, the cost of that operation and, above all, the fact that the processed product is, by definition, a different product from that placed under the system at the outset. There is not therefore the slightest reason for the two provisions to be interpreted analogously.

14. Furthermore, if such an analogous interpretation were appropriate, the rule of compulsory proportionality between re-exported and non-re-exported compensating products would be applied to all cases where processing arrangements were discharged otherwise than by re-export. There would in fact be no reason for limiting it only to cases of discharge by placing of the secondary compensating products under the system of processing under customs control.

What is more, if such an analogous interpretation were to be deemed appropriate, it would not only be allowed but would also be compulsory, being necessary to ensure what was regarded as the correct operation of the Community rules. It seems clear to me that, if that had been its intention, the Community legislature would have laid down an

express rule to that effect, rather than expressly confining the obligation of proportionality solely to the case of release of secondary products for free circulation.

15. Finally, it does not seem to me that any importance can be attached to the fact that the customs authority is entitled to refuse to issue an authorization whenever it finds that the expressly prescribed economic conditions are not fulfilled.

It is not in fact reasonable to consider withholding authorization solely because a trader has opted for a particular way of discharging the inward processing arrangements when that option is expressly made available to him by the basic regulation.

16. In the light of the foregoing, I suggest that the Court give the following answer to the Bundesfinanzhof:

Article 18(2)(d) and Article 18(3) of Council Regulation (EEC) No 1999/85 of 16 July 1985 on inward processing relief arrangements must be interpreted as meaning that the authorization for discharge of inward processing arrangements by placing of the secondary compensating products under the system of processing under customs control cannot be made subject to quantitative limitations.