De minimis thresholds in APEC

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Executive summary

A *de minimis* regime provides streamlined border clearance and exemption from customs duties and other taxes. These features generate economic benefits by refocusing public revenue collection on more efficient revenue sources, reducing the costs borne by importers, and accelerating the delivery of imports.

Most APEC economies have *de minimis* regimes but thresholds range from under USD1 to more than USD1,000, and eligibility varies. These design features affect the balance of economic benefits and costs that a regime produces.

This study assesses, in some detail, the *de minimis* regimes of Canada, Indonesia, Japan, Malaysia, the Philippines, and Thailand — the APEC-6 economies for ease of reference. We chose them as being broadly representative of the APEC region in terms of geography and economic development. The study has estimated the net economic benefit of four alternatives — representing *de minimis* thresholds of USD50, USD100, USD150, and USD200. Tables 1 and 2 have the key results.

The USD200 threshold generated the largest net economic benefit — around USD5.9 billion a year for the APEC-6, equivalent to about USD30.3 billion for all 21 APEC members. In relative terms the latter is around 0.086% of APEC-21 gross domestic product (GDP).

Resource savings in government administration are the largest benefit. Under all scenarios, cuts in government administration accounted for 76% of the benefits, while savings in business compliance were virtually all of the rest. The latter are particularly important for small and medium sized enterprises (SMEs) as they generally face disproportionate burdens in completing customs formalities.

Savings in time in transit have a clear economic benefit. The longer products take to get to market, the more likely they will perish, become outdated, be displaced by superior alternatives, or lose the interest of potential buyers. Previous research has shown that a 10% cut in delivery time will, other things being equal, expand exports of time-sensitive manufactures by over 4%. For low value consignments, however, the transit time savings are generally small compared to the others.

A notable characteristic of the results is the relatively small impact that an increase in threshold has on government revenue. The loss of tariff revenue is less than 1% of the savings under the USD200 scenario and only 0.7% of those under the USD100 scenario. Although the loss of VAT revenue is more difficult to estimate, at worst it is no more than 4% of the savings under the USD200 scenario and less under the rest.

The revenue loss is much lower than many may have expected. The potential revenue base has been substantially eroded by preferential tariff rates under Free Trade Agreements (FTAs) and the existing *de minimis* exemptions. This is true even for those economies that have relatively high applied Most Favoured Nation (MFN) tariff rates.

The composition of the results is broadly the same for each of the scenarios and reflects the basic economics of this category of imports — relatively large numbers but relatively low aggregate value. Hence the volume-based impacts, such as those on customs and business processing costs loom larger than the value-based ones, such as those involving transit delays and tax collections.

Table 1: Net economic benefit of alternative de minimis thresholds, USD billion per year

Alternative Threshold USD	APEC-6 Economies (a)		APEC-21 Net Economic Benefit
	Net Economic Benefit	NEB as Share of APEC-6 GDP (%)	
50	0.031	0.001	0.16
100	3.89	0.056	19.8
150	4.90	0.071	25.0
200	5.93	0.086	30.3

Note: (a) Canada, Indonesia, Japan, Malaysia, the Philippines and Thailand.
Source: Estimates by ITS Global Asia Pacific.

Table 2: Net economic benefit of alternative de minimis thresholds, by selected APEC economy (a), USD million per year

Alternative Threshold USD	CA	ID	JP	MY	PH	TH
50	30.6	0	0	0	0.28	0.35
100	3,771	38.8	0	0	16.9	61.8
150	4,662	44.4	104	0	18.7	70.3
200	5,453	48.7	304	22.5	20.7	78.5

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH).
Source: CAPEC and Trade Data International Pty Ltd, estimates by ITS Global Asia Pacific.

Overall we judge our results to be robust. Indeed the conservative nature of our approach means that more refined estimates are likely to yield higher net benefits than we have estimated not lower ones.

Most, if not all, APEC economies would benefit by increasing their existing thresholds by a substantial amount. APEC could assist this process by agreeing to recommend a minimum threshold level to its members with the option of a higher level to better suit individual circumstances. This would leverage the benefits from unilateral action.

These conclusions have been strongly reinforced by recent research. For example, the Productivity Commission, the Australian Government's independent economic advisory body, is currently reviewing Australia's *de minimis* regime. Although Australia has the highest *de minimis* threshold in APEC and a substantial GST rate (10%), the Commission has found that any reduction in the threshold would impose a substantial net cost on the economy.

An increase in *de minimis* thresholds need not jeopardise border security as advance cargo reporting is required by most countries, irrespective of the declared value of the imports. A higher *de minimis* threshold can free up the resources to address the more pressing security issues.

The policy implications are straightforward. A commercially attractive *de minimis* arrangement makes sound economic sense. While the optimal level of the threshold remains an open question, the direction of change in APEC is clear.

1. Background to the Study

The facilitation of trade is attracting increasing interest in international and domestic policy circles, including in APEC (APEC 2007). Trade facilitation seeks to reduce the transaction costs faced by exporters and importers.[2] Reducing such costs stimulates international trade, investment and business innovation, which are the foundations of sustained improvements in community living standards in real terms.

A key aim of trade facilitation is the simplification of customs procedures and a key way to simplify customs procedures is to exempt merchandise from indirect taxation — e.g. customs duty, VAT, GST, and sales taxes — below a specified minimum — or *de minimis* — value. The World Trade Organization (WTO), the Organisation for Economic Co-operation and Development (OECD), the World Customs Organization (WCO), and the International Chamber of Commerce (ICC) have all recommended the adoption of such thresholds.

A *de minimis* threshold reduces the compliance costs imposed on importers and accelerates delivery of the merchandise. It also allows governments to refocus their revenue collection efforts on those parts of the indirect tax base that yield higher net revenue.

Most APEC economies have *de minimis* arrangements but they vary considerably which can significantly affect the balance of their economic benefits and costs. Thresholds range from less than USD1 to more than USD1,000 and the products eligible for the exemption also vary.

Asia Pacific Economic Cooperation (APEC) Leaders have committed their governments to the achievement of a 10% improvement in supply chain performance, after taking into account the circumstances of individual economies.

At Big Sky, Montana in the United States on 20 May 2011, the APEC Ministers Responsible for Trade (MRT) agreed that reducing the time, cost, and uncertainty of moving goods and services remains a top priority for APEC and accordingly instructed their officials to continue with the development of the APEC Supply-Chain Connectivity Framework (SCCF) Action Plan. The priorities for the Action Plan include the simplification of customs procedures and the implementation of commercially useful *de minimis* thresholds.

One proposal that has been put forward would set a baseline *de minimis* value for all APEC economies, with individual economies encouraged to adopt higher *de minimis* thresholds as they see fit. All APEC members have agreed to further work on the idea. As a consequence, with the support of the Express Association of America the Peterson Institute for International Economics in Washington, DC undertook an economic study into the benefits and challenges of *de minimis* regimes (Hufbauer & Wong 2011).

As the study by the Peterson Institute had focused on the experience of the United States, the Conference of Asia Pacific Express Carriers (CAPEC) engaged ITS Global Asia Pacific (ITS) and the Centre for Customs and Excise Studies (CCES) at the University of Canberra to assess the *de minimis* arrangements that apply in APEC at the present time, the reasons for their adoption, and the economic benefit that would flow from applying higher *de minimis* thresholds across the APEC region. Based on the results of its assessment, the study was to make policy recommendations, including on the appropriate baseline *de minimis* arrangements for APEC.

2. *De minimis* regimes in APEC

This Chapter identifies the principal aspects of the *de minimis* regimes that apply in Canada, Indonesia, Japan, Malaysia, the Philippines and Thailand at the present time and, where possible, the underlying policy rationale for the specified threshold and its supporting arrangements. We have chosen these economies as being broadly representative of the APEC region as a whole, both in terms of geography and economic development.

There is scant public information available in relation to the policy underpinnings for the setting of particular *de minimis* thresholds. This issue was also recently highlighted in the Australian context by the Productivity Commission (2011, p. 161).

Approaches were made to each of the individual customs administrations in question requesting background information on their *de minimis* policy arrangements. The majority were either unable

or unwilling to provide that detail even though some countries are in the process of or have recently reviewed their *de minimis* arrangements.

The analysis has therefore drawn some of its conclusions from studies conducted in New Zealand, the United Kingdom and most recently in Australia. While acknowledging that the trade and border management environment in these countries differs from that pertaining in many of the APEC economies selected for this study; it is strongly arguable that the policy considerations surrounding decisions to adopt a particular *de minimis* threshold are homogeneous. Support for this view can be found in the research conducted by Yang (2008) in relation to the Philippines. This broader analysis on the rationale for *de minimis* and the implications for specific thresholds is set out in the following Chapter of this report.

Table 2.1: Current de minimis thresholds, selected APEC economies

Country	Local Currency	USD Equivalent (a)
Canada	CAD20	20
Indonesia	USD50	50
Japan	JPY10,000	127
Malaysia	MYR500	166
Philippines	PHP15	0.35
Thailand	THB1,000	33

Note: (a) exchange rates calculated as at 8 August 2011.

Table 2.1 sets out the current *de minimis* threshold in each of the selected APEC economies in domestic currency and its United States Dollar (USD) equivalent. Details of the legal and policy framework for each *de minimis* regime follow, to the extent to which that information is publicly available.

2.1 Legal and policy frameworks by economy

2.1.1 Canada

The applicable regulatory framework is the *Postal Imports Remission Order*[3] and the *Courier Imports Remission Order*[4] which apply to both commercial and non-commercial imports.

Under these Orders, if someone imports an item that is worth CAD20 or less, the importer does not have to pay duty or taxes on the item. If the item is worth more than CAD20, the applicable duty, the GST (Goods and Services Tax) or HST (Harmonized Sales Tax), and any PST (Provincial Sales tax) must be paid on the item's full value.

GST is levied at a rate of 5% but certain goods and services are exempt or zero-rated (WTO 2011). The zero-rated products include groceries, residential rent, medical services, and financial services.

Items that do not qualify for the CAD20 exemption include:

- tobacco
- books, periodicals, magazines
- where the supplier is required to register under Subdivision D of Division V of Part IX of the *Excise Tax Act* and is not so registered
- alcoholic beverages, and
- goods ordered through a Canadian post office box or a Canadian intermediary.

In addition the Courier Low Value Shipment (LVS) Program streamlines the processing of low-value shipments through customs while providing the express courier industry with expedited release. This is done through:

- a single combined cargo report and release document called the 'cargo/release list' for goods valued under CAD 1,600
- the courier is required to provide separate cargo/release lists for cargo valued at less than CAD2,020 and for cargo valued between CAD20 and CAD1,600.

Hufbauer and Wong (2011) suggest that Canada mainly has a low de minimis threshold because the Federal Government imposes a tax on value-added (GST), which applies to imports as well as domestic sales, and is concerned about the potential loss of GST revenue. This concern is amplified by the fact that the United States, Canada's neighbor and largest trading partner, does not impose a VAT-style of indirect tax.

2.1.2 Japan

Goods with a customs value of JPY10,000 or less are exempted from customs duty and consumption tax. This treatment is provided by:

- paragraph 3, Article 14 of the Customs Tariff Law

- Section 21, Article 16 of the Cabinet Order for Enforcement of the Customs Tariff Law

- paragraph 14 of the General Notification of the Customs Tariff Law, and

- No. 1 of paragraph 1, Article 13 of the *Law for the Collection of Excise Taxes on Imports*.

Consistent with the treatment that is accorded by *de minimis* regimes elsewhere, imports into Japan are only exempted from the consumption tax and not from other domestic taxes — for example, liquor tax, tobacco tax, etc. The consumption tax is a VAT-style tax and is levied at the rate of 5% (WTO 2011).

Furthermore, the *de minimis* exemption is not applicable to certain designated articles[5] for which tax exemption is considered inappropriate because of their impact on domestic industry or for other reasons, even if their customs value does not exceed JPY10,000.

The criteria for determining whether the customs value is JPY10,000 or less are as follows:

- The customs value of imported goods per declaration should not exceed JPY10,000. When multiple declarations are made for one invoice in order to divide the invoice's articles into several units, the total customs value of all the articles belonging to the invoice should not exceed JPY10,000.

- For parcel post, the customs value of all articles enclosed in one package should not exceed JPY10,000. If a shipment is divided (to avoid weight limits, etc.) and sent from a given sender to a given receiver at the same time, the total amount of customs value of all the parcels shipped separately from the sender to the recipient should not exceed JPY10,000.

2.1.3 Indonesia

Article 6 of Customs Regulation Number P-05/BC/2006 provides that 'Courier express shipments with value not more than USD50 are exempted from import duty and taxes'.

Value-added tax (VAT) is applied at a rate of 10% to most goods and services. The exceptions include: certain mining and drilling products; certain minerals; basic necessities; food and drink served in hotels and restaurants; shares, bonds, and other commercial paper; healthcare; orphanage, and funerary;

postal; banking, insurance, and financial; religious; educational; non-commercial art; non-commercial broadcasting; public transport; manpower; and hotel services (WTO 2007a).

The luxury goods tax is applied at various rates:

- 10% on bottled water, soft drinks, cosmetics, radios and tapes, luxury houses, and townhouses

- 20% on carpets, sanitary goods, and luxury home appliances such as air conditioners

- 30% on non-government ships, sports equipment, certain television receivers, and motor vehicles with fewer than ten seats

- 40% on alcoholic beverages, imported leather goods, imported precious metals, private aircraft, and firearms; 60% on two-wheeled motor vehicles, and

- 75% on luxury yachts, and trailers and semi-trailers for camping or home use (WTO 2007a).

There is very little publicly available information on the *de minimis* threshold in Indonesia.

2.1.4 Malaysia

Express consignments with a *de minimis* value of MYR500 are exempted from the payment of customs duties. The direct release of non-dutiable express shipments below MYR2,000 without a formal declaration is permitted.

Malaysian Government has stated that the purpose of its *de minimis* threshold is:

> … trade and business facilitation, effective delivery of services and reducing the cost of doing business…to enhance efficiency and effectiveness in the delivery of goods and services, the Government is also promoting the growth of integrated logistics services (WTO 2005a, pp. 1-2).

The WTO has reported that the Malaysian authorities are planning to introduce a broadly-based VAT-type of tax of goods and services (GST) to replace the existing system of sales taxes and taxes on services, which generally involve tax rates of between 5% and 10% (WTO 2005c; 2009). It is not clear whether the Government is going to extend their *de minimis* arrangements to the GST when it is introduced.

2.1.5 The Philippines

Section 709 of the *Tariff and Customs Code* provides that:

> a Collector [of Customs] shall have discretionary authority to remit the assessment and collection of customs duties, taxes and other charges when the aggregate amount of such duties, taxes and other charges is less than 15 pesos[6] and he may dispense with the seizure of articles of less than 15 pesos in value except in cases of prohibited importations or the habitual or intentional violation of the tariff and customs laws.[7]

The Philippines imposes a value added tax (VAT) at a rate of 10% (proposed to be raised to 12%). The exemptions from VAT include: agricultural and marine food products; agricultural inputs; coal and petroleum products; books, newspapers and magazines; and passenger and/or cargo vessels of more than 5,000 tons (WTO 2005b).

The following import consignments need only complete the informal entry process:

- articles of a commercial nature that are intended for sale, barter or hire, the dutiable value of which does not exceed PHP2000, and

- personal and household effects or articles, not in commercial quantities, that are imported in a passenger's baggage, mail, or otherwise for personal use.

The following have to complete the formal entry process, regardless of value and whatever purpose and nature of the importation:

- articles of a commercial nature intended for sale, barter, or hire, the dutiable value of which is more than PHP2000, and

- those articles which the Collector of Customs may require, upon the recommendation of the Tariff Commission, for the protection of a local industry.

2.1.6 Thailand

Under the *de minimis* threshold, postal items or express consignments with an FOB value that does not exceed THB1,000 may be imported free of tax and duty.

In addition to the customs duties, Thailand levies three indirect taxes: excise tax, interior tax (10% of amount of excise tax), and value-added tax (VAT). All three are levied on imports at the same rates as on domestic production (WTO 2007b).

The VAT is applied at a rate 7% to nearly all goods and services. The exemptions are books, education, hospitals, unprocessed agricultural products, fertilisers, animal feeds, pesticides, and certain other social goods and services. The WTO has reported that the Thai authorities have delayed their decision to restore the VAT to 10% (WTO 2007b).

To assist the Royal Thai Customs in determining data requirements and the exact procedure to be applied, imported express consignments that are being presented for immediate release are divided into the following categories:

- Non-Dutiable documents – comprising correspondence and documents having no commercial value and which are not subjected to duties and taxes under Part II of the Customs Tariff Decree B.E. 2530. Any items that are prohibited or restricted are not included;

- Non-dutiable consignments – comprising

    (a) consignments not subjected to duties and taxes under Part II of the *Customs Tariff Decree* B.E.2530 (any items that are prohibited or restricted are not included),

    (b) low-value consignments, imported via an airport, of which the value does not exceed THB 1,000 and which are exempted from applicable taxes and duties under Part IV, Heading 12 of the *Customs Tariff Decree* B.E.2530 (any items that are prohibited or restricted are not included), and

    (c) trade samples of no commercial value which are exempted from applicable taxes and duties under Part IV, Heading 14 of the *Customs Tariff Decree* B.E.2530 (any items that are prohibited or restricted are not included),

- Dutiable consignments of which the FOB value does not exceed THB 40,000 (any items that are prohibited or restricted are not included), and

- Consignments other than those listed under the previous three headings.

To a large extent, the above four categories follow the WCO *Guidelines for the Immediate Release of Consignments* (WCO 2000).

The Royal Thai Customs provides simplified import procedures for inbound express consignments provided that the FOB value of the shipments is less than THB40,000. Shipments above that threshold have to undergo the formal entry process.

2.2 Relevance to management of border protection

Hufbauer and Wong have stated that:

> … within the Asian part of the APEC region, the *de minimis* threshold is a good barometer of the LPI [the Logistics Performance Index published by the World Bank (2009)]. Countries with higher *de minimis* exemption levels tend to have better LPI scores (the correlation coefficient is 0.6). *De minimis* reform can be a harbinger of broader improvements in customs facilitation (Hufbauer & Wong 2011, p. 3).

Since a high correlation co-efficient does not necessarily imply either the degree of causation or its direction, we have sought to test this statement by comparing the selected APEC economies against a series of performance benchmarks in the following publications:

- the World Bank's Doing Business Report 2011 (World Bank 2010)

- the World Bank's Logistics Performance Index 2010 (World Bank 2009), and

- the World Economic Forum's *Global Enabling Trade Report 2010* (WEF 2010).

Table 2.2 provides the details of the comparisons. It shows that while there is some correlation between the *de minimis* threshold and the performance of border management there is not necessarily a direct relationship between the two. Nevertheless, it is an issue that is worth exploring in more detail to determine the actual influence of a particular *de minimis* threshold on border performance.

Table 2.2: Border management performance by select APEC economies, rank order

Economy	Doing Business (a)		Logistics Performance Index (b)			Global Enabling Trade Report (c)		
	Overall	Trading Across Borders	Overall	Customs Efficiency	Timeliness	Overall	Border Admin- istration	Composite[8]
Canada	7	41	14	13	5	8	18	19/30/11
Indonesia	121	47	75	72	69	68	67	67/44/88
Japan	18	24	7	10	13	25	16	17/18/15
Malaysia	21	37	29	36	37	30	44	48/29/52
Philippines	148	61	44	54	42	92	74	56/55/119
Thailand	19	12	35	39	48	60	41	36/14/71

Notes: (a) *Trading Across Borders* rankings are based on three sub-indicators: all documents required by customs and other agencies to export and import; document preparation, customs clearance and technical control, port and terminal handling, inland transport and handling (time taken to export and import); and cost in USD per 20-foot container, no bribes or tariffs included (World Bank Group 2010a). (b) Logistics Performance Index components are: efficiency of the customs clearance process; quality of trade and transport-related infrastructure; ease of arranging competitively priced shipments; competence and quality of logistics services; ability to track and trace consignments; frequency with which shipments reach the consignee within the scheduled or expected time (World Bank Group 2010b). (c) Global Enabling Trade Report, Border Administration sub-index components are: efficiency of customs administration, efficiency of import-export procedures, transparency of border administration (WEF 2010).

3. Determinants of current *de minimis* regimes

3.1 *De minimis* as a concept

The concept of *de minimis* in relation to duties and taxes is not itself controversial. The concept is an acknowledgment that at some point the costs involved in assessing and collecting duties and taxes will actually exceed the revenue gained (OECD 2009; Simpson 2009; NZ Customs Service 2011; Productivity Commission 2011).

The recently published report on the *Economic Structure and Performance of the Australian Retail Industry* by the Productivity Commission (2011) draws on the Henry Tax Review to make this point:

> On the other hand, the administrative arrangements for taxes recognise that there are circumstances under which it is inefficient to impose administration and compliance costs on the government and the community in an attempt to collect small amounts of revenue. The costs to government, business and consumers entail efficiency losses and are a deadweight loss for the community. Therefore, from the viewpoint of maximising the welfare of all Australians, the question may be whether there are likely to be bigger losses in efficiency from trying to provide equal treatment by collecting taxes on all imports, than from the distortions created by differential tax rates for foreign and domestic retailers (Henry 2009).

As the Henry Tax Review noted:

> Related to the issue of complexity are the costs of administering and complying with the tax and transfer system. These costs represent a net loss to the economy, because the resources engaged in these activities could otherwise be put to more highly valued uses. Recent research suggests there is an optimal level of system complexity and operating costs, one that balances administration and compliance costs with improved efficiency and distributional outcomes (Henry 2009, p. 21).

New Zealand Customs describes the issue in this way:

> A de minimis represents a trade-off between two aspects of taxation design; that is, integrity, which suggests that the intended rates of taxation are collected without discrimination – all like transactions treated alike for taxation assessment etc. ... and administrative efficiency, which suggests that accounting for, and collection of, every last dollar of taxation revenue due cannot be practically or efficiently achieved as a point will be reached where more is being spent on administrative and collection processes than will be collected in revenue (NZ Customs 2011, p. 8).

This tension between tax revenue and costs of its administration is not just an issue highlighted by national customs and tax administrations. It is an issue that is well established at an international level.

In the *Global Enabling Trade Report 2009* published by the World Economic Forum (WEF), Simpson points out that:

> There is a significant cost to government and business, in terms of administrative burdens and delays, resulting from subjecting shipments of minimal value to full customs formalities. All WTO Members should adopt the practice of having *de minimis* exemptions from full formalities for small shipments. It is common in income tax regimes to provide for simplified tax returns for persons having only small incomes. Much of the logic that lies behind this policy is applicable to collection of tax information on goods crossing borders ... Related to but separate from the issue of waiving full customs formalities for small value shipments is the more sensitive issue of waiving collection of small amounts of duties and taxes. Even in a moment such as the present, when public revenues are reduced, governments that do not already have them should establish value limits below which shipments will not be subject to taxation; collecting taxes on such shipments is a procedure that is not cost effective (Simpson 2009, p. 64).

The WCO, the pre-eminent international body on customs matters, has made express provision for *de minimis* regimes in its Revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures (Revised Kyoto Convention). Among other things, the revised Kyoto Convention states that:

> National legislation shall specify a minimum value and/or a minimum amount of duties and taxes below which no duties and taxes will be collected (Transitional Standard 4.13).

Moreover, in relation to Transitional Standard 4.13 of the Revised Kyoto Convention the WCO has subsequently stated that:

> ... the collection and payment of duties and taxes should not be required for negligible amounts of revenue that incur costly paperwork, both for the Customs administration and the importer/exporter. Customs administrations must establish and specify in national legislation amounts below which duties and taxes need not be collected and paid (WCO Guidelines to the Revised Kyoto Convention).

3.2 *De minimis* as trade facilitation

In the context of customs clearance the *de minimis* threshold is used in two ways:

- firstly, as a 'value' threshold below which duties and taxes are not collected and no customs declaration is required, and

- secondly, as a 'reporting' threshold for goods in respect of which a full customs declaration must be submitted.

In other words many customs administrations adopt two levels of *de minimis*. Goods whose value falls between the two thresholds are usually the subject of a simplified customs declaration. The significance of these thresholds is the documentation associated with the relevant declaration requirement and the implications this has for clearance times and compliance effort. As acknowledged by New Zealand Customs:

> For consignments required to undergo full customs formalities, the importer must submit to a customs administration detailed information on the classification, origin, and valuation of the goods at a consignment level to satisfy valuation elements for the calculation of duty, and statistical data for balance of trade purposes .... (NZ Customs Service 2011, pp. 8-9).

The OECD has also recognised the potential of *de minimis* procedures as a trade facilitation measure. In examining trade facilitation reform for Sub-Saharan Africa it has noted that:

> De minimis procedures could allow consignments valued below a de minimis level (i.e. threshold) to be exempted from formal customs clearance procedures, such as the submission of an import declaration, and be subject only to the submission of a consolidated manifest (such as an airway bill of lading [*sic*] or a commercial invoice) or simplified documentation. Furthermore, for some of these consignments, the collection of duties and taxes and other regulatory impediments may be waived and immediate release issued, based on information contained in the consolidated manifest detail records ... (OECD 2009, p. 37).

De minimis arrangements are particularly important for small and medium-sized enterprises (SMEs) as they generally face a disproportionate compliance burden with respect to the completion of customs formalities. A 2003 OECD paper reported an EU study of customs procedures as finding that 'firms with fewer than 250 employees incur trade transaction costs that are 30-45% higher per consignment than those falling on larger firms' (Walkenhorst & Yasui 2003, p. 12). This was partly because of an inability of such businesses to take advantage of the simplified procedures that the authorities generally made available.

Indeed, additional formalities often end up being more inefficient '… since they have created an additional cost burden, added to the time it takes to clear goods and also created further opportunities for solicitation of "facilitation payments"' (OECD 2009, p. 39).

These costs increase the perception of risk and act as a barrier for SMEs considering entry into new markets. The effect becomes more pronounced in times of economic downturn when SMEs become particularly vulnerable to added cost burdens. As Brooks and Stone have stated:

Flexibility, as well as timeliness, will become more valuable as greater trade implies greater potential vulnerability to external shocks such as financial turmoil…..Factors such as delays in customs clearance, unofficial payments, and poor governance are particularly damaging because they impede flexibility (Brooks & Stone 2010, p. 156).

The quantum of a threshold is in inverse proportion to the compliance burden. There can be little doubt that the lower the *de minimis* threshold, the higher the administrative burden to traders and, in particular, SMEs (Hummels 2001; Hornok & Koren 2010).

The significance of a lower *de minimis* threshold in the context of the administrative and compliance burden is its impact on time and administrative costs. In particular, a lower threshold means increased documentation due to the larger volume of consignments requiring a full customs declaration. Increased documentation means increased time for both business and government to prepare and process that documentation and an adverse impact on delivery time (de Souza et al. 2007).

Hornok and Koren point out that document preparation is the most time-consuming of four procedures specified in the *Trading across Borders* database maintained by the World Bank for its annual *Doing Business Report*. Document preparation represented about 50% of the total time of delivery for the average country — see Table 3.1 below.

In Hummels' research on time as a trade barrier he concludes that:

> ... each day in travel is worth an average of 0.8% of the value of the good per day, equivalent to a 16% tariff for the average length ocean shipment ... Estimates indicate that each additional day in ocean transit reduces the probability that a country will export to the US by 1% (all goods) to 1.5% (manufactured goods) (Hummels 2001, p. 3).

One might expect an even more dramatic effect of time delays on time-sensitive cargo such as that regularly transported by express companies and in fact that is the case. Djankov, Freund and Pham find that '... a 10% increase in time reduces exports of time-sensitive manufacturing goods by more than 4%, all else equal' (Djankov, Freund & Pham 2010, p. 172).

Table 3.1: Time Taken by & Cost of Import Processes (a)

Procedure	Days per TEU (b)		Cost (USD) per TEU (b)	
	Mean	As % of total	Mean	As % of total
Document preparation	13.7	51.7	306.1	19.0
Customs clearance & inspection	3.7	14.0	213.7	13.2
Port & terminal handling	4.5	16.8	317.0	19.6
Inland transport from seaport to importer's premises	4.7	17.5	778.0	48.2
ALL	**26.6**	**100**	**1614.8**	**100**

Notes: (a) The time taken and the fees incurred in importing a shipping container of widely traded non-perishable merchandise (b) twenty-foot equivalent unit, a standardised measure of shipping container volume.

Adapted from Hornok and Koren (2010) and World Bank Group (2010a).

In fact traders react to any increase in administrative burden by sending fewer shipments of larger size and use larger-shipment transport modes more often to spread the freight and administrative costs over a larger number of individual items.

In extreme cases it may lead to the cessation of trade with that country altogether (Hornok & Koren 2010; Productivity Commission 2011). The *de minimis* level therefore has a flow-on effect on choice of transport mode and therefore on the total landed cost of goods. It can mean that what was an economic transaction becomes uneconomic because:

> [T]he choice is on the frequency/size of a shipment and the trade-off is timeliness versus smaller per shipment administrative costs. The demand for timeliness requires relatively small and frequent shipments, while the burden of per shipment administrative costs can be mitigated by reducing the frequency, and increasing the size, of shipments (Hornok & Koren 2010, p. 3).

It is generally accepted that entry processes can be an impediment to trade and this adverse potential is behind the inclusion of 'trade facilitation' in the current WTO Doha Round of multilateral trade negotiations. Determinations on *de minimis* can have a negative impact on entry processes as noted previously and therefore have that potential to hinder trade, particularly where low value shipments are an input to business. As the Productivity Commission has recently stated in relation to Australia's circumstances:

> Competition from international retailers can be important in driving efficiency in the Australian retail industry. In addition many businesses currently receive goods which enter Australia under the LVT [low value threshold]. Longer delays or unnecessary charges associated with processing such imports will also hinder those businesses and there will be very limited additional revenue collected ... (Productivity Commission 2011, p. 159).

3.3 Does *de minimis* increase non-compliance?

An argument that is raised in relation to the setting of a particular threshold is that it encourages non-compliance by traders; that is, traders will engage in 'under-invoicing', 'split shipments' and other forms of valuation fraud to avoid customs formalities and the payment of duties and taxes.

These concerns have been behind the recent decision of the UK Government in its 2011 budget to reduce the level of the UK threshold from £18 to £15 from November 2011. Previously, the stance of the UK Government was a reluctance to reduce the threshold because of the demands it would place on HM Revenue and Customs but this view has now shifted to favour an industry protection perspective.

The decision to lower the threshold in the UK has been a reaction to government concerns that some UK retailers had been taking advantage of the low value threshold by selling goods over the internet, VAT-free, from subsidiaries based in Jersey and Guernsey. The estimated loss to government revenue from that practice had increased from around £80 million to £130 million over the past five years at the same time as having an adverse effect on UK SMEs who argued that they were unable to compete with large companies operating VAT-free in the Channel Islands and elsewhere.

Research on crime displacement in the context of customs reform in the Philippines raises serious questions about the effectiveness of lowering thresholds on non-compliance — see Box 3.1. In that case the work has concluded that lowering the duty threshold as part of a decision to increase enforcement actually led to a net loss of revenue for the Philippine government (Yang 2008). This phenomenon is worth exploring in more detail, given the propensity for governments to justify low thresholds on the basis of reducing revenue leakage and improving compliance.

In Australia, the Australian Customs and Border Protection Service (ACBPS) undertook an 'enhanced compliance campaign' in relation to low value imports over the period from January to March 2011. The campaign was designed to '… treat concerns raised by industry about non-compliance with the low value threshold'. Some 33,000 physical examinations were undertaken on international mail articles and 32,000 assessments were undertaken on air and sea cargo declarations to assess compliance with the low value threshold. According to the ACBPS, '[T]hese 65,000 interventions resulted in 1,942 instances of undervaluation and bulk orders in breach of the low value import threshold ... revenue underpayments ... totalled $718,000' (ACBPS 2011, pp. 4-5).

Box 3.1: Case Study – Philippines

PHILIPPINES – INCREASED INSPECTION OF LOW VALUE SHIPMENTS
In 1990 the Philippine Government progressively lowered the minimum value threshold above which pre-shipment inspection had to occur. The policy rationale for lowering of the threshold was to improve Customs enforcement.
In a review of the Philippine Government's actions, Yang concluded that 'the empirical analysis finds that when the Philippine Government increased enforcement by expanding inspections to low-value shipments, imports from treatment countries shifted differentially to an alternative duty-avoidance method: shipping via duty-exempt export processing zones' (2008, p. 2)
The lowering of the threshold was not economic. As Yang concluded:
'Conservative estimates of tariff revenue gains and losses (net of PSI fees) suggest that the minimum value threshold reductions were a starkly uneconomic proposition, leading to significant losses in net revenue for the Philippine government...The minimum value threshold reductions led to two types of revenue gains. First, because importers were no longer able to avoid the PSI requirement by valuing shipments between $5000 and $500, import duty collections should have increased on shipments that would not have been inspected before. Second, shipments were not subject to PSI (thus saving inspection fees) if they were shifted to valuation under $500 or to export processing zones. I estimate that total revenue gains from these two sources amounted to roughly $24.6 million...
These revenue gains were considerably overshadowed by two kinds of costs to the Philippine government. First, the cost of additional inspections of shipments valued between $500 and $5000 would have amounted to $28 million. Second, losses in import duties due to shifts to the other methods of duty avoidance would have totalled $33.3 million. These gross revenue losses balanced against gross revenue gains imply that the minimum value threshold reductions led to a net loss of $36.8 million for the Philippine government.' (2008, p.12)
Source: Yang 2008.

The ACBPS report on this compliance campaign does not provide any detail on the resource and administrative costs that were associated with the campaign so it is not possible to provide a cost-benefit analysis. However, the ratio of non-compliance against interventions is about 3%. This places some question marks over its cost-effectiveness, particularly when combined with the report's conclusion that estimates of the revenue leakage due to non-compliance with the low-value threshold were 0.66% of total revenue collected in the 2009-2010 financial year (ACBPS 2001, p. 5).

Similarly, an increase in *de minimis* thresholds does not jeopardise border security since advance cargo reporting is required by most APEC economies, irrespective of the declared value of the goods. As Hufbauer and Wong point out in their research in relation to the United States, de minimis thresholds can actually have the effect of freeing up resources…to deal with more important security and product safety issues' (Hufbauer & Wong 2011, p. 2).

3.4 What is the appropriate *de minimis* level?

Determining the appropriate quantum of de minimis threshold is fundamentally an assessment of where the balance lies between revenue gained, on the one hand, and the overall costs to business and government of compliance and customs administration, on the other (NZ Customs 2011; Productivity Commission 2011). This assessment differs from country to country depending on a diverse range of political, trade and socio-economic factors.

Table 3.2 has a comparison between the contrasting conclusions reached by Australia and New Zealand respectively within a similar timeframe that is informative in this respect, given the high degree of commonality that exists between these two economies.

Table 3.2: Contrasting conclusions on de minimis thresholds

Australia: Productivity Commission 2011	New Zealand: NZ Customs Service 2011
Australia should retain its current low value threshold of $1000. While data are limited, the Commission estimates that with current processes, without the low value threshold, about $578 million of revenue would be collected and over $2 billion of collection costs would be borne by businesses, consumers and government. These costs are a deadweight loss to the community ... The costs and benefits of implementing a new process should be assessed. The low value threshold should only be lowered to a level which still remains cost-effective.(p. 151)	Customs considers that NZ's *de minimis* is at an appropriate level based on its costs of transaction processing ... A higher *de minimis* would reduce overall compliance and administration costs and encourage low value importations, but it would also have the effect of undermining the integrity of the taxation system and reduce government revenue. The impacts of setting a *de minimis* based on a customs value of $650 or $1000 have been examined. The taxation revenue foregone under these options is estimated to be up to $10.4 million and $24 million per annum respectively, which would exceed the combined compliance and administration costs of collecting it, based on current practice and cost structures. An increase in the *de minimis* therefore does not appear to be justified (p. 2)
Source: Productivity Commission 2011.	*Source:* NZ Customs 2011.

What is clear is that accurate data is necessary for governments to make an informed decision as to where they should set the *de minimis* threshold for their economy. As the Productivity Commission has stated:

> A number of factors affect the calculation of the amount of revenue foregone and the possible impact of any changes to the threshold. The accuracy of any estimates will be affected by the reliability of data on the:
>
> - Number, value, and distribution of low value consignments entering [Australia] through international mail, air cargo and sea cargo;
>
> - Rate of duty applicable to low value consignments;
>
> - Value of consignments which are GST [VAT] exempt, addressed to businesses registered for GST [VAT], or to non-profit organisations exempt from GST [VAT];
>
> - Level of other costs (such as freight, insurance and customs duty) which may be included in calculations of the value of taxable importation for calculation of GST [VAT]; and
>
> - Extent to which any change in the threshold may affect the behaviour of importers and alter the value of consignments entering [Australia] (Productivity Commission 2011, p. 168).

Again, as a comparison, it is interesting to note that the Common Market for East and Southern Africa (COMESA) and the East African Community have each adopted a threshold of USD500 in support of simplified customs documentation and procedures so as to facilitate trade between their members.[9] Box 3.2 has the details.

Box 3.2: Case Study – Common Market for East and Southern Africa

COMESA – SIMPLIFIED CUSTOMS AND ORIGIN DOCUMENTATION
A simplified trade regime for selected types of commodities is being promoted by COMESA member countries.
Small-scale traders benefit from a simplified customs document and a simplified certificate of origin. Goods that originate from COMESA member states and whose value does not exceed USD 500 per consignment qualify automatically for duty-free entry anywhere in the COMESA market. In the East African Community too, a simplified certificate of origin for cross-border trade of a maximum value of USD500 is in force since the 1st July 2007.
This was agreed by COMESA Trade Ministers at the Business Summit and Exhibition held in Kigali, Rwanda in May 2007. It intended to apply initially to maize, rice, beans and traditional food crops such as cassava, as well as cotton and dairy products.
Source: OECD 2009, p. 39.

In relation to the United States, Hufbauer and Wong found:

> ... that the net gain from raising the de minimis threshold on the existing volume of shipments would be about $17 million, taking into account the cost savings to all affected parties — customers, express firms, US Postal Service, and Customs and Border Protection. In other words, the loss of tariff revenue would be more than offset by the savings to the multiple parties in the delivery chain (Hufbauer & Wong 2011, p. 6).

The UK Government, on the other hand, gave particular prominence to the issue of tax avoidance in making its decision to reduce the threshold from £18 to £15 with effect from November 2011.

4. Economic costs and benefits of *de minimis* reforms

4.1 Overview of results of economic analysis

The results of the economic analysis are summarised in Tables 4.1 to 4.3. A detailed description of the methodology and approach that was used in the evaluation is in Annex A.[10] The full results of the analysis are set out in Annex B.

4.1.1 Aggregate results

Table 4.1 has our estimates of the aggregate net economic benefit for the six APEC economies — Canada, Indonesia, Japan, Malaysia, the Philippines, and Thailand — under a range of alternative scenarios. We chose these economies as being broadly representative of the APEC region in terms of geography and economic development. In 2010 they accounted for 24% of regional GDP and their GDP per capita averaged USD14,600, compared to USD12,900 for the region as a whole.[11]

Each of these scenarios involved the application of a minimum *de minimis* threshold. The values involved were USD50, USD100, USD150 and USD200. They each assumed that all imported merchandise below the threshold value was exempt from all indirect taxation, including tariffs. For the purposes of the evaluation, the *de minimis* arrangements were assumed to be unchanged if the current threshold exceeded the minimum level specified for the scenario in question.

Our estimates of the benefits and costs of each scenario is expressed in both monetary terms — in this case in USD for ease of comparison — and as a percentage of the aggregate GDP of the six economies in the study. For ease of reference these six economies are collectively referred to as the APEC-6, while the full APEC membership is referred to as the APEC-21.

Table 4.1 also includes an estimate of the net economic benefit of each scenario for all 21 APEC economies. These estimates involve the projection of the net benefit of each scenario for the APEC-6 to the rest of the region, based on its share of APEC-6 GDP. This assumes that the APEC-6 economies are broadly representative of APEC as a whole.

Table 4.1: Net economic benefit of alternative de minimis thresholds in APEC, USD billion per year

Alternative Threshold USD	APEC-6 Economies (a)		APEC-21 Net Economic Benefit
	Net Economic Benefit	NEB as Share of APEC-6 GDP (%)	
50	0.031	0.001	0.16
100	3.89	0.056	19.8
150	4.90	0.071	25.0
200	5.93	0.086	30.3

Note: (a) Canada, Indonesia, Japan, Malaysia, the Philippines and Thailand.
Source: Estimates by ITS Global Asia Pacific.

Table 4.2: Net economic benefit of alternative de minimis thresholds, by APEC economy (a),
USD million per year

Alternative Threshold USD	CA	ID	JP	MY	PH	TH
50	30.6	0	0	0	0.28	0.35
100	3,771	38.8	0	0	16.9	61.8
150	4,662	44.4	104	0	18.7	70.3
200	5,453	48.7	304	22.5	20.7	78.5

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH).

Source: CAPEC and Trade Data International Pty Ltd, estimates by ITS Global Asia Pacific.

Table 4.3: Composition of net economic benefit of alternative de minimis thresholds, select APEC
economies (a), USD million per year

Component of Net Economic Benefit	Alternative Threshold			
	USD 50	USD 100	USD 150	USD 200
Saving in merchandise transit time	0.07	16	26	33
Saving in government administration	23.92	2,981	3,765	4,548
Saving in business compliance	7.38	920	1,157	1,399
Less Tax revenue foregone	0.12	29	40	52
Net economic benefit	31.26	3,917	4,900	5,928
Benefit-cost ratio (b)	270	137	125	115

Notes: (a) Canada, Indonesia, Japan, Malaysia, the Philippines and Thailand (b) The ratio of the total resource savings to the tax revenue foregone.

Source: Estimates by ITS Global Asia Pacific.

Table 4.2 breaks down the aggregate net benefit estimate for APEC-6 by individual economy, while Table 4.3 breaks it down by its functional components — the resource savings that would be generated in merchandise transit time, government administration, and business compliance, and the costs in terms of the tax revenue foregone from extending the taxation exemptions.

In summary, we estimate that a minimum *de minimis* threshold of USD200 would generate an aggregate net benefit for the APEC-6 economies of around USD5.9 billion a year. This is equivalent to about USD30.3 billion for all 21 APEC members or some 0.086% of APEC-21 GDP.

4.1.2 Results for individual economies

All six economies would realise a net benefit from raising their *de minimis* threshold, no matter how small the increase. Where a scenario would not change an economy's threshold, of course, there was neither any benefit nor any cost. This was the case for Malaysia under the USD150, USD100 and USD50 scenarios, for Japan under the USD100 and USD50 scenarios, and for Indonesia under the USD50 scenario.[12]

The size of the net benefit varied substantially across the six economies. Most of the variation reflected a combination of the extent of an economy's current *de minimis* threshold and the stage reached in its economic development. The higher an economy's GDP per capita, the more intensively it tends to use low value imports for business (intermediate inputs) and household use (final consumption). The most obvious manifestation of this characteristic is the increasing tendency to use air freight for the delivery of low value consignments, even though it is significantly more expensive than mail or sea freight. For these reasons, expressing the net economic benefit as a share of GDP can provide a better indication of the results from a comparative perspective.

We expect Canada to experience the highest net benefit under all scenarios, in both absolute and relative terms. For a threshold of USD200, its net benefit amounted to USD5.45 billion a year or 0.35% of its GDP. These outcomes are largely a consequence of the fact that Canada makes, by far, the most intensive use of low value imports[13] and has one of the lowest *de minimis* threshold levels in the region.

We estimated the net benefit for Japan at about USD303 million (USD200 scenario) and USD104 million a year (USD150 scenario). Although it is the second largest economy in APEC, Japan does not rely on low value imports as intensively as any of the other APEC-6 economies. Moreover, Japan has the second highest *de minims* threshold of the APEC-6, so a much higher proportion of its low value imports already benefit from *de minimis* entry. As a consequence the net economic benefit of the USD200 scenario was the equivalent of 0.006% of Japanese GDP, the lowest result within the APEC-6, and only slightly ahead of Indonesia's (0.007%).

While Malaysia has the second most intensive use of low value imports, it has the highest *de minimis* threshold in the group. Accordingly the net benefit from the USD200 scenario (USD22.6 million a year) is equivalent to 0.017% of GDP but none of the other scenarios would generate any benefit as the existing threshold already exceeds the assumed minima.

The situation for Thailand is the reverse of that for Malaysia. Thailand is a less intensive user of low value imports but currently has a much lower *de minimis* threshold. Under the USD200 scenario we estimated a net benefit (USD78.5 million a year) that was equivalent of 0.025% of GDP, the second highest among the APEC-6. Thailand's results under the other scenarios generally maintain this ranking. The exception is the USD50 scenario, which approximates the current threshold.

The Philippines ranks in the middle of the APEC-6 in terms of its intensity of use of low value imports but it has the lowest *de minimis* threshold in the group. We estimated that the USD200 scenario would generate a net economic benefit of USD20.7 million a year. This was equivalent to 0.011% of GDP, which puts it in a mid-ranking position in the group by that measure. This is unchanged under the other scenarios.

Indonesia ranks second lowest, after Japan, in terms of intensity of use of low value imports and fourth lowest in terms of *de minimis* threshold. Indonesia's much larger GDP compared to the other ASEAN members in the group means that its net benefit from the USD200 scenario ranked much higher in monetary terms (USD48.7 million a year) than it did as a share of GDP (0.007%). Its results under the other scenarios generally mirror these outcomes.

4.1.3 Composition of net economic benefit

Savings in the costs of government administration dominate the results for APEC-6 under the all scenarios. Extension of the more streamlined customs and other border clearance procedures, which are generally associated with a *de minimis* clearance channel, are estimated to account for 76% of the savings that were estimated for the USD200 scenario.

The other critical source of benefits is the savings in the compliance costs incurred by business from extension of more streamlined border clearance procedures. These are estimated to account for 23% of the resource savings generated by the USD200 scenario. The pattern is broadly the same, however, for each of the other scenarios.

A notable characteristic of the results of the economic evaluation is the negligible impact that higher *de minimis* thresholds have on tax revenue. The revenue loss is equivalent to less than 1.0% of the savings under all of the scenarios. As would be expected this share declined with the level of the minimum *de minimis* threshold.

In fact the revenue foregone only approximates the smallest of the resource savings under all scenarios — namely, the savings in merchandise transit time. The more streamlined customs procedures allow

delivery times to be cut by up to 60% for eligible consignments; their relatively low aggregate value, however, means that their overall impact is much smaller than the volume-based impacts on government administration and business compliance costs.

Each of the main components of the scenario estimates of net economic benefit is described in more detail below. This discussion includes an explanation of the determinants of the results that were obtained, as well as the sensitivity of those results to the key assumptions that were used in the development of the spreadsheet model used in estimation process.

Before doing so, we will outline the projections of the volumes and values of low value imports by the APEC-6 on which the economic analysis was based and on which the results of all of the analytical scenarios critically depend.

4.2 Nature and extent of low value imports

The most critical input in the economic evaluation are estimates of the value and volume of those import transactions affected by an expansion of the *de minimis* arrangements in each of the selected economies. As we saw in Table 4.2, by far the more important of these two variables is the volume of import transactions under each of the *de minimis* scenarios. Indeed the lower the *de minimis* threshold, the more pronounced is the domination of transaction volumes on the final result.

Unfortunately the information that is publicly available on low value import transactions, is sparse and of uncertain quality. In principle the border agencies collect extensive information on air and sea cargoes, such as the classification of the merchandise under the Harmonized System, their country of origin, and their declared value for customs purposes. In practice, this information can be very costly for customs agencies to collect, check and validate, particularly in developing economies, while the usefulness of the information can vary to a considerable degree.

In the light of this, we have adopted an approach to the estimation of the value and volume of low-value import transactions by each of the APEC-6 economies that is both straightforward and cautious. This was done in the knowledge that the estimates of net economic benefit, which were derived from them, would be highly conservative. We are confident that a more accurate approach to the estimation of low-value import transactions would only increase the absolute size of the net benefit that we have calculated for each of the threshold scenarios.

Our approach draws on the results of recent research on Australia (CIE 2011). This research was undertaken on behalf of CAPEC for an official inquiry that is, among other things, looking into the *de minimis* arrangements in Australia and their impact on the retail industry in that country.[14]

The Centre for International Economics (CIE) estimated how the volume and landed value of imports by the different modes varied along the spectrum of consignment values, from the bottom of that range upwards. Its results indicated that mail and sea cargo accounted for 84% of the total value of all imports by Australia with a landed value of less than AUD200, and 87% of those imports with a value under AUD100. In the case of the import volumes, international mail and sea cargo were responsible for 89%of the total number of consignments under the AUD200 scenario and 88% of the total under the AUD100 scenario.

Despite an extensive literature review, we were unable to find any other estimates of the distribution of low-value imports by unit value and by volume, let alone those that were more comprehensive in terms of their coverage of the values and volumes that were involved for this category of imports.

In the light of this, we had no choice but to project the results from our survey of air express transactions to arrive at estimates for all low-value import transactions by all modes in each of the APEC-6 economies.

Our projections were based on the modal shares estimated by the CIE for low value imports by Australia by air, sea and international mail (CIE 2011). In the absence of other relevant information, we have also assumed — most conservatively, we believe — that CAPEC members handled all the air cargo in each of these economies.

The spreadsheet model that we have developed to estimate the net economic benefit under different threshold scenarios, however, allows each of these assumptions to be varied on a case-by-case basis. For each economy, the model calculates the annual equivalent of the value of CAPEC imports under each threshold from our survey of a week's transactions. Based on this value the model projects the total value of all air cargo imports and the total value of all imports by all modes under the scenario — using the CIE estimate of the market share for each mode that was referred to above.[15] The difference between the two is the total value of the mail and sea cargo for the scenario. The formula has been repeated to project the total number of consignments by each mode under the scenario for the economy in question.

Our projections for the imports by each of the APEC-6 economies under each threshold scenario are set out in Table 4.3 (import values) and Table 4.4 (import volumes). The economies in question are indicated by their two-character ISO codes.[16] The projections for each of the other scenarios are set out in Annex A.

Table 4.3: Projected value of de minimis imports by air, sea & mail under alternative thresholds, by APEC economy (a), USD million per year

Alternative Threshold USD	CA	ID	JP	MY	PH	TH
50	15.33	1.05	6.39	1.80	0.76	1.08
100	2,165	105	661	199	83	121
150	3,030	128	822	305	102	156
200	3,720	140	915	353	115	182

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH).
Source: CAPEC, CIE 2011, and estimates by ITS Global Asia Pacific.

Table 4.4: Projected volume of de minimis imports by air, sea & mail under alternative thresholds, by APEC economy (a), thousand consignments per year

Alternative Threshold USD	CA	ID	JP	MY	PH	TH
50	846	84	483	96	56	82
100	61,950	5,03	29,332	6,323	3,469	5,078
150	76,394	5,630	33,228	7,924	3,930	5,827
200	89,206	6,156	36,637	9,061	4,351	6,510

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH).
Source: CAPEC and Trade Data International Pty Ltd, estimates by ITS Global Asia Pacific.

The projections in Tables 4.3 and 4.4 have a number of notable features.

The projected volume of consignments of USD200 or less by all modes for Indonesia is consistent with the Indonesian customs data on this category provided by Trade Data International — Annex D has the details. After adjusting for timing differences, the projections in Tables 4.3 and 4.4 are only 10% less than the volumes recorded in the customs data This suggest that the projection methodology and assumptions are broadly reliable, if somewhat conservative.

On the other hand the projected annual value of imports in this category by Indonesia is less than half the aggregate value suggested by the Indonesian customs data using the same threshold — consignments of USD200 or less. The frequency distribution of consignments in the Indonesian customs data is significantly less skewed towards lower consignment values than is the case for the results of either our survey of air express imports by Indonesia or research into low value imports by other APEC economies (CIE 2011; Hufbauer & Wong 2011). This is puzzling and does not admit any easy conclusions.

The intensity of use of low value imports — measured as a share of GDP — varies very considerably across the APEC-6 economies. It is lowest in Japan and highest in Canada; a result that holds for both the volume and the value measures of intensity. Given the projection methodology that we used, both sets of results are, of course, a direct reflection of the results that we obtained from our survey of transactions by CAPEC members in these two economies.

The differences in intensity of use may be a reflection of the basic economic geography of the APEC-6 economies and their regulatory treatment of international freight services.

For example, Canada shares the longest land border in the world with the United States — most Canadian economic activity is physically located closer to the United States than to the rest of Canada. The two also share a common language, a common system of commercial laws, and a common business culture. Not surprisingly these two economies have the most intensive bilateral trading relationship in the world, which one would expect to see reflected, among other things, in the intensity with which low value imports were used in Canada.

In sharp contrast Japan is bound by sea and does not have nearly as much in common with its major trading partners, in terms of institutions that facilitate trade. Again one would expect to see this manifest itself in the intensity with which Japan used low value imports.

4.3 Savings in government administration

An inherent part of any *de minimis* regime is a customs clearance process that is substantially more streamlined than the one generally used. The general clearance process tends to be relatively costly in terms of government administration. It involves a case-by-case assessment of each transaction based on the collection of extensive documentation, the possibility of physical inspection of the merchandise in question, and the involvement of multiple government agencies responsible for border protection.

As low value imports are characterised by high transaction volumes compared to the aggregate value of what is being imported, savings in the cost of government administration loom large in any question of extending the *de minimis* threshold or the merchandise that it covers. So much so that the savings in government administration accounted for 72% of the benefits estimated for all of the threshold scenarios.

For the present study we undertook a literature review to identify any published estimates or public sources of the resource costs of customs clearance as well as the cost differences between general and *de minimis* clearances. The review concentrated on finding the capital and operating costs of clearance costs for each of the entry channels in economies that had customs arrangements and levels of economic development that were similar to those of the APEC-6 but did not find anything particularly useful for the purposes of this evaluation.

We have therefore inferred the unit costs of customs clearance from an examination of the user charges and fees that are levied by customs and border protection agencies.

The Australian Productivity Commission (PC) used this approach to examine the impact of a change in the Australian *de minimis* threshold on the costs of customs administration in that jurisdiction. The PC used the charges and fees levied by the ACBPS as a proxy for the costs of customs administration in Australia (Productivity Commission 2011). It was also the approach that the CIE had proposed to the Commission for this inquiry (CIE 2011).

Customs clearance charges are unlikely to yield an overestimate of the costs of customs clearance. The General Agreement on Tariffs and Trade (GATT) expressly requires that fees and charges levied for any services rendered in respect of imports — or exports for that matter — are limited to the approximate cost of the services in question and may not represent an indirect protection to domestic goods or taxation of trade for fiscal purposes.[17]

Due to the difficulties of accurately measuring all of the costs associated with customs clearance, most WTO members do not try to recover all of their import processing costs in clearance fees and charges. For this reason we were conscious that, other things being equal, the highest of the observed levels of fees and charges were likely to be the best proxy for the costs of customs clearance.

Of those that we have examined, the charges levied by the ACBPS were the most promising for the purposes of the economic evaluation. By law the Service is required to set its charges so as to fully recover the costs it incurs in processing imports by each mode, without regard to the value of the goods.[18] Given this requirement and the GATT obligation not to over-recover import processing costs, we consider that its charges are the best indicators of the resource cost of conducting a full customs clearance for a low value import consignment by each of the modes in question.

The ACBPS charges AUD40.20 per declaration for the electronic clearance of mail and air cargo and AUD50.00 per declaration for the electronic clearance of sea cargo. Its charges for manual clearance are somewhat higher — AUD48.85 per declaration for international mail and air cargo and AUD65.75 per declaration for sea cargo.

For the purposes of the economic evaluation, we have converted the electronic clearance charges to their USD equivalents at market exchange rates.[19]

To reflect the different economic situation and circumstances faced by each of the economies under evaluation compared to that in Australia, we have multiplied these USD equivalents by the ratio of GDP per worker in the economy in question to the GDP per worker in Australia in each case. In calculating this ratio, the GDP values, of course, have to be expressed in USD.[20] This approach assumes that, if the GDP per worker in USD in one of the APEC-6 economies is half that of Australia, so too will be the relative cost of an equivalent customs clearance in that economy.

The USD values estimated for each of the APEC-6 economies on this basis are set out in Table 4.5. These were used to evaluate the savings in public administration costs under all the threshold scenarios on the basis that the resource cost for a *de minimis* clearance is negligible. For each of the scenarios, the unit costs in Table 4.5 were multiplied by the change in the number of *de minimis* clearances that were estimated for the relevant mode and scenario.

In the absence of concrete evidence to the contrary, we also assume that any compliance assurance program would not necessarily have to involve substantially greater costs to cover any enhanced *de minimis* regime in an effective manner.

Table 4.5: Cost of low value import transactions to customs administration, select APEC economies (a), USD per consignment

Mode of delivery	CA	ID	JP	MY	PH	TH
Air & mail cargo	38.74	5.06	36.61	14.14	3.37	8.38
Sea cargo	48.19	6.29	45.53	17.58	4.19	10.42

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH).

Source: CAPEC and Trade Data International Pty Ltd, estimates by ITS Global Asia Pacific.

4.4 Savings in business compliance costs

The more streamlined customs procedures that are applied under a *de minimis* regime can be expected to reduce the significant compliance costs that a general customs clearance regime imposes on importers either directly or indirectly thorough their agents. Our estimates indicate that savings in business compliance costs under the USD200 threshold scenario would account for over a quarter of the gross savings from such a change.

Competition will ensure that the agents will eventually pass on any such costs savings to their clients in the form of lower fees or higher quality of service, and the importers, in turn, will pass the savings onto their customers in the form of lower product prices.

Our literature review only identified a few published estimates of the potential for savings in business compliance costs from switching low value transactions from a general customs clearance channel to a *de minimis* one.

Hufbauer and Wong (2011) estimated that increasing the *de minimis* threshold in the United States from USD200 to USD800 would generate savings in business compliance costs of up to USD33 million a year in respect of inwards international mail and air express cargoes.

This estimate was based on an assumed saving in employee time of 0.15 hours in completing the customs documentation for a low value transaction and a labour cost of USD21 per hour to cover wages and labour on-costs, such as the employer's health insurance and pension contributions. In addition Hufbauer and Wong (2011) estimate that the statutory storage requirements in respect of completed customs documentation cost air express firms in the United States about USD1 million a year. Their calculations imply that business compliance costs in the United States for full customs clearance of low value imports amount to USD6.60 per consignment.

The CIE (2011) found that switching from the general to the *de minimis* clearance channel in Australia would generate significant savings in business compliance costs. Customs brokers and air express carriers reported that a formal declaration took about 10 to 15 minutes of a broker's time and their typical rate for the service was charged out at AUD60 to AUD80 per hour — around USD66 to USD88 per hour at current rates. The CIE quoted the fees charged by online customs brokers in respect of low value consignments as ranging upwards from AUD50 per consignment — equivalent to USD55 per consignment.

Using what it considered was a conservative approach, CIE estimated the saving in business compliance costs from switching from full formal to *de minimis* compliance in Australia was AUD30 per consignment. This was substantially more than what has been estimated by Hufbauer and Wong (2011) for the United States. Even allowing for the greater economies of scale that would be available to express firms in the United States, there appears to be significant disagreement between the CIE estimate and that of Hufbauer and Wong.

For our purposes we have preferred to take the most conservative approach to each of the components that made up the relevant business compliance costs — the time taken by an importer or their agent to fulfil the customs requirements and the opportunity cost of that time.

We consider that 15 minutes seems to be a reasonable allowance for the minimum amount of time that it takes a knowledgeable person to arrange a low value customs clearance for a private business, while AUD60 per hour is a minimum estimate of the opportunity cost of that time based on the fee rates charged by customs brokers. This gives a minimum business compliance cost of AUD15 per transaction, and we stress that it is a minimum estimate.

To apply this estimate to any of the APEC-6 economies, it needs to be adjusted to take account of the relative differences in GDP per capita, as was the case in estimating the savings in public administration

to reflect the different economic situation and circumstances faced by each of the economies under evaluation compared to Australia or the United States.

The USD unit values that were estimated for each of the APEC-6 economies are in Table 4.6. These values were used to evaluate the savings in public administration costs under all the threshold scenarios on the assumption that the compliance cost for a *de minimis* clearance was negligible. For each of the threshold scenarios, the unit costs in Table 4.6 were multiplied by the change in the number of *de minimis* clearances for the relevant mode under that scenario.

Table 4.6: Cost of business compliance for low value imports, select APEC economies (a), USD per consignment

Mode of delivery	CA	ID	JP	MY	PH	TH
Air & mail cargo	14.46	1.89	13.66	5.27	1.26	3.13
Sea cargo	14.46	1.89	13.66	5.27	1.26	3.13

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH).

Source: CAPEC and Trade Data International Pty Ltd, estimates by ITS Global Asia Pacific.

4.5 Savings in merchandise transit time

In trade, as in all economic activity, time has an economic cost. The longer a product takes to get from the producer to the final consumer, the more likely the product is to perish, to be out of date, to be displaced by a superior alternative, or to simply lose the interest of consumers. There is also an opportunity cost in having working capital tied up in inventory. Hence saving the time merchandise has to spend in transit has an economic benefit; the extent of which depends on the nature of the product.

This study used the approach previously adopted by the APEC Secretariat for both the interim and final assessments of the Second APEC Trade Facilitation Action Plan (PSU 2010; 2011). APEC has used the economy-wide valuations of time that have been developed Professor David Hummels of Purdue University (Hummels 2001a; 2001b; 2007).

This study used the Hummels' estimates of the *ad valorem* tax equivalent of a day's transit time for products classified on the basis of the UN Standard International Trade Classification (SITC) (Hummels 2001b). We converted these SITC tax equivalents to a HS basis by aligning the two classification systems and estimated a weighted average of the value of a transit day for low value imports at the four-digit level of the HS. For this purpose, we used the HS product composition that we had previously estimated from our analysis of Indonesian import transactions of USD200 or less — Annex D has the details.

Our calculation put the value of a transit day at 1.08% of the value of the consignment. As we had no other comprehensive information of how the product composition of low value consignments might vary across the APEC region, we have used this value for each of the six economies, as well as all the scenarios, in the study.

This value is significantly higher than the estimate of 0.4% calculated by Hufbauer and Wong (2011) for the United States, which was also based on the Hummels' work referred to above. Their estimate was, however, based on a much wider range of consignment values and a much narrower range of HS classes than were evident from our analysis of Indonesian imports in Annex D.

The latter may also reflect the fact that the Hufbauer and Wong study was focused on imports by the United States with a consignment value between USD200 and USD800.[21] This value range is likely to be characterised by considerably greater product specialisation but is well outside the focus of our study.

Given the lack of data on the composition of low value imports by the rest of the APEC-6 economies, we have used an *ad valorem* tax equivalent of 1.08% to value a transit day to each of them for all low value imports.

For each mode and scenario combination the time saving was the product of:

- the daily *ad valorem* tax equivalent

- the increase in the aggregate value of de minimis imports by that mode as a consequence of the assumed threshold level, and

- the average time saving for the mode in question as a consequence of the assumed threshold level.

The estimates of the increase in value of de *minimis* imports were based on the import volume projections previously outlined in Tables 4.3 and 4.4. The savings in air cargo transit time for each economy were taken from the results of our survey of CAPEC members. The results that we obtained are set out in Table 4.7.

In the case of sea cargo, the size of the assumed saving in transit time was based on the results of the most recent Time Release Survey by the Japanese Customs and Tariff Bureau. The Bureau conducts regular surveys of the time between submission of an import declaration and the release of the cargo in question.

The Bureau used its 2009 Time Release Survey to compare customs processing times for sea cargo that had entered Japan under its Approved Economic Operator (AEO) program with the equivalent times for sea cargo that entered through the general customs clearance channel.[22] The Bureau found that the clearance times for the AEO cargoes were, on average, 60% faster than those for general cargoes (Igarashi 2010).

Table 4.7: Saving in merchandise transit time with de minimis customs clearance, select APEC economies (a), days per consignment

Mode of delivery	CA	ID	JP	MY	PH	TH
Air & mail cargo	0.5	1.6	0.5	0.5	1.6	1.3
Sea cargo	0.6	2.4	1.2	0.6	1.2	1.2

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH).
Source: CAPEC and Trade Data International Pty Ltd, estimates by ITS Global Asia Pacific.

To put these results into an appropriate context, the World Bank's annual series of *Trading across Borders* surveys have consistently put Japan well below the APEC average in terms of the time taken by importers in negotiating what the survey terms as 'Customs clearance and technical control' (World Bank Group 2010). From this we conclude that the transit saving achieved through the Japanese AEO program should, as a minimum, approximate what could be achieved through the *de minimis* clearance of sea cargo.

Accordingly we have used a saving of 60% to estimate the transit time saving for sea cargo by all of the APEC-6 economies. It has been applied to the total time taken in 2010 by sea cargoes to complete customs clearance and technical control in each of the APEC-6 economies, as estimated by the World Bank from its annual *Trading across Border* survey (World Bank Group 2010).

This is a conservative assumption. Greater savings should be possible. Nevertheless, the relatively low value-to-volume ratio that applies to low value imports means that the value of the time savings are small relative to the savings based on transaction volume — such as public administration and private compliance costs.

4.6 Taxation revenue foregone

The tariff revenue foregone from a higher *de minimis* threshold will vary with the HS classification of the imported merchandise covered by the threshold, the origin of the imports, and the tariff schedule of the importing economy.

For the HS composition of the merchandise, we drew on the results of our analysis in Annex B, which examined the composition of imports by Indonesia with a landed value of USD200 or less. This reflected the clear absence of any real alternatives in this regard. In our view the substantial differences that we have identified previously between air cargo imports and those by all modes argued against the use of the former as the basis for the estimates of the foregone revenue.

We have estimated a weighted average MFN tariff rate for low value products for each of the APEC-6 economies — Table 4.8 has the results. Each weighted average was based on the Tariff Schedule published by the economy in question.

Table 4.8: Weighted average tariff rates on import consignments of USD200 or less, select APEC economies (a), per cent

Tariff Measure	CA	ID	JP	MY	PH	TH
MFN tariff rate	4.70	7.70	1.66	14.68	6.79	10.41
Applied tariff rate (b)	0.77	2.45	1.55	7.14	3.59	5.33
Revenue yield (c)	0.77	2.43	0.28	0.97	3.59	5.31

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH)
       (b) MTN rate less adjustment for preferential tariff rates under existing FTAs
       (c) Applied rate less deduction for de minimis exemptions.

Source: WTO; estimates by ITS Global Asia Pacific.

Our estimate involved weighting the MFN tariff rates in the tariff schedule for each economy in the study by the product shares at the four-digit HS level we previously calculated for imports of USD200 or less per consignment — Annex B has the details of the estimation of the product shares.

Multiplying the average MFN rate by our projection of the increase in value of *de minimis* imports up to the proposed *de minimis* threshold level gave an approximation of the potential revenue loss for the threshold scenario in question. It needs to be adjusted, however, for the impacts of preferential tariff rates and the current *de minimis* revenue exemptions.

Since it established the ASEAN Free Trade Area (AFTA) in the early 1990s, ASEAN has concluded five FTAs with major trading partners, including China (2002), the Republic of Korea (2005), Japan (2008), India (2009) and Australia and New Zealand (2009). ASEAN has also concluded the ASEAN Trade in Goods Agreement (ATIGA) to complete the process of tariff liberalisation within ASEAN by 2010 for the original six member states and by 2018 for the newer ones.

The depth, scope and pace of tariff liberalisation under each agreement varies by ASEAN economy, product and trading partner. In some agreements, such as the ASEAN–India FTA, certain sectors or products are excluded from the liberalisation provisions in the Agreement. In others, such as the AANZFTA, scope of the tariff liberalisation is far more comprehensive.

The time available for the study did not allow for a highly time consuming, product-by-product assessment of each of the four ASEAN economies, let alone of Canada and Japan as well. We have therefore assumed that all low value imports by the five from any of their FTA partners are duty free. We have applied a similar assumption to Canada in respect of its North American Free Trade Agreement (NAFTA) partners and Japan in respect of its FTA partners.

Adjusting for the duty free rates we have assumed are in the process of being applied to imports from FTA partners, gives an estimate of the effective applied tariff rate for each of the APEC-6 economies in the study. They are presented in Table 4.8.

We have also assumed that the tariff revenue lost due to the existing *de mininis* threshold is the existing threshold level as a percentage of the threshold level specified in the scenario under analysis. This

percentage is multiplied by the applied tariff rate and gives the revenue yield for each economy under the scenario in question. These estimates are also set out in Table 4.9. They may be thought of as the indicators of the long-run impact on revenue after the tariff preferences that have been included in recent FTAs are fully implemented.

In most of the economies in the study the scope for revenue loss is much lower than many may expect. This is due to a combination of relatively low MFN rates in all but two of the economies and extensive departures from MFN rates for much of the trade of all six due to the proliferation of FTAs.

The spreadsheet model developed for the study does not estimate the impact of changes to *de minimis* thresholds on other indirect tax revenue. This reflects the technical challenges of modelling complex tax regimes with different rates for different products at different stages of production. It is, nevertheless, possible to use the model to test the sensitivity of its results to a range of broad assumptions about the nature of the indirect tax regimes in the APEC-6.

Except for Malaysia, all APEC-6 economies currently impose a VAT style of tax at each stage in the production of most goods and services but Malaysia is planning to replace its sales and services taxes with such a tax. These taxes are currently levied at rates of 5% (Canada and Japan), 7% (Thailand), and 10% (Indonesia and the Philippines). The rate in Malaysia is expected to be no more than 10%.

Applying these headline VAT rates to the projected change in the value of imports, which enter via the *de minimis* channel, gives an indication of the maximum amount of VAT revenue that could be foregone by lifting the threshold under each scenario. The impact that such a revenue loss would have on the earlier estimates of net economic benefit for the APEC-6 economies, as well as the implications for all APEC members, are summarised in Tables 4.10 and 4.11.

Table 4.10: Net economic benefit of alternative de minimis thresholds in APEC, VAT sensitivity test, USD billion per year

Alternative Threshold USD	APEC-6 Economies (a)		APEC-21 Net Economic Benefit
	Maximum VAT Revenue Foregone	**Net Economic Benefit**	
50	0.001	0.031	0.16
100	0.135	3.754	19.2
150	0.189	4.712	24.0
200	0.237	5.691	29.0

Notes: (a) Canada, Indonesia, Japan, Malaysia, the Philippines and Thailand.
Source: Estimates by ITS Global Asia Pacific.

Table 4.11: Net economic benefit of alternative de minimis thresholds, by APEC economy (a), VAT sensitivity test, USD million per year

Alternative Threshold USD	CA	ID	JP	MY	PH	TH
50	30.2	0	0	0	0.2	0.3
100	3,663	28.48	0	0	8.6	53.4
150	4,511	31.7	101	0	8.5	59.5
200	5,268	34.9	296	17.7	9.2	65.8

Notes: (a) Canada (CA), Indonesia (ID), Japan (JP), Malaysia (MY), the Philippines (PH) and Thailand (TH).
Source: CAPEC and Trade Data International Pty Ltd, estimates by ITS Global Asia Pacific.

The message of the sensitivity test is clear-cut. The loss of VAT revenue does not qualitatively change any of the results that were discussed above.

Our estimates of VAT revenue foregone are certainly excessive. They assume that the headline tax rate applies to all low value imports. In fact each of the APEC-6 economies exempts certain types of merchandise from their VAT liability but no allowance has been made for these exemptions.

Most importantly no allowance has been made for the fact that a high proportion of low value imports are business inputs.

VAT regimes, including those of the APEC-6, tax the value that is added at each stage of production by allowing businesses to claim a tax credit for any VAT that has been paid on their business inputs. If VAT has not been paid on them, for whatever reason, the VAT liability for the product they were used to make is increased by the amount of the unpaid tax. In other words any VAT that is not collected at an earlier stage of production should be collected by the time the final product is sold to the consumer.

This means that the only VAT revenue that is foregone by raising a *de minimis* threshold relates to the merchandise, which is imported by or on behalf of households. All the available evidence suggests that this is a clear minority of the aggregate value imported as low value consignments.

5. Conclusions and recommendations

A *de minimis* regime provides more streamlined border clearance procedures than apply to other imports. These reduce the costs borne by importers and accelerate delivery of merchandise, which both benefit the final consumer. Such a regime allows governments to refocus their revenue collection on the higher yielding parts of the tax base.

Most APEC economies have *de minimis* arrangements but they vary considerably from economy to economy. Thresholds range from under USD1 to more than USD1,000 and the products that are eligible for exemption vary. These differences can significantly affect the balance of the economic benefits and costs that a regime generates.

This report highlights the principal characteristics of the *de minimis* arrangements that currently apply in Canada, Indonesia, Japan, Malaysia, the Philippines and Thailand together with their underlying rationales. It then evaluates the economic benefits and costs of generally increasing those thresholds, particularly those that are set at the lower levels.

These six economies have been chosen as being broadly representative of the APEC region as a whole, in the expectation that results obtained here will be able to be extended to the other economies of the region.

A major impediment to advancing our understanding of these issues, however, has been the paucity of basic information available to the public. This problem has been well documented by the Australian Productivity Commission, which is in the process of undertaking a public inquiry into the *de minimis* arrangements in that jurisdiction.

The lack of information has constrained the sophistication that could be applied to the economic analysis. Nevertheless, based on conservative assumptions, we have been able to estimate the order of magnitude of the net economic benefit that would be generated by alternative *de minimis* arrangements. For this purpose the analysis has assessed a series of minimum thresholds — namely USD50, USD100, USD150 and USD200.

A minimum threshold of USD200 would generate a net benefit of USD5.9 billion a year for the six economies, which is equivalent to around 0.086% of their collective GDP. Extension of this result to the rest of the APEC membership would imply a net benefit of about USD30.3 billion for all 21 economies.

Decreasing the minimum threshold merely reduces the extent of the net benefit and does so more than proportionately. It remains true, nevertheless, that any increase in the threshold in any of the six economies is better than none.

Some 98% of the net benefit from the USD200 threshold is accounted for by savings in the cost of government administration and business compliance, the balance being modest savings in the transit time of imported merchandise. The tariff revenue foregone is a very minor consideration, as it amounts to less than 1% of the benefits. The same broad pattern was evident across all six economies.

The dominance of government administration and business compliance savings on the results is not surprising. It simply reflects the basic economics of this category of imports — relatively large numbers but relatively low aggregate value. Hence the volume-based impacts, such as those on customs and private business processing costs, must loom larger than the value-based impacts, such as those involving transit delays and tariff collections. In the case of the latter, the potential revenue base has already been substantially eroded by preferential tariff rates to FTA partners and the existing *de minimis* exemptions that are in place, even in those economies with relatively high applied tariff rates.

Although it was not possible to model the impact of *de minimis* thresholds on VAT revenue, a sensitivity test based on the maximum possible revenue loss did not qualitatively change the above results. The actual impact is likely to be much less than this maximum as there is only a net loss of VAT revenue on imports by or on behalf of households. The vast majority of low value imports are business inputs so any VAT not collected at the border can be expected to be collected on the final product.

Our conclusions have been strongly reinforced by the Productivity Commission, the Australian Government's independent economic advisory body. The Commission is reviewing the *de minimis* threshold applied in Australia. Although Australia has the highest threshold in APEC and a 10% GST, the Commission has concluded that any reduction would impose a net cost on the economy, and a substantial one at that.

Notwithstanding the severity of the information constraints on the analysis of the *de minimis* issue, these orders of magnitude are unlikely to change with the application of more information or better quality data. At this level we judge the results to be robust, at least for the six economies that we have examined in any detail. Indeed the conservative nature of the analytical approach should mean that more refined estimation is likely to yield higher net benefits than what we have estimated.

For a start, the estimates in this report have made no allowance for any behavioural response to raising the thresholds. Competition will ensure that the savings in transit time and business compliance costs generated by higher thresholds will eventually be passed on to domestic producers and consumers in the form of lower prices and higher quality products. These changes will, in turn, stimulate increased output by downstream industries and increased consumption by households. Neither impact has been accounted for here but both would benefit the community as a whole.

The size of these behavioural benefits would be significantly increased by a coordinated approach within APEC to raising *de minimis* thresholds and broadening their coverage across the region. The leverage that is available is similar to what multilateral liberalisation of trade barriers through the WTO can achieve compared to unilateral liberalisation. After all, a coordinated increase in *de minimis* thresholds is functionally and economically equivalent to a coordinated cut in trade barriers for intermediate products, which are the fastest growing component of global trade.

The policy implications of our results are therefore quite straightforward. A commercially attractive *de minimis* arrangement makes sound economic sense for all economies. While the optimal level of the threshold for any economy remains somewhat of an open question, the direction of change is quite clear from a practical perspective.

Most, if not all, APEC economies would benefit by increasing their existing thresholds, and by a substantial amount. APEC could assist this process by agreeing to recommend a minimum threshold level to its members with the option of a higher level to better suit individual circumstances.

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Notes

1 The views expressed in this report are those of its authors. The consultants, ITS Global Asia Pacific (ITS) and the Centre for Customs and Excise Studies (CCES), take no liability for commercial decisions taken on the basis of information in this report. The information is accurate to the best of the consultants' knowledge, however the consultants advise that no decision with commercial implications which depends upon government law or regulation or executive discretion should be taken by any person or entity without that party's having secured direct advice from the government agency concerned in writing.

2 Transaction costs are the resource costs incurred in searching out, negotiating, and completing an economic exchange. They include the costs that government regulation and taxation imposes on these processes. Transaction costs need to be distinguished from the costs of producing what is exchanged, which are sometimes referred to as 'transformation costs' to underline this distinction.

3 *Financial Administration Act*, section 17, Order-in-Council P.C. 1985-2954, October 3, 1985 (Canada Gazette, Part II, p. 4291) as amended by Order-in-Council P.C. 1986-1400, June 12, 1986 (Canada Gazette), Part II, p. 2616) and Order-in-Council P.C. 1992-1432, June 24, 1992 (Canada Gazette, Part II, p. 3098).

4 *Financial Administration Act*, section 17, Order-in-Council P.C. 2955 as amended by Order-in-Council P.C. 1986-1401 and Order-in-Council P.C. 1992-1431.

5 The principal articles that have been designated as those to which duty exemption is not applicable are as follows: Leather bags, handbags, gloves, etc., knitted apparel, ski boots, leather shoes and footwear with leather soles.

6 The original legislation specified a threshold of PHP10 but it was amended subsequently.

7 A Bill to increase the threshold to PHP 2,500 has been introduced into the Philippines Senate but it does not seem to have been passed at this time.

8 This composite figure represents the sub-index breakdown as outlined above.

9 The Member States of COMESA are Burundi, Comoros, the Democratic Republic of the Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, the Seychelles, the Sudan, Swaziland, Uganda, Zambia, and Zimbabwe.

10 Annexes A to D are available from the authors. If you wish to view them, please email editor@worldcustomsjournal.org.

11 These estimates are based on the April 2011 edition of the *World Economic Outlook* database (IMF 2011).

12 This is because their existing thresholds are equivalent to USD150 (Malaysia), USD129 (Japan) and USD50 (Indonesia).

13 This intensity is measured in terms of the total value of imports, valued at USD200 per consignment or less, as a share of GDP.

14 Among other things, the inquiry by the Australian Productivity Commission is examining the *de minimis* arrangements that apply in Australia. On 4 August 2011 the Commission has released its Draft Report for public comment (Productivity Commission 2011).

15 The approach may be expressed formally as follows: TV [total value of imports by all modes] = TV_a [total value of imports by air cargo] / S_a [air cargo's share of the total value of all imports by all modes].

16 The ISO 3166 codes are: CA (Canada); ID (Indonesia); JP (Japan); MY (Malaysia); PH (the Philippines); and TH (Thailand).

17 General Agreement on Tariffs and Trade (GATT 1954), Article VII.1.

18 The legal authority for this is the *Import Processing Charges Act 2001*. The charges are widely published by the Service (Australian Customs Service 2006). As far as we are aware, Australia is the only APEC economy that has mandated the full recovery of customs processing costs.

19 The conversion was at a USD to AUD exchange rate of 1.1000.

20 The GDP and employment data in question were sourced from the April 2011 edition of the *World Economic Outlook* database (IMF 2011).

21 The current *de minimis* threshold in the United States is USD200 (PC 2011).

22 An Approved Economic Operator (AEO) is a private business involved in the international movement of goods in whatever function that has been approved by or on behalf of a national Customs administration as complying with World Customs Organization or equivalent supply chain security standards. The requirement for an AEO program is a key component of the WCO Framework of Standards to Secure and Facilitate Global Trade (SAFE) (WCO 2007).

Stephen Holloway

Steve Holloway, Dean of Studies (Education/Research) and Principal Director of the Centre for Customs and Excise Studies, and an Adjunct Professor in the Faculty of Business, Government and Law, University of Canberra, has had 25 years' experience in customs and international trade, including 20 years with the Australian Customs Service. He has worked closely with international organisations, customs and revenue administrations and the private sector on international trade and border management including customs reform and modernisation, international logistics, the international regulation of intellectual property, legislative reform and strategic export controls.

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Jeff's experience has involved research and advice on international trade, including the transaction costs that are imposed on merchandise trade by government regulation and other policy measures along international supply chains. He was responsible for the development of the methodology that has been used for the estimation of trade transaction costs in APEC economies and oversaw the application of that methodology to both the Interim and Final Assessments of the Second APEC Trade Facilitation Action Plan, which his firm conducted for the APEC Secretariat. This program was the precursor to APEC's Supply Chain Connectivity Framework Action Plan.

Prior to moving into private consultancy, Jeff held senior executive positions in several Australian Government departments, was seconded to the OECD, Paris, and has presided over or participated in a number of public inquiries.