25 November 1987

# UNITED STATES CUSTOMS USER FEE

*Report by the Panel adopted on 2 February 1988*
*(L/6264 - 35S/245)*

## I. INTRODUCTION

1. At the requests of the delegations of Canada and the European Economic Community, the Council agreed to establish the Panel, on 4 March 1987, and authorized the Council Chairman to draw up the terms of reference

gave Brazil, Chile, Hong Kong, Mexico, New Zealand, Peru, Sweden on behalf of the Nordic countries, and Switzerland this opportunity. Australia, Hong Kong, India, Japan, New Zealand, Per

10. The merchandise processing fee is collected at the port of entry by Customs

18. Section 13031(a)(9), as amended, exempts the following three classes of merchandise from the merchandise processing fee:

(a) Articles provided for in schedule 8 of the Tariff Schedules of the United States, i.e. articles exported and returned; personal exemptions; governmental importations; importations of religious, educational, scientific and other institutions; samples and articles admitted free of duty under bond; non-commercial importations of limited value; and other special classification provisions;

(b) Products of the insular possessions of the United States; and

(c) Products of countries listed in TSUS General Headnote 3(e)(vi) or (vii) (least developed developing countries, and beneficiary countries of the Caribbean Basin Economic Recovery Act (CBERA)).

19. Information provided by the United States showed that, of total 1986 imports of $369 billion, these three exemptions would have resulted in the merchandise processing fee not being applied to approximately $102 billion (approximately 28 per cent by value). The formula for calculating the fee in subsequent years is designed to recover the entire cost of "commercial operations" from the fees paid by non-exempt imports. The formula is to divide projected expenses of the commercial operations budget by the projected value of non-exempt imports for that year.

20. The United States reported that, according to the most recent data available, receipts from the merchandise processing fee for FY 1987 collected during the ten months it was in force (1 December 1986 to 30 September 1987) were $536 million. Estimated receipts for FY 1988 were $540 million, assuming application of the 0.17 per cent ad valorem fee provided for in the legislation and no change in any other provision of that law. The cost and revenue estimates supplied by the United States are summarized in Annex I of this report.

## III. MAIN ARGUMENTS

### A. Summaries

21. Canada requested the Panel to find that the United States merchandise processing fee violated the General Agreement because:

(i) it was neither commensurate with the cost of service rendered, nor limited in amount to the approximate cost of those services, as required by Articles II and VIII;

(ii) it constituted taxation for fiscal purposes, contrary to Article VIII, to the extent that:

(a) the fee was charged for government activities which could not be considered services rendered to the importers in question; and

(b) it was imposed at a rate leading to collection of funds exceeding the cost of the services provided during the period in which the fee was charged; and

(iii) it represented indirect protection to domestic products, contrary to Article VIII.

22. Canada requested the Panel to find, therefore, that the ad valorem merchandise processing fee, a

23. The European Economic Community requested the Panel to find that without prejudice to the conformity of the merchandise processing fee with other GATT provisions:

(i) The ad valorem merchandise processing fee introduced by the United States was inconsistent with Articles II and VIII; and

(ii) its introduction therefore constituted a prima facie nullification or impairment of benefits accruing to the Community.

24. The United States requested the Panel to find that:

(i) the merchandise processing fee was commensurate with the cost of services rendered, and therefore was consistent with Article II of the General Agreement; and

(ii) the fee was approximately equivalent to the cost of services rendered, and represented neither an indirect protection to

it was not proportionate, except by coincidence, with the value of the goods. Likewise, the fact that the revenue from the fees was used to pay for technical laboratories and commercial customs fraud enforcement meant that importers importing products which did not need to be submitted to technical laboratories were contributing towards the cost of those laboratories, and that importers who were not and could not be suspected of customs fraud were contributing to the cost of fraud enforcement. Both of these features of the US fee system were contrary to the plain words of Articles II and VIII.

28. The United States did not agree that Articles II and VIII required contracting parties to match fee levels to the cost of services on a shipment-by-shipment basis. The United States argued that Articles II:2(c) and VIII:1(a) clearly permitted contracting parties to impose user fees that recovered the full costs of services rendered and were not in excess of such costs. Neither Article II nor Article VIII required that fees be "equal to" the cost of services rendered, but merely that they be "commensurate", or limited to the "approximate" cost. The legislative history of the merchandise processing fee indicated clearly the desire of Congress to conform to these provisions. The merchandise processing fee, as enacted, was commensurate with the cost of Customs commercial operations, as the total amount collected would approximately match salaries and expenses for such activities.

29. Canada did not agree that a user fee would be consistent with the GATT merely by virtue of the fact that the total revenue collected did not significantly exceed the total cost of services rendered. Such fees were levied, and charges are collected, on the basis of individual shipments. The "approximate cost" should therefore be calculated on the basis of the services rendered to individual shipments in connection with importation, and this calculated cost should represent an upper limit of the fee which could be charged. An indication that "approximate cost of services rendered" was intended to apply to an approximation of the cost of services for individual shipments was the inclusion of a list of services in Article VIII:4, some of which were applicable to only a limited number of shipments. For example, only a small percentage of imports into the United States were subject to quantitative restrictions or licensing requirements but, under the current ad valorem fee system, the cost of providing these "services" was spread across all imports. Similarly, the requirement for quarantine, sanitation and fumigation services would occur with respect to a limited number of imports, but the US divided these charges among all imports paying fees. Evidence that the drafters had intended that "cost of services" would relate to individual entries rather than the cost as a whole could also be found in the words of Article II:2 to the effect that "Nothing in this Article shall prevent any contracting party from imposing at any time on the importation of any product …" (emphasis added). Therefore, the "total cost" method of calculating fees was inconsistent with both Articles II and VIII when the fee collected was higher than the cost of services rendered, for example in the case of high value or bulk shipments. Shipments of duty-free products, where the US Customs did not have to calculate or collect the applicable duty, could also be subject to fees higher than the cost of services rendered.

30. The European Economic Community maintained that a comparison of the total merchandise processing fees collected with the total cost of the US Customs' "commercial operations" was not the test to be applied under Articles II and VIII. If this were the only requirement, user fees could be imposed on any basis, on any range of products, in accordance with any rules, as long as the revenue from them covered the total cost of the customs service collecting them, e.g. by a system which imposed fees on agricultural but not industrial products. Yet clearly any range of products, however defined, should not have to bear a disproportionate share of the cost of operating the customs service in question. Moreover, if the US theory were correct in that total cost was the only relevant criterion, it would be necessary for the Panel to determine which activities of the US Customs could correctly be considered as commercial customs

31. The United States replied that the GATT clearly permitted recovery of the costs of services rendered to importers; the problem was that of finding a fair and administrable allocation method that would avoid a protective effect and maximize stability and predictability in trade transactions. Both Articles II:2(c) and VIII:1(a) left it open to each contracting party how to collect user fees. These provisions did not rule out the use of a systematic method such as a flat fee or an ad valorem fee. The negotiating history confirmed this interpretation.[1] The drafting of the initial GATT provisions on user fees had been conducted against a background of a number of countries maintaining ad valorem user fees. When the GATT had entered into force, the provisions of Article VIII:1(a) were only hortatory in nature. When Article VIII:1(a) was made obligatory in 1955 ad valorem user fees were still widely practiced. It was not reasonable to infer from the historical record that the countries imposing ad valorem fees had intended to make their own ad valorem fees GATT-illegal. The more reasonable inference was that at that time, ad valorem fees were not generally considered to be GATT-inconsistent. No ruling has ever been made rejecting an Article VIII fee because it was assessed on a basis linked to the value of merchandise. Such a finding would be surprising, in view of the significant number of contracting parties, including some EEC Member States, still using such fees. A 1986 survey by the United States Customs had shown that over 50 countries out of 79 countries surveyed charged some type of user fee; seventeen contracting parties had been found to charge on an ad valorem basis or a basis related to the value of imported merchandise. The results of this survey were communicated to the Panel. In the most recent GATT examination of border fees, contained in the Report of the Working Party on the Accession of the Democratic Republic of the Congo (Zaire) (18S/89), the aspect of the statistical fee objected to had been its level (3 per cent ad valorem), not its ad valorem nature. The United States hoped that the Panel would take into account the significance of its decision not only for the United States but also for many other contracting parties.

32. The United States argued that each of the options for a GATT-consistent user fee had its advantages and disadvantages. Any approach could produce arbitrary results in some cases. For instance, a transaction-based fee assessed at a flat rate per entry might avoid valuation of individual entries. However, countries sharing a land border with the United States would benefit disproportionately from a fee assessed on that basis, as they made extensive use of consolidated entry procedures permitting entry of multiple shipments on one entry form. Furthermore, the calculation and collection of duties amounted to a minor workload factor in entry processing; determination of the proper classification for a shipment was a more complex process, and was required for all entries regardless of the relevant rate of duty. The trend in US Customs operations was away from transaction-by-transaction accounting, and towards increased automation of operations, di

distribute the cost of Customs commercial services". An ad valorem fee provided more certainty and was more administrable for the importing public, for foreign exporters and for Customs than were the alternatives.

33. The United States maintained that Article VIII did not require contracting parties to match fee levels to the cost of services on a shipment-by-shipment basis. By any commercial or accounting definition, the cost of a service included both the direct cost of the service and the indirect costs that the service-providing organization

of the customs authority in question. The EEC had never suggested that indirect costs should be excluded from the cost base of a user fee or that they should be cross-subsidized from general tax revenue. However, if some importers were allowed to make a disproportionately small contribution to the cost of the whole Customs Service, and others were obliged to make a contribution which was more than the cost of providing services to them, the government concerned could not claim that the costs which were not paid for by under-contributing importers were "overhead costs". Any objective and bona fide method of estimating the average cost of clearance would normally be compatible with GATT. The EEC accepted that a customs user fee had to be allocated in some way. But Article VIII required fee levels to be matched approximately to the cost of providing the customs clearance on a shipment-by-shipment basis. The EEC did not say that only a flat rate fee was permitted under GATT. However, in the abstract, all other things being equal, it was clear that in a system where the cost of clearance was similar for all types of goods - and in which the national authorities had seen no reason to regard some kinds of clearance as more costly than others - a flat rate fee was much more likely to be consistent with GATT than an ad valorem fee, which automatically overcharged importers of high-value consignments and undercharged importers of low-value consignments. If the clearance of certain types of imports was more costly, e.g. because of the need for special testing, their clearance might be subjected to a higher fee. However, the cost for such special services should only be borne by those who used or ca[illegible]ve defects, that did not make the US system compa[illegible]nts across common land frontiers coul[illegible]nsidered a defect; if they were [illegible]f the cost savings involve[illegible]y it was wrong to [illegible]lorem customs user[illegible]

of services in connection with importation for which fees might be charged. All of the services enumerated were specific actions/requirements for getting goods into, or out of, a country, such as licensing, analysis, inspection and quarantine. The decision to provide a limited list of services clearly showed that the drafters had not expected a country to defray completely all costs of providing customs clearances through the mechanism of fees charged to importers. Various additions to the list had been considered during the drafting of the ITO and the GATT. Some of these had been adopted and others rejected. For example, it had been agreed to include the phrase "such as consular invoices and certificates" (EPCT/C.II/54/Rev.1, page 25) but not the addition to the list of "(i) Port facilities" (EPCT/W/67). This showed clearly that the drafters had envisaged limits on the activities for which fees could be charged. Some programmes the United States had included under the heading "Commercial Operations", such as clearance of carriers, could not reasonably be considered as services rendered in connection with importation of products. Not only was the clearance of a carrier a different activity from the clearance of merchandise, but the United States was already charging each vehicle and vessel a user fee for clearance under another user fee system. Additionally, included under "Commercial Operations" activities were enforcement of anti-dumping and countervailing duty orders, activities related to commercial fraud investigations, investigations

laboratories, legal rulings, and general regulatory audit and commercial fraud enforcement. Regulatory audit, combined with policing of customs fraud, had made it possible to be very selective in devanning and inspecting shipments. Without this a substantially higher proportion of shipments would have had to be inspected, with increased processing time for all imports.

40. Concerning other specific elements of the "commercial operations" budget tha

43. (c) The cost of "commercial operations" for the first two months of Fiscal Year 1987. Canada argued that the cost of Customs "commercial operations" for the first two months of FY 1987 (October-November 1986), when the merchandise processing fee wao

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not services that could be charged to importers who paid the merchandise processing fee should be a charge on general revenues, and thus a fee used to pay for such activities would be taxation for fiscal purposes.

53. The European Economic Community also considered that the merchandise processing fee represented a taxation of imports for fiscal purposes. The enactment of the fee until 30 September 1989 indicated that it was a contributory measure to the reduction of the US budget deficit. Explanations of the budget reduction process in the US Congress clearly demonstrated the link between the introduction of the fee and the objective to thereby reduce the budget deficit.

54. The United States stated that

relevant. The question of administration of consular fees had been addressed in the Recommendation by the CONTRACTING PARTIES of 30 November 1952 (1S/25) on "The Abolition of Consular Formalities and Code of Standard Practices". According to its paragraph 1 "Any consular fee should not be a percentage of the value of the goods but should be a flat charge". This Recommendation had been slightly modified in the Recommendation of 30 November 1957 (6S/25) to read "No consular charge should be assessed as a percentage of the value of goods but should be a flat charge". The Recommendation of 1952, as amended in 1957, had been reaffirmed in general terms by the CONTRACTING PARTIES in the Recommendation of 31 October 1962 (11S/214).

57. The European Economic Community stated that it would be pointless to say that importers should not be asked to pay too many fees and charges, even those which might be imposed for services specifically rendered to them, if they could legally be asked to pay a disproportionate contribution to the overall cost of customs processing. From a broader perspective the EEC took the position that service fees of the kind involved in this case were an anachronism in the modern world. It was questionable whether the collection of duties could be regarded as "services" provided. Neither the importer nor any private commercial party to any import transaction benefitted in any way from being obliged to comply with whatever importation formalities might be required. As a

60. The European Economic Community stated that the customs user fee had a considerable negative effect on its exports to the United States market. It was estimated to cost its exporters about $175 million in 1987.

## IV. SUBMISSIONS BY INTERESTED THIRD PARTIES

61. Australia called the Panel's attention to Article II:1(b), which required that products covered by a schedule should "be exempt from all other duties or charges of any kind imposed on or in connection with importation in excess of those imposed on the date of this Agreement or those directly and mandatorily imposed thereafter by legislation in force in the importing territory on that date". Australia considered that the merchandise processing fee, having the effect of raising duties and charges beyond the level existing when the United States schedule of bindings had been negotiated, was inconsistent with the United States obligations under that provision. It viewed the exception of Article II:2(c) as inapplicable because it did not consider the fee commensurate with the cost of services. Australia considered that the fees were also inconsistent with Article VIII as they appeared to have been imposed for fiscal purposes, were not related to the cost of the customs services rendered to the importer, and were a protection provided to United States industry. Benefits accruing to Australia under the General Agreement were therefore nullified or impaired within the meaning of Article XXIII:1(a). The United States had a number of commodities bound to Australia under Article II. Many items covered by ceiling bindings were entered at or near the bound rate and in such circumstances an additional fee breached even a ceiling binding.[3] The ad valorem fee particularly discriminated against shipments of bulk commodities, including a number of Australia's major exports, where the charge was disproportionately high in relation to the service performed. Also, since the merchandise processing fee had been imposed in addition to a "port user fee", Australia was concerned at the additional

trade of other contracting parties and to consult promptly with any contracting party whose interests were affected by the operation of the Agreement. It appeared that the United States intended to recover costs associated with the import of products from these areas by imposing greater than proportional fees on other contracting parties. It was a matter of concern that this discriminatory practice could

costs

65. New Zealand stated that if a charge such as the United States merchandise processing fee was compatible with Articles II and VIII, it would appear to be attractive for many contracting parties to consider. The basis of calculation of fees and charges, in terms of Article VIII, was to be the "approximate cost of services rendered". Any degree of flexibility in this provision implied by the term "approximate" seemed to relate to the degree of precision in calculating the cost rather than in the basis of the actual charging itself. For this basic reason it was difficult to reconcile an ad valorem basis with the basis prescribed by Article VIII. This contrast could be underlined by comparing the terms of this provision with those of Article VII:2(a). It was difficult to envisage that there would be a systematic relationship between value of imported goods and cost of services rendered. Yet, if a value was relatively high it would carry a relatively high charge. Also, the ad valorem charge might be particularly non-transparent, because it would be extremely difficult, if not impossible, to ensure that aspects of customs administration which were actually outside the ambit of fees and charges imposed "on or in connection with importation or exportation" were not built into the charges. The above considerations applied in respect of all imports, but were even more important in the case of bound items. A concession granted in respect of a given item created a particularly clear and firm obligation. The wording of Article II pertaining to these obligations clarifies and renders more precise the logic of Article VIII. The cost of services, for which permission to levy a charge was granted in Article II:2(c), was limited strictly to those applicable to the specific product subject to a concession. The first sentence of Article II:2 made this clear: "Nothing in this Article shall prevent any contracting party from imposing at any time on the importation of any product, etc." This, furthermore, was consistent with the nature of obligations in respect of a concession because it was granted in respect of a particular product. If an ad valorem system was applied there would be the possibility that the costs arising from Customs administration more generally (including those which would arise from the administration of other concessions negoti

30 September 1987, Singapore's estimated exports of about S$9,100 million for the same period would incur a payable customs user fee of approximately S$20 million. This would be an additional cost over and above the usual customs brokers' and other fees. Singapore was concerned about the effects on its exports to the United States which this additional fee would have. The merchandise processing fee might reduce the competitiveness of Singapore's exports in the US market, especially for products which were price-sensitive, and might have the indirect effect of encouraging potential US importers to source their merchandise from domestic suppliers.

## V. FINDINGS AND CONCLUSIONS

68. Having reviewed the arguments made by Canada and

issue, especially in the case of consignments

originated as a standard term to be incorporated in each contracting party's schedule of concessions (see E/PC/T/153) and was not raised to the text of Article II until some time later (E/PC/T/201).[8]

76. Second, it was necessary to determine what type of fees were incorporated within the basic concept of "services rendered" in Articles II:2(c) and VIII:1(a). The Panel concluded that there was a rather well established general understanding of this concept, demonstrated more by practice than by the actual text of the General Agreement. In its original form, as found in Article 13 of the United States' Suggested Charter of September, 1946, Article VIII was explicitly addressed to "fees, charges, formalities and requirements relating to all customs matters", and this definition was followed by an illustrative list which is virtually the same as the list now included in Article VIII:4. The illustrative list includes various aspects of the customs process such as "consular transactions", "statistical services", and "analysis and inspection". The text of Article VIII was later changed to enlarge the scope of that provision. Notwithstanding the fact that the enlarged scope gave a different meaning to the illustrative list in paragraph 4, GATT practice since 1948 has tended to interpret that illustrative list according to its original meaning, as a list of those customs-related government activities which the draftsmen meant when they referred to "services rendered". Thus, GATT proceedings have treated the following types of import fees as being within Article II:2(c) or VIII:1(a): consular fees (CP.2/SR.11 (pages 7-8):jETBT1 0 0 1 2

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of services" limitation in Articles II and VIII. The complainants stressed that they did not intend to question the ad valorem method itself. They suggested, for example, that they would not object to an ad valorem fee that had a ceiling limitation equal to the average cost of processing an individual customs entry. The aspect of the United States fee the complainants wished to challenge was its tendency to impose fees exceeding the average cost of processing an individual entry. When the rate of an ad valorem fee is calculated by dividing the total costs of customs processing by the total value of the imports processed, the fee will, when imposed without upper limits, automatically exceed the average cost of processing whenever it is applied to entries of greater-than-average value.

79. The Panel agreed with the parties that the GATT consistency of this type of ad valorem fee turned on the meaning of the "cost of services" limitation in Article II:2(c) and Article VIII:1(a). The Panel understood the central contentions of the parties to be as follows: Canada and the EEC had argued that "cost of services rendered" should be interpreted to mean the cost of the customs processing activities ("services") actually rendered to the individual importer with respect to the customs entry in question, or, at least, the average cost of such processing activities for all customs entries of a similar kind. Both complainants had stressed that the normal practice with respect to service fees was to require persons to pay only for the services rendered to them. The United States had argued that the "cost of services" limitation did not require exact conformity between fees and costs, but only that the fee be "commensurate with" the cost (Article II:2(c)), or limited to the "approximate" cost (Article VIII:1(a)). It had argued that, stated in these terms, the "cost of services" requirements would be satisfied if the total revenues from the fee did not exceed the total cost of the government activities in question, and if the fee were otherwise fair and equitable in its application. The United States had stressed that the ad valorem structure of the merchandise processing fee was the most equitable and least protective method by which such a fee could be imposed.

80. The Panel agreed with Canada and the EEC that the ordinary meaning of the term "cost of services

distortive means of levying such a tax. That structure would have the lowest ad valorem impact for whatever amount was being collected[9], it would create no distortion in relative prices between imports, it would be the most predictable for traders and investors, and it would be the simplest and least costly to administer. The United States had represented that the importers affected by the merchandise processing fee preferred its present method to all others. The Panel had no difficulty in believing that this was so.

84. The Panel was of the view, however, that the interpretation proposed by the United States presented an equally serious problem with regard to the policy objectives of the General Agreement. The problem was that the United States interpretation would enlarge the "service fee" authority granted by Articles II:2(c) and VIII:1(a), more importantly the former. Article II:2(c) is a rather extraordinary exception. It authorizes governments to impose new charges on imports in excess of the ceiling established by a tariff binding. Given the central importance assigned by the General Agreement to protecting the commercial value of tariff bindings, any such exceptions would req16 Tm/F8 11 Tf(the) Tj0.16 603.12 T

the absence of any previous challenge to their ad valorem character during this long period demonstrated that most contracting parties considered ad valorem fees to be consistent with Articles II and VIII. The United States had cited several instances in which the CONTRACTING PARTIES had examined particular ad valorem fees without objecting to their ad valorem character, and had placed particular stress upon the fact that, notwithstanding the large number of ad valorem fees in force in 1955, the governments maintaining such fees had agreed to make Article VIII:1(a) mandatory in the 1955 Review Session amendments.

88. The Panel had examined all of the instances cited by the United States, as well as others that came to light during the course of its research. This examination had persuaded the Panel that the evidence did not support the conclusion advocated by the United States. The Panel believed it would be of assistance to include the results of this examination in its report.

89. The Panel first noted that a substantial number of the service fees reported in GATT documents appeared to have had excessively high rates, a problem that would normally have led to legal challenges far more readily than questions of ad valorem structure. The fact that, for the most part, these rather obvious legal shortcomings also appeared not to have been challenged suggested that many of these fees had simply not been subject to the rules of Articles II and VIII, or had otherwise escaped attention. The Panel found some support for the former hypothesis in the fact that most service fees existing on the date of a government's accession to GATT were immune fr

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91. The Panel found five cases in which individual ad valorem service fees had been investigated by the CONTRACTING PARTIES.[12] The Panel found that in three of the cases the ad valorem method had not been challenged, but that in each case the failure to challenge it could be accounted for by reasons other than an assumption of its validity, either because the fee was immune from legal attack on that issue, or because the government imposing the fee had promptly agreed to remove it for other reasons.[13] In the

charge alone would not satisfy the requirements of Article II. After the statement and explanation

97. As noted in the previous section of this report, the Panel was of the view

103. With respect to all but one of these remaining activities, the Panel was satisfied that the challenged activities were both proximate enough, and of sufficiently

substantial. Out of total 1986 imports of $369 billion, the total value of imports exempted from the fee would have been approximately $102 billion, or about 28 per cent if measured by value.

108. The United States gave a full

114. In response to the general problem of overcharges, the United States argued that the problem was essentially self-correcting under the US law, because funds from the merchandise processing fee were sequestered in a separate account that could only be expended for the "commercial operations" budget of the Customs Service. Excess revenues in one year simply constituted a surplus that must be used to reduce the fee in years following.

115. With regard to overcharges due to the second reason, i.e. incorrect rates, the Panel recognized that the "cost of services" limitation was a legal standard that could not be applied with precision in advance, at least not at the upper limit. Under any method of assessment seeking total reimbursement for the costs in question, governments would of necessity have to set the level of the fee on the basis of cost and revenue estimates, with a procedure for correcting overcharges when they occurred. The Panel considered that the United States system of sequestered accounts was a reasonable solution to the problem of overcharges due to incorrect estimates. The Panel noted the complainants' argument that the size of the overcharge in FY 1987 due to an incorrect rate (i.e. revenues of $535 million for costs of $505 million) exceeded normal tolerances. The Panel was not provided with the data on which the 1987 calculations were made, but, having been supplied by the parties with an array of differing cost and revenue estimates made during FY 1987, the Panel did not

(iv) Does the US merchandising processing fee represent either "an indirect protection to domestic products" or "a taxation of imports … for fiscal purposes" within the meaning of Article VIII:1(a)?

118. Having considered at some length the issues raised by the parties under the "cost of services" limitation in Articles II:2(c) and VIII:1(a), the Panel then considered whether the arguments of the parties had raised any further issues concerning the US merchandise processing fee under the second and third criteria stated in Article VIII:1(a).

119. The only issue raised by the parties under the third criterion prohibiting "taxation of imports … for fiscal purposes" was the question of whether total revenues exceeded total attributable costs, an issue which the Panel dealt with fully under the "cost of services" requirement.

120. The only specific issue raised by the parties under the second criterion was whether the 0.22 and 0.17 per cent ad valorem charges constituted "an indirect protection to domestic products" due to their effect on certain classes of price-sensitive imports. It was not necessary for the Panel to decide whether the "indirect protection" criterion actually involved a requirement of no adverse trade effects. The Panel concluded that, even if it did, it had not been demonstrated that these ad valorem charges had had a trade distorting effect.

Were the exemptions from the US merchandise processing fee granted to imports from certain countries inconsistent with the MFN obligation of Article I:1?

121. In a submission to the Panel, India, appearing as an intervening party

in this case. It was, of course, open to any contracting party who wished to raise this issue, or any other issue pertaining to the US merchandise processing fee, to commence dispute settlement proceedings in its own right under the General Agreement.

## VI. SUMMARY

125. The Panel found that:

(a) The term "cost of services rendered" in Articles II:2(c) and VIII:1(a) must be interpreted to refer to the approximate cost of customs processing for the individual entry in question, and that consequently the ad valorem structure of the United States merchandise processing fee was inconsistent with the obligations of Articles II:2(c) and VIII:1(a) to the extent it caused fees to be levied in excess of these approximate costs.

(b) The United States merchandise processing fee, as applied in Fiscal Year 1987 and as established for Fiscal Year 1988, also exceeded the "cost of services rendered" within the meaning of Articles II:2(c) and VIII:1(a) to the extent it included charges for the cost of the following activities of the US Customs Service:

(i) airport passenger processing;

(ii)

ANNEX I

Estimated Costs of US Customs Service "Commercial Operations" Referred to in Paragraph 17 of this Audit

| | Estimated cost in FY 1987* | | Estimated Budget for FY 1988** | |
|---|---|---|---|---|
| | FTE | Amount $'000 | FTE | Amount $'000 |
| Passenger Processing | | | | |
| Cargo Operations | | | | |
| Appraisement/Classification | | | | |
| Regulatory Audit | | | | |
| Technical & Legal Support | | | | |