

Costs and benefits of the moratorium on customs duties on electronic transmissions

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Background

1998: WTO Ministerial Declaration on Global Electronic Commerce

- Comprehensive work programme to examine all trade-related issues relating to global electronic commerce

2017: 1st Joint Statement on Electronic Commerce

- Initiate exploratory work towards future WTO negotiations on trade-related aspects of e-commerce

2019: 2nd Joint Statement on Electronic Commerce

- Confirm the WTO Members' intention to commence WTO negotiations and achieve a high standard outcome

2020: Philippines joined the Joint Statement Initiative (JSI) on E-commerce

Outline

Moratorium on customs duties on electronic transmissions

- Overview
- Global estimates of impacts

Possible impacts on the Philippines

- Estimates of potential foregone revenues
- Other factors to consider

Custom duties on electronic transmissions (ET)

Customs duties on ET

- 1998 – “will continue their current practice of not imposing customs duties on electronic transmissions”. Has been renewed every two years (except for 2003-05)
- Under the JSI, some members want a permanent ban while others oppose
- Permanent ban now a feature in some RTAs
 - CPTPP - “on electronic transmissions, including content transmitted electronically”
 - USMCA - “on or in connection with the importation or exportation of digital products transmitted electronically”
 - CECA – “on or in connection with the importation or exportation of digital products by electronic transmission”

Proponents of a permanent ban

- Moratorium has facilitated exponential growth in the use of the Internet and burgeoning digital economy
- A permanent ban signals greater certainty to consumers and business.
- Customs duties will be cost-prohibitive, technologically infeasible.
- Customs duties will have distortive effects on growth of the digital economy.

Opponents of a permanent ban

- Net importers worry that they will suffer greater revenue losses
- Options would be limited in terms of protecting domestic products and services traded online
- Level playing field needed between domestic and foreign suppliers of digital products and services
- With zero tariffs, developing countries will tend to depend on imports of digital products from developed countries

Estimated per annum tariff revenue loss due to a moratorium on ET

	Physical Imports of Digitizable Products (\$Mn)	Estimated On-Line Imports or ET of Digitizable Products (\$Mn)	Estimated Total Imports of Digitizable Products (\$Mn)	Simple Average of Bound Duties in 2017 (%)	Simple Average of MFN Duties in 2017 (%)	Potential Tariff Revenue Loss using Average Bound Duties (\$Mn)	Potential Tariff Revenue Loss using Average MFN Duties (\$Mn)
WTO Developing members (excluding LDCs)	28 399	51 558	79 957	12.6	6.5	10 075	5 197
WTO High-Income	81 604	62 962	144 566	0.2	0.2	289	289
Sub-Saharan Africa	1195	4474	5669	46.4	10.9	2 630	618
Middle East - North Africa	1 011	4 360	5 371	18.9	8.43	1 015	453
WTO LDC members (31)	191	2 804	2 995	50.3	11.5	1 506	344

Source: Banga (2019)

Banga (2019) methodology

- *Step 1*: Identification of 49 products in the Harmonized System which are digitizable (i.e., which were earlier traded only in physical form but with advancement in technology are being traded both in physical form as well as electronically):
 - **Photographic and Cinematographic Films (5)**
 - **Printed Matter (20)**
 - **Sound and Media (12)**
 - **Software (7)**
 - **Video Games (5)**
- *Step 2*: Estimation of the physical trade
- *Step 3*: Estimation of 'online' imports using growth analysis

Criticism

Not included:

- Economic and domestic tax losses that may arise if duties are implemented
- Significant enforcement and compliance costs involved in implementing electronic tariffs

Overestimation:

- Not all physical media or paper-based products would be digitized
- The price of digitally-delivered items declining over time

Lee-Makiyama and Narayanan (2019)

Global estimates – no consensus

Summary of empirical estimates of potential foregone revenue

Study	Duty type	Average total revenue losses					
		million USD		% of total customs revenues		% of total government revenues	
		Developed countries	Developing countries	Developed countries	Developing Countries	Developed countries	Developing countries
Schuknecht and Pérez-Esteve (1999)	Applied rates	233.4	613.5	0.7	0.9	0.01	0.13
Teltscher (2000)	Applied rates	264	449.3	1.39	0.7	0.02	0.07
WTO (2016)	Applied rates	117.2	236.8	0.2	0.65	0.01	0.06
Banga (2017)	Bound rates	24.5	255.8	0.03*	0.15*	0.00*	0.01*
Banga (2019)	Applied rates	123.8	2,788.50	0.16*	1.58*	0.00*	0.08*
	MFN duties	212.2	3,482.90	0.24*	2.00*	0.00*	0.10*
	Bound rates	212.2	8,043.90	0.24*	4.35*	0.00*	0.23*

Note: *Estimates calculated using the World Development Indicators (WDI)

Andrenelli, A. and J. López González (2019)

Lee-Makiyama and Narayanan (2019) - Using CGE, tariffs on digitally deliverable services would lead to GDP losses of USD 10.5 billion for developing countries.

Look beyond tariffs

- Consider impacts across the economy.
- The revenue loss likely to be relatively small.
- Gains in consumer welfare and export competitiveness.
- Domestic consumers, not foreign firms, that usually bear the burden of tariffs.
- Tariffs can be unstable source of income. Non-discriminatory forms of taxation (e.g., value-added taxes or goods and services taxes) can be alternatives.

Andrenelli and López González (2019)

Feasibility (1/2)

- How will a tariff system for electronic transmissions work in practice?
- The nature of data flows
 - Packets take different routes when flowing between two countries, often crossing different third countries.
 - The ultimate origin and destination of data flows is often a technical issue.
 - In some instances, what might seem to be a domestic transfer involves a cross-border flow.

Casalini & López-González (2019); ICC (2019)

Feasibility (2/2)

- Data should be valued at use rather than by volume
- Ad valorem assessments are unworkable
- Non-ad valorem assessments would be highly distortive
- “Data is the new oil” - misleading

Casalini & López-González (2019); ICC (2019)

Potential impacts on the Philippines

ET #1: Digitizable products

Physical Imports of Digitizable Products (USD 1000) (a)	575,085
Estimated Online Imports or ET using Growth Analysis (USD 1000) (b)	606,486
Total Imports of Digitizable Products (USD 1000) (c)	1,181,570
Simple Average of Bound Duties on Imports of Digitizable Products for the Latest Year (2017/2016) (d)	27.22
Simple Average of MFN Duties on Imports of Digitizable Products for the Latest Year (2017/2016) (e)	4.38
Potential Tariff Revenue Loss using Bound Duties on Physical Imports of Digitizable Products (USD 1000) $f = (a) * (d/100)$	156,538
Potential Tariff Revenue Generation from Imports via Electronic Transmissions (ET) using Bound Duties (USD 1000) $g = (b) * (d/100)$	165,085
Total Tariff Revenue Loss from Moratorium using Bound Duties (USD 1000) $h = f + g$ OR $h = c * (d/100)$	321,623
Total Tariff Revenue Loss from Moratorium using MFN Duties (USD 1000) $i = c * (e/100)$	51,753

Source: Communication with Rashmi Banga (2020)

ET #2: Imports of services (Mode 1 or Cross-border supply of services) (2017)

Simple Average of Bound Tariffs on Digitizable Products (%)	Imports of all Services under Mode 1 (USD Mn)	Potential Tariff Revenue Loss if ET are Digital Deliveries (as per OECD 2019) using Simple Average Bound Duties on Digitizable Products (USD Mn)
27.22	15,629	4,254

Source: Communication with Rashmi Banga (2020); Kozul-Wright and Banga (2020)

Philippine services imports (USD Mn), Mode 1(2017)

EBOPS DESCRIPTION	MODE 1
Manufacturing services on physical inputs owned by others	
Maintenance and repair services not included elsewhere	
Transport	4,470.01
Tourism and business travel	
Health services	91.55
Education services	0
Construction	
Insurance and financial services	2,007.63
Charges for the use of intellectual property n.i.e.	751.39
Telecommunications, computer, information and audiovisual services	799.97
Other business services (excluding trade-related)	3,053.72
Heritage and recreational services	0
Other personal services	0
Trade-related services (Distribution)	4,455.09
Total Services	15,629.35
Total Services minus Transport and Distribution	6,704.26

Source: https://www.wto.org/english/res_e/statis_e/trade_datasets_e.htm accessed on October 6, 2019

ET #3: Philippine imports of services via Mode 1 or Cross-border supply of services excluding Transport & Distribution services (2017)

	Bound Tariffs	MFN Tariffs
Simple Average Tariff of Digitizable Products (%)	27.22	4.38
Imports of all Services under Mode 1 excluding transport & distribution services (USD Mn)	6,704	6,704
Potential Tariff Revenue Loss (USD Mn)	1,824.90	293.65

Source: Authors' computation

ET #4: Imports of Digitally-deliverable services for the Philippines (2017)

An aggregation of insurance and pension services, financial services, charges for the use of intellectual property, telecommunications, computer and information services, other business services and audiovisual and related services

	Bound Tariffs	MFN Tariffs
Simple Average Tariff of Digitizable Products (%)	27.22	4.38
Imports of Digitally deliverable services (USD Mn)	8,660.42	8,660.42
Potential Tariff Revenue Loss (USD Mn)	2,357.37	379.33

Source: Authors' computation

Summary of Potential Tariff Revenue Losses (USD million)

Potential tariff revenue loss if electronic transmissions are imports of...	Bound Tariffs	MFN Tariffs
ET #1: Digitizable Products (Physical Imports of Digitizable Products and Estimated Online Imports using Growth Analysis)*	321.62	51.75
ET #2: Mode 1 services imports*	4,254.31	684.57
ET #3: Mode 1 services imports except transport & distribution services**	1,824.90	293.65
ET #4: Digitally deliverable services imports**	2,357.37	379.33

Sources: *Banga (2020), **Authors' computations

Potential losses in perspective (2017)

	Foregone revenues USD Mn	National Government Revenues	National Tax Revenues	Indirect taxes	Import duties and taxes
USD Mn		49,539	45,083	23,996	9,178
ET #1: Digitizable Products (Physical Imports of Digitizable Products and Estimated Online Imports using Growth Analysis)					
Bound Tariffs	321.62	0.65%	0.71%	1.34%	3.50%
MFN Tariffs	51.75	0.10%	0.11%	0.22%	0.56%
ET #2: Mode 1 services imports					
Bound Tariffs	4,254.31	8.59%	9.44%	17.73%	46.35%
MFN Tariffs	684.57	1.38%	1.52%	2.85%	7.46%
ET #3: Mode 1 services imports except transport & distribution services					
Bound Tariffs	1,824.90	3.68%	4.05%	7.60%	19.88%
MFN Tariffs	293.65	0.59%	0.65%	1.22%	3.20%
ET #4: Digitally deliverable services imports					
Bound Tariffs	2,357.37	4.76%	5.23%	9.82%	25.69%
MFN Tariffs	379.33	0.77%	0.84%	1.58%	4.13%

Source of various government revenues – <https://www.dof.gov.ph/data/statistics-bulletin/>
2017 end of period exchange rate USD 1 = PhP 49.92

But actual revenue intake could still be much less

Even if technically feasible, the application of customs duties on ET still constrained by other policies:

- CMTA De minimis
- ITA commitments
- Florence agreement
- Trade in services commitments

CMTA De minimis

- The Customs Modernization and Tariff Act (CMTA) or Republic Act (RA) No. 10863 increased the de minimis value from P10 to **P10,000**.
- De minimis is the value of goods for which no duty or tax is collected. Specifically, Section 423 of the CMTA, provides that "no duties and taxes shall be collected on goods with freight onboard (FOB) or free carrier (FCA) value of P10,000.00 or below."
- Certain products are not covered under the new de minimis rule, such as prohibited and restricted importations.

Information Technology Agreement

- ITA-1 (1996) - eliminate and bind customs duties at zero for 217 products (includes software)
- ITA-2 (expansion) (2015) - additional 201 products (includes video games)
- E.O. 21 s.2017

Florence Agreement

- Agreement on the Importation of Educational, Scientific and Cultural Materials.
- The Philippines has been a signatory since August 2, 1952. It stipulates that no Customs duties or any other charges, including value added tax (VAT), be applied to imported educational, scientific and cultural materials
- The agreement covers books, publications, and documents including music sheets, maps, and charts; works of art and collector's pieces; and visual and auditory material; scientific instruments or apparatus; articles for the blind.

Trade in services commitments

- If electronic transmissions are considered as services these would be governed by GATS.
- Imposing duties would violate National Treatment obligations where commitments have been made since duties are, by definition, discriminatory.
- PH specific commitments with “None” (i.e., no limitations) under National Treatment in Mode 1 (Cross-border supply)
 - **GATS** (non exhaustive): packet-switched data transmission services, circuit-switched data transmission services, On-line information and data base retrieval, Electronic data exchange, Videotex, financial advisory services, commercial banking, credit card services, etc.
 - **AFAS** Package 9 (non exhaustive): architectural services, data base services, R&D services on agri sciences, R&D services on economics, Interdisciplinary research and experimental development services on ICT, advertising services, interior design services, electronic e-mail, Content development services sold to telecommunications companies, data and message transmission services, data network services, electronic message and information services, data and message transmission services, data network services, electronic message and information services, production services of animated cartoons of any kind, motion picture projection services in private screening rooms, singer group and band entertainment services, etc.

Other factors

- Philippines is a net exporter in services
 - Mode 1 (Cross-border supply)
 - Digitally-deliverable services
- Philippine participation in ICT/digital global value chains (IT-BMP sector, multi-country research, creative sector, etc.)
- Economy-wide impact on productivity
- National policy priorities
 - The Philippine Development Plan 2017-2022 - develop high-value added, competitive, and sustainable sectors.
 - The Micro, Small, and Medium Enterprise (MSME) Development Plan 2017-2022 encourages the use of digital technologies and platforms
 - Inclusive, Innovation and Industrialization Strategy (i3s)

Summary

- Potential revenue losses vary depending on the definition/scope of electronic transmissions
 - Based on estimates of digitizable products, the foregone revenue of a moratorium represents about 0.10% and 0.65% of national government revenues using the average MFN rate and the bound tariff rate, respectively. Estimates based on broader definitions of electronic transmission range from 0.59% to 1.38% and from 3.68% to 8.59% of national government revenues using the average MFN rate and bound rate, respectively.
- But actual revenue intake could be less due to technical and policy constraints
- National interest suggests that we look at other tax measures for the digital economy



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policy research

PIDS Discussion Paper 2020-46

“Costs and Benefits of New Disciplines on Electronic Commerce”

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