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Customs Administration Strategies for Improved Revenue Mobilization in METAC Countries

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Customs Administration Strategies for Improved Revenue Mobilization in METAC Countries

This note summarizes the results of a webinar hosted by METAC and the IMF Fiscal Affairs Department on customs modernization strategies for revenue mobilization—held on October 28, 2020, and attended by senior management of customs administrations of Afghanistan, Jordan, Morocco, Sudan, Tunisia and Yemen. Participants discussed medium-term planning, challenges and possible strategies for improved revenue mobilization, and capacity development needs. They highlighted the importance of customs' role in domestic revenue mobilization, including as a support function to domestic tax administrations, noting that more efforts are needed to strengthen their capacities to modernize—and that this has become more urgent due to the implications of COVID-19. The key outcomes from this webinar are consistent with METAC's current capacity development to customs administration and provide further ideas to plan future support.

ROLE OF CUSTOMS ADMINISTRATIONS IN FISCAL REFORMS

The COVID-19 pandemic has exacerbated fiscal risks and vulnerabilities in METAC countries. Debt levels have increased, current accounts have deteriorated, and foreign investment inflows into the region have declined. The deterioration of fiscal situations was partly due to increased spending to manage and contain the pandemic, and significantly lower revenues in 2020, due to lower economic activity, and temporary tax breaks to alleviate the cash impact on businesses and households.

Some countries introduced measures to address the short-term implications of the pandemic. But some of the implications on revenue (and spending) are likely to extend well into the medium-term. Moreover, countries need to build more resilient and responsive revenue systems to address similar future shocks.

Trade and tariff policies are important tools in revenue policy and administration, especially in developing countries. This is particularly so since taxes (including customs tariffs) on imports are a mainstay of government revenues.¹ Customs administrations have a role to play in revenue collection, including enforcing tax transactions across fiscal

borders—between domestic and foreign tax systems. The case of indirect taxes (e.g. value-added taxes (VATs), excise taxes on imported goods) is obvious, but customs also play a key role in enforcing other domestic taxes, such as the corporate income tax on cross-border transactions in goods (for instance, by providing valuable information on the cost of imports, origin, and controlling the volume and cost of exports).

Coordination with domestic tax administration is another key role of customs, where they contribute indirectly to safeguarding tax revenues. This include creating a trade-friendly environment to encourage trade and investment (which in turn create tax base), reduce tax evasion and avoidance, address smuggling, and ensure that tax incentives (e.g. VAT and tariff exemptions) accrue to those who are legally entitled to benefit from them.

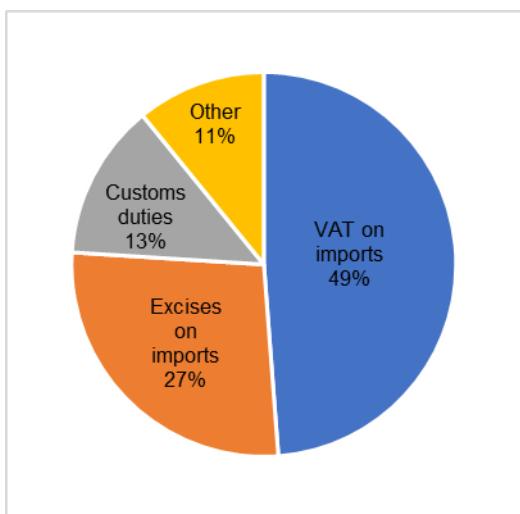
A modern customs administration is one that balances its various responsibilities to ensure a high level of compliance with revenue objectives, while intervening as little as possible in the legitimate movement of goods and people across borders. An increasingly global world brings opportunities to this task, in terms of a higher potential revenue, but also compliance challenges.

¹ About one-third of tax revenues in METAC countries is collected by customs administrations.

CUSTOMS REVENUE COLLECTION AT A GLANCE

Five countries participating in the webinar reported high shares (as a percent of total tax collections) of revenue collected by customs. These range from an estimated 31 percent in Jordan to 52 percent in Afghanistan, with an average of 39 percent—consistent with the estimate for all 14 METAC countries (footnote 1). Unsurprisingly, the largest component of revenue collected by customs in the countries who answered the survey is VAT (Figure 1).

Figure 1. Composition of Customs Revenue Collections (most recent year, percent of total taxes)



Source: Authorities and authors' calculations.

Customs duty revenues collected by customs administrations have declined in the past three decades due to trade liberalization. However, total revenue collections by customs remains important, and has even increased in some countries. This is because tariff revenues were replaced by broader domestic taxes on consumption (VAT and excises), which are collected by customs administration when goods are imported. Despite the fact that a large share of these revenues (primarily VAT)

² METAC held a workshop on tax expenditures in December 2019, which discussed challenges of tax expenditures to customs administrations and revenue collections more broadly. Participants agreed that these challenges are significant. However, at the time of the

is offset against taxes paid later on domestic transactions, customs administrations act as a withholding agent for domestic tax administrations, and an effective risk management tool for collection of consumption and production taxes on imported goods.

Customs duty exemptions and other tax incentives increase the compliance risks to revenue collections. These policy-based incentives are often significant, but their cost, in terms of foregone revenue, is not always accounted for in budget documents. Customs administrations, in collaboration with domestic tax administrations and ministry of finance's macro-fiscal units or tax policy units, need to ensure that information on foregone revenue is communicated to policymakers, and its implications for revenue leakage and corruption is well explained. This is good practice in advanced economies, and increasingly so in developing economies.² When poorly controlled, tax incentives provided at the point of entry into a country weakens the withholding role of customs and create opportunities for evading taxes on domestic value added.

MODERNIZATION STRATEGIES FOR IMPROVED REVENUE MOBILIZATION

Good International Practices

Customs modernization strategies require capacity building at the organizational and operational levels. At the first level, customs administration should target the objective of improving performance to conduct customs tasks, including revenue collection. This is typically achieved through better organizational structures, strategic and change management, management methods, and investment and optimal resource allocations, all based on

workshop, only two METAC countries (out of 14) reported publicly on tax expenditures (Jordan and Morocco).

organizational risk management.³ It should also have enabling factors, notably a modern legal framework, supporting ICT systems, a satisfactory level of staff performance and integrity, and business continuity plans to respond to crises, such as the COVID-19 pandemic.

At the operational level, a modern Customs administration should have the capacities to perform risk-based controls. This should cover clearance, post-audit controls, tracing and controlling diversion risks, deterring offences through case management, and management of preferential duty and tax regimes.

Challenges for Customs Modernization in METAC Countries

Participants in the webinar discussed the results of a survey conducted by the webinar organizers on key strategic and operational challenges. The survey asked customs administrations to rate the challenges on an ascending scale of 1 to 5. Figure 2 reports the results for the top 10 challenges, and Table 1 reports details on the full range of challenges in the survey.⁴

Strategic Management

All participating countries indicated that they have multi-year modernization strategies, adopted by their respective authorities (typically,

the ministry of finance). These are supported by annual operational plans and are widely communicated to staff across the institution. Some countries indicated that their plans reflect achievements (or lack of) in previous years. And although all countries reported that their plans include measurable key performance indicators, they generally did not spell out how they operationalize improvement in performance over time.

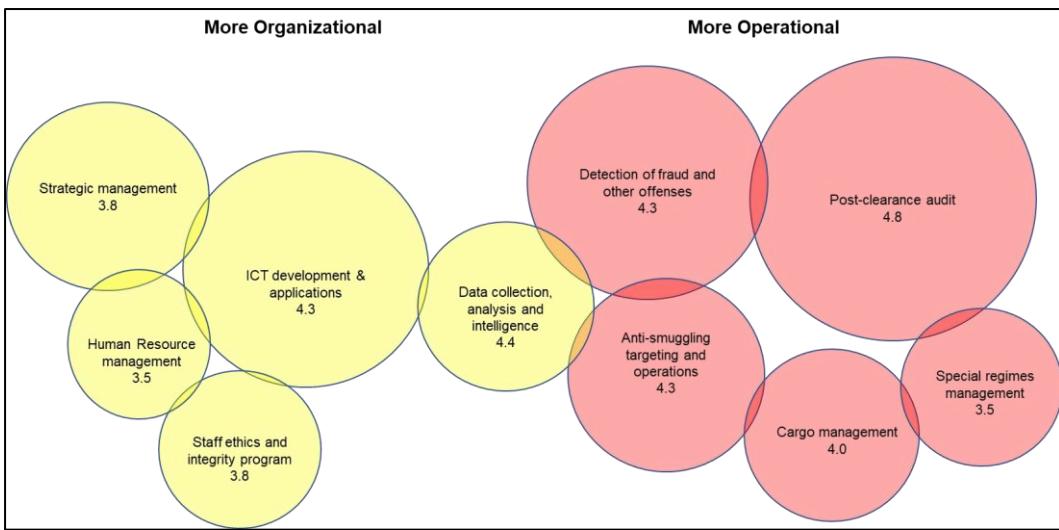
Organizational and Operational challenges

Customs administrations face challenges in their modernization strategies and plans. Some are country-specific, while others are common to all countries. As expected, many of these challenges are interconnected (Figure 2). For example, capacity building in “post-clearance audit” needs better targeting to companies; thus, “detection of fraud and offence” (i.e. risk management) is imperative. In turn, this requires adequate capacity in “data collection, analysis and intelligence”, which must be supported by “ICT development & application”. As a whole, these challenges represent the eco-system of the customs administration; strengthened “strategic management” can ensure optimal allocation of resources to obtain the best performance possible in each area.

³ Organizational risk management compares productivity across an organization and rebalances its resource allocation so that productivity is equalized across its various functions and sectors.

⁴ The simple averages reported in Figure 2 and Table 1 can hide important variations in the weights that customs authorities attach to these challenges.

Figure 2. Top Ten Challenges Reported by Countries (Weighted Score)



Source: Authorities and authors' calculations.

Table 1. Average Ranking of Key Strategic and Operational Issues (scale of 1 to 5, with 1 being least challenging and 5 most challenging)

	Simple Average
Strategic management (planning, monitoring and management)	3.8
Regular reporting (e.g., revenue collection, excessive delay)	3.0
Business continuity plan	3.0
Organizational structure	2.5
Human resource management (recruitment, promotion, relocation, etc.)	3.5
Human resource development (training-related)	3.0
Staff ethics and integrity program	3.8
ICT development and applications	4.3
Data collection and analysis, Intelligence	3.8
Internal audit (ethics, revenue and other performance)	3.7
Customs department brokers management	3.3
Cooperation with tax department	3.3
Cooperation with foreign customs administrations	3.0
Communication and stakeholder relations (internal and external)	3.3
Legal framework (e.g., obsolete, not consolidated)	2.3
Cargo management (e.g., manifest, deconsolidation, gate control)	4.0
Import clearance procedures (e.g., trade facilitation)	3.5
Assessment of valuation, classification and origin, advance ruling	3.3
Bond management (e.g., release before clearance), arrears management	2.8
Economic operator's compliance management	3.0
Detection of fraud and other offense (targeting and risk management)	4.3
Penalties, administrative and judicial proceedings	3.0
Appeal and review mechanism	3.3
Confiscation and auction	3.0
Authorized Economic Operator or similar program	2.5
VAT (or GST) introduction	2.7
Excise management	2.7
Post-clearance audit	4.8
Special regimes management	3.5
Anti-smuggling targeting and operations	4.3
Other (related to revenue collection/ leakage control)	4.0
Average	3.3

Source: Authorities and authors' calculations.

Note: Four out of six countries are included in the average, reporting by the other two was partial or incoherent.

LESSONS AND MEDIUM-TERM PRIORITIES

Customs administrations in METAC countries are important revenue collection agencies, accounting for over 1/3 of tax revenue. All customs administrations who participated in the webinar noted that they have multi-year strategic plans. However, they face considerable challenges in implementing them. Capacity development can therefore target reviews of country strategies to identify implementation bottlenecks and improve implementation capabilities.

METAC and the IMF Fiscal Affairs Department will scale up their support to customs administrations, with emphasis on revenue collection. This will target organizational and operational issues, including compliance risk management, business continuity (e.g. post-COVID-19); implementation of targeted components of strategic modernization plans; and support to plan and implement reforms for revenue mobilization.

Discussions at the webinar identified the following key priority areas, in which METAC can usefully support countries:

- Development and application of procedures based on international standards, for valuation, application of rules of origin, tariff classification of goods, clearance procedures, and transit.
- Strengthening trade control progressively through properly designed post-clearance audit programs.
- Consistent application of risk-based control selectivity.
- Strengthening control of special regimes and exemptions.
- Improving effectiveness in the fight against fraud and smuggling.
- Setting up procedures for the exchange of information and cooperation with tax and non-tax

administrations, and with foreign customs administrations.



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