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Committee on Customs Valuation

TREATMENT OF VALUATION OF COMPUTER SOFTWARE

Report by the Technical Committee on
Customs Valuation on National Practices

At the meeting of 4-5 May 1982, the Committee on Customs Valuation decided to request the Technical Committee to ascertain what the present national practices of the Parties were with regard to the treatment of valuation of computer software (VAL/M/4, paragraph 46).

At the meeting of 20-24 September 1982, the Technical Committee examined the issue. The report of the Technical Committee which was received through the secretariat of the Customs Co-operation Council, is attached to this note.

REPORT

BY THE TECHNICAL COMMITTEE ON CUSTOMS VALUATION
ON THE PRACTICES FOLLOWED WITH RESPECT
TO THE TREATMENT OF COMPUTER SOFTWARE

INTRODUCTION

1. At a meeting held in Geneva on 4 and 5 May 1982, the Committee on Customs Valuation requested the Technical Committee on Customs Valuation to ascertain and report on practices at present employed by Signatories to the Agreement, in respect of the Customs valuation of computer software.
2. The Secretariat of the Customs Co-operation Council accordingly circulated Doc. 28.837 inviting administrations which had implemented the Agreement to furnish information on the subject; Signatories not yet applying the provisions of the Agreement were also invited to comment. The document specified that the subject under consideration concerned only the Customs valuation of computer programs, data or other instructions carried on media such as tapes or disks usable in data processing systems, and did not cover programs which were an integral part of the data processing equipment itself (for example, the programs and data contained in an integrated circuit in a calculator). In addition to the request for any information of a general nature on the subject under consideration, the document included a series of specific questions on the way the Agreement is applied in five particular situations involving the importation of computer software.
3. At its Fourth Session in Brussels from 20 to 24 September 1982, the Technical Committee reviewed and after minor amendments approved the following Report and analysis of the replies received from 9 (Austria, the European Economic Community, Finland, Japan, New Zealand, Norway, Sweden, the United States and Yugoslavia) of the 11 Signatories which have implemented the Agreement, 1 non-Signatory which has implemented (Australia) and 1 non-Signatory (South Africa) which intends to implement next year.
4. To facilitate examination the Report has been divided into three parts, namely :
 - I. General comments;
 - II. Summary of replies on the specific questions;
 - III. Conclusions drawn from the replies.

I. General comments

5. The Australian Administration states that in its country the Customs value of computer software media, such as tapes or disks, is the total price paid or payable for the goods, as required by Article 1 of the Agreement. The value of any computer software carried by the media will be part of the Customs value if it is included in the price of the goods or takes the form of a royalty or licence fee to which Article 8.1 (c) applies.
6. The Austrian Administration feels that it could be argued that the information component of software might be included in the dutiable value. However, current Austrian practice in this field corresponds to the valuation practices in effect prior to the implementation of the Code. Computer software is therefore essentially valued on the basis of (a) the cost of the carrier media, (b) the cost of the recording of the program, and (c) a profit on these elements and excluding the information component of software.
7. The European Economic Community states that when the transaction value is applied to media bearing software, the software is regarded as being part of the imported goods. In application of the Interpretative Note on "price actually paid or payable", that price is taken as the total payment made or to be made by the buyer to or for the benefit of the seller for the imported goods (i.e. media plus software). Where the buyer pays for a right of reproduction the relevant amount is not an element of the Customs value.
8. In Japan, when Article 1 of the Agreement applies to imported goods with software (i.e. (i) software recorded on carrier media and (ii) software incorporated in data processing equipment), their Customs value is to be calculated on the basis of the total payment made by the buyer to or for the benefit of the seller. However, the charges for the right to reproduce the imported goods are not to be included in the Customs value.
9. Since adopting the Code on 1 July 1982, New Zealand has retained on a temporary basis its previous valuation method for software pending completion of a study of import duty levels required for this product. The increased duty yield resulting from the valuation of software under the Code is considered as not being so much a valuation problem as a tariff problem. New Zealand agrees that an amendment to Article 1 would be necessary to exclude the information component from the Customs value.
10. Sweden points out that the situations presented for comment show that it is very difficult to calculate the Customs value for computer software imported on carrier media, and that different results are arrived at depending on differences in agreements between buyers and sellers. There is a case for an

agreement with special rules for calculating the Customs value for computer software. The Swedish Administration is of the opinion that the value of computer software imported on carrier media should not be included in or added to the price invoiced for the carrier media.

11. The United States Administration, in reporting the application of specific rates of duty to the goods under consideration, noted however, that in response to a ruling request initiated for the purpose of determining the value to be posted on the entry for statistical purposes, it was determined that the licensing fees for software are essentially payments for the right to reproduce the information contained on the media and that on the basis of the Note to Article S.1 (c) of the Agreement stating "charges for the right to reproduce the imported goods in the country of importation shall not be added to the price actually paid or payable for the imported goods in determining the Customs value", such fees were non-dutiable. The United States continues to hold this view.
12. Although not yet a Party to the Agreement, the South African Administration commented that a thorough study regarding the Customs value of software under the Agreement had found nothing in the Agreement to justify the elimination of the information component from the dutiable value of the program. South Africa is aware of the proposed amendment to the Agreement and appreciates the reason for it. The proposal nevertheless serves as confirmation that others had also come to the conclusion that the Customs value of computer software is the actual price paid or payable therefor.
13. The South African Administration also states that according to information obtained, programs are now supplied from suppliers' libraries and are only slightly modified to suit individual requirements. Prices are therefore relatively moderate. In cases where it is necessary for a special program to be designed for one user in South Africa, such a program would normally be developed and written in that country.
14. In reply to the request for an estimate of the proportion of software importations (a) on sale, (b) under licence or on hire, (c) any other categories of transaction, Australia, Austria, the European Economic Community, Finland, Japan, New Zealand and Sweden stated that they were not in a position to supply the required information. In the United States well over 90 % of software importations are under licence or hire, the remainder being sold.

II. Summary of replies on the specific questions

15. Of the Signatories which have implemented the Agreement, two (Norway and the United States) reported that imports of the goods under consideration would not be subject to ad valorem duties under their tariffs and, accordingly, these administrations did not furnish replies to the specific situations.
16. For the reasons noted in Part I of this report Austria did not furnish replies to the specific situations.
17. The New Zealand responses to the specific situations indicated that they were opinions rather than practices and they have therefore been included in this Part as parenthetical notes, i.e. (New Zealand - 95,000 currency units).

Situation I

A user purchases from an unrelated seller and imports a disk on which has been recorded a payroll accounting program for use on the importer's own computer. The price paid is 18,000 currency units which includes the cost of the disk (300 currency units) and the recording of the program (1,000 currency units). The buyer has unrestricted ownership of the program but has no right to reproduce the program for resale to others.

Under the present application of the Agreement, what would be the practice with respect to the Customs value of the imported software ?

18. The six Administrations (Australia, the European Economic Community, Finland, Japan, Sweden and Yugoslavia) which replied to this question reported that the Customs value of the imported carrier media bearing software would be 18,000 currency units, corresponding to the price actually paid or payable for the goods. Sweden further noted that the value would not be influenced by the restriction concerning reproduction (New Zealand - 18,000 currency units).

Situation II (four questions)

An importer imports a software package recorded on a magnetic tape. The package contains a number of programs covering an entire accounting, inventory and cost control system specifically designed for the importer. The importer pays a licence fee of 95,000 currency units which includes the cost of the reel and tape (800 currency units) and the recording of the programme on the tape (1,500 currency units). Under the terms of the licensing agreement the exporter is obliged for a period of 12 months to correct any errors found in the programs, free of charge. During the same 12-month period the seller will modify or update the programs at a price of 7,500 currency units. After the 12-month period, modifications and updates will be provided at a fee to be agreed by the parties at the time. In each instance, the seller provides a new tape which includes the entire program inclusive of the corrections or modifications.

What would be the practice with respect to the Customs value of the original importation invoiced at the licence fee of 95,000 currency units ?

19. Five Administrations (Australia, the European Economic Community, Finland, Japan and Yugoslavia), stated that under the provisions of Article 1 of the Agreement the value of the original importation would be 95,000 currency units (New Zealand - 95,000 currency units).
20. The Swedish Administration noted that it seems doubtful if Article 1 can be applied since there is no price paid or payable for the imported goods. In practice the transaction value has been replaced by a licence fee. Article 7 seems to be applicable and the valuation should be based on the principal Rules in Article 1. It is likely that the licensee acquires the same rights as if he had purchased the package. For the program imported on three occasions within 12 months 102,500 currency units are paid. This amount will form the total transaction value for the tape imported during the first year. It has to be divided in three values.

What would be the practice with respect to a subsequent importation invoiced free of charge containing the entire program but incorporating corrections ?

21. Two Administrations (Australia and the European Economic Community) consider that the Customs value would be 95,000 currency units. Australia also points out that under Australian Customs law the importer would be eligible to apply for a refund of duty paid in relation to the importation of the original tape (New Zealand - 95,000 currency units).
22. The European Economic Community comments that rules provided under Customs procedures would avoid double taxation.
23. Finland states that the value of the shipment would be determined under the first possible secondary method and the transaction value of the first shipment would be adjusted accordingly.
24. Japan reports that since the subsequent importation incorporating corrections is invoiced free of charge, it is to be valued in accordance with the provisions of Article 2 et seq. of the Agreement. In this case, a value which does not include any consideration of software is to be taken as the Customs value.
25. Sweden's opinion is given above in the reply to the first question.
26. Yugoslavia would value the shipment on the basis of the value of the medium and the cost of the recording of the program, i.e. 2,300 currency units.

What would be the practice with respect to a subsequent importation invoiced at 7,500 currency units containing the entire program but incorporating a modification ?

27. For five Administrations (Australia, the European Economic Community, Finland, Japan and Yugoslavia) the Customs value would be 7,500 currency units (New Zealand - 7,500 currency units).
28. Sweden's view is given above in the reply to the first question.

What would be the practice with respect to an importation over 12 months later which contains the entire program but incorporates a modification, invoiced at an agreed fee of 22,300 currency units ?

29. All the replying Administrations (Australia, the European Economic Community, Finland, Japan, Sweden and Yugoslavia) consider that the Customs value would be 22,300 currency units (New Zealand - 22,300 currency units).

Situation III

Under the terms of a licensing agreement an exporter ships a software package recorded on a magnetic tape to an unrelated importer. The licensing agreement provides that the importer will pay a one-time licensing fee of 15,000 currency units for the right to use the program. In addition, the importer has the right to sublicense the program to third parties. The remuneration to the exporter for this right consists of 15 currency units each time the program is sublicensed and a monthly royalty fee of 10 % of the sublicense fees paid to the importer by his sublicensees.

Upon importation of the magnetic tape, the invoice accompanying the shipment reflects the licence fee of 15,000 currency units and 250 currency units for (a) the cost of the tape; (b) recording; (c) packing, transportation and insurance; and (d) a profit mark-up of 10 % on Items (a), (b) and (c).

Under the present application of the Agreement, what would be the practice with respect to the Customs value of the imported software ?

30. Australia reported that the Customs value would be 15,250 currency units, representing the transaction value in accordance with Articles 1 to 8 (subject, however, to facts relating to transportation and insurance costs). The Australian Administration specifies that the remuneration to the exporter of 15,000 currency units each time the program is sublicensed by the importer as well as the monthly royalty fee would not be part of the Customs value if they represent payments to the exporter for the right to reproduce the program. If further enquiries revealed that they were not made in respect of such a right, Article 1.1 (c) would apply because no adjustment could be made for them at the time the goods were declared, in accordance with Article 8. In that case the Customs value would have to be established by one of the alternative methods to Article 1.

31. The European Economic Community understands that the tape is copied under the terms of the licensing agreement; consequently this element refers to right of reproduction and (as in Situation IV) does not form part of the Customs value.
32. In Finland, the Customs value would be the total invoice amount.
33. Japan notes that the difference between Situation II and Situation III is not necessarily clear. If the payment of the licence fee is made separately from that for the goods being valued and such fee is distinguished from Items (a) to (d) on the invoice, the Customs value will be calculated on the basis of Items (a) to (d). In Japan, a licence fee as a consideration stipulated under a licensing agreement is the subject of payment for invisible transaction. As far as software is concerned, the licence fee paid in this manner is not to be taken into consideration when calculating the Customs value.
34. In Sweden, the Customs value would be 15,250 currency units. The right to sublicense the program and the stipulated payments for executing this right should not influence the transaction value (see the Note to Article 3.1 (c) concerning reproduction of and reselling imported goods).
35. Yugoslavia did not consider the example clear and could not give a reply.
36. (New Zealand - 250 currency units. Presumably the tape is being copied in the country of importation under the terms of the licensing agreement. The licence fee is non-dutiable.)

Situation IV

An importer, a programming firm, buys certain specialized programs from an unrelated foreign supplier in the form of tape cassettes. The price paid is 5,000 currency units per program, of which 5 % represents the cost of the cassette and recording. The importer is licensed to duplicate the imported cassettes and the duplicates are resold to users of the programs. Each time the importer sells a program he must remit 1,000 currency units to the foreign supplier. The imported cassettes used for duplication are never resold.

What would be the practice with respect to the Customs value of the imported software invoiced at 5,000 currency units ?

37. Five Administrations (Australia, the European Economic Community, Finland, Japan and Sweden) reported that Customs value would be 5,000 currency units (New Zealand - 5,000 currency units).

38. The Yugoslav Administration considers that the Customs value of the imported software would be 250 currency units (the cost of the cassette and recording), and that the rest of the invoiced price relates to charges for the right of reproduction.

Situation V

An importer purchases 1,000 module cartridges usable in pocket calculators from an unrelated seller. The importer is a supplier for a number of calculator manufacturers in the country of importation. Each module contains in its circuitry a non-erasable software program which, when fitted to the pocket calculators, carries out a specific task. The 1,000 modules are sold to the importer by an unrelated seller at a price of 50,000 currency units including packing and all delivery charges to the country of importation.

Under the present application of the Agreement, what would be the practice with respect to the Customs value of the imported modules ?

39. The six Administrations which answered the question (Australia, the European Economic Community, Finland, Japan, Sweden and Yugoslavia) reported that the Customs value would be 50,000 currency units (except that Australia would deduct delivery charges because it applies the Agreement on an f.o.b. basis) (New Zealand - 50,000 currency units).

III. Conclusions

40. From the replies received to the Questionnaire the situation can be summarized as follows :
41. Of the seven implementing Signatories applying ad valorem duties which have replied, five (the European Economic Community, Finland, Japan, Sweden and Yugoslavia) have reported practices wherein the Customs value of computer software is based on the total price actually paid or payable for the imported software. It has however been specified that any sum paid for the right of reproduction would not be includible in the Customs value. Two non-Signatories, Australia and South Africa, have expressed similar opinions.
42. Austria, whilst sharing the view that under the terms of the Agreement it could be argued that the information component of software might be included in the dutiable value, nevertheless continues to value software without reference to this component.

43. New Zealand, noting that an amendment would be necessary to exclude the information component of software from the Customs value, has temporarily retained its previous valuation method pending a study of import duty levels.
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