



8 November 2021

(21-8430)

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General Council

Original: English

## WORK PROGRAMME ON ELECTRONIC COMMERCE

### THE MORATORIUM ON CUSTOMS DUTIES ON ELECTRONIC TRANSMISSIONS: NEED FOR CLARITY ON ITS SCOPE AND IMPACT

The following communication, dated 5 November 2021, is being circulated at the request of the delegations of India and South Africa.

#### 1 SCOPE OF THE MORATORIUM

1.1. The 1998 Declaration on Global Electronic Commerce<sup>1</sup>, stated that Members will "continue their current practice of not imposing customs duties on electronic transmissions". This language has been replicated in subsequent decisions renewing the moratorium.

1.2. We quote from our earlier submission, WT/GC/W/798 dated 11 March 2020.

1.3. We believe that there are two main interpretations regarding its scope:

- a) The moratorium on customs duties applies to the 'transmission' but not the content of the transmission. This line of thinking has been taken up by Indonesia. In statements at MC11, Indonesia had said:

"In regards to the discussion on the moratorium on customs duties on electronic transmissions, it is our understanding that such moratorium shall not apply to electronically transmitted goods and services. In other words, the extension of the moratorium applies only to the electronic transmissions and not to products or contents which are submitted electronically. The Indonesian Head of Delegation shared this understanding with the Director-General and his team yesterday and today, in which they responded with a positive confirmation."

For this reason, we would like to insert a footnote in the outcome document which states "it is understood that such moratorium shall not apply to electronically transmitted goods"<sup>2</sup>.

1.4. The implication of this interpretation is that since the moratorium is only applicable to the transmission, Members would be able to put customs duties on the transmitted content. The prohibition of customs duties therefore only refers to the 'transmission' – the bits and bytes. Any possible revenue implications will be limited in nature given the scope of the moratorium.

1.5. Indonesia has also expanded its HS code (Chapter 99) to include goods which can be digitized i.e. intangible goods.

- b) There is in literature a number of studies that define the scope of the moratorium on customs duties on electronic transmissions as applicable to physical goods which have become digitized, or which are digitizable. Indeed, studies on the impact of the moratorium since

<sup>1</sup> WTO 1998 WT/MIN(98)/DEC/2, 25 May.

<sup>2</sup> WTO 2017 'Statement by Indonesia: Facilitator's Consultation on Electronic Commerce, MC11 declaration, and other relevant plenary sessions', delivered on 13 December, WT/MIN(17)/68, 20 December.

1998 have focused on the tariff revenue losses resulting from the digitization of physical goods. These studies have included (non-exhaustively):

- Schuknecht and Pérez-Esteve (1999)<sup>3</sup> – they used a list of goods that included cinematographic film, newspapers and videogames to provide upper bound estimates of possible tariff revenue losses when these products are digitized.
- WTO (2016)<sup>4</sup> – the Secretariat updated their analysis of tariff revenue losses. Using a list of 30 HS 6-digit goods and their applied rates, they looked at the reduced imports on 'digitizable' goods and thus the revenue losses.
- UNCTAD (2017)<sup>5</sup> and UNCTAD (2019)<sup>6</sup> also calculated tariff revenue losses from goods that have become digitized and which are digitizable.

1.6. Due to technological developments, there is a rapid rise in the growth of online trade of digitizable goods. This explains the concern around the impact of digitization of goods on tariff revenue.

1.7. A submission by 13 WTO Members, WT/GC/W/799/Rev.1 dated 29 June 2020, relying on OECD (2019), presumes the scope of the moratorium to include foreign value-added ICT enabled services like business services. These recent submissions seem to have expanded the scope of the moratorium to include services without giving any rationale/argument to support this understanding.

## 2 THE IMPACT OF THE MORATORIUM

2.1. In our submission, WT/GC/W/798, we had stressed that re-consideration of the moratorium is critical for developing countries to preserve policy space to regulate imports, generate revenue through a simple and direct instrument such as customs duties and achieve digital industrialization.

2.2. WT/GC/W/799/Rev.1, on the other hand, argues that the overall benefits of duty-free electronic transmissions outweigh the potential forgone government revenues due to the e-commerce moratorium. Relying on OECD (2019), it outlines the role of the use of foreign value-added ICT enabled services like telecommunication services, financial services or other business services, in achieving positive economic outcomes.

2.3. There are certain conceptual and methodological issues in the arguments made in WT/GC/W/799/Rev.1, as well as in OECD (2019), hereinafter referred to as 'the submissions'. We elaborate on these issues below:

### 2.2 Tariff Revenue Loss

2.4. In our previous submission, WT/GC/W/798, we highlighted that based on the identification of a small number of digitizable goods in five areas, namely, printed matter, music and video downloads, software and video games, UNCTAD estimated a loss in tariff revenue of more than US\$10 billion per annum globally because of the moratorium, 95% of which is borne by developing countries.

2.5. These submissions attempt to make the revenue foregone on account of the e-commerce moratorium seem insignificant by showcasing this revenue loss in terms of its share in customs revenue and total government revenue. However, even compared in this manner, it is evident that the percentage of government revenue lost for developing countries is higher than that for the developed countries. The percentage of customs revenue lost for developing countries is 4.35% while that for the developed countries is a mere 0.24%. It is evident that the cost of the moratorium

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<sup>3</sup> Schuknecht, L and Pérez-Esteve 1999 'A Quantitative Assessment of Electronic Commerce', Staff Working Paper ERAD, No. 01, WTO, Geneva.

<sup>4</sup> WTO 2016 'Fiscal Implications of the Customs Moratorium on Electronic Transmissions: The Case of Digitisable Goods', JOB/GC/114, 20 December.

<sup>5</sup> UNCTAD 2017 'Rising Product Digitisation and Losing Trade Competitiveness'  
[https://unctad.org/en/PublicationsLibrary/gdsecidc2017d3\\_en.pdf](https://unctad.org/en/PublicationsLibrary/gdsecidc2017d3_en.pdf)

<sup>6</sup> UNCTAD 2019 'Growing Trade in Electronic Transmissions: Implications for the South', UNCTAD Research Paper, No. 29.

is almost completely borne by the developing countries for extending duty free quota free market access, largely for the developed countries.

2.6. These submissions conclude that the amount of physical trade replaced by 3D printing is expected to be limited. UNCTAD (2019) provides a deeper analysis on the status of 3D printing though. It indicates that while 3D printing is currently at a nascent stage in developing countries, its market has grown annually by 22% in the period 2014-2018 and it is estimated that if investment in 3D printing is doubled, it could potentially replace almost 40% of cross-border physical global trade by 2040<sup>7</sup>. Such a growth is expected to significantly increase the potential tariff revenue loss.

### 2.3 Impact on SMEs and Digital Industrialization

2.7. Interestingly, when assessing the total trade of electronic transmissions, these submissions consider only digitizable goods and conclude that these remain modest but when estimating the impact of the moratorium on exports, especially of SMEs, these submissions considers the extended scope of the moratorium by including services<sup>8</sup> and find the impact to be huge. Defining the scope of the moratorium is therefore important in order to estimate its impact.

2.8. These submissions state that the use of 3D printing is growing slowly since the opportunities for mass production and economies of scale are limited and the inputs, materials and time required for 3D printing further constrain its use for manufacturing complex items. In this context, it is highlighted that with recent technological advances, namely high-speed sintering, mass production is becoming possible with 3D printers, where mass-producing up to 100,000 (smaller) components in a day will be possible at a speed which is 100 times faster<sup>9</sup>. According to D'Aveni (2015)<sup>10</sup>, the advent of additive manufacturing in the US hearing aid industry meant that, in less than 500 days, 100% of the industry was transformed and not one company stuck to the traditional mode of manufacturing.

2.9. These submissions do not reflect the impact that new technologies such as 3D printing can have on domestic industries especially MSMEs in developing countries. As outlined before, while 3D printing is currently at a nascent stage in developing countries, its market is expected to grow at a rapid pace. The most affected sectors could include sectors such as textiles and clothing, footwear, auto-components, toys, mechanical appliances, and hand tools, etc. which generate large scale employment for low skilled workers and are sectors in which most MSMEs operate. This could have a catastrophic effect on the ability of developing countries to protect their nascent domestic industries including MSMEs<sup>11</sup>.

2.10. If, "customs duties on electronic transmissions" cover not only digitised and digitizable goods but also digitally transmitted services, as asserted by a couple of institutions recently, then the negative impact of continuing with the moratorium on developing countries would be even greater. Effectively, this implies that the economy of the future (the digital economy) is totally liberalised. History has shown that trade policies are integral to successful economies' development trajectory and are critical in advancing industrial policy.

### 2.4 Methodological concerns

2.11. OECD (2019) mainly quotes studies that use Computable General Equilibrium (CGE) Models and those that use partial equilibrium models like SMART simulations. An important caveat in these studies is that they estimate the impact of tariff liberalization on only physical goods which are digitizable but are still being imported physically. However, as the UNCTAD Research Paper 29 has argued, the moratorium applies on customs duties on electronic transmissions, and not on the physical imports of products. Therefore, the results of these studies do not hold for electronic transmissions.

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<sup>7</sup> UNCTAD Research Paper No 47 (2020).

<sup>8</sup> UNCTAD Research Paper No 58 (2021).

<sup>9</sup> Ibid.

<sup>10</sup> Richard D'Aveni, 'The 3-D Printing Revolution' (2015) Harvard Business Review <https://hbr.org/2015/05/the-3-d-printing-revolution> accessed 1 June 2021.

<sup>11</sup> UNCTAD Research Paper No 58 (2021).

2.12. OECD (2019) quotes ECIPE (2019) which uses CGE models to provide the broader economic impact of the moratorium on consumption, investment, revenue, welfare and GDP. Using studies based on CGE modelling is problematic in itself given the well-recognised fact that most of these models are based on unrealistic assumptions which do not hold true in the real world. The models are based on the assumption of perfect competition in all sectors and in all countries, which implies that monopolies do not exist. Existence of monopolies in the digital arena like Google, Microsoft, etc. is a well-known fact. Further, the models are based on the Armington assumption according to which foreign and domestic products are not perfect substitutes and increase in tariff on a product would imply a fall in the use of the product, resulting in production losses and the associated losses in employment, investments and overall welfare. A detailed critique of the studies using CGE models can be found in Banga, R. (2019)<sup>12</sup>.

## 2.5 Impact on Policy Space

2.13. These submissions do not address concerns of the developing countries with respect to the importance of preserving their policy space. Customs duties are used by countries to support nascent domestic industries, regulate an unwanted surge in imports and facilitate industrialization. The development experience of nearly all countries across the world makes it evident that tariffs are amongst the most effective policy tools for achieving these objectives. Customs duties have been resorted to by developed countries to provide protection to their industry and to enable them to become internationally competitive. It is only fair that the developing world be given a similar opportunity. Thus, retaining the policy space to impose customs duties becomes an important objective in itself.

2.14. These submissions argue that digital technologies such as 3D printing are unlikely to have far-reaching implications on trade in the near term. As indicated before, 3D printing is expected to grow rapidly. Hence, it can jeopardize two decades of negotiated tariffs on industrial products under Uruguay Round, further constraining the policy space of the developing countries.

2.15. It is also argued that that exporters from developing countries need to import digitizable products in order to improve their production and exports of many products and services. Removal of the moratorium in no way means that Members will necessarily impose customs duties across the board. The key is policy space and to use such policy space appropriately for domestic digital industrialization and generation of local jobs in the era of Industry 4.0.

## 2.6 Application of Internal Non-Discriminatory Taxes as an alternative to Tariffs

2.16. The submissions suggest that instead of imposing tariffs on electronic transmissions, governments could consider imposing non-discriminatory internal taxes for raising revenue. However, a large body of literature, as highlighted in Devika et al (2020)<sup>13</sup>, suggests that the tariff revenue losses may not be recovered by governments in developing countries, and especially in low-income countries, due to the presence of a large informal sector which tends to remain out of the tax net. This finding confirms earlier work by Emram and Stiglitz (2005)<sup>14</sup>. Further, according to Devika et al (2020) a 1% decline in effective tariff rate is associated with a 1.98%-3.22% decline in total tax revenue.

2.17. Internal taxes are not an alternative to customs duties and serve a different purpose. For countries that want to promote digital industrialisation, customs duties should remain part of the toolbox to be deployed based on the strategic objectives of each country in pursuit of industrial policy.

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<sup>12</sup> "Modelling Impact of Moratorium on Electronic Transmissions using CGE: A Critique" published in *Advances in Social Sciences Research Journal*, 6(8) 391-400.

<sup>13</sup> Devika Dutt, Kevin P. Gallagher and Rachel D. Thrasher, "Trade Liberalization And Fiscal Stability In Developing Countries: Does The Evidence Tell Us?", *Global Policy Insights*; See also, Emram and Stiglitz (2005 'On selective indirect tax reform in developing Countries', *Journal of Public Economics*, vol. 89, no. 4, pp. 599-623.

<sup>14</sup> Emram and Stiglitz (2005 'On selective indirect tax reform in developing Countries', *Journal of Public Economics*, vol. 89, no. 4, pp. 599-623.

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### **3 ARE DEVELOPING COUNTRIES ENJOYING THE BENEFITS OF THE DIGITAL ECONOMY?**

3.1. It is often claimed that new digital technologies can provide developing countries with new income generation opportunities, including for their Micro and Small and Medium Sized Enterprises (MSMEs). As noted in our submission WT/GC/W/798, most developing countries are experiencing profound challenges due to the infrastructure/technological divide, the skills divide, and the market power of global digital platforms.

#### **3.2 Digital divide**

3.2. The rapid growth of digital technology has reshaped our daily lives and the internet has become one of the most fundamental infrastructures around the world. According to the World Economic Forum, each additional 10% of internet penetration can lead to a 1.2% increase in per capita GDP growth in emerging economies. During the pandemic, the digital connectivity has kept people, governments and businesses connected. Yet half of the world's population is without internet access, with the vast majority concentrated in developing countries and LDCs.

3.3. The digital divide manifests itself in terms of lack of digital infrastructure, which includes broadband infrastructure and data infrastructure, along with lack of digital skills. According to ITU data, 87% of people are using the internet in developed countries, compared with 44% in developing countries. Connectivity gaps in rural areas are especially serious in LDCs, where 17% of the rural population live in areas with no mobile coverage at all, and 19% of the rural population is covered by only a 2G network. The COVID-19 pandemic has exacerbated existing digital divides both between and within countries. With many essential services pushed online, there is a real and present danger that those without broadband internet access could be left ever further behind.

3.4. The capacity to store and process data is an important aspect of data driven economy. According to the Digital Economy Report, UNCTAD (2019)<sup>15</sup>, out of a total of 4,422 so-called colocation data centres, 80% are in developed countries, with one country alone accounting for about 40%. Africa and Latin America together account for less than 5% of the world's colocation data centres. The Cloud market is also highly concentrated where the share of top five providers, with 4 out of the five based in one country, exceeds 75%.

#### **3.3 Anti-competitive practices**

3.5. The narrative that online sales help MSME vendors to expand their sales and exports by linking with online retail platforms, as reflected in WT/GC/W/799/Rev.1 and OECD (2019), may not be entirely accurate. This narrative completely ignores the considerable challenges that the third-party vendors, including MSMEs, face in selling their products through online retail platforms due to the rent-seeking and other practices followed by many of these large platforms. The report of a bipartisan investigation in the US by the Committee on the Judiciary, Subcommittee on Antitrust, Commercial and Administrative Law, titled 'Investigation of Competition in Digital Markets' outlines some of these practices that pose challenges to MSMEs. It is apprehended that on account of these practices, followed especially by the super online retail platforms, most MSMEs may not be able to sustain their online businesses.

3.6. Developing countries and LDCs are facing multiple challenges in the digital age which have become more severe due to the ongoing pandemic. Given most developing countries and LDCs are net importers of digitised and digitizable goods, the moratorium can have significant implications for digital industrialization of these countries.

3.7. In the backdrop of the challenges posed by the prevalence of digital divide and anti-competitive practices of some of the dominant players, it is critical for the developing countries and LDCs to focus on improving domestic physical and digital infrastructure, creating supportive policy and regulatory frameworks and developing digital capabilities to develop strong domestic digital industry and a conducive ecosystem around it.

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<sup>15</sup> Digital Economy Report, UNCTAD (2019).

#### 4 CONCLUSION

4.1. World Bank (June 2020) has estimated that COVID-19 will push 71 million people into extreme poverty in 2020 largely from LDCs and developing countries<sup>16</sup>. This highlights the importance for LDCs and developing countries retaining their policy space to develop a viable domestic digital industry. Customs duties are a simple and effective policy tool in the hands of the governments, especially in times of crisis.

4.2. It is important for member states to review the decision taken in 1998 to have a moratorium on customs duties on electronic transmissions. This decision was taken with no consensus on the scope of the moratorium and no notion on how the digital revolution will unfold.

4.3. In December 2019, members had agreed to extend the moratorium for six months up to June 2020 and re-invigorate the work under the Work Program on Electronic Commerce which requires structured discussion on trade related issues related to global e-commerce, taking into account the economic, financial and development needs of the developing countries.

4.4. In order to enable the WTO Membership to take an informed decision in MC12 on whether or not to extend the moratorium on customs duties, it is necessary to have complete clarity on the definition of electronic transmissions, consensus on the scope of the moratorium and a comprehensive understanding of the impact of the moratorium.

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<sup>16</sup> <https://blogs.worldbank.org/opendata/updated-estimates-impact-covid-19-global-poverty>