

# ***Transparency and Accountability***

## ***Monitoring and Reporting Methods Under An Arms Trade Treaty***

**Sergio Finardi and Peter Danssaert**



**International Peace Information Service and TransArms-R**

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# Transparency and Accountability

## Editorial

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## The Report - Executive Summary

Without an understanding of the existing practices of States regarding their commonly agreed standards for the monitoring and reporting of their international transfers of conventional arms,<sup>1</sup> it will be very difficult to draft many of the basic provisions of the Treaty to ensure compliance and enforcement.

This report therefore seeks to clarify and discuss existing terminology and reporting practices for State regulation of international transfers of goods and services and for international transfers of conventional arms. It is hoped that this will also help contribute to the development of common international standards for monitoring and reporting international transfers of conventional arms. Standardization of statistical requirements and reporting methods is of paramount importance for the ATT to be effective.

Robust reporting and transparency mechanisms in the Treaty will stem from the adoption of a clear set of common standards. This would facilitate international cooperation and assistance between regulatory, reporting and judicial agencies to better implement the ATT.

Submissions by States on the ATT, as well as discussions reflected in UNIDIR documents, propose types of international transfers that an ATT should include in its scope.<sup>2</sup> At the third and fourth UN Preparatory Committee meeting of States on the ATT in March and July 2011, the Chair also proposed ways of defining transfers, transactions and activities that could be included in the scope of an ATT according to the submissions of States.<sup>3</sup> From these proposals, it can be seen that the implications of the various ways States define, account, and control international transfers in general and international transfers of conventional arms and supporting services have not yet received sufficient attention.

The possibility of establishing “common international standards” is dependent not only on a clear understanding of the intricacies that lie behind seemingly plain terms such as import and export or transit and re-export, but first and foremost on a clear understanding of the different ways national and international systems have been designed by States to deal with the monitoring and accounting of international transfers-related activities.

For example, the standardization of statistical requirements and reporting methods for international trade in goods and services has been the object of several initiatives

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<sup>1</sup> See Introduction for definition.

<sup>2</sup> See: *A Global Arms Trade Treaty: What States Want*, published by Amnesty International on behalf of the Arms Trade Treaty Steering Committee, October 2007, (AI Index: POL 34/004/2007); *Documento de debate del Comité Conductor del Tratado Internacional sobre el Comercio de Armas: Ámbito de Aplicación Transferencias y Transacciones que debe Contemplar el Tratado Internacional sobre el Comercio de Armas* (IANSA, Mar 09-77); Sarah Parker, *Implications of States' Views on an Arms Trade Treaty* (UNIDIR, January 2008); Sarah Parker, *Analysis of States' Views on an Arms Trade Treaty* (UNIDIR, October 2007); *Traités sur le commerce des armes: ce que veulent les États* (IANSA, October 2007); *A Global Arms Trade Treaty: What States Want* (IANSA, April 2007)

<sup>3</sup> Chairman's Draft Paper, 3 March 2011 and 14 July 2011

by international organizations. In 1995, the International Monetary Fund (IMF) launched the General Data Dissemination System initiative, aimed at helping States to increase the consistency, standardization, and quality of their statistics<sup>4</sup> and consequently the quality of international statistics based on States' submissions to the UN agencies.<sup>5</sup> However, sixteen years later the standardization of such methods and reporting systems is still far from complete. In addition, the formation of large regional trade agreements (RTAs)<sup>6</sup> - such as the European Union,<sup>7</sup> the Mercosur,<sup>8</sup> and the NAFTA,<sup>9</sup> - has often caused a loss of trade data. This loss of data can be correlated with the enacting of rules aimed at simplifying or abolishing the Customs documentation for the intra-bloc trade.

To reflect the necessity of an informed discussion on common standards this report includes three main parts, divided in several chapters:

1. Part 1 seeks to clarify the trade terminology and to present trading and reporting systems for international transfers of goods (including Free Trade Zones and similar free trade areas), international transport services and, in Appendix A, contractual terms of trading (Incoterms).
2. Part 2 deals with methods and practices followed by States for accounting and reporting their international transfers of conventional arms, as defined above, including practices related to Free Trade Zones and the contractual terms under which conventional arm are traded
3. Part 3 offers proposals and recommendations.

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<sup>4</sup> IMF, *"The General Data Dissemination System, Guide for Participants and Users."* IMF 2007

<sup>5</sup> The IMF presently (January 2012) provides trade statistics (including directions of trade) for 187 countries.

<sup>6</sup> It is worth noting that there are 214 RTAs (bilateral and multi-lateral) presently (January 2012) in force, according to the World Trade Organization (WTO). See: <http://rtais.wto.org/ui/PublicAIIRList.aspx>

<sup>7</sup> The European Union (as "European Communities" in the WTO from 1995 to 2009) is a "single Customs union and single trade policy and tariff" (WTO)

<sup>8</sup> "Mercado Común del Sur, Mercado Comum do Sul, Ñemby Ñemuha (Southern Common Market). Argentina, Brazil, Paraguay, Uruguay, 1991 for Goods, 2006 for Services.

<sup>9</sup> "North American Free Trade Agreement." Canada, Mexico, United States of America, 1993 for Goods and 1995 for Services.

## I. Introduction

The current negotiations in the United Nations to develop an Arms Trade Treaty (ATT) offer an historic opportunity for States to agree rules and procedures for a *“legally binding treaty establishing common standards on the import, export and transfer of conventional arms”*, according to UN Resolution 61/89 and further Resolution 63/240,<sup>10</sup> thereby enhancing transparency and accountability in a field that has been plagued by irresponsible and illegal practices that have cost the lives of millions.

The discussion of common standards for monitoring and reporting under a new global ATT system drawing from, but not limited to, existing State practice is not just a technical issue to be dealt with amongst specialists. It is an essential part of ensuring that all the elements of the Treaty will function effectively as a shared security system that helps to prevent conflict and protect human rights.

For example, the above-mentioned UN Resolutions mention *“import, export and transfer”* as different activities that the ATT should cover. If “transfer” is a different activity from import and export, the word should not be used for denoting all the activities covered by the ATT.

The distinction between import/export and transfer is repeated in various UN Resolutions. For example, Resolution 61/89 (December 18, 2006) states: *“Recognizing that the absence of common international standards on the import, export and transfer of conventional arms is a contributory factor to conflict...”*<sup>11</sup>. Resolution 63/240 (dated January 8 2009) uses the same conceptual formulation: *“...legally binding treaty on the import, export and transfer of conventional arms which provides a balance giving benefit to all”*.<sup>12</sup>

In earlier UN Resolutions, however, the word “transfer” seems to encompass all forms of international arms transactions. Resolution 46/36 on *“General and Complete Disarmament”* (December 6 1991) states: *“(f) Arms “exports and imports” represent in the present resolution, including its annex, all forms of arms transfers under terms of grant, credit, barter or cash.”*<sup>13</sup>. Resolution 62/278 (dated August 17, 2007) states: *“3. On 16 January 2007, the Secretariat addressed a note verbale to all Member States requesting them, in preparation of their views, to consider including information on the following: (a) elements of the conventional arms trade that should be included in the scope of the future arms trade treaty; (b) principles, guidelines and parameters that should govern the international transfer of conventional arms; and (c) any other features that might contribute to the development and adoption of an effective arms trade treaty.”*<sup>14</sup>

The July 2011 ATT PrepCom Chairman’s Draft Paper states that the scope of the ATT should include *“export, import and transfers of conventional arms”*, but in various

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<sup>10</sup> See: UN Resolutions 61/89 and 63/240 (United Nations, *“Open-ended Working Group towards an Arms Trade Treaty New York, 13-17 July 2009”*), New York 20 July 2009, A/AC.277/2009/1.

<sup>11</sup> See: *“Towards an arms trade treaty: establishing common international standards for the import, export and transfer of conventional arms”*, A/RES/61/89, 18 December 2006.

<sup>12</sup> *Towards an arms trade treaty: establishing common international standards for the import, export and transfer of conventional arms”*, A/RES/63/240, 8 January 2009.

<sup>13</sup> *“General and complete disarmament - L - Transparency in armaments”*, A/RES/46/36, 6 December 1991

<sup>14</sup> *“Towards an arms trade treaty: establishing common international standards for the import, export and transfer of conventional arms”*, A/62/278, 17 August 2007.

parts of the same Draft Paper the word “transfer” is used to mean all forms of arms transfer and transactions, for example in “B. *Potential consequences of arms transfer*”, and in Annex A “a. *Transfer (includes import, export, re-export, temporary transfer, transshipment, transit, transport, leases, loans, and gifts of conventional arms)*”. Annex A further clarifies that in addition to “export” and “import” other activities should be covered by the ATT (such as, inter alia, re-import, re-export, transit, trans-shipment, transport services and brokering).<sup>15</sup>

Furthermore, the Draft Paper indicates that the scope of the ATT should also include all main conventional arms categories<sup>16</sup> as well as their ammunition, parts and component, but adds “*technology and equipment specially and exclusively designed and used to develop, manufacture, or maintain any of the categories*” of the weapons listed in the Scope<sup>17</sup>. This is a useful but still somewhat limited definition.

For the purposes of this report, “**conventional arms**” means all types of military and non-military weapons, munitions, armaments and related parts and technology (including such items destined for use by internal security forces), while “**international transfers**” means the physical movement of equipment and the tangible or intangible movement of technology into or from national territory and includes the transfer of title to and control over the equipment and technology.<sup>18</sup> However, this report will argue<sup>19</sup> in favor of the inclusion, in the ATT Scope, of significant movements of conventional arms - as defined above - to the territory of other States even if they do not imply a transfer of title or control over the equipment (the so-called “internal flows”).<sup>20</sup> In addition, “services” (in support of the international transfers) refer to brokering, financial and transport services, but by way of illustration this report will only focus on transport services.

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<sup>15</sup> ATT PrepCom, *Chairman’s Draft Paper*, 14 July 2011, Annex A.

<sup>16</sup> “*Tanks, Military Vehicles, Artillery Systems, Military Aircraft (manned or unmanned), Military Helicopters (manned or unmanned), Naval Vessels (surface and submarine vessels armed or equipped for military use), Missiles and Missile Systems (guided or unguided), Small Arms, Light Weapons*”.

<sup>17</sup> ATT PrepCom, *Chairman’s Draft Paper*, 14 July 2011.

<sup>18</sup> See: “*General and Complete Disarmament: Transparency in Armaments - Report on the Register of Conventional Arms*”, A/47/342, 14 August 1992; ATT PrepCom, *Chairman’s Draft Paper*, 14 July 2011, Annex A.

<sup>19</sup> See Part III

<sup>20</sup> See Part III Proposal and Recommendations. See for the discussion on “internal flows”: “*Continuing operation of the United Nations Register of Conventional Arms and its further development*”, A/64/296, 14 August 2009, §15.

## Part I - Trade Terms, Accounting and Reporting

It is important for the consistency of application of the ATT, and therefore its effectiveness that the provisions of an ATT are based upon internationally agreed trade terminology. This section therefore outlines the currently accepted State practice with respect to such terms.

### Chapter 1 - Trade Terminology

National laws and international trade agreements regulate international trade activities such as Import/Export, Re-Import/Re-Export, Temporary Import and Export, Transit; Trans-shipment; and Re-Transfer (and for Trade in Services: Debit and Credit). Customs tariffs are applied (or not applied) according to the terms of applicable trade agreements. National laws and international initiatives indicate the methods to collect, account and report information on international transfers of goods and services and their direction.

The establishment of an internationally agreed trade terminology lies at the basis of meaningful international reporting systems for the international movement of commodities. Paragraphs 1.1/1.9 below summarize the meaning of trade terms according to the methodological sections of the most authoritative international sources and provide indications of the way related trade activities are statistically accounted for.<sup>21</sup> Paragraph 1.10 and related sub-paragraphs below provide a discussion of the classification methods and contractual practices used in the international transfers of goods and services.

These derive from established State practices and thus a variety of international organizations - such as the U.N. Statistical Division (UNSD); the International Monetary Fund (IMF); the World Trade Organization (WTO); the World Bank (WB); the U.N. Conference on Trade and Development (UNCTAD) – and multinational organizations such as the Organization for Economic Cooperation and Development (OECD) and the European Union (EU) – prepare and publish international trade statistics on the basis of internationally agreed reporting requirements and trade terminology.<sup>22</sup>

#### 1.1. Imports and Exports

**a. Imports and exports** refer to physical goods (as opposed to services) leaving (export) or entering (import) the customs territory of a country with a definitive

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<sup>21</sup> The authors made every effort to simplify the treatment of a matter that has extremely complex aspects. The quoted sources provide explanations and clarifications, but they do not exhaust the range of problems arising from an array of diverse legal, business, and Customs practices at national and international level. Ultimately, only an in-depth review of these practices at national and port of entry level may provide the knowledge that is necessary for an ATT-related monitoring activity.

<sup>22</sup> Unfortunately, during the years, changes in methods and reporting requirements make comparisons between their reports on different periods difficult and sometimes impossible. For example, in 1993 the European Union changed the way data on its intra-trade (trade among its members) are collected, passing from a system in which data were based on Customs declarations to a system in which data are collected from firms' reports on their transactions. These changes resulted not only in loss of continuity with the previous time-series, but also in lower accuracy and under-reporting. The changes also affected the accuracy and consistency of the UN COMTRADE database that is based on Customs declarations.

passage of titles of property between two trading partners and for which customs duties are paid. The goods are 'cleared for home use' and free circulation inside the customs territory (imports) or for 'outright exportation' (exports).

**b. clearance for home use** *"means the Customs procedure which provides that imported goods enter into free circulation in the Customs territory upon the payment of any import duties and taxes chargeable and the accomplishment of all the necessary Customs formalities; goods in free circulation means goods which may be disposed of without Customs restriction"* (Revised Kyoto Convention).<sup>23</sup>

**c. outright exportation** *"means the Customs procedure applicable to goods which, being in free circulation, leave the Customs territory and are intended to remain permanently outside it"* (Revised Kyoto Convention).<sup>24</sup>

**d. the Customs territory** of a country is *"the territory in which customs law of a country applies in full"*.<sup>25</sup>

For accounting purposes, it is worthwhile to note that under the Revised Kyoto Convention – the main international convention for international trade – *"the Customs shall not require evidence of the arrival of the goods abroad as a matter of course"*<sup>26</sup>;

In addition, the U.N. International Merchandise Trade Statistics (IMTS) Manual states that *"certain exports and imports are often not covered in customs records and hence might not be included in the national IMTS [...] Countries might exclude specific goods such as oil and gas exports or imports and exports of goods for military use from IMTS"*.<sup>27</sup>

## **1.2. European Union Intra-Trade: Arrivals and Dispatches<sup>28</sup>**

### **a. Arrivals**

*"Arrivals in a given Member State include: a) goods in free circulation which enter the statistical territory of the Member State; b) goods which have been placed under the customs procedure for inward processing or processing under customs control (for processing) in another Member State and which enter the statistical territory of the Member State in question; c) Some goods movements are included in statistics based on specific conditions. In particular, aircraft and ships whose ownership has been transferred from a person established in another Member State to a person established in the Member State in question are included in the statistics of arrivals of this latter Member State"*.

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<sup>23</sup> See: *International Convention on the Simplification and Harmonization of Customs procedures* (Kyoto Convention, 1974). The *Revised Kyoto Convention* (1999) entered into force on February 3, 2006. Annex B. [http://www.wcoomd.org/Kyoto\\_New/Content/content.html](http://www.wcoomd.org/Kyoto_New/Content/content.html)

<sup>24</sup> *Revised Kyoto Convention*, quoted, Annex C.

<sup>25</sup> United Nations, Department of Economic and Social Affairs Statistics Division, *Expert Group on International Merchandise Trade Statistics*, First Meeting, New York, 3-6 December 2007

<sup>26</sup> *Revised Kyoto Convention*, quoted, Annex C.

<sup>27</sup> U.N. Department of Economic and Social Affairs, Statistics Division, *"International Merchandise Trade Statistics: Supplement to the Compilers Manual."* United Nations, March 7, 2008.

<sup>28</sup> All quotations are from: European Commission, Eurostat, *"Statistics on the trading of goods – User guide."* Luxembourg 2006.

## **b. Dispatches**

*"Dispatches from a given Member State include: a) goods in free circulation which leave the statistical territory of the Member State bound for another Member State; b) goods which have been placed under the customs procedure for inward processing or processing under customs control (for processing) in the Member State and which are destined for another Member State; c) Some goods movements are included in statistics based on specific conditions. In particular, aircraft and ships whose ownership has been transferred from a person established in the Member State in question to a person established in another Member State are included in the statistics on dispatches of the former Member State".*

## **1.3. European Union Extra-Trade: Imports and Exports<sup>29</sup>**

### **Imports**

*"Imports into a given Member State include: a) goods which enter the statistical territory of the Member State from a non-member country and are:*

- placed under the customs procedure for release into free circulation (good that will be consumed in the importing Member State or dispatched to another Member State), either immediately or after a period in a customs warehouse;*
- placed under the customs procedure for inward processing or processing under customs control (usually goods destined to be processed for subsequent re-export) either immediately or after a period in a customs warehouse. b) some movements of goods are included in statistics based on specific conditions. In particular, aircraft and ships whose ownership has been transferred from a person established in a non-member country to a person established in the Member State in question are included in import statistics of this Member State".*

### **Exports**

*"Exports from a given Member State include: a) goods which leave the statistical territory of the Member State bound for a non-member country after having been:*

- placed under the customs export procedure (final export, export following inward processing, etc.);*
- placed under the customs outward-processing procedure (usually goods destined to be processed for subsequent re-import); b) some goods movements are included in statistics based on specific conditions. In particular, aircraft and ships whose ownership has been transferred from a person established in the Member State in question to a person established in a non-member country are included in export statistics of that Member State".*

## **1.4. Re-Imports**

**a. Re-Imports** are *"domestic goods imported in the same state as previously exported, without any substantial transformation occurring on the goods while they*

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<sup>29</sup> All quotations are from: European Commission, Eurostat, *"Statistics on the trading of goods – User guide."* Luxembourg 2006.

*were outside the territory [...]. For the goods to be included in re-imports, a nonresident [of the re-importing country] must have acquired the goods, then resell them to a resident (in cases where there was no change of ownership, they are omitted from imports, for example, goods for repair or goods sent for processing)."*<sup>30</sup>

**b. Goods exported with "notification of intended return"** *"means goods specified by the declaring as intended for re-importation, in respect of which identification measures may be taken by the Customs to facilitate re-importation in the same state. "Re-importation in the same state" "means the Customs procedure under which goods which were exported may be taken into home use free of import duties and taxes, provided they have not undergone any manufacturing, processing or repair abroad [...] Re-importation in the same state [...] shall also not be refused on the grounds that, during their stay abroad, the goods have undergone operations necessary for their preservation or maintenance provided, however, that their value at the time of exportation has not been enhanced by such operations".*<sup>31</sup>

## **1.5. Re-exports**

**a. Re-exports** *"are foreign goods (goods produced in other economies and previously imported) that are exported with no substantial transformation from the state in which they were previously imported [...]. For goods to be included in re-exports [...] a resident of [the re-exporting] country must acquire, and then resell the goods with the goods passing through the [re-exporting] country territory".*<sup>32</sup>

**b.** *"Re-exports refer to exports of foreign goods which were previously imported and which remained in the same state. Cases which fall within this category are exports of goods which previously were imported into a customs warehouse, a free zone or under the inward processing procedure. Goods could also have entered free circulation and then be re-exported in the same state".*<sup>33</sup>

## **1.6. Temporary imports, exports, re-exports**

**a. Goods for which a "temporary admission" is granted** *are "brought into a country or dispatched from it with a reasonable expectation of subsequent withdrawal or return within a limited time".*<sup>34</sup>

**b. Temporary admission** *"means the Customs procedure under which certain goods can be brought into a Customs territory conditionally relieved totally or partially from payment of import duties and taxes; such goods must be imported for a specific purpose and must be intended for re-exportation within a specified period and without having undergone any change except normal depreciation due to the use made of them. [...] Goods temporarily admitted shall be afforded total*

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<sup>30</sup> See: IMF, *Balance of Payments and International Investment Position Manual (BPM6)* Sixth Edition, December 2008, Pre-publication draft <http://www.imf.org/external/pubs/ft/bop/2007/pdf/BPM6.pdf>

<sup>31</sup> U.N. Department of Economic and Social Affairs, Statistics Division, *"International Merchandise Trade Statistics: Supplement to the Compilers Manual."* United Nations, March 7, 2008.

<sup>32</sup> See: IMF, *Balance of Payments Manual (BPM6)*, quoted 2008.

<sup>33</sup> *International Merchandise Trade Statistics: Supplement to the Compilers Manual*, quoted, 2008.

<sup>34</sup> United Nations, Department of Economic and Social Affairs Statistics Division, *Expert Group on International Merchandise Trade Statistics*, First Meeting, New York, 3-6 December 2007.

*conditional relief from import duties and taxes, except for those cases where national legislation specifies that relief may be only partial. [...] The Customs shall fix the time limit for temporary admission in each case”.*<sup>35</sup>

It should be noted that “[Temporary] admission with total conditional relief from duties and taxes should be granted to the goods referred to in the Annexes to the Convention on Temporary Admission (Istanbul Convention) of 26 June 1990.” Among these goods there are the “Goods imported for humanitarian purposes”.<sup>36</sup>

Temporary goods “are excluded from international merchandise trade statistics [...] since they do not add to or subtract from the stock of material resources of the country through which they pass”.<sup>37</sup>

## **1.7. Transit/Customs Transit**

**a. Goods in transit** are “goods entering and leaving a country with the exclusive purpose of entering a third country”.<sup>38</sup> “Movements of goods in transit are usually required to be carried out under Customs supervision, i.e. under a Customs transit regime during which the payment of duties and taxes is suspended during the transit. To preserve the interest of the transit country whilst allowing the suspension of the payment of duties and taxes Customs transit systems may require a financial guarantee to be provided, also sometimes referred to as a bond”.<sup>39</sup>

**b. Customs transit** “means the Customs procedure under which goods are transported under Customs control from one Customs office to another”; **Customs transit operation** “means the transport of goods from an office of departure to an office of destination under Customs transit”; **office of departure** “means any Customs office at which a Customs transit operation commences”; and **office of destination** “means any Customs office at which a Customs transit operation is terminated”.<sup>40</sup>

Goods in transit may or may not originate from a land-locked country (a State with no seacoast). If they originate from a land-locked country and are intended for a port of exit in another country, the U.N. Convention on the Law of the Sea establishes the right “of access of land-locked States to and from the sea and freedom of transit.”

**Transit State** “means a State, with or without a sea-coast, situated between a land-locked State and the sea, through whose territory traffic in transit passes”; Thus, **traffic in transit** “means transit of persons, baggage, goods and means of transport across the territory of one or more transit States, when the passage across such territory, with or without trans-shipment, warehousing, breaking bulk or change in the mode of transport, is only a portion of a complete journey, which begins or terminates within the territory of the land-locked State. [...] For the convenience of

<sup>35</sup> Revised Kyoto Convention, quoted, Annex G.

<sup>36</sup> International Merchandise Trade Statistics: Supplement to the Compilers Manual, quoted, 2008.

<sup>37</sup> International Merchandise Trade Statistics: Supplement to the Compilers Manual, quoted, 2008

<sup>38</sup> International Merchandise Trade Statistics: Supplement to the Compilers Manual, quoted, 2008

<sup>39</sup> UNCTAD Trust Fund for Trade Facilitation Negotiations, Technical Note 17, “Bonded Customs Regimes (Customs Transit Regimes and transit guarantees).” UNCTAD, February 2009.

<sup>40</sup> Revised Kyoto Convention, quoted, Annex E.

*traffic in transit, free zones or other customs facilities may be provided at the ports of entry and exit in the transit States, by agreement between those States and the land-locked States”.*<sup>41</sup>

It should be noted that Goods in Transit “are excluded from international merchandise trade statistics [...] since they do not enter the local economy or – more precisely – do not add to or subtract from the stock from the stock of goods of the country”.<sup>42</sup>

For example, in the European Union, “goods in transit (either in simple transit or transit involving trans-shipment) across the European Union area are not included in trade statistics. However, goods which enter the European Union area are released into free circulation and are then transferred from the Member State of entry to another Member State or, conversely, originate in one Member State but leave the European Union area through another where customs procedures are carried out, must be included in statistics”.<sup>43</sup>

Moreover, “goods in transit” are not required to use the same transport modality or transport means all along their route. If the same modality (a railway, for example) is not available all along the route that connects the office of departure with the office of destination, the goods in transit (or the unit of transport into which they are loaded, such as a container) can be transferred from one transport modality to another, provided certain mandatory Customs procedures for their identification as 'goods in transit' are observed.

## **1.8. Trans-loading**

The operation of changing transport modality or means of transport is called 'trans-loading'. Technically speaking, trans-loading refers only to a change in transport modality (in particular road/rail), but the term is also frequently used to indicate a change of mean of transport inside the same modality (for example from a larger to a smaller ship).

Trans-loading is a transport operation and should not be confused with trans-shipment, which is a Customs procedure.

## **1.9. Trans-shipment**

**a. Trans-shipment** “means the Customs procedure under which goods are transferred under Customs control **from the importing means of transport to the exporting means of transport** within the area of one Customs office which is the office of both importation and exportation. [...] The Customs should accept as the Goods declaration for trans-shipment any commercial or transport document for the consignment concerned which meets all the Customs requirements. This acceptance

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<sup>41</sup> [http://www.un.org/Depts/los/convention\\_agreements/texts/unclos/closindx.htm](http://www.un.org/Depts/los/convention_agreements/texts/unclos/closindx.htm). Part X, Articles 124, 125, and 128.

<sup>42</sup> *International Merchandise Trade Statistics: Supplement to the Compilers Manual*, quoted, 2008

<sup>43</sup> “Ten Member States (Belgium, Denmark, Latvia, Luxembourg, Hungary, the Netherlands, Austria, Poland, Portugal and the United Kingdom) do not follow this practice in their national figures and goods in transit are excluded from statistics. Before 1998 Belgium also did not cover these flows.” See European Commission, Eurostat, “Statistics on the trading of goods – User guide.” Luxembourg 2006, Methods

*should be noted on the document. [...] When the Customs consider it necessary, they shall take action at importation to ensure that the goods to be trans-shipped will be identifiable at exportation and that unauthorized interference will be readily detectable".<sup>44</sup>*

It should be noted that under the Kyoto Convention it is a requirement of States that *"trans-shipment should not be refused solely on the grounds of the country of origin of the goods, the country from which they arrived or their country of destination".<sup>45</sup>*

In a broader and less technical meaning, trans-shipment may also indicate the operation for which goods (containerized or bulk) are unloaded from an importing vessel at the trans-shipment hub and then loaded onto another vessel (feeder) in the same hub, to be further transported to their final destination **in the same country of first arrival**. Thus a "hub" could be port, airports, rail connections, logistics centers where a Customs office is present. In this case, the goods arriving at the hub are not intended for export to another country, but solely for another location inside the same importing country. The imported goods are declared only at the Customs office of their final destination. In maritime transport, this procedure is called **"Carriage of goods coastwise"**. At the first importing point (the first trans-shipment hub) Customs shall require the master of the vessel to present a **"trans-shipment permit"**: *"a single document giving details of the vessel, listing the goods to be carried under the carriage of goods coastwise procedure and stating the port or ports in the Customs territory at which they are to be unloaded. This document, once endorsed by the Customs, shall constitute the authorization for the conveyance of the goods under the carriage of goods coastwise procedure".<sup>46</sup>*

The term "trans-shipment" does not apply to the trans-loading of goods in transit that are already under the Customs procedure for "goods in transit". As stated above, goods in transit can undergo a change in modality or means of transport inside the transit State, but the change does not activate a trans-shipment procedure.

It is important to note that 'trans-shipments' and 'Carriage of goods coastwise' *"are excluded from international merchandise trade statistics [...] since they do not enter the local economy or – more precisely – do not add to or subtract from the stock of goods of the country".<sup>47</sup>*

## **1.10. Transfers and Re-transfers**

The term "transfer" has both a broader meaning than "trade" and also a technical and more particular meaning.

As indicated in several UN documents, the term "transfer" simply indicates a tangible or intangible movement of goods and/or services into and from a national territory. The term "transfer" is broader than "trade" because it includes international "movements" of articles that are not part of the international trade in goods and services, but are part of exchanges between governments and government entities.

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<sup>44</sup> *Revised Kyoto Convention*, quoted, Annex E

<sup>45</sup> *Revised Kyoto Convention*, quoted, Annex E

<sup>46</sup> *Revised Kyoto Convention*, quoted, Annex E

<sup>47</sup> *International Merchandise Trade Statistics: Supplement to the Compilers Manual*, quoted, 2008

For example, in the field of international defense and nuclear relationships between States, "transfers" refer to government-to-government or government-to-company shipments of conventional arms and nuclear or sensitive material that fall under the provisions of defense/energy cooperation and military assistance agreements and that do not involve normal Customs operations.

Therefore, in the meaning above, "transfers" and "re-transfers" are not, strictly speaking, international trade terms. In particular, and contrary to what it is often stated in commentaries on the ATT, **re-transfers and re-exports are not similar concepts or operations**. Re-exports always involve a commercial dimension and the absence of substantial modifications of the goods, whereas re-transfers may or may not involve an economic dimension and a modification of the goods.

Re-transfers occur when items received under the provision of the above-mentioned agreements and programs are transferred to a third party by the original end-user.<sup>48</sup> The third party may (1) or may not (2) be an entity inside the original receiving country and may or may not be part of the original agreements or programs.

In the first case, a re-transfer occurs when the initial end-user intends to transfer the items to another company based in the same country, for further processing or for use in manufacturing projects. If the original agreement did not include the latter company as a potential end-user, the first end-user must obtain permission by the State of origin.

In the second case, re-transfers occur when the first end-user intends to transfer the items to a company based abroad. If the original agreement included the foreign third party as an actual or potential partner in the use of the items (as for example in a multi-national defense manufacturing project), the re-transfer still falls inside the domain of government-to-government transfers, for which Customs regulations do not apply and **these re-transfers should not be called re-exports**. If instead the original end-user intends to ship the items - as such or as components of another defense or nuclear system - to a company based abroad as a matter of sales, it must not only obtain permission from the State of origin but also apply for an export license, as in all other commercial sales. In the latter case, provided that the items did not undergo substantial modifications, the re-transfers are legitimately called re-exports and fall under the normal Customs procedures and regulations.

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<sup>48</sup> See, for example, the US regulation: Defense Institute of Security Assistance Management, "The Management of Security Assistance." Twenty-Seven, October 2007. "A third-party transfer is any retransfer of title, physical possession or control of defence articles, training or technical data acquired under authorized USG transfer programs from the authorized recipient to any person or organization which is not an employee, officer or agent of that recipient country. A change in end-use is considered a third party transfer. Examples of possible third-party transfers include: • Retransfer of possession or title of defence articles or related technical data to any other foreign government: a) Retransfer of possession or title of defence articles related technical data to any private companies; b) Retransfer of possession or title of defence articles to bona fide museums within the original receiving country; c) Retransfer of possession or title of defence articles to private education organizations within the original receiving country. Change of end-use is defined as any change in the usage of defence articles and services that deviates from the original purposes for which the items were sold. Examples of possible changes of end-use could be: a) Withdrawal of military end items from the operational inventory for display at a government run museum; b) Use of unserviceable/non-repairable vehicles as targets on a firing range; c) Transfer of demilitarized military end items or machinery from the armed forces to civil government or educational institutions; d) Demilitarization and redistribution of defence articles re-cycled among host government agencies; e) Demilitarization and complete disposal of defence articles such that the materiel is no longer considered a defence article."

It should be noted that “substantial modifications” to the original items can usually be performed only with the consent of the State of origin and, if the permission is granted, the sale of such substantially modified items to a third entity abroad **can legitimately be called “exports”**.<sup>49</sup>

### 1.11. Offsets<sup>50</sup>

Offsets are contractual arrangements between industrial and trade partners and are of increasing importance for the international arms trade and production. Offsets are “*industrial compensation practices required as a condition of purchase in either government-to-government or commercial sales of defense articles and/or defense services [...]*”.<sup>51</sup>

Offset contracts may be entirely related to goods and services (direct offsets) for military and internal security operations or they may involve an exchange of other goods and services (indirect offsets.) Offset contracts include several different types of benefit and agreement such as the following:<sup>52</sup>

**Co-production:** in this case the buyer builds part of the arms system - that which is the object of the contract. The main potential advantages here are the creation of jobs in the buying country and the acquisition of the related technological know-how. Sometimes, this kind of arrangement also includes clauses that allow the buyer to also use the seller's technological know-how in fields not directly related to the immediate object of the transaction.

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<sup>49</sup> Most transfers of defence items include a clause that forbids re-exports without the consent of the State of origin, both in government-to-government transfers and in commercial transactions.

<sup>50</sup> See: US General Accounting Office, *Trade Offsets in Foreign Military Sales*. GAO Report, April 13, 1984; Neuman, S. G. *Coproduction, Barter, and Countertrade: Offsets in the International Arms Market.* In *Orbis* Vol. 29 (Spring), pp. 183-213, 1985; Wulf, H. (ed), *Arms Industry Limited*. Stockholm, SIPRI, Oxford Un. Press, 1993; Hall, P., S. Markowski “*On the Normality and Abnormality of Offsets Obligations.*” *Defence and Peace Economics* Vol. 5, pp. 173-188, 1994; Mussington, D. *Arms Unbound. The Globalization of Defense Production*. Washington, Brassey's, 1994; Lumpe, L. , “*Economic Costs of Arms Exports: Subsidies and Offsets.*” Testimony to the US Congress, May 23, 1995; Keller, W. W. *Arm in arm , the political economy of the global arms trade*. New York, Basic Books, 1995 (Chapter 2, 41-46; Chapter 4, 134-144); Hartung, W.D., *Welfare for Weapons Dealers: The Hidden Costs of the Arms Trade*. New York, World Policy Institute, New School for Social Research, 1996; Martin, S., *The economics of offsets, defence procurement and countertrade*. Amsterdam, The Netherlands, Harwood Academic Publishers, 1996; Gasparini Alves, K. Hoffman (editor), *The Transfer of Sensitive Technologies and the Future of Control Regimes*, New York, UNIDIR, 1997 (in particular Chapter 13 Export/Import monitoring Mechanism); Guay, T.R. *At arms' length: the European Union and Europe's defence industry*. New York, St. Martin's Press, 1998; Susman, G.I., O' Keefe, S. (eds.) *The Defense Industry In The Post-Cold War Era. Corporate Strategies And Public Policy Perspectives*. Kidlington, Oxford, Elsevier Science, Pergamon Press, 1998; Gasparini Alves, P., K. Hoffman (eds.) *The Transfer of Sensitive Technologies and the Future of Control Regimes*. New York, U.N., UNIDIR, 1997; Gurtov, M., B-M. Hwang *China's Security. The New Role of the Military*. Boulder, Lynne Rienner, 1998; Inbar, E. *The politics and economics of defence industries*. London, Portland, Ore, Frank Cass, 1998 (in particular chapter 4 “Too Small to Vanish, too Large to Flourish: Dilemmas and Practices of Defence Industry Restructuring in West European Countries”); Abel, P. *Manufacturing trends: globalising the source*. In Lumpe, L. (ed.) *Running guns. The Global Black Market in Small Arms*. London, Zed Books, 2000; Brauer, J., *Economic Aspects of Arms Trade Offsets*. In International Conference on Defense Offsets and Economic Development, Cape Town, 25-27 September 2002; Brzoska, M., *The economics of arms imports after the end of the cold war*. In *Defence and Peace Economics*, vol 15, issue 2, 2004.

<sup>51</sup> See: Bureau of Export Administration *Offsets in Defense Trade: 1999 Report to Congress.*” U. S. Department of Commerce, December 9, 1999. See also: Schinasi, K. *Defense Trade. Observations on Issues Concerning Offsets*. Washington, DC, U.S. General Accounting Office, December 15, 2000. The definition is from the U.S. Federal Register (1994).

<sup>52</sup> Finardi, S, C. Tombola, *Le strade delle Armi* [The Arms Trade Routes]. Jaca Book, Milano, 2002, Ch.2

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**Licensed production:** in this case the buyer usually manufactures the whole arms system. The license may or may not include the buyer's rights to independently export the system in question. The potential creation of jobs and the possibility to enter the international defense market are the main advantages of this type of arrangement.

**Sub-contracting:** here the buyer manufactures non-core parts of the arms system. Differences in wage costs make sub-contracting arrangements between developed and developing countries particularly attractive and may enable the subcontractors to acquire technical experience..

**Overseas investments:** are when the selling country commits to invest in the buying country in order to establish joint ventures or subsidiaries and consequently expand the military or security goods production base of the buying country.

**Technology transfer:** this type of agreement usually focuses on technical assistance and often even involves the temporary relocation of R&D to the buying country, in order to develop either the arms system object of the contract or a different one.

Offset agreements can be used to facilitate the imports of armaments because they may allow for different forms of countertrade, for example:

**Barter trade:** armaments exchanged for an equivalent value of a certain commodity (oil, etc.).

**Counter-purchase:** during a certain time period the seller commits to buy or to find a buyer for certain goods of the importing country as a partial payment for the armament.

**Buy-back:** the seller engages to buy back "products derived from the original exported product".

It should be noted that the US Department of Commerce reported that,<sup>53</sup> during the 1990s, 88% of all defense related contracts signed between European countries and US arms manufacturers included offsets clauses, a percentage nearly three times higher than the average with other world regions.<sup>54</sup>

### 1.12. Barter trade

The barter trade is a form of 'countertrade', i.e. goods or services in exchange for goods and services. Barter is a *"one-time transaction only, bound under a single contract that specifies the exchange of selected goods or services for another of equivalent value"*.<sup>55</sup>

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<sup>53</sup> US Department of Commerce, *Offsets in Defense Trade: 1999 Report to Congress*, Washington, Bureau of Export Administration, December 9, 1999

<sup>54</sup> Finardi, S. C. Tombola, *Le strade delle Armi* [The Arms Trade Routes]. Jaca Book, Milano, 2002, Ch. 2.

<sup>55</sup> See: Bureau of Export Administration, *Offsets in Defense Trade: 1999 Report to Congress*. U. S. Department of Commerce, December 9, 1999. See also: Schinasi, K. *Defense Trade. Observations on Issues Concerning Offsets*. Washington, DC, U.S. General Accounting Office, December 15, 2000. The definition is from the U.S. Federal Register (1994).

## Chapter 2 - Trading Systems

The current practice of States is to use three different systems for accounting and reporting their international trade which thus have significant implications for the reporting by States of international movements of conventional arms: (i) the UN-recommended "General Trade System"; (ii) the Special Trade System; and (iii) the "Relaxed" Special Trade System (the latter system refers to countries that adopt the Special Trade System but do include in their statistics certain international transfers that are excluded in the "strict" Special Trade System).

The European Union countries adopt a mix of the two main systems, depending upon national regulations and the direction of trade (trade with non-EU and trade with EU countries are treated differently).<sup>56</sup> Among other peculiar characteristics, each trade system differs according to what constitutes the statistical territory and how goods entering and leaving free trade zones and similar special economic areas are treated, as summarized below.

### 2.1. General Trade System

Countries that use the General Trade System consider as imports and exports all merchandise that leaves or enters their economic territory. An economic territory for these purposes *"can be any geographic area or jurisdiction for which statistics are required. Although in many cases an economic territory is a country, that is not necessarily the case and it includes: airspace, territorial waters, and continental shelf; territorial enclaves in the rest of the world; any free zones, or bonded warehouses or factories operated by offshore enterprises under customs control"*.<sup>57</sup>

It is important to note that in the General Trade System, the economic territory coincides with the statistical territory and therefore the trade statistics of a country that use this system record all merchandise entering or leaving the economic territory, including the special economic zones based in its territory – such as Free Trade Zones, Free Ports, Free Industrial Areas, etc. The only exceptions are "Goods in Transit", "Trans-shipment", and "Temporary Admissions".

### 2.2. Special Trade System

States that use the Special Trade System treat only a part of their economic territory as a statistical territory. Goods entering or leaving their special economic zones are not recorded in their international trade statistics.

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<sup>56</sup> European Commission, Eurostat, *"Statistics on the trading of goods, User guide."* Luxembourg 2006.

<sup>57</sup> See: United Nations, Department of Economic and Social Affairs Statistics Division, *Expert Group on International Merchandise Trade Statistics*, First Meeting, New York, 3-6 December 2007. See also OECD "Glossary of Statistical Terms" and United Nations, *"International Merchandise Trade Statistics, Concepts and Definitions."* United Nations, New York, 1998.

### **2.3. Relaxed Special Trade System**

Other States use the Relaxed Special Trade System and include in their trade statistics "(a) goods for inward and outward processing and (b) goods that enter or leave industrial free zones".<sup>58</sup> In other words, countries that use this system do not record goods entering or leaving special economic zones if those goods did not undergo "inward and outward processing" or did not pass through an industrial free zone.

### **2.4. The European Union System<sup>59</sup>**

As described by the European Commission and the EU's statistical arm Eurostat, "*EU countries use the special trade system (including inward and outward processing)*". More particularly, the EU has adopted various methods to record international trade: extra-EU trade is recorded according to a variation of the Special Trade System (Extrastat), whereas intra-EU trade is recorded according to the EU Intrastat system, based on the collection of data from companies.<sup>60</sup>

Some aspects of the regulations of European countries and of the EU regulations are of particular importance as highlighted below.

a) In EU statistics, "*outward flows from a Member State to a non-member country are called 'exports'; outward flows from one Member state to another are called 'dispatches'. Inward flows from a non-member country are called 'imports'; inward flows from another Member State are called 'arrivals'*"<sup>61</sup> [...] It should be noted, however, that data published by individual Member States of their own trade do not always follow the concepts and definitions applicable for data transmitted to Eurostat".

b) "*Statistics on extra-EU trade are compiled on a special trade basis. Intra-EU trade statistics, however, which are defined specifically in terms of the Intrastat system and do not have a direct link to customs procedures, are not compiled on a general or special trade basis*".<sup>62</sup>

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<sup>58</sup> U.N. Department of Economic and Social Affairs, Statistics Division, "*International Merchandise Trade Statistics: Supplement to the Compilers Manual.*" United Nations, March 7, 2008.

<sup>59</sup> All quotations of this section are from European Commission, Eurostat, "*Statistics on the trading of goods – User guide.*" Luxembourg 2006, Methods.

<sup>60</sup> "*Intrastat is a statistical data collection system on intra-Community trade in goods where data are collected directly from companies. It basically records all physically movement of goods between Member States, including electricity.*" U.N. Department of Economic and Social Affairs, Statistics Division, "*International Merchandise Trade Statistics: Supplement to the Compilers Manual*", United Nations, March 7, 2008. Chapter 6.

<sup>61</sup> It is worth noting that "*when publishing trade flows the same terminology is used as applied for trade with non-EU countries: dispatches are called exports and arrivals are called imports.*" See U.N. Department of Economic and Social Affairs, Statistics Division, "*International Merchandise Trade Statistics: Supplement to the Compilers Manual.*" United Nations, March 7, 2008. Chapter 6.

<sup>62</sup> "*For their national figures of extra-trade, however, Denmark, Greece, Ireland and the United Kingdom publish only according to the general trade system but provide extra-EU trade data to Eurostat on a special trade basis. Germany, Estonia, Cyprus and the Netherlands publish trade figures as well on a general and a special trade basis.*" [...] "*All Member States base their measurement of intra-EU trade on Intrastat system rules. However, the United Kingdom publishes their national figures of intra-EU trade fully on a general trade basis, including goods under custom control. They differ, therefore, from the*

c) Certain transactions use alphanumeric codes: “[...] alphanumeric codes are used in intra- and extra-EU trade statistics to identify confidential [...] data: [...] Codes containing the letter S: Confidential data; Code 88WWW000: Aircraft components, for which a simplified declaration applies As a general definition, data used by the national and Community authorities for the production of Community statistics are considered confidential when they allow statistical units to be identified, either directly or indirectly, so disclosing individual information. [...] Data can be classed as confidential for all types of trade flows (imports, exports, arrivals or dispatches); confidentiality can concern both value and quantity variables, all the partner countries and a particular partner country”.

d) Recording of certain other transactions by EU Member States is discretionary, and in particular “vessels and aircraft; [...] military goods; [...] motor vehicle and aircraft parts”.

e) EU Member States may hide their trade partners: “if a Member State wishes to conceal the destination or the origin of a product, the code of the partner country is replaced by a ‘secret country’ code. This usually distinguishes between intra-EU trade and extra-EU trade”.

f) EU statistics exclude some categories of goods, such as:

- “Emergency aid for disaster areas”;
- “Goods for and after repair<sup>63</sup> and the incorporated replacement parts”;
- “Goods dispatched to national armed forces stationed outside the statistical territory and goods received from another Member State which had been conveyed outside the statistical territory by the national armed forces, as well as goods acquired or disposed of on the statistical territory of a Member State by the armed forces of another Member State which are stationed there.”

## **2.5. Rates of adoption of U.N.-recommended accounting systems**

Another variation in existing State practices is the rate of adoption of trade accounting systems, which has important consequences for how goods in general and conventional arms in particular are monitored and reported. In 1996 and 2006, the UN Statistical Division carried out an inquiry into the “*compliance of States with the recommendations contained in the International Merchandise Trade Statistics: Concepts and Definitions [...] and compilation guidelines outlined in International Merchandise Trade Statistics: Compilers Manual*”<sup>64</sup>. The 2006 inquiry included 173 questions and a total of 132 UN Member States participated, both developed and developing countries.<sup>65</sup>

Only 55% Member States of the developed countries declared to the UN that Customs records are their main source of trade data. For example, the European

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figures they provide to Eurostat.” See European Commission, Eurostat, “*Statistics on the trading of goods – User guide*.” Luxembourg 2006, Methods.

<sup>63</sup> Potentially hidden in this exclusion are refurbishment works on components of arms, in particular barrels of small arms.

<sup>64</sup> “*An overview of National Compilation and Dissemination Practices Updated Chapter 1 of International Merchandise Trade Statistics: Supplement to the Compilers Manual*”, U.N. Comtrade website, May 2009. The original Chapter 1 was published in March 2008.

<sup>65</sup> The distinction is for statistical purpose only.

Union does not require Customs declarations (the Single Administrative Document, SDA) for their intra-EU trade. The European Union only requires Customs documents for the EU extra-trade of its Member States. This method may lead to various shortcomings when reporting the real origin of items traded within the EU and eventually exported to countries outside the EU. From a reporting point of view, the 'country of origin' for a shipment exported from the EU, is the country from where the shipment left the EU territory.

Thus, for example, if an arms manufacturer based in country A inside the EU sells what are described as 'civilian' specification pistols to a company based in country B inside the EU, which in its turn sells those pistols to a company based in country C outside the EU, the statistics of country C and the EU international trade statistics will show country B, not country A, as the origin country for those pistols. The company based in country A could therefore use the company based in country B as a hard-to-detect means to mask the real destination for the arms it sells abroad. An example of such practices is the case of Beretta military weapons sold as "civilian pistols to a British firm, which then obtained a license from the UK authorities to export those same pistols to the Iraq Provisional Authority in July 2004. Statistically, Italy never exported those "civilian" pistols to Iraq.<sup>66</sup>

Another key factor affecting States' trade reporting practices is the growing global tendency towards the establishment of trade blocs and regional Customs Unions where intra-bloc trade no longer requires Customs declarations since this leads to an increasing loss of trade data based on official documents. The UN inquiry revealed that "[...] a high percentage of countries (40.2%) do not follow the recommendation to apply the general trade system of recording which is calling for the inclusion of all goods entering or leaving the economic territory of a country. This is in particular the case for developed countries with 54.8% of them indicating that they disseminate trade data only on the basis of the special trade system"<sup>67</sup>. "Just about half of countries have procedures in place to record movements in and out of commercial or industrial free zones. On the other hand, inclusion in trade statistics of goods admitted into or withdrawn from the customs warehouses is possible in 61.2% of countries [...]". However, "less than 20% of countries are able to include in trade statistics goods entering or leaving their offshore territories, possessions, dependencies etc (including outer space installations) as well as their country's embassies, military bases and other territorial enclaves in other countries"<sup>68</sup>. Therefore, the trade movements of goods through hundred of free trade zones<sup>69</sup> are unaccounted or not completely accounted for by States.

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<sup>66</sup> See: Amnesty International, *Blood at the Crossroads*, 2008, p. 47-49.

<sup>67</sup> "An overview of National Compilation and Dissemination Practices Updated Chapter 1," quoted, May 2009, Section G.

<sup>68</sup> An overview of National Compilation and Dissemination Practices Updated Chapter 1," quoted, May 2009, Section G.

<sup>69</sup> See: Finardi, S., E. Moroni, *State of Exception. Free Trade Zone and Ports in the World Economy*. Milan, F. Angeli, 2001.

## Chapter 3 - Commodity Classification Systems

Classification systems aim to harmonize the way commodities and services are described and coded. They facilitate the collection of duties and tariffs, as well as assist in the preparation by States of statistics on international trade in goods and services by States and international organizations. Thus, the design of commodity classification systems and their shortcomings is highly relevant to the existing and potential reporting by States of trade in conventional arms.

The main international classification systems for goods/commodities are (i) the "Harmonized System" (HS, developed by the World Customs Organization), and (ii) the "Standard International Trade Classification" (SITC, developed by the U.N. Statistical Division).

The United Nations requires that States use the five-digit level for reporting to the U.N. their import and export data. These commodity classification systems assign a one-digit code to each general group of commodities and services. In addition, each general code includes sub-codes at different levels of specification.

Over the years of their development, the HS and the SITC systems have both undergone several changes in design, notably HS1992, HS1996, HS2002; HS2007 for the Harmonized system and SITC Revisions 1, 2, 3, and 4 for the Standard system). Nevertheless, both the WCO (World Customs Organization) and the U.N. provide correlation tables to allow for historical comparisons of data records between the codes of each HS or SITC version or for comparison of data between HS and SITC codes. In 2002, the U.N. Statistical Division also prepared the "Central Product Classification" system to include data on the international trade of both goods and services.

Publicly available trade data in reports arising from these systems is varied according to how many digits in the tariff codes are suppressed. At the national or Customs level such data reporting on the basis of the codes may reach a 10 or 12-digit level of specification, but most of the international data based on the codes is only made available publicly at a five-digit level.

The publicly available level of specifications under HS (6-digit) and SITC (5-digit) systems for "arms and ammunition" are therefore usually still too generic. As explained in more detail below in Chapter 5, the five-digit level of specification does not allow for a detailed description of the traded items and a minority of Member States restrict or fail in their reporting practices over time. Nevertheless, some States – for example the United States - allow for on-line searches of data based on codes up to the 10-digit level, thereby showing the potential for increased public reporting using coding systems.<sup>70</sup>

It is therefore worth examining more closely the manner in which State practice has developed and varies using the international commodity classification codes.

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<sup>70</sup> See: USA Trade Online.

### **3.1. The Harmonized System (HS)**

The Harmonized Commodity Description and Coding System was established by the *"International Convention on the Harmonized Commodity Description and Coding System"* (Brussels 1983), maintained and developed by the WCO. In the words of the Brussels Convention *"the 'Harmonized Commodity Description and Coding System' [...] means the Nomenclature comprising the headings and subheadings and their related numerical codes, the Section, Chapter and Subheading Notes and the General Rules for the interpretation of the Harmonized System, set out in the Annex to this Convention"*.<sup>71</sup>

The WCO describes this harmonized system (HS) as *"a multipurpose international product nomenclature [...] that] comprises about 5,000 commodity groups; each identified by a six digit code, arranged in a legal and logical structure and is supported by well-defined rules to achieve uniform classification. The system is used by more than 200 countries and economies as a basis for their Customs tariffs and for the collection of international trade statistics. Over 98% of the merchandise in international trade is classified in terms of the HS"*.<sup>72</sup>

The official interpretation of the HS classification system is defined in official *"Explanatory Notes"*, which were last published by the WCO in 2006 in a five-volume edition. The last version of the HS (HS2007) system entered into force in January 2007.

### **3.2. Standard International Trade Classification (SITC)**

This commodity classification system has also been developed over many years of State reporting practice and review. According to the U.N. Statistical Division, *"the original SITC was issued in 1950 and came as a result of discussions begun during the League of Nations era concerning methods for promoting greater comparability of foreign trade statistics. The Revised SITC (1961) was issued to show links between SITC and the Brussels Tariff Nomenclature, a customs tariff nomenclature then in use in Europe and elsewhere. In the next decade, further changes in patterns of trade, as well as technological advances, led to the development of SITC, Revision 2. In 1986, SITC, Revision 2, was replaced by SITC, Revision 3. SITC, Revision 3, consists of 3,118 basic headings and subheadings broken down into 261 groups, 67 divisions and 10 sections. It is defined in terms of the 1988 Harmonized System"*.<sup>73</sup>

Under SITC Revision 4 - accepted by the U.N. Statistical Commission in March 2006 - the codes for "Arms and Ammunition" remained unchanged except for the five-digit code 891.21 (Cartridges for riveting or similar tools and parts thereof), incorporated in code 891.24 (Cartridges and parts thereof, n.e.s.).

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<sup>71</sup> World Customs Organization, *"International Convention on the Harmonized Commodity Description and Coding System"*. Brussels 1983, 1986 (entered in force in 1988). WCO website.

<sup>72</sup> World Customs Organization website.

<sup>73</sup> U.N. Department of Economic and Social Affairs, Statistics Division, *"International Merchandise Trade Statistics, Compilers Manual"*, United Nations, 2004.

### **3.3. Central Product Classification (CPC)**

The first version of the CPC (then called “Provisional” system) was introduced by the U.N. Department of Economic and Social Affairs Statistics Division in 1990.

Version 1.0 was introduced in 1998 and the present version 1.1 in 2002. This system of classification is described by the U.N. Statistical Division as *“a complete product classification covering goods and services. It is intended to serve as an international standard for assembling and tabulating all kinds of data requiring product detail, including industrial production, national accounts, service industries, domestic and foreign commodity trade, international trade in services, balance of payments, consumption and price statistics. Other basic aims are to provide a framework for international comparison and promote harmonization of various types of statistics dealing with goods and services”*.<sup>74</sup>

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<sup>74</sup> United Nations Statistical Commission, “Central Product Classification, CPC Version 1.1.” United Nations Statistical Commission, March 2002.

## Chapter 4 - Partner country attribution and FTZ

Especially important for consistent transparency and democratic accountability in the reporting of international transfers of goods and services (and for the application of tariffs and quota) is the question of how to apply partner country attribution to trade data. This is obviously vitally important for the monitoring activities that would enable the implementation of the ATT to be effective with regard to trade and other transfers of conventional arms.

In State practices there are generally three methods for attributing the partner country to an international transfer:<sup>75</sup>

- a) Country of origin/consumption;
- b) Country of consignment/destination;
- c) Country of purchase/sale.

The U.N. recommends that countries should record imports and exports according to the first method, supplemented by the second method. The U.N. and the IMF<sup>76</sup> do not usually recommend that States use the third method. However, each of these methods present problems of data consistency and traceability.

### 4.1. Country of origin/consumption

This method for attributing the partner country to an international transfer uses the following definitions. For **imports**: *"the country of origin of a shipment is determined by rules established by each country that are generally based on two criteria: a) the criterion of goods 'wholly produced' (obtained) in a given country, where only one country enters into consideration in attributing origin; b) the criterion of 'substantial transformation', where two or more countries have taken part in the production of the goods".*<sup>77</sup>

For **exports**: *"the country of consumption of a good is parallel to the concept of country of origin for imports. The country of consumption is the country in which the goods are expected to be used for private or public consumption or as inputs in a production process".*<sup>78</sup>

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<sup>75</sup> Other criteria, such as the "country of shipment" for which the trading partner is derived by the last shipping document, are not considered here because these methods introduce even more ample distortions in the accounting processes. See paragraph 145 in U.N. Department of Economic and Social Affairs, Statistics Division, *"International Merchandise Trade Statistics, Compilers Manual."* United Nations, 2004.

<sup>76</sup> U.N. Department of Economic and Social Affairs, Statistics Division, *"International Merchandise Trade Statistics, Compilers Manual."* United Nations, 2004; See also Markie Muryawan, "Partner Country Attribution." Economic and Social Commission for Western Asia (ESCWA), Workshop on the compilation of IMTS and the application of methodological concepts, 28 October – 2 November 2007, Amman, Jordan.

<sup>77</sup> Mark Van Wersch, IMF Committee on Balance of Payments Statistics, Geographic Classification of Goods Imports and Exports from a National and Economic/Currency Union Perspective." "Draft Issues Paper (Cuteg) # 17, November 2004.

<sup>78</sup> U.N. Department of Economic and Social Affairs, Statistics Division, *"International Merchandise Trade Statistics, Compilers Manual."* United Nations, 2004.

International rules under the Kyoto Convention require that country of origin certificates shall accompany the traded goods. Nearly all of the States that participated in the above-mentioned UN inquiry (see Chapter 2) declared that they use the 'country of origin' method for their imported goods (90.2% in total and 96.8% for Developed Countries).

Recording 'country of origin' for imports has the *"advantage of showing the direct relationship between the producing country (the country in which goods originate) and the importing country. This information is regarded as indispensable for matters of trade policy and negotiations, for administering import quotas, etc. [...] However, there are limitations to the use of data compiled on a country-of-origin basis"*.<sup>79</sup> In effect, *"...such an approach does not permit a symmetrical recording of the same trade transactions by the exporting country (A) and the importing country (C) if the goods were directed through country B. Both countries B and C would in that case record an import from country of origin A"*.<sup>80</sup>

For example, in 1989, an arms trading company A, based in the United States, imported 10,000 automatic rifles from a manufacturer B based in Bulgaria. Trade statistics of both countries for 1989 recorded the related import/export movements and, according to the country of origin criterion, Bulgaria was named as the partner country for this US import. Company A stored the automatic rifles in its facilities, waiting for an opportunity to re-sell the rifles to one of its customers. Five years later an opportunity showed up and the rifles were re-exported to Honduras without any manufacturing changes and in a shipment accompanied by their certificate of origin. However, which country, Bulgaria or United States, was recorded as the country of origin by Honduras?

The responsibility of national authorities to strictly regulate movements of arms and to avoid the authorization of transfers of such items where there is a substantial risk of misuse would be enshrined in the ATT if it is to be effective. For example, if the authorities could foresee that those automatic rifles would be used in Honduras to commit severe human rights violations, the country of origin method may lead the international community to attribute Bulgaria, and not the United States, with the licensing responsibility of having shipped the rifles.

The U.N. Manual describes this problem of attribution in the method of reporting as follows: *"Attribution of imports to the country of origin [...] can explain many significant differences between the statistics of trading partners in cases when goods move from the country of origin to the country of destination via third countries. Suppose goods were produced in country A, sold and shipped to country B and afterwards resold and dispatched to country C. In such a case, the trade statistics of country B will show exports to country C, but statistics of country C will not attribute its imports to country B; they will indicate that goods were imported from country A"*.<sup>81</sup>

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<sup>79</sup> Mark Van Wersch, IMF Committee on Balance of Payments Statistics, Geographic Classification of Goods Imports and Exports from a National and Economic/Currency Union Perspective." "Draft Issues Paper (Cuteg) # 17, November 2004.

<sup>80</sup> Mark Van Wersch, IMF Committee on Balance of Payments Statistics, quoted, 2004

<sup>81</sup> U.N. Department of Economic and Social Affairs, Statistics Division, "International Merchandise Trade Statistics, Compilers Manual." United Nations, 2004.

## **4.2. Country of consignment/destination**

The second method for attributing the partner country to an international transfer uses these different definitions. For **imports**: *"the country of consignment is the country from which goods were dispatched to the importing country, without any commercial transactions or other operations which change the legal status of the goods taking place in any intermediate country"*.

For **exports**: *"the country of consignment - also referred to as country of destination or country of last destination - is the country to which goods are dispatched by the exporting country, without - as far as it is known at the time of exportation - being subject to any commercial transactions or other operations which change the legal status of the goods"*.<sup>82</sup>

This second method is viewed as having some advantages. *"In general, the method of compiling data by the country of consignment/destination offers the possibility of obtaining consistent statistics and reasonable comparability since it promotes the recording of the same transactions by importing and exporting countries."*<sup>83</sup> This method also offers a possibility of avoiding the problems of attribution associated with the first method described in section 4.1 above. However, there are still inconsistencies in State practice, with only some countries that record their imports according to this method but nearly all that record their exports according to the same method. According to the UN inquiry, not more than 47% of the countries surveyed (and 77.4% for developed countries) declared that they use this 'country of consignment' method for recording their imports. In contrast, a large majority of 90.6%, (and 93.5% for developed countries) recorded exports according to this second method of attributing the 'country of last destination'.

From the point of view of ATT-related monitoring activities, the country of consignment/destination method of recording could at first sight offer the potential of more consistent and transparent reporting of conventional arms trade and transfers. However it should be noted that this method of attribution may also generate data that leads to wrong conclusions: *"[t]he entire value of a transaction [...]"* can be attributed *"to a country that may only be the location of a distribution warehouse or middleman"*,<sup>84</sup> such as, for example, countries that are sometimes notoriously used as *"plaques tournantes"* for shipments of arms to high risk destinations or illegitimate recipients.

## **4.3. Country of purchase/sale**

The third method for attributing the partner country to an international transfer is yet again based on different definitions. Here *"the country of purchase is the country where the purchaser's co-contractor (seller of the goods) resides. The country of sale is the country where the seller's co-contractor (purchaser of the goods) resides."* *"If both countries collect data on a purchase/sale basis, the country of purchase will*

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<sup>82</sup> U.N. Department of Economic and Social Affairs, Statistics Division, *"International Merchandise Trade Statistics, Compilers Manual."* United Nations, 2004.

<sup>83</sup> *"International Merchandise Trade Statistics, Compilers Manual."* 2004, 1998, quoted.

<sup>84</sup> *International Merchandise Trade Statistics, Compilers Manual."* 2004, 1998, quoted

*record goods as exports to the country of sale, and the country of sale will record the same goods as imports from the country of purchase”.*<sup>85</sup>

However, according to the UN inquiry, only 29.5% of the countries surveyed (and 9.7% of developed countries) used the 'country of purchase' method as the main or additional method for partner country attribution in their statistics on imports; and only 22% of the countries (0% of developed countries) used this 'country of sale' method for partner country attribution in their statistics on exports.

The main weakness of this method is the attribution of a partner country to the records when in fact the buyer or the seller is not actually located in the country of origin or destination. *“The compilation of statistics on a purchase/sale basis also presents a country with the problem of how to obtain the required information when the goods are sent to a recipient in a country other than the country where the buyer is located and when the goods are received from a country other than the country where the seller is located”.*<sup>86</sup>

This method, however, may provide useful information on countries that serve as bases for arms brokering activities for transactions between two third countries which would be otherwise invisible. In fact, the other two methods mentioned above do not allow for the identification of the country in which a transaction has been brokered (the 'country of sale'). In the first 'country of origin' method described above, the pair is the country of manufacturing/country of destination. In the second 'country of consignment'<sup>87</sup> method described above, the pair is the 'country of consignment'/'country of destination'.

#### **4.4. Problems of consistency**

It is worth noting that many other problems may also affect the consistency of international trade statistics and therefore the future effectiveness and objectivity of ATT-related reporting and monitoring activities. Among those problems are the following:

a) **Coverage:** *“Specific goods or types of transactions may be defined differently, and may be included in trade statistics by one partner but excluded by the other (e.g., leased goods, military goods, goods imported or exported for or after repair)”.*<sup>88</sup>

b) **Time of recording:** for example, *“in one country the trade flow may be attributed to the time period in which the invoice is received in the importing country, while another country may attribute the transaction to the time period in which the amounts owed to the customs administration are paid. As a result, a given import may be recorded as having occurred in a different month/year from the corresponding export”.*<sup>89</sup>

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<sup>85</sup> *International Merchandise Trade Statistics, Compilers Manual.*” 2004, 1998, quoted

<sup>86</sup> *International Merchandise Trade Statistics, Compilers Manual.*” 2004, 1998, quoted

<sup>87</sup> Remind that “country of consignment” means the country where the goods are “consigned” for export, not the country where the goods are received.

<sup>88</sup> *International Merchandise Trade Statistics, Compilers Manual.*” 2004, 1998, quoted

<sup>89</sup> *International Merchandise Trade Statistics, Compilers Manual.*” 2004, 1998, quoted

c) **Difference in commodity classifications:** despite the fact that *"all major trading countries have adopted the Harmonized System for commodity classification"*<sup>90</sup> [...] *there are differences in interpreting and applying HS, both within the same country and among different countries.*"<sup>91</sup> The differences may also stem from the fact that the Customs of the exporting country have accepted a classification of the goods according to a particular code (for example, "parts for civilian firearms"), whereas the Customs of the importing country may have ascertained that the goods were of a different nature (for example, "parts for military firearms"). Therefore, the exporting country may have recorded the goods as exports of parts for civilian firearms and the importing country recorded the goods as imports of "parts for military firearms." Consequently, the statistics of the two countries in such cases may have no match for the transaction in question.

d) **Exclusion of certain trade activities:** The answers given by countries to the above-mentioned UN inquiry also reveal that only 61.4% of the countries recorded *"goods traded in accordance with barter"*<sup>92</sup> *agreements,"* and only 59.8% of the countries (but 90.3% for developed countries) recorded *"goods for military use"* in their trade statistics. Finally, only 33.3% of the countries (29% for developed countries) recorded *"goods seized by Customs and subsequently resold"* and only 50% of the countries (54.8% for developed countries) recorded *"goods entering or leaving the economic territory illegally"*.

It should be noted that in the IMF's Balance of Payments and International Investment Position Manual - one of the main reference for States in the compilation of their international statistics - the IMF recommends that illegal transactions should be accounted for in international statistics: *"Illegal transactions are treated the same way as legal actions. Illegal transactions are those that are forbidden by law [...] Macroeconomic statistics, including international accounts, cover all economic phenomena irrespective of whether they are illegal or legal [...] exclusion of illegal transactions could lead to an imbalance in the international accounts."*<sup>93</sup> However, the European Union statistics manual states that EU statistics *"do not generally include illegal trade, for obvious practical reasons, although figures for Germany include illegal trade that has been discovered"*.<sup>94</sup>

## 4.5. Free Trade Zones

Free trade zones, free ports and similar entities are used for international arms transfers and are potential targets for export/import operations aimed at hiding the real origin or destination of arms and ammunition shipments. Therefore the trade and movements of such items through these expanding areas is highly relevant for States to record and report consistently upon.

There are many types of free trade zone. According to the Kyoto Convention, "free zones" are *"part of the territory of a Contracting Party where any goods introduced*

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<sup>90</sup> See the Definitions section.

<sup>91</sup> *International Merchandise Trade Statistics, Compilers Manual.* 2004, 1998, quoted

<sup>92</sup> See the Definitions section for the meaning of "barter trade."

<sup>93</sup> See: IMF, *Balance of Payments and International Investment Position Manual (BPM6)* Sixth Edition, December 2008, Pre-publication draft. <http://www.imf.org/external/pubs/ft/bop/2007/pdf/BPM6.pdf>

<sup>94</sup> See European Commission, Eurostat, *"Statistics on the trading of goods - User guide."* Luxembourg 2006, Methods.

*are generally regarded, insofar as import duties and taxes are concerned, as being outside the Customs territory”.*<sup>95</sup>

**Table 1 – Main types of Free Zones**

| Type  | Description                 | Type | Description                    |
|-------|-----------------------------|------|--------------------------------|
| CZ    | Customs Zone                | FTZ  | Free Trade Zone                |
| CFZ   | Customs Free Zone           | IEPZ | Industrial EPZ                 |
| DFEPZ | Duty Free EPZ               | IFZ  | Industrial Free Zone           |
| EFZ   | Export Free Zone            | IPZ  | Investment Promotion Zone      |
| EPFZ  | Export Processing Free Zone | JEZ  | Joint Enterprise Zone          |
| EPZ   | Export Processing Zone      | MQ   | Maquiladora                    |
| FTZ   | Foreign Trade Zone          | PEZ  | Privileged Export Zone         |
| FECZ  | Free Economic Zone          | SEZ  | Special Economic Zone          |
| FEPZ  | Free EPZ                    | TFTZ | Tax Free Trade Zone            |
| FEZ   | Free Export Zone            | TFZ  | Tax Free Zone                  |
| FPZ   | Free Production Zone        | ZJE  | Zone of Joint Entrepreneurship |

Source: The World Bank, *Special Economic Zones Performance, Lessons Learned, and Implications for Zone Development*. Washington, DC, 2008; U.N. Centre on Transnational Corporations. *The Challenge of Free Economic Zones*. New York, United Nations, 1991

Free zones are Customs-cordoned spaces (near or inside a port, an airport, a logistics distribution center, an industrial area, etc.) where traders and manufacturers ship, store or transform their goods without paying customs duties. Goods may enter and exit the FTZ freely, with the purpose of being eventually either imported in the Customs territory of the hosting country (after paying the appropriated duties) or shipped to another country. In free ports and airports, ships and aircraft enter and leave without mandatory customs inspections.

Presently, there are more than 2,700 active special economic zones<sup>96</sup> located in the developed countries (272 in the United States, 87 in France, 62 in the United Kingdom, for example), in transitional countries (160 in Hungary, 92 in Czech Republic, for example) and developing countries.<sup>97</sup>

A sizeable number of these zones are Export Processing Zones, Free Industrial Zones, and Free Trade Zones that are dedicated to the manufacturing, assembling or trading of particular categories of products (electronics, textiles, garments, vehicles, etc.) and the potential threat of their use for passage or processing of arms is viewed as relatively low by the authorities. In contrast, those free trade zones, free ports and free airports or free trade zones inside ports (trans-shipment ports) and airports (air cargo trade and trans-shipment), are instead viewed as potential targets for international arms transfers of dubious legitimacy.

Regulations of free zones vary from country to country, and are usually complex. Such regulations require careful analysis in order to evaluate the threats they may pose for transparency and accountability in international transfers of conventional arms.

<sup>95</sup> "Revised Kyoto Convention" (1999, 2006), quoted.

<sup>96</sup> The World Bank, *Special Economic Zones Performance, Lessons Learned, and Implications for Zone Development*. Washington, DC, 2008.

<sup>97</sup> For the history and development of the special economic zones see: Finardi, S., E. Moroni, *State of Exception. Free Trade Zone and Ports in the World Economy*. Milan, F. Angeli, 2001

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Several free zones, and in particular free ports and airports, function as redistribution centers and their potential use for disguising origin and destination of goods is inversely proportional to the capacity or willingness of the hosting country to perform routine inspections of the activities carried out in these zones.

The director of the Port of Entry, the director of the zone (in particular Free Trade Zones, FTZ), and the relevant Customs authority, have the power to refuse admission of foreign goods into the zone and to inspect whatever shipment they may consider of interest for law enforcement or monitoring activities. In many cases, the goods entering the FTZ must be declared on Customs forms, with their value and all applicable Customs tariff codes. The goods entering the FTZ are also usually inventoried and stored into assigned spaces to facilitate the work Customs must perform in case the goods will later enter the fiscal territory. Any transformation (except repackaging) of the foreign goods entering a FTZ must in theory receive approval by the director of the Port of Entry or by Customs and FTZ authorities. However, in many cases corruption, inefficiencies, or simply the volume of traffic, present a different and potentially dangerous reality.

## Part II - Reporting arms transfers under the ATT

### Chapter 5 - Accountability, transparency and verification

#### 5.1. *Proposals in the Chairman's Draft Paper July 2011*

The ATT PrepCom *Chairman's Draft Paper* (14 July 2011) includes certain proposals for "*record keeping, reporting and transparency*" under an ATT. These provisions appear to build on practices already adopted by most of the main arms exporting countries and by the WCO.<sup>98</sup>,

Under the section in the Draft Paper entitled "Record keeping, reporting and transparency" proposals are made regarding the measures States Parties should adopt and which obligations they must respect under the ATT:

1. maintaining records of "*all arms authorizations, transfers and denials*" with details such as "quantity, model/type, arms transfers authorized and refused, arms actually transferred, details of transit State(s), recipient State(s) and end users".
2. maintaining records "*of all arms imports and shipments of arms that transit their territory*" with same details as above,
3. submitting an annual report to the "*Implementation Support Unit of all activities undertaken in order to accomplish the implementation of this Treaty, including inter alia, domestic laws, regulations and administrative measures*",
4. submitting an annual report "*to the Implementation Support Unit ...for the preceding year concerning the transfer of arms*" as detailed in points 1 and 2 above.

#### 5.2. *Lack of enforcement and transparency mechanisms proposed*

*Chairman's Draft Paper* states that: "*Each State party shall adopt legislation or other appropriate measures to ensure its ability to enforce domestically the obligations of this treaty and to prohibit the transfer of arms from any location under that State's jurisdiction and control unless authorized in accordance with this Treaty, including*

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<sup>98</sup> 177 member countries in 2010. The WCO maintains information and intelligence-sharing instruments and risk-management, such as the Global Network of Regional Intelligence Liaison Offices (RILO) and Customs Enforcement Network (CEN), and the initiative for Global Supply Chain Security. The Global Supply Chain Security initiative (June 2003) includes: "a) an international convention on Mutual Administrative Assistance in Customs Matters (Johannesburg Convention); b) the WCO Data Model and a list of essential data elements required for the identification of high risk consignments; c) international Customs guidelines on advance cargo information; d) guidelines for the development of national laws for the collection and transmission of Customs information; e) high level guidelines for co-operative arrangements between WCO Members and the private sector to increase supply chain security; f) enhancements of the WCO's information and intelligence strategy including the operation of its global Regional Intelligence Liaison Offices network; g) a new internet-based Databank on advanced technology to enable WCO Members to identify products and services for the detection of illegal consignments and contraband." [http://www.wcoomd.org/home\\_wco\\_topics\\_epglobalsupplychainfacilitationandsecurity.htm](http://www.wcoomd.org/home_wco_topics_epglobalsupplychainfacilitationandsecurity.htm) . The Initiative could be easily adapted to include a focus on international arms transfers.

*appropriate law enforcement and judicial mechanisms.*" The draft paper does not include a proposal for an international mechanism charged with verification of States' enforcement obligations and compliance under the Treaty. States will do this themselves by submitted annual reports.

In the Draft Paper no procedure is proposed to analyze or publish such annual reports.. Other than "*serve as the repository for annual reports submitted by States Parties as part of their Treaty obligations*", the Implementation Support Unit is not envisaged as the entity that may publish the States' reports, nor any other entities seems to have a mandate for making the States' report public.

If the "record keeping, reporting and transparency" provisions included in the *Chairman's Draft Paper* will be adopted in the ATT without modification, the ATT will not serve as an instrument for obtaining publicly verifiable data on international transfers of conventional arms, and therefore ensuring democratic accountability.

If national parliaments and civil society have no possibility to know and verify what States have declared to the Implementation Unit and to compare States' declarations of arms consignments and destinations, the "reporting requirements" of the ATT will not address the generally low level of national reporting and accountability of States as it is now (see below on national reporting of arms exports and imports). This would likely undermine the implementation of the ATT provisions in national law and practice.

### **5.3. Absence of specification in reporting proposals**

The *Chairman's Draft Paper* does not make proposals on another issue that is of fundamental importance for transparency and accountability: the level of specification in reporting international transfers of conventional arms. As reported in the Introduction of this report, the *Chairman's Draft Paper* lists, in the Scope section, most of the main types of conventional weapons, munitions, and related equipment as well as parts, technologies and some services. However, the draft paper does not indicate at which level of specification each category should be reported by States.

Choosing a common standard on the level of specification for recording and reporting the publicly available data on international arms transfers would be an important step on the road of transparency and democratic accountability. As mentioned in Chapter 3, the level of specification for publicly available international statistics is presently five or six-digit, while national Customs data are sometimes available at the 10-digit level. Very broad categories, modeled on the list of the Wassenaar Arrangements or national classifications, would serve neither the purpose of transparency nor democratic accountability in most instances.

It is clear that for the ATT to function consistently and effectively to curb irresponsible arms transfers and prevent illicit trafficking, a bespoke system of recording and reporting must be developed. For example, a ten-digit level of specification is necessary if States are to share objective information on transfers and other activities, and if under the Treaty the publication of such information is to become the norm so as to introduce the real transparency so often called for by the General Assembly.

State secrecy and commercial confidentiality regarding the international transfer of conventional arms all too often becomes excessive and senseless, and can endanger public safety and the rule of law based on respect for universal human rights. The “privatization” of information collected with taxpayers’ money and denial of citizens and elected assemblies the right to scrutinize information about the arms trade allows irresponsible decision making to go undetected and unquestioned..

With few exceptions, the present inconsistent systems of statistical recording and lack of transparent reporting on international transfers of conventional arms would, if they remain unreformed, severely undermine the efficacy of the ATT.

#### **5.4. National reports**

There are approximately 40 countries that have a substantial defense production and around other 60 countries that manufacture arms and ammunition on a smaller scale. Only 36 countries make their reports on international transfers of conventional arms publicly available.<sup>99</sup> Out of those 36 countries, 21 are European Union countries, while 6 EU countries (Cyprus, Greece, Latvia, Lithuania, Luxembourg, and Malta) do not publish national reports, but communicate their data to the EU annual report.<sup>100</sup> In addition to the 21 EU countries, national reports are published by 14 other countries - Albania, Australia, Belarus, Bosnia-Herzegovina, Canada, Croatia, Macedonia, Montenegro, Norway, Serbia, South Africa, Switzerland, Ukraine, and United States.<sup>101</sup> Major arms producers, such as Russian Federation and China, as well as many medium to small producers of arms such as Argentina, Belarus, Bangladesh, Brazil, Chile, Colombia, Egypt, India, Indonesia, Iran, Israel, Kazakhstan, Mexico, Moldova, Myanmar, Pakistan, Peru, South Korea, Thailand, Turkey, Singapore, Uganda, Venezuela, and Zimbabwe do not publish accounts of their international transfers of conventional arms.

Several reports are produced in the country’s national language only. The level of specification of delivered or imported conventional arms is, for almost all countries, based on the broad categories established by the Wassenaar Arrangement “Munitions List” and other lists modeled on that list. Most of these reports therefore do not allow scrutiny of international arms transfers where a greater level of specification is needed. For example, if a State records a shipment or set of shipments of tear gas that has been severely misused abroad just as Military List Category 7 (Chemical or biological toxic agents, “riot control agents”, radioactive materials, related equipment, components and materials) and no further specification is provided, no democratic assembly or civil society could check and raise a warning..

##### **5.4.1 National reports at a glance**

Table 2 summarizes the main types of information included in 37 country’s last national report available. Some national reports by European States actually include less information than the ones available in the EU annual report. Some States that

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<sup>99</sup> See SIPRI National Reports Archive, <http://www.sipri.org/>

<sup>100</sup> European Union, Twelfth Annual Report According to Operative Provision 8 of the European Union Code of Conduct on Arms Exports, 2011 (on 2009).

<sup>101</sup> See SIPRI National Reports Archive, <http://www.sipri.org/>

## Transparency and Accountability - Common Standards for the ATT

published statistics for the years 2009 or 2010 had not published reports for years and some other States published their reports for the first time in 2009 or 2010, indicating some political willingness to improve transparency in the arms trade.

**Tab. 2 – Status of information provided in national reports to January 2012**

Legenda: LEV-LIV = Licensed for Export/Import value; AE-AI = Actual Export/Import value; OD = Origin/Destination; ML = According to a Military List; FD = Further Details on items; DU = Dual-use goods included and specified

| Country             | On year | LEV | LIV | AE                 | AI  | OD  | ML  | FD  | DU  |
|---------------------|---------|-----|-----|--------------------|-----|-----|-----|-----|-----|
| 1. Albania          | 2010    | no  | no  | yes                | yes | yes | yes | yes | yes |
| 2. Australia        | 2004    | no  | no  | yes                | no  | yes | no  | no  | yes |
| 3. Austria          | 2009    | yes | no  | yes                | no  | yes | yes | no  | no  |
| 4. Belarus          | 2008    | no  | no  | no                 | no  | no  | no  | no  | no  |
| 5. Belgium          | 2011 1Q | yes | yes | no                 | no  | yes | yes | yes | yes |
| 6. Belgium Regional | 2010    | yes | yes | no                 | no  | yes | yes | yes | yes |
| 7. Bosnia-H.        | 2009    | yes | yes | no                 | no  | yes | yes | yes | yes |
| 8. Bulgaria         | 2010    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 9. Canada           | 2009    | no  | no  | yes                | no  | yes | yes | no  | yes |
| 10. Croatia         | 2010    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 11. Czech R.        | 2010    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 12. Denmark         | 2010    | yes | yes | no                 | no  | yes | yes | no  | yes |
| 13. Estonia         | 2010    | no  | no  | yes                | yes | yes | yes | no  | yes |
| 14. Finland         | 2010    | yes | no  | yes                | no  | yes | yes | yes | yes |
| 15. France          | 2010    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 16. Germany         | 2010    | yes | no  | yes                | no  | yes | yes | no  | yes |
| 17. Hungary         | 2010    | yes | yes | yes                | yes | yes | yes | no  | yes |
| 18. Ireland         | 2010    | yes | no  | no                 | no  | yes | yes | no  | yes |
| 19. Italy           | 2010    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 20. Macedonia       | 2006    | yes | no  | yes                | no  | yes | yes | no  | yes |
| 21. Montenegro      | 2009    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 22. Netherlands     | 2010    | yes | no  | yes                | no  | yes | yes | no  | yes |
| 23. Norway          | 2010    | no  | no  | yes                | no  | yes | yes | yes | yes |
| 24. Poland          | 2010    | yes | no  | no                 | no  | yes | yes | yes | no  |
| 25. Portugal        | 2008    | yes | yes | yes                | yes | yes | yes | no  | no  |
| 26. Romania         | 2010    | yes | no  | yes                | no  | yes | yes | no  | no  |
| 27. Serbia          | 2009    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 28. Slovakia        | 2010    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 29. Slovenia        | 2010    | yes | yes | yes                | no  | yes | yes | no  | no  |
| 30. South Africa    | 2010    | no  | no  | yes                | yes | yes | no  | no  | no  |
| 31. Spain           | 2010    | yes | yes | yes                | yes | yes | yes | yes | yes |
| 32. Sweden          | 2010    | yes | no  | yes                | no  | yes | yes | yes | no  |
| 33. Switzerland     | 2010    | no  | no  | yes                | no  | yes | yes | no  | no  |
| 34. UK              | 2010    | yes | no  | yes                | no  | no  | no  | no  | no  |
| 35. Ukraine         | 2010    | no  | no  | yes <sup>102</sup> | no  | yes | yes | no  | no  |
| 36. USA DCS         | 2010    | yes | no  | yes                | no  | yes | no  | no  | no  |
| 37. USA FMS         | 2010    | yes | no  | yes                | no  | yes | yes | no  | no  |
| Yes                 |         | 28  | 16  | 30                 | 14  | 35  | 32  | 17  | 24  |
| No                  |         | 09  | 21  | 07                 | 23  | 02  | 05  | 20  | 13  |

Source: Listed countries national reports, available at SIPRI, National Reports Database.

<sup>102</sup> The Ukraine annual report (since 2004) includes only exports, broken down by categories, including small arms and light weapons. There no values but only quantities. Total number of licenses granted for weapons and dual-use items are provided only in the 2004 and 2005 reports.

Some reports from major arms exporting countries are practically useless,<sup>103</sup> due to the way their tables and information are built and presented to suppress meaningful data, while some other national reports are now made less transparent than in the past.<sup>104</sup>

#### **5.4.2 The case of Italy's annual report**

Noteworthy among the national reporting systems is Italy's based on Law 185/90. This law mandates the government to make public the reports prepared by a) the presidency of the Council of Ministers; b) the Ministry of Foreign Affairs; c) the Ministry of Interior; d) the Ministry of Defense; e) the Ministry of Finance; f) the Ministry of Economic Development. Each ministry reports in detail each operation it has authorized or controlled or otherwise is required to monitor. This data is used to produce a report divided in three volumes (Vol. I, 840 pages; Vol. II, 1021 pages, Vol. III, 1,191 pages, for a total of 3,052 pages in the last edition).<sup>105</sup>

Particularly important are the reports by the Ministry of Foreign Affairs (for authorizations), the Ministry of Interior (Customs data for actual exports), and the Ministry of Finance (financial institutions that provide the letter of credit for transfers; companies involved in each authorization and detail of the military equipment being authorized; value of brokering activities related to each transfer). The national report covers imports and exports, re-imports and re-exports, temporary imports and exports, governmental programmes, and transfers by the Ministry of Defence under various titles. However, the national report does not include commercial transfers of what are deemed as "civilian" firearms and ammunition, whose data are nevertheless reported by the Office of National Statistics (ISTAT) using various HS tariff codes.

Over the years since its establishment, Law 185/90 has been politically attacked several times by the Italian arms manufacturers' lobby, leading to modifications that have made the last reports less transparent than earlier reports. For example, it is no longer possible to link a financial institution to a precise transfer.<sup>106</sup> In addition,

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<sup>103</sup> The United Kingdom national reports ("Strategic Export Control" and "UK Defence Statistics") are likely the worst in terms of information provided, clarity and transparency and are practically useless. The "Strategic Export Control Quarterly Reports" include detailed information for licenses granted and country of destination, but not on actual exports. The Strategic Export control site provides a database that repeats the information included in the quarterly reports. The United Kingdom does not provide data on actual exports to the EU annual report. See: Defense Analytical Service Agency, Ministry of Defence, *UK Defence Statistics* (<http://www.dasa.mod.uk/>); Department of Trade and Industry, *Strategic Export Controls Report*. (<http://www.fco.gov.uk>); SBAC (Society of British Aerospace Companies), *UK Aerospace Industry Survey, annual*.

<sup>104</sup> Since 2010, the United States report on Direct Commercial Sales (State Department) no more lists for each country the type of items licensed, but just a reference to a broad category of the US military list. In addition, the 2010 report is in the non-searchable pdf format and a text recognition operation is necessary for being able to search the document, differently from the past editions. The total at the end of the tables is no more provided and it is necessary to add each country total to obtain the final value. The reports by the US DoD for Foreign Military Sales includes information on value per destination but not on the type of military equipment transferred. See U.S. Dept. of State (Sec. 655 of the Foreign Assistance Act), *Direct Commercial Sales Authorizations for Fiscal Year*; US Dept. of Defense, Defense Security Cooperation Agency (DSCA), Historical Facts Books, Deputy for Financial Comptroller ([www.dsca.osd.mil](http://www.dsca.osd.mil)).

<sup>105</sup> See: Presidenza del Consiglio dei Ministri, *"Relazione sulle operazioni autorizzate e svolte per il controllo dell'esportazione, importazione e transito dei materiali di armamento nonché dell'esportazione e del transito dei prodotti ad alta tecnologia"*, Rome, March 31, 2011, vol. I, II, and III.

<sup>106</sup> Finardi, S., C. Tombola, *Le strade delle armi* [Arms Trade Routes], F. Angeli, Milano, 2002, Appendix "A case study: the revision of Law 185/90". For more analyses and articles on recent revisions and attempted

all volumes are purposely presented in a non-searchable pdf document, obliging researchers to perform text-recognition operations on 3,000 pages. Despite these shortcomings, Italy's report on international transfers of (military) conventional arms is probably the most complete and transparent among the reports of the main arms exporting countries and could help serve as one model for a new bespoke system of record keeping and reporting developed to serve the purposes of the ATT.

### **5.5. Commercial arms sales and Free Trade Zones**

Commercial transfers of conventional arms (imports and exports) are sales of military equipment including weapons of war and many internal security weapons and munitions as well as "civilian" firearms between manufacturing or trading companies of a country (including State-owned companies and arms dealers and brokers) and foreign entities (foreign armed force and police, companies, arms dealers, individuals, etc.).

Most of these transfers first require a government license, specific to a particular transfer or for multi-year transfers. Government agencies grant the licenses to whom they deem are suitable entities and for legitimate trade, both for exporting and importing. In contrast to certain government-to-government sales and gifts regulated by different specific instruments, commercial sales fall within the domain and regulations of international trade. They pass through Customs verification and are accounted in national and international trade statistics. States that use the Special Trade System (as described above in Chapter 2) do not report their arms transfers and trade to the U.N. (for "national security" reasons), but several States that use the Relaxed Special Trade System record their arms transfers and trade and do report to the United Nations.

Arms transfers passing or making use of special economic areas, such as the Free Trade Zones, are of particular concern from a statistical and monitoring point of view. The *Chairman's Draft Paper* (July 2011) on the ATT does not include provisions for the accounting and monitoring of arms transfers that use Free Trade Zones and only refer to international transfers that enter country's fiscal jurisdiction. As mentioned in section 4.5 above, the inability or unwillingness of States to effectively monitor international transfers of conventional arms that use FTZs and similar special economic areas may create large loopholes in ATT-related verification activities.

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revisions of the law, as well as links to the annual report, see: Campagna Banche Armate, by Giorgio Beretta (no relationship with the manufacturer!), [www.banchearmate.org/home.htm](http://www.banchearmate.org/home.htm); see also: Unimondo at [www.unimondo.org](http://www.unimondo.org); Rete Disarmo at [www.disarmo.org](http://www.disarmo.org); for data and analyses on Italian production and trade of civilian and military small arms see OPAL at [www.opalbrescia.it](http://www.opalbrescia.it) (the research center publishes an annual report); Archivio Disarmo for data and information on Italy's arms trade at [www.archiviodisarmo.it/template.php?pag=51705](http://www.archiviodisarmo.it/template.php?pag=51705); the magazine *Altreconomia* at [www.altreconomia.it](http://www.altreconomia.it); the three-volume series by C. Buonaiuti and A. Ludovisi (editors) "*Il commercio delle armi*", "*Le spese militari nel mondo. Il costo dell'insicurezza*", "*L'industria militare e la difesa europea*" (Milan, Jaca Book, 2004, 2006, 2008); the essay "*Finanza e armamenti. Istituti di credito e industria militare tra mercato e responsabilità sociale*" by C. Buonaiuti and G. Beretta (editors), F. Vignarca, Edizioni Plus, Pisa University Press at [www.edizioniplus.it/italiano/AspFiles/libro.asp?codlibro=709](http://www.edizioniplus.it/italiano/AspFiles/libro.asp?codlibro=709); the essay/interview with Prosecutor Camillo Davigo, by C. Tombola "*Arms, security, and justice*" in OPAL report "Difendiamoci dalle armi" (2010).

According to the UN inquiry mentioned in Chapter 2,<sup>107</sup> only 50% of the 132 respondent authorities to the inquiry declared that they recorded goods entering or leaving the Zones, and less than 20% declared they were able to record transfers from and to their offshore territories, dependencies, possessions, and military bases in foreign countries. So this is a very serious loophole in the international system of reporting that has to be addressed.

### **5.5.1. The illustrative case of Cyprus**

The Republic of Cyprus (ROC or DK, Kipriaki Dhemocratia) controls the Southwestern part of Cyprus island and it is recognized as a State by the U.N. The Northeastern part of the island is controlled by Turkish Republic of Northern Cyprus (TRNC) recognized only by Turkey. Free trade zones are present in both the ROC and the TRNC. The ROC had two FTZs/free ports, Larnaca and Limassol, but a government decree dated June 9, 2011 abolished the Limassol FTZ.<sup>108</sup> The TRNC's FTZ is located in Famagusta (Magusa Free Port and Zone),<sup>109</sup> and continue the tradition of free port of Famagusta, one of the oldest free ports in the Mediterranean area (XIII/XIV Centuries). Both zones offer similar facilitations and follow the pattern established for most of the FTZs in the world.

According to the ROC government, the following ministries and agencies are responsible for export control: (a) the ministry of Foreign Affairs (MFA); (b) the ministry of Commerce, Industry and Tourism, entrusted with the export control licensing and reception of applications for license for export of controlled items including goods in transit or transshipment; (c) the Law Office of the Republic, entrusted with the drafting of legal instruments and the institution of any criminal proceedings including those related to export-import control violations; (d) the Cyprus Department of Customs & Excise, responsible for export control and enforcement.

#### **5.5.1.1. Operations permitted in the Cyprus FTZ**

It is worth noting what kinds of activities are permitted in a FTZ, using as an example the Larnaca FTZ.<sup>110</sup>

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<sup>107</sup> "An overview of National Compilation and Dissemination Practices Updated Chapter 1 of International Merchandise Trade Statistics: Supplement to the Compilers Manual." U.N. Comtrade website, May 2009. The original Chapter 1 was published in March 2008.

<sup>108</sup> [http://www.mof.gov.cy/mof/mof.nsf/DMLcustoms\\_en/DMLcustoms\\_en?OpenDocument](http://www.mof.gov.cy/mof/mof.nsf/DMLcustoms_en/DMLcustoms_en?OpenDocument)

<sup>109</sup> <http://www.cypnet.co.uk/ncyprus/city/famagusta/freeport/page0.htm>

<sup>110</sup> According to the ROC Ministry of Commerce, Industry and Tourism, "The operation of the Free Zones is ruled by the provisions of the Free Zone Law (N. 69/75), the Free Zones (Administration and Control) Regulations of 1981 (P.I . 276/81) and by the Free Zones Customs Regulations as they were modified to comply with the EU Regulations. "There is one Free Zone in Cyprus that is situated in Larnaca area near the airport and operates since 1980. The objectives of the establishment of the Free Zone are the following: a) the attraction of foreign investments, b) the creation of employment opportunities , c) the increase of exports and the inflow of foreign currency, d) the utilization of the geographical position of Cyprus, as well as the advanced infrastructure.[...] "Any person can apply to the Ministry of Commerce, Industry & Tourism for obtaining a license for establishing an industrial unit within the Larnaca Free Zone for operating trade work or manufacturing. The license is granted by the Minister of Commerce, Industry & Tourism after consultation with the Minister of Finance according to the provisions of the articles 6 and 7 of the Free Zones Law (No 69 of 1975). A license is also required by the Director of Customs & Excise Department according to the provisions of article 60 of the Customs, Code Law.N.94 (I)/2004 (P.I 387/2004." See also:

*"Activities that can take place in a Free Zone. Any industrial, commercial or service activity shall be authorized in a Free Zone. The carrying on of such activities shall be notified in advance to the customs authorities, which may impose certain prohibitions or restrictions, having regard to the nature of the goods concerned or the requirements of customs supervision. The customs authorities may prohibit persons who do not provide the necessary guarantees of compliance with the provisions laid down in the Customs legislation from carrying on an activity in a Free Zone.*

*"Both Community and non-Community goods may be placed in a Free Zone. Imported non-Community goods entering the Larnaca Free Zone shall be placed under warehousing procedure by presenting to customs a warehousing entry bearing the words "F.Z. Type II" Larnaca. Community goods [EU] after their arrival in the Republic and provided their Community status has been proven, are released immediately without any customs procedure. All goods (non-Community and Community) are entered in the stock-records kept by the company stationed in the Free Zone.*

*"There is no time limit for the stay of goods in Free Zones. However, for certain goods, which are covered by the common agricultural policy, specific time limits may be imposed. Non-Community goods placed in a Free Zone may, while they remain in a Free Zone: be released for free circulation under the conditions laid down by that procedure; undergo the usual forms of handling; be placed under the inward processing procedure; be placed under the procedure for processing; be placed under the temporary importation procedure; be transferred to a customs warehouse; be abandoned; be destroyed.*

*Goods leaving a Free Zone may be exported or re-exported from the customs territory of the Community; be brought into another part of the customs territory of the Community."*

### **5.5.1.2. Cyprus international arms transfers and re-exports**

As an important financial and transit/logistics hub, the ROC is obviously at risk of illegal activities,<sup>111</sup> but, contrary to what some have claimed, FTZ and transit hubs – including the Larnaca FTZ – do not pose a risk because of the possibility of illegal activities (after all, FTZs are likely the most guarded places in a country's fiscal territory) but because of the legal activities they allow. The following example may explain why.

With a population of about 797,000 in 2009, the ROC has an army (National Guard) of 12,000 soldiers, plus a police force (including maritime police) of 4,800. Cyprus does not have any arms production. Therefore, all its arms exports come from items previously imported.

For the years 2008, 2009,<sup>112</sup> and 2010, according to ROC declarations to the UN system of commodity trade statistics, Cyprus imported infantry weapons and civilian arms to a total value of US\$43.7 million. ROC's trading partner countries declared to the UN that they exported infantry weapons and civilian arms to Cyprus to a total

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<http://www.mof.gov.cy/mof/Customs/customs.nsf/All/6D61C14C3E95345CC22572A6003BCBD5?OpenDocument>

<sup>111</sup> US Department of State, *Money Laundering and Financial Crimes Country Database*, Bureau for International Narcotics and Law Enforcement Affairs, Washington May 2011.

<sup>112</sup> Data retrieved from UN Comtrade database for SITC code Rev. 3: 89111, 89112, 89113, 89114, 89121, 89122, 89123, 89124, 89129, 89131, 89139, 89191, 89193, 89195, 89199.

value of about US\$45 million in the same years, a fair match considering that the time of arrivals in Cyprus of shipments forwarded in December 2010 could be the early 2011.

For the same years, Cyprus declared to have exported infantry weapons and civilian arms to a total value of US\$47.3 million, of which US\$31.9 million were re-exports.<sup>113</sup> The difference with imports values may be explained by transformations to the imported arms that took place in Cyprus or by different market conditions for those items valuation at the time of export from Cyprus, or more simply by the fact that items imported in previous years were eventually exported. Destinations included countries of concern for that period, such as Armenia, Bangladesh, Bahrain, Israel, Jordan, Kuwait, Lebanon, Libya, Malta, Morocco, Pakistan, Qatar, Seychelles, Sri Lanka, Sudan, Syria, Tunisia, and Ukraine.

However, in the years 2008, 2009, and 2010, importing countries declared they had received from Cyprus infantry weapons and civilian arms to a total value of only US\$6.6 million. Therefore, there was a considerable discrepancy between trade partners' declarations and declarations by Cyprus (US\$47.3 million). This discrepancy may be explained by the fact that a number of States did not report their trade data to the U.N. in the same years or by the possibility that part of the shipments did reach their destinations indicated by Cyprus, but only entered into FTZs. If the country of destination recorded its trade according the Special Trade System then the goods entering or leaving FTZs would not be accounted for and not reported in the trade statistics of that country. Thus, after a couple of these legal passages through FTZs, the real origin of a batch of arms or ammunition is hardly traceable.

### **5.5.1.3. Verifications and controls**

An analysis of specific type of arms imported by Cyprus and same types of arms re-exported from Cyprus, reveals that Cyprus and its FTZ function as a temporary depot for arms that are directed to other destinations. By exporting to Cyprus or to its FTZ first, the original exporting countries may hide the real final customers of their arms shipments. It is in fact difficult to understand the logic or economic value of using Cyprus – an island in the East Mediterranean – as a temporary depot for arms apparently destined, sometimes the same year, to countries equally close by, or even more close by than Cyprus, to the original exporting countries. It is shippers' common practice to use the FTZs as hubs in which goods are deposited tax-free while the shippers wait favorable market conditions to forward the goods further to their destinations, but this scenario hardly applies to the arms markets where prices are not the result of seasonal variations. Therefore, there is not an economic reason behind the choice of Cyprus and its FTZs as first destination of arms that are subsequently exported, sometimes to very questionable destinations.

It is worth noting that 4,811, 4,433, and 4,289 ships docked at ROC ports in 2009, 2010 and 2011, respectively, and the ports moved cargoes for a total of 22.5 million tons in the three years. The same ports moved an average of 350,000 containers

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<sup>113</sup> Re-exports mean that the items should not have undergone "*substantial transformation*". Ascertaining if the goods have or have not undergone "*substantial transformation*" might not be always easy or possible. The operation entails a discretionary evaluation by Customs, because certain mechanisms or works that may have changed the arms' characteristics may not always be self-evident.

(TEU) yearly,<sup>114</sup> the means of choice for most of the conventional arms traded, in particular ammunition, small arms, and light weapons.

Customs and ports authorities have the right to inspect every cargo, irrespective of its destination, including the FTZs. Inspections can discover shipments of illegal goods or goods bound to illegal destinations, but Customs officials intervene only if they are reasonably sure to find something irregular because the speed of Customs operations is of paramount importance for the success of a port. Inspections block or delay the flows of Customs clearance and are therefore limited to shipments that risk-assessment programs detect as potentially problematic. Unfortunately, when shippers are known and end-users seem legitimate, Customs are less likely to inspect the cargo and the following example<sup>115</sup> may explain how an illegal shipment passed through Customs undetected.

In 2004, the US Department of Defense had contracted a US-based arms dealing firm - Taos Industries (Alabama) – to ship thousands of Beretta 92S military pistols to a US military base in Iraq for the Coalition Provisional Authority (CPA).<sup>116</sup> However, the pistols were not shipped directly from Italy to Iraq. They were firstly shipped to the United Kingdom. To arrange the deal with Beretta, Taos used a UK-based company, Super Vision International Ltd,<sup>117</sup> and an established UK arms manufacturer, Helston Gunsmiths, was included in the Beretta export license as the consignee of the pistols in the UK.<sup>118</sup> The pistols were then shipped to Iraq in July 2004, but were not recorded as delivered and officially accepted in Iraq until 18 April 2005.<sup>119</sup> Several of them were later found in the hands of insurgents by the US intelligence. The Beretta company had illicitly refurbished the pistols<sup>120</sup> and had obtained export documents that mistakenly described the pistols as “civilian”, whose exports are regulated by Law 110/75 (1975) and not by the stricter Law 185/90 (1990) for military weapons, which requires documentation aimed at avoiding possible diversion.<sup>121</sup> The Italian company had sold the pistols for an estimated value of €2.5 million. In the export license application Beretta had indicated a UK company as the consignee but that UK firm was not found to be the real buyer of the

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<sup>114</sup> See: <http://www.cpa.gov.cy/CPA/page.php?pageID=26&mpath=/11&langID=0>

<sup>115</sup> See: Amnesty International, TransArms, and IPIS vzw, *“Blood at the Crossroads: Making the case for a global Arms Trade Treaty”*, Amnesty International ACT 30/011/2008; Tombola, C., *“Eight years and Counting for the Trial on Beretta’s Ghost Pistols”*, in OPAL (Research center on small arms, Brescia) annual report 2012, forthcoming.

<sup>116</sup> “Italian Guns for Iraqi Insurgents,” by N. Vallini, *Il Corriere della Sera*, May 25, 2005, English translation, <http://www.corriere.it/english/beretta.shtml>

<sup>117</sup> Super Vision International Ltd - domiciled at Claridge House, 29 Barnes High Street Barnes, London and directed by Chris Bradbury <http://www.applegate.co.uk/company/12/30/880.htm>.

<sup>118</sup> “UK guns in al-Qaeda hands,” by M. Townsend and B. McMahon, *The Observer*, March 19, 2006; “Inquiry into secret guns-for-Iraq deal,” by D. Kennedy and P. Bompard, *The Times*, April 1, 2006; “Iraqi Guns,” File On 4, BBC, May 23, 2006.

<sup>119</sup> BBC, Radio 4, Transcript of file on 4 programme: - ‘Iraqi Guns’, 23 May 2006; porter Allan Urry stated that: “but we’ve seen a verification certificate for them which says they weren’t delivered and accepted by the authorities in Iraq until April 18 2005 or earlier.”

<sup>120</sup> Brescia Court, First Penal Section, Dr. Enrico Fischetti, President, May 11, 2005. Text of the sentence rejecting Beretta’s Appeal. The prosecutors found that the pistols seized in Iraq were part of a lot of pistols Beretta 92S manufactured by Beretta and sold between 1978 and 1980 to the Italian ministry of Interior. They also found that the Ministry of Interior, without a proper dismissal documentation, gave back to Beretta the same weapons (for a total of 44,926 pistols, barrels and spare parts) between February 2003 and April 2004 in exchange of an equal number of new model Berettas. At that time, Beretta did not have the license to refurbish pistols.

<sup>121</sup> In June 2003, the Italian Parliament modified the Law 185/90, cancelling the provision requiring arms manufacturers to accompany export documentation with an end-user certificate.

pistols.<sup>122</sup> No Customs or licensing officials checked the real contents of the shipment, likely because it involved well-known government entities and companies that did not raise suspicion. As first destination, the United Kingdom was used to hide the real customer of the arms shipped from Italy, with Taos effectively adopting the same technique that traders use when they ship arms through FTZs.

## 5.6. The U.N. database COMTRADE

On the basis of the HS and SITC commodity classification (see chapter 3), the U.N. Statistical Division maintains a database (COMTRADE) on international trade that includes data on imports, exports, re-imports and re-exports for all the commodities traded in the world from 1962, as reported by States, Territories, and Dependencies. The aggregate data submitted to the U.N. comes from States' national reports on their merchandise trade, using Customs data and other sources<sup>123</sup> and according to the trade system they follow. COMTRADE allows for public on line searches based on a) classification system (HS, SITC, BEC<sup>124</sup>); b) reporting countries (importers and exporters); c) codes; d) trade flow (import, export, re-import, re-export), e) year.

The publicly available level of detail under HS (6-digit) and SITC (5-digit) systems for "arms and ammunition" is usually still too generic to allow public users of COMTRADE to track a particular arms shipment. Moreover, most countries have adopted confidentiality rules that allow a party to request the competent national authorities to obscure transactions or partner countries in their reports. In addition, for ships and aircraft, the 5- or 6-digit level data available from COMTRADE does not allow for distinguishing military and civilian items. A 10-digit level would allow much greater precision in public reporting but States suppress this level of detail..

Under the SITC system, for example, commercial sales of infantry weapons and civilian arms and parts fall under the 1-digit code 8 ("*Miscellaneous manufactured articles*") and its 2-digit and 3-digit specifications (code 89 for "*Miscellaneous manufactured goods non elsewhere specified*" and code 891 for "*Arms and Ammunition*"). Sub-code 891 is in its turn divided in four 4-digit codes (8911, 8912, 8913, and 8919), each further divided in 5-digit codes.<sup>125</sup>

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<sup>122</sup> Brescia Court, First Penal Section, May 11, 2005, quoted. Helston Gunsmiths of Cornwall was mentioned as a consignee; the real buyer was Super Vision International Ltd.

<sup>123</sup> According to the United Nations "*International Merchandise Trade Statistics, Concepts and Definitions.*" (New York, 1998) "*there are a variety of sources that can be used to compile international merchandise trade statistics, including customs records, enterprise surveys, administrative records associated with value added taxes, and currency exchange records. Customs records are the most prevalent source...*" [...] "*In a growing number of cases, full coverage of international merchandise trade statistics cannot be achieved by use of customs records only, either because the relevant transactions are no longer subject to customs controls or customs surveillance, or because the record keeping may not be adequate from the statistical point of view. [...] Many countries utilize enterprise surveys as a means to collect data on transactions which may not be captured by customs authorities (e.g., trade in electricity, water, gas, petroleum and goods for military use).*"

<sup>124</sup> Broad Economic Categories

<sup>125</sup> The U.N. Statistical Division provides tables that correlate HS and SITC codes and different versions of HS and SITC systems. For example, what in the Harmonized Commodity Description Version 2002 is code 930200 ("*Revolvers & pistols, designed to fire live ammunition*") corresponds with code 98114 in the SITC system Rev. 4.

For example, the 4-digit code 8911 includes four 5-digit codes:

- 89111 for “Tanks and other armored fighting vehicles, motorized, whether or not fitted with weapons, and parts of such vehicles”;
- 89112 for “Military weapons (other than revolvers, pistols and the arms of heading 891.13)”;
- 89113 for “Swords, cutlasses, bayonets, lances and similar arms and parts thereof and scabbards and shields thereof”;
- 89114 for “Revolvers and pistols, designed to fire live ammunition”.

In COMTRADE, queries return tables according to the above-mentioned criteria (reporter, partner, year, code, etc.) with values in US\$ and weight or units. Data on trade flows of countries whose authorities do not report arms transfers to COMTRADE can often (but not always) be retrieved by using the declarations of all other countries that have the non-reporting countries as trade partners.

Nevertheless, the usefulness of COMTRADE for understanding the direction and value of the world trade in arms is limited. As already noted, the level of specification is insufficient for a meaningful assessment of what is really traded and, in the case of aircraft and ships, the level of specification hides the civilian or military nature of the traded items. In addition, while certain government-to-government transfers are recorded by merchandise trade statistics<sup>126</sup>, other ones<sup>127</sup> are not and so remain outside the reach of COMTRADE.

COMTRADE data sets are as good as States transmit them and discrepancies, mistakes, and lack of data affect the worthiness of the system. For example, in 2005 France reported that it sold about €20.2 million of arms (mainly for ML4, bombs, torpedo, missiles, rockets, military explosives),<sup>128</sup> but those transfers were not recorded in COMTRADE data. However, COMTRADE is presently the only commodity trade data system that at least allows non-governmental actors to track certain conventional arms shipments at world level, including for countries that do not report their international transfers of conventional arms.

One of most useful provisions to include in an ATT would be a rule requiring States Parties to report in a full, timely and precise manner their arms imports and exports to COMTRADE and to mandate a 10-digit specification for the relevant codes.

### **5.6.1. COMTRADE and code 891 “Arms and Ammunition”**

How much trade in conventional arms does COMTRADE capture? If COMTRADE data for SITC code 891 is compared with available data from national or international reports and official communications by States, the total world value recorded by COMTRADE seems insufficient for a meaningful evaluation, even considering that

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<sup>126</sup> According to the United Nations “*International Merchandise Trade Statistics, Concepts and Definitions*.” (New York, 1998) goods traded on government account should be included in merchandise trade statistics and should include “*goods for both civilian and military use which cross borders as a result of, for instance, regular commercial transactions of Governments, goods under government foreign aid programmes (whether or not the goods constitute a grant, a loan, a barter or a transfer to an international organization) and war reparations and restitutions*.”

<sup>127</sup> If COMTRADE data are compared with national reports on conventional arms transfers, it is evident that COMTRADE data do not include all transfers.

<sup>128</sup> Ministère de la Défense, *Rapport au Parlement sur les exportations d’armement de la France*, 2005, citato e European Union, *Eight Annual report according to operative provision 8 of the European Union Code of conduct on arms exports*, 2005; see also European Union, *Eight Annual Report According to Operative Provision 8 of the European Union Code of Conduct on Arms Exports*, 2006 (on 2005).

items included in code 891 are only a portion of the items traded in international transfers of conventional arms. For a year for which there should be a consolidated set of data, the year 2009, COMTRADE reports world total exports (in FOB terms)<sup>129</sup> at US\$11,273,796,299 and world total imports at US\$10,632,123,286.<sup>130</sup> (in CIF terms).<sup>131</sup>

Table 3 below shows the main countries that did not report their trade to COMTRADE in 2009. Tables 4 and 5 show what the 94 countries that reported to COMTRADE had declared for their exports and imports in 2009 for code 891. To date (January 2012) several countries have not yet made available to COMTRADE data for the years 2008, 2009, 2010.<sup>132</sup>

**Table 3 - Selected Countries that did not report to COMTRADE.**

|                      |                  |
|----------------------|------------------|
| Country              | Country          |
| Afghanistan          | Iraq             |
| Andorra              | Kuwait           |
| Angola               | Laos             |
| Bangladesh           | Lesotho          |
| Benin                | Liberia          |
| Botswana             | Libya            |
| Brunei Darussalam    | Mauritania       |
| Cameroon             | Mongolia         |
| Central African Rep. | Morocco          |
| Chad                 | Mozambique       |
| Comoros              | Myanmar          |
| Congo                | Papua New Guinea |
| Cuba                 | Philippines      |
| DPRK                 | San Marino       |
| D.R. Congo           | Seychelles       |
| Equatorial Guinea    | Sierra Leone     |
| Eritrea              | Somalia          |
| Gabon                | Swaziland        |
| Gambia               | Tajikistan       |
| Gibraltar            | Timor-Leste      |
| Greenland            | Turkmenistan     |
| Guinea               | Tuvalu           |
| Guinea-Bissau        | Ukraine          |
| Haiti                | Uzbekistan       |
| Indonesia            | Vanuatu          |
| Iran                 | Venezuela        |

Source: UN Statistical Division, COMTRADE, <http://comtrade.un.org/db> "Non-available data". Some of the listed countries have never reported their trade to COMTRADE.

<sup>129</sup> Free on Board, see Annex A for definition.

<sup>130</sup> Theoretically, at world level the value of imports and exports should be equal but various elements may concur to the discrepancy, including non coincidental time of recording and differences in values recorded by Customs of the partner countries. Data in CIF terms are higher than data in FOB terms because they include not only the value of the items traded but also the cost of importing them

<sup>131</sup> Cost, Insurance, Freight, see Annex A for definition.

<sup>132</sup> Source: COMTRADE

**Tab. 4 - Countries declaring exports under SITC code 891 in 2009**

| Reporter           | Trade Value US\$ | Reporter               | Trade Value US\$ |
|--------------------|------------------|------------------------|------------------|
| 1. USA             | 4,450,748,031    | 19. Australia          | 104,938,921      |
| 2. Canada          | 940,165,961      | 20. Belgium            | 101,740,080      |
| 3. Italy           | 633,343,764      | 21. Portugal           | 81,135,408       |
| 4. Switzerland     | 527,889,680      | 22. Croatia            | 65,350,828       |
| 5. Germany         | 508,924,000      | 23. China              | 63,539,061       |
| 6. Norway          | 496,218,070      | 24. Austria            | 58,000,349       |
| 7. Israel          | 410,550,000      | 25. Côte d'Ivoire      | 52,592,925       |
| 8. France          | 380,393,025      | 26. Denmark            | 52,328,841       |
| 9. Brazil          | 334,840,906      | 27. Lebanon            | 50,491,037       |
| 10. Japan          | 274,569,120      | 28. India              | 44,312,978       |
| 11. Spain          | 241,465,006      | 29. Slovakia           | 41,444,021       |
| 12. Rep. of Korea  | 238,707,836      | 30. Russian Federation | 40,459,134       |
| 13. Czech Rep.     | 192,325,789      | 31. Serbia             | 37,715,240       |
| 14. Poland         | 169,646,112      | 32. Mexico             | 22,627,794       |
| 15. Sweden         | 134,406,222      | 33. Argentina          | 14,816,819       |
| 16. Finland        | 129,603,137      | 34. Cyprus             | 14,179,025       |
| 17. United Kingdom | 122,015,509      | 35. Senegal            | 13,379,414       |
| 18. Turkey         | 116,859,006      | 36. Thailand           | 12,567,737       |
| 37. Rwanda         | 8,780,554        | 54. China, Hong Kong   | 1,730,001        |
| 38. Greece         | 8,632,253        | 55. Trinidad Tobago    | 1,674,071        |
| 39. Singapore      | 8,275,260        | 56. Djibouti           | 1,211,677        |
| 40. Romania        | 7,574,611        | 57. Estonia            | 1,198,926        |
| 41. Chile          | 6,789,492        | 58. Latvia             | 1,083,876        |
| 42. Saudi Arabia   | 6,464,615        | 59. Sudan              | 912,746          |
| 43. Qatar          | 6,185,139        | 60. Tanzania           | 715,968          |
| 44. Lithuania      | 6,043,694        | 61. Egypt              | 432,488          |
| 45. Pakistan       | 5,951,110        | 62. Kenya              | 363,391          |
| 46. Malaysia       | 3,803,631        | 63. Hungary            | 329,000          |
| 47. Peru           | 3,607,968        | 64. Panama             | 243,138          |
| 48. Colombia       | 3,422,943        | 65. Cambodia           | 210,448          |
| 49. Netherlands    | 3,157,524        | 66. Malta              | 205,709          |
| 50. Montenegro     | 2,886,853        | 67. Luxembourg         | 196,825          |
| 51. New Caledonia  | 2,695,343        | 68. Uganda             | 124,835          |
| 52. New Zealand    | 2,167,608        | 69. Nigeria            | 113,880          |
| 53. Ireland        | 1,988,868        | 70. Zimbabwe           | 111,568          |
| 71. Nepal          | 90,868           | 83. China, Macao SAR   | 2,794            |
| 72. Fiji           | 29,700           | 84. Jamaica            | 1,748            |
| 73. Mayotte        | 19,821           | 85. French Polynesia   | 1,414            |
| 74. El Salvador    | 12,753           | 86. Zambia             | 1,394            |
| 75. Aruba          | 10,615           | 87. Nicaragua          | 942              |
| 76. Guatemala      | 10,318           | 88. Dominican Rep.     | 500              |
| 77. Malawi         | 8,040            | 89. Ecuador            | 493              |
| 78. Bahamas        | 8,000            | 90. Ethiopia           | 170              |
| 79. Yemen          | 7,556            | 91. Georgia            | 118              |
| 80. Iceland        | 5,649            | 92. Sri Lanka          | 105              |
| 81. Uruguay        | 3,506            | 93. Samoa              | 39               |
| 82. Honduras       | 2,954            | 94. Madagascar         | 3                |

Source: Elaboration on COMTRADE data

**Tab. 4 - First 100 Countries declaring imports under SITC code 891 in 2009**

| Reporter           | Trade Value US\$ | Reporter                | Trade Value US\$ |
|--------------------|------------------|-------------------------|------------------|
| 1. USA             | 4,155,443,067    | 25. Estonia             | 49,398,604       |
| 2. Saudi Arabia    | 1,160,802,906    | 26. Sweden              | 48,079,752       |
| 3. Canada          | 709,450,612      | 27. Austria             | 45,800,342       |
| 4. Australia       | 425,234,450      | 28. Russian Federation  | 43,053,421       |
| 5. Norway          | 304,220,680      | 29. Côte d'Ivoire       | 37,827,359       |
| 6. Rep. of Korea   | 290,033,559      | 30. Pakistan            | 36,631,152       |
| 7. United Kingdom  | 281,665,117      | 31. New Zealand         | 35,013,169       |
| 8. Switzerland     | 278,107,357      | 32. Finland             | 31,441,293       |
| 9. Thailand        | 222,250,727      | 33. Greece              | 29,514,452       |
| 10. Japan          | 217,526,624      | 34. Turkey              | 28,633,332       |
| 11. Spain          | 215,282,393      | 35. Kenya               | 28,189,868       |
| 12. Portugal       | 207,372,606      | 36. India               | 26,784,652       |
| 13. Germany        | 181,311,000      | 37. Slovakia            | 22,795,532       |
| 14. France         | 175,909,645      | 38. Croatia             | 22,105,028       |
| 15. Czech Rep.     | 160,667,161      | 39. Lebanon             | 20,970,032       |
| 16. Colombia       | 151,672,058      | 40. Cambodia            | 20,813,941       |
| 17. Poland         | 148,936,288      | 41. Latvia              | 20,428,783       |
| 18. Italy          | 139,170,265      | 42. Argentina           | 15,292,014       |
| 19. Sudan          | 79,804,724       | 43. Ireland             | 13,566,656       |
| 20. Malaysia       | 79,444,065       | 44. Cyprus              | 12,968,005       |
| 21. Belgium        | 77,711,895       | 45. Netherlands         | 12,650,106       |
| 22. Brazil         | 64,478,542       | 46. Honduras            | 12,324,653       |
| 23. Denmark        | 63,922,104       | 47. Viet Nam            | 11,953,735       |
| 24. Mexico         | 61,442,528       | 48. Trinidad and Tobago | 10,017,867       |
| 49. Dominican Rep. | 8,315,345        | 75. Panama              | 1,747,927        |
| 50. Burkina Faso   | 8,156,208        | 76. Nepal               | 1,729,775        |
| 51. Guatemala      | 7,919,679        | 77. Iceland             | 1,727,445        |
| 52. Peru           | 6,888,583        | 78. Nigeria             | 1,663,781        |
| 53. El Salvador    | 6,704,839        | 79. Niger               | 1,662,306        |
| 54. Singapore      | 6,472,126        | 80. Malta               | 1,446,187        |
| 55. Chile          | 6,162,421        | 81. Nicaragua           | 1,288,104        |
| 56. Lithuania      | 6,136,555        | 82. Zimbabwe            | 1,123,191        |
| 57. Egypt          | 6,123,376        | 83. Zambia              | 1,065,492        |
| 58. Luxembourg     | 5,679,781        | 84. China, Macao SAR    | 915,370          |
| 59. Paraguay       | 5,317,602        | 85. Rwanda              | 900,426          |
| 60. China          | 4,873,622        | 86. Sri Lanka           | 844,123          |
| 61. Uganda         | 4,751,258        | 87. Mauritius           | 658,407          |
| 62. Romania        | 4,300,008        | 88. Djibouti            | 562,572          |
| 63. Tunisia        | 3,728,999        | 89. Tanzania            | 520,818          |
| 64. Serbia         | 3,721,085        | 90. Bahamas             | 437,119          |
| 65. Costa Rica     | 3,371,584        | 91. French Polynesia    | 369,110          |
| 66. China, HK SAR  | 3,103,278        | 92. Mayotte             | 348,315          |
| 67. Montenegro     | 3,079,993        | 93. Ecuador             | 297,167          |
| 68. Senegal        | 3,052,555        | 94. Aruba               | 173,682          |
| 69. Bolivia        | 2,928,212        | 95. Madagascar          | 159,243          |
| 70. Hungary        | 2,845,000        | 96. Malawi              | 127,150          |
| 71. Jamaica        | 2,680,768        | 97. Faeroe Islands      | 122,356          |
| 72. New Caledonia  | 2,679,770        | 98. Guyana              | 93,567           |
| 73. Bahrain        | 2,372,281        | 99. Bulgaria            | 83,817           |
| 74. Uruguay        | 2,234,204        | 100. Fiji               | 56,973           |

Source: Elaboration on COMTRADE data

## Chapter 6 - The ATT Scope on Services

The ATT PrepCom *Chairman's Draft Paper* (14 July 2011) includes in ATT Scope certain activities that should fall under the category of "Services", such as transport and brokering (where it is not clear whether the latter may include financial services). In fact, any services relating to the international transfer of conventional arms of whatever nature or form to any entity located in the territory of another state, or to an institution of the government of another state, should be regulated and considered as part of the ATT Scope. For the purposes of this report, the following definitions apply to brokering, financial, and transportation services.<sup>133</sup>

### 6.1. Brokering services

"Brokering services" have been described by the U.N. Group of Governmental Experts on preventing illicit brokering in small arms and light weapons to mean: (1) serving as a finder of business opportunities to one or more parties to a transaction involving international transfers of conventional arms, as defined in this report; (2) putting relevant parties in contact; (3) assisting parties to a transaction involving the same above-mentioned items in proposing, arranging or facilitating agreements or possible contracts between them; (4) assisting parties to a transaction involving the same items in obtaining the necessary documentation; or in arranging the necessary payments; 5) purchasing or selling conventional arms in order to facilitate an international transfer of conventional arms to a third party.<sup>134</sup>

### 6.2. Financial services

"Financial services" mean activities aimed at providing payment, whether in currency, goods, services or other form, to the manufacturer, seller, exporter, importer or broker of conventional arms to be internationally transferred; (2) providing a loan, mortgage, letter of credit or other credit instrument for payment within the terms of the transfer of the same items.

### 6.3. Transportation services

"Transportation services" mean activities aimed at (1) transporting conventional arms from or across the territory of a State to the territory of another State; (2) controlling the means of transport of conventional arms from or across the territory of a State to the territory of another State; (3) arranging the transport of conventional arms from or across the territory of a State to the territory of another State.

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<sup>133</sup> The authors of this report, while assuming full responsibility for the text, acknowledge the contribution by Mike Lewis, Oliver Sprague, and Brian Wood in the development of the ATT Scope on services, born from discussions and works carried out in 2009 and 2010 at the International Secretariat of Amnesty International

<sup>134</sup> United Nations, "*Report of the Group of Governmental Experts established pursuant to General Assembly resolution 60/81 to consider further steps to enhance international cooperation in preventing, combating and eradicating illicit brokering in small arms and light weapons*", A/62/163, 30 August 2007

While for the brokering activity the Chairman's Draft Paper propose States to register and control brokers who want to engage in arms transfers, no provision is envisaged for the control of transport or financial services.

The international trade in transport services deserves particular attention because logistics companies, freight forwarders, and carriers are at the core of the international supply-chains that, in an increasingly globalized world, move arms along the international routes that connect the "buyers" with the "sellers".

The attention that policymakers and civil society organizations have dedicated to the role of transport services in the international transfers of conventional arms - and to the accounting systems for reporting the international exchange of these services - is insufficient. In fact, monitoring transport services may be the key provision for the implementation and enforcement of the Arms Trade Treaty.<sup>135</sup>

#### **6.4. International trade in freight transport services**

Logistics companies, freight forwarders, and carriers engage in the international transport of arms as providers of logistics and transport services for the military communities; for arms manufacturing companies; and for arms brokers and dealers. In turn, these companies use the services of international gateways such as seaports and airports. Monitoring the activities of logistics and transport companies, as well as of international gateways, should be an indispensable part of arms control policies and the ATT Scope on Services.<sup>136</sup>

Monitoring international transport services for transfers of conventional arms will also often provide a means for understanding the role that certain countries play in the international arms trade. For example, the prominent role that carriers based in Denmark, Norway, and Greece play in international freight services should require those countries to assume special responsibilities to regulate and report on such services under the ATT,...

The services that transport and logistics companies provide to sellers and buyers in the international trade are accounted for in a country's "*Balance of Payments Statistics*," annually prepared by the I.M.F on the basis of reports by States and IMF calculations, and according to the reporting recommendations of the Balance of Payments Manual.<sup>137</sup>

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<sup>135</sup> TransArms and the International Peace Information Service have since 2003 maintained a databank on transport companies and brokers involved in defence logistics and international transport of conventional and non-conventional arms. The databank is hosted by TransArms Europe, an affiliated NGO based in Italy. The databank project and its design were initially developed by TransArms with the research contribution of the Peace Research Institute of Oslo (PRIO) in 2003 and then further modified in 2006, when it passed to TransArms Europe. It presently includes information on about 2,000 transport companies, thousands of aircraft and ships, as well as events related to the transport of arms, accompanied by relevant original documentation.

<sup>136</sup> See: "*Dead on Time: arms transportation, brokering and the threat to human rights*." Amnesty International and TransArms, 2006.

<sup>137</sup> See: IMF, *Balance of Payments and International Investment Position Manual (BPM6)* Sixth Edition, December 2008, Pre-publication draft. <http://www.imf.org/external/pubs/ft/bop/2007/pdf/BPM6.pdf>

The Balance of Payments statistics record the value of goods and services that residents and governments of a country annually exchange with residents and governments of other States. The exchange of transport services is accounted for as a Debit/Credit transaction. This is in contrast to the exchange in goods (import/export). The payments that a resident of country A makes to a resident of country B is accounted for as a Debit from country A, and payments a resident of country B receives from a resident of country A is accounted for as a Credit from country A.

Unfortunately, several countries - and in particular countries that host international or "open" registries for maritime and aviation companies<sup>138</sup> - have very poor records of reporting on international transport services performed by their "residents" and sometimes they have no statistics at all. This poses several problems for developing monitoring activity under the likely ATT.

Relevant for an ATT-related monitoring activity is the section of the *Balance of Payments Statistics* that deals with "Freight Services" and "Other Transport Services".

Freight services are transport services that cover "*the transport of objects other than people.*"<sup>139</sup> Freight services are performed by carriers, freight forwarders and by Customs agents. Carriers are operators of transport assets, such as ships, aircraft, railcars, and trucks., Freight forwarders are companies that, on behalf of a shipper, take care of the transport of goods covering all required transport modalities and also prepare transport and Customs documentation, as well as storage and packaging on demand. Customs agents clear the goods for Customs purposes.<sup>140</sup> These companies share with the seller and the buyer part of the responsibilities related to the transfers of the goods.

Statistics on trade in Services also include data under the "Other Transport Services" category. This category includes services "*that are auxiliary to transport and not directly provided for the movement of goods and persons.*"<sup>141</sup> Among these services, some are relevant from a potential ATT-related monitoring activity, including "*cargo handling*", "*storage and warehousing, packing and repackaging*", "*air traffic control*", and "*agents' activities associated with freight transport (e.g., freight forwarding and brokerage services)*".<sup>142</sup>

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<sup>138</sup> See: "*Dead on Time: arms transportation, brokering and the threat to human rights.*" Amnesty International and TransArms, 2006, Chapter 3.

<sup>139</sup> See: IMF, *Balance of Payments Manual*, quoted, 2008.

<sup>140</sup> Freight forwarders (sometimes called maritime or aviation "agents") are often global logistics companies that cover all the necessity of a supply-chain, from owning and organizing storage facilities to brokering carriers' services and can act as Customs clearance agents. Some large transport companies (carriers) also act as logistics companies and provide services similar to those ones of the freight forwarders.

<sup>141</sup> See: IMF, *Balance of Payments Manual*, quoted, 2008.

<sup>142</sup> See: IMF, *Balance of Payments Manual*, quoted, 2008. According to the Manual, "an agent is a party who acts on behalf of or as a representative for another party. Transactions arranged by an agent on behalf of a principal should be attributed to the principal, not to the agent. For example, if an agent issues tickets on behalf of an airline resident in another economy, the transactions and positions related to those tickets are attributed to the airline. However, an agent may also undertake transactions on its own account, including the agency services it provides to the principal."

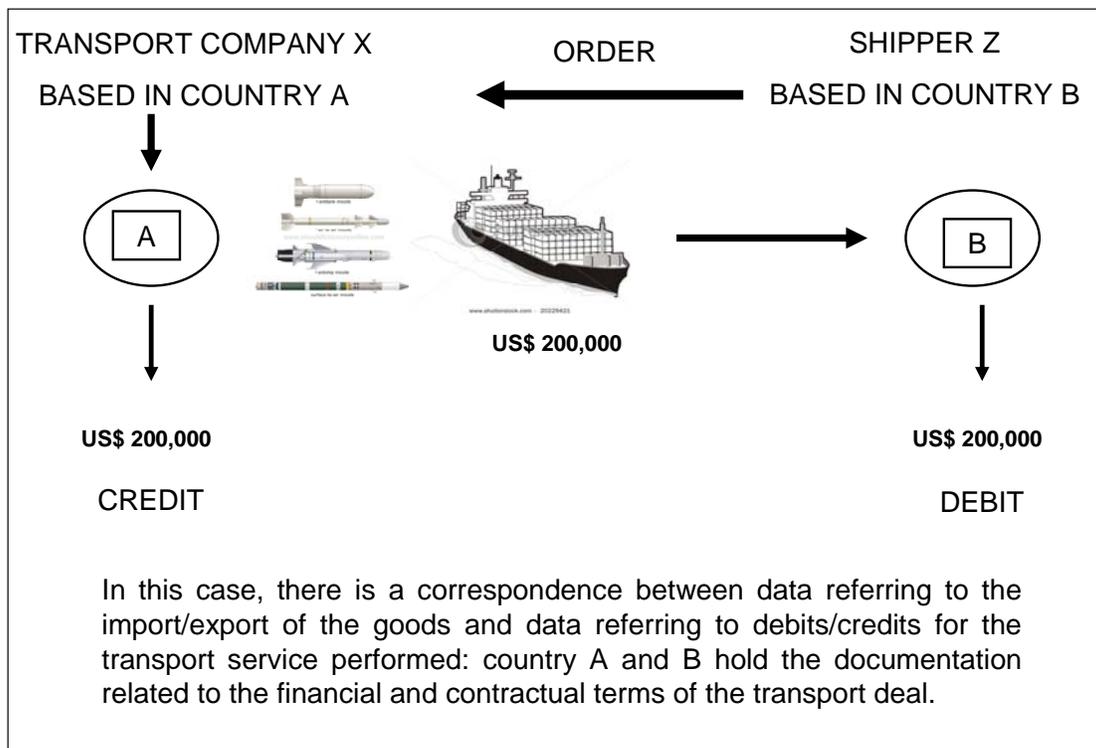
## 6.5. Reporting systems for Freight Transport Services

The Balance of Payments statistics reports the value and direction of Freight Services according to standards that deserve attention because they may affect the ATT-related information-gathering activities. The following cases may serve as examples of reporting standards.

### Example 1

A shipper Z based in country B hires a transport company X based in country A to move arms from country A to country B.

The shipper Z based in country B incurs in a debit relative to company X based in country A. This debit is accounted for in the Debit side of the balance of international payments of country B. Conversely, the revenue gained by the transport company X is accounted for in the international balance of payments of country A as a Credit.

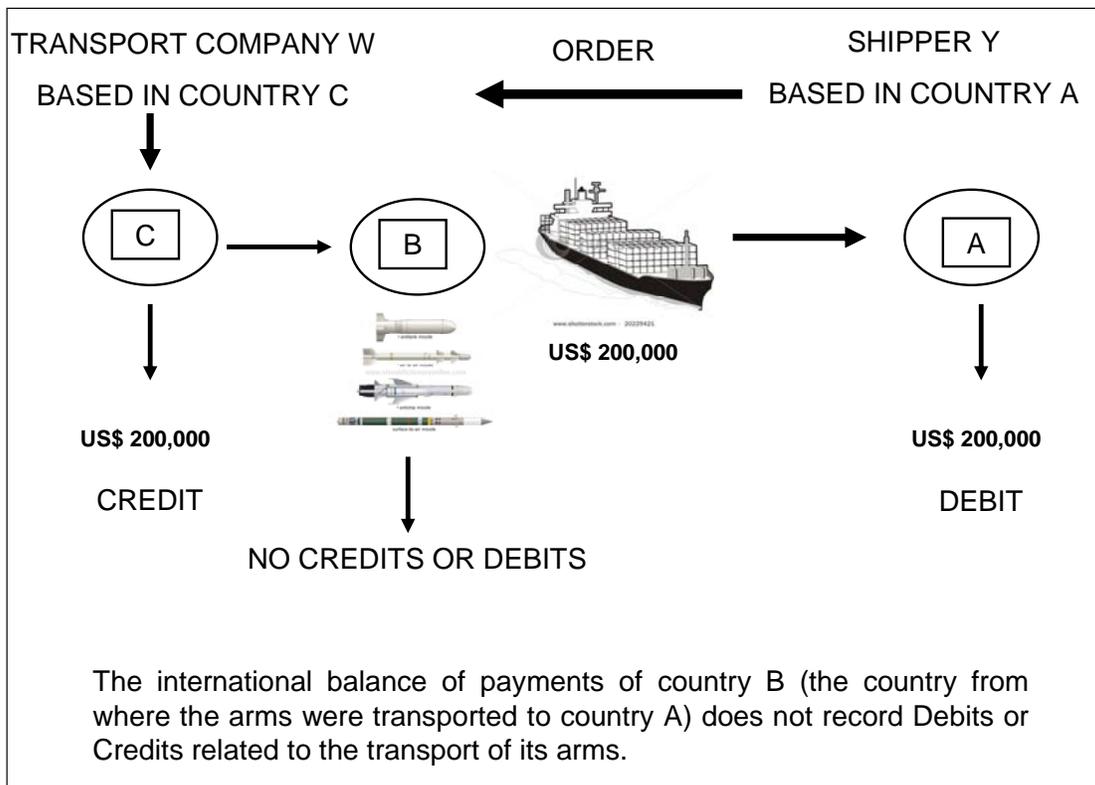


## Example 2

A shipper Y based in country A hires a transport company W based in country C to move arms from country B to country A.

This case may happen when there is shortage of transport capacities in country A and B or for technical or geographic reasons.

In this case, the debit of the shipper Y is accounted for in the Debit side of country A (where the shipper, or importer, is a resident), but the revenue gained by transport company W is accounted for as a Credit in the balance of international payments of country C.



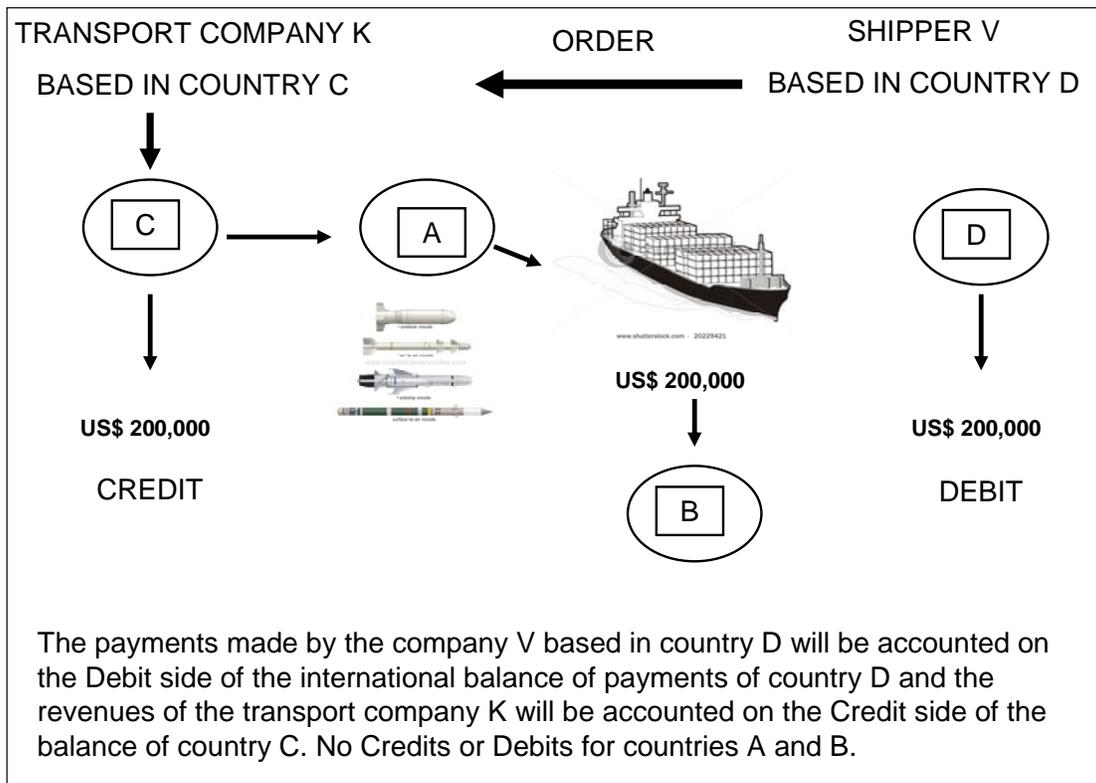
### Example 3

A shipper V based in country D hires a transport company K based in country C to transport arms from country A to country B.

This case may happen, for example, when a parent company wishes to move arms or components from one of its subsidiaries based in country A to a customer or another of its subsidiaries based in country B. If the transport contract is between the parent company and the transport company, the entity based in country A and the entity based in country B will not incur an international payment for that transport service. Consequently, the international balance of payments of country A and B will not record Debits or Credits related to that transport.

The payments made by the parent company V based in country D will be accounted on the Debit side of the international balance of payments of country D and the revenues of the transport company K will be accounted on the Credit side of the balance of country C.

Countries A and B – the export and import points for the transfer of the arms – will not hold the documentation on the financial and contractual terms of the transport service. Actually, only countries C and D will hold the contract documentation.



## Annex A - Main contractual practices: Incoterms

Contractual terms for international trade define obligations and responsibilities of the parties and are therefore extremely important for ATT-related verification activities. Both government-to-government and commercial transfers of conventional arms may be subjected to contractual practices as defined by the Incoterms, but government-to-government transfers usually follow in addition their own procedures.<sup>143</sup>

A gradual change of the presently prevalent contractual practices in international transfers of conventional arms may produce, if widely adopted, exceptional results in terms of transparency and accountability.

In 1936, the International Chamber of Commerce (ICC), an international organization based in Paris,<sup>144</sup> established the so-called Incoterms, with the purpose of providing the international business and trade community a **unified terminology for the main trading practices**. Each Incoterm, copyrighted by the ICC, "*refers to a type of agreement for the purchase and shipping of goods internationally*".<sup>145</sup>

Up to September 2010 there were "*13 different terms, each of which helps users deal with different situations involving the movement of goods.*" "[Incoterms] deal with the documentation required for global trade, specifying which parties are responsible for which documents."<sup>146</sup> "*The scope of Incoterms 2000 is limited to matters relating to the rights and obligations of the parties to the contract of sale with respect to the delivery of goods sold. Incoterms 2000 do NOT apply to the contract of carriage.*"<sup>147</sup>

The structure of Incoterms used a four-category sequence, according to the following characteristics:

- Terms beginning with E occur when "*a seller's responsibilities are fulfilled when goods are ready to depart from their facilities*".<sup>148</sup> "*The seller only makes the goods available to the buyer at the seller's own premises*".<sup>149</sup> Term: Ex-Works;
- Terms beginning with F refer "*to shipments where the primary cost of shipping is not paid for by the seller.*"<sup>150</sup> "*The seller is called upon to deliver the goods to a carrier appointed by the buyer.*"<sup>151</sup> Terms: FCA, FAS and FOB

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<sup>143</sup> See, for example: Defense Institute of Security Assistance Management, *The Management Of Security Assistance*, The Twenty-Seventh Edition (Green Book), International Standard Serial No. 1532-0359, October 2007, Wright-Patterson AFB, Ohio; US DoD, *DCSA Customer Guide*, Washington 2006; Society of International Affairs, *Foreign Military Sales Export Primer*, June 2004.

<sup>144</sup> <http://www.iccwbo.org>; and <http://www.iccwbo.org/incoterms/id3045/index.html>.

<sup>145</sup> *Foreign Trade Online*, Markham, Ontario, Canada: <http://www.foreign-trade.com>. Due to copyright restrictions, the reported definitions use a different wording for the same ICC Incoterms.

<sup>146</sup> *Idem*.

<sup>147</sup> See: WACO (World Air Cargo Organization), a Swiss registered/non-profit organization, based in Hofheim (Frankfurt).

<sup>148</sup> WACO, quoted.

<sup>149</sup> See EMCEE, "Incoterms 2000" guidelines at [http://www.emceecom.com/customer\\_information.html](http://www.emceecom.com/customer_information.html), quoted with permission. E-mail dated June 15, 2009.

<sup>150</sup> WACO, quoted.

<sup>151</sup> EMCEE, quoted.

## Transparency and Accountability - Common Standards for the ATT

- Terms beginning with C *“deal with shipments where the seller pays for shipping.”*<sup>152</sup> *“the seller has to contract for carriage, but without assuming that risk of loss of or damage to the goods or additional costs due to events occurring after shipment and dispatch”.*<sup>153</sup> Terms: CFR, CIF, CPT and CIP
- Terms beginning with D *“cover shipments where the shipper/seller's responsibility ends when the goods arrive at some specific point. Because shipments are moving into a country, D terms usually involve the services of a customs broker and a freight forwarder. In addition, D terms also deal with the pier or docking charges found at virtually all ports and determining who is responsible for each charge”.*<sup>154</sup> *“The seller has to bear all costs and risks needed to bring the goods to the place of destination”.*<sup>155</sup> Terms: DAF, DES, DEQ, DDU and DDP

Some Incoterms have only been applied to contracts of sales that used the sea/inland waterways modality of transport while some other ones applied to all modalities, including air transport.

**Table A - Incoterms 2000 – Contracts of sale and transport modality**

| Group | Incoterm   | Any Modality | Sea/Inland Waterways |
|-------|--|--------------|----------------------|
| E     | EXW - Ex Works (named place)                       | X            |                      |
| F     | FCA - Free Carrier (named place)                   | X            |                      |
| F     | FAS - Free Alongside Ship*                         |              | X                    |
| F     | FOB - Free On Board                                |              | X                    |
| C     | CFR - Cost and Freight                             |              | X                    |
| C     | CIF - Cost, Insurance and Freight                  |              | X                    |
| C     | CPT - Carriage Paid to (place of destination)      | X            |                      |
| C     | CIP - Carriage and Insurance Paid to (place of d.) | X            |                      |
| D     | DAF - Delivered at Frontier (place)                | X            |                      |
| D     | DES - Delivered Ex Ship                            |              | X                    |
| D     | DEQ - Delivered Ex Quay*                           |              | X                    |
| D     | DDU - Delivered Duty Unpaid (place of destination) | X            |                      |
| D     | DDP - Delivered Duty Paid (place of destination)   | X            |                      |

Source: Elaboration from ICC Incoterms 2000.

On September 2010, the ICC decided to reduce the 13 Incoterms to 11. The new rules came into effect on January 1, 2011. In order to adapt the rules to the present practices of the transport and trade industries, two new Incoterms, DAT (Delivered at Terminal) and DAP (Delivered at Place), were developed to substitute DAF, DES, DEQ and DDU terms. The new 11 Incoterms have been divided into two classes, according to the mode of transport to which they apply (see below for explanation of the acronyms).

<sup>152</sup> WACO, quoted.

<sup>153</sup> EMCEE, quoted.

<sup>154</sup> WACO

<sup>155</sup> EMCEE

"The first class includes the seven Incoterms® 2010 rules that can be used irrespective of the mode of transport selected and irrespective of whether one or more than one mode of transport is employed".<sup>156</sup> The seven terms are as follows:

**Table B - Incoterms 2010 – Contracts of sale and transport modality**

| Group | Incoterm                       | Any Modality |
|-------|--------------------------------|--------------|
| EXW   | EX WORKS                       | X            |
| FCA   | FREE CARRIER                   | X            |
| CPT   | CARRIAGE PAID TO               | X            |
| CIP   | CARRIAGE AND INSURANCE PAID TO | X            |
| DAT   | DELIVERED AT TERMINAL          | X            |
| DAP   | DELIVERED AT PLACE             | X            |
| DDP   | DELIVERED DUTY PAID            | x            |

Source: Elaboration from ICC Incoterms 2010.

"In the second class of Incoterms® 2010 rules, the point of delivery and the place to which the goods are carried to the buyer are both ports, hence the label "sea and inland waterway" rules".<sup>157</sup>

**Table C - Incoterms 2010 – Contracts of sale and transport modality**

| Group | Incoterm                   | Sea/Inland Waterways |
|-------|----------------------------|----------------------|
| FAS   | FREE ALONGSIDE SHIP        | X                    |
| FOB   | FREE ON BOARD              | X                    |
| CFR   | COST AND FREIGHT           | X                    |
| CIF   | COST INSURANCE AND FREIGHT | X                    |

Source: Elaboration from ICC Incoterms 2010.

The following paragraphs provide definitions and explanations of the previous 13 Incoterms (in order of group E, F, C, and D) and the new 2 Incoterms entered into force in January 2011. Contracts made under DAF, DES, DEQ, DDU terms still remain valid and the ICC recommends traders to specify the Incoterms version they are using (2010, 2000, or earlier version). Definitions and explanations are from the U.S. Foreign Trade Online (FTO) and EMCEE company website,<sup>158</sup> respectively. Definitions and explanations for DAT and DAP terms are from Freightline International (FI).<sup>159</sup>

### **A.1. EXW (EX-Works)**

"In an EX-Works transaction, goods are basically made available for pickup at the shipper/seller's factory or warehouse and "delivery" is accomplished when the merchandise is released to the consignee's freight forwarder. The buyer is responsible for making

<sup>156</sup> ICC website, <http://www.iccwbo.org/Incoterms/index.html?id=40772>

<sup>157</sup> ICC website, <http://www.iccwbo.org/Incoterms/index.html?id=40772>

<sup>158</sup> See EMCEE, "Incoterms 2000" guidelines at [http://www.emceecom.com/customer\\_information.html](http://www.emceecom.com/customer_information.html), quoted with permission. E-mail dated June 15, 2009.

<sup>159</sup> <http://www.freightline-international.co.uk/pages/news.php>

*arrangements with their forwarder for insurance, export clearance and handling all other paperwork". (FTO)*

*"The seller delivers when he places the goods at the disposal of the buyer at the seller's premises or another named place (i.e. works, factory, warehouse, etc.) not cleared for export and not loaded on any collecting vehicle. This term represents the Minimum Obligation for the Seller, and the buyer has to bear all costs and risks involved in taking the goods from the seller's premises. However, if the parties wish the seller to be responsible for the loading of the goods on departure and to bear the risks and all costs of such loading, this should be made clear by adding explicit wording to this effect in the contract of sale. This term should not be used when the buyer cannot carry out the export formalities directly or indirectly. In such circumstances, the FCA term should be used, provided the seller agrees that he will load at his cost and risk". (EMCEE)*

## **A.2. FCA (Free Carrier)**

*"In this type of transaction, the seller is responsible for arranging transportation, but he is acting at the risk and the expense of the buyer. Where in FOB the freight forwarder or carrier is the choice of the buyer, in FCA the seller chooses and works with the freight forwarder or the carrier. 'Delivery' is accomplished at a predetermined port or destination point and the buyer is responsible for Insurance". (FTO)*

*"The seller delivers the goods, cleared for export, to the carrier nominated by the buyer at the named place. It should be noted that the chosen place of delivery has an impact on the obligations of loading and unloading the goods at that place. If delivery occurs at the seller's premises, the seller is responsible for loading. If delivery occurs at any other place, the seller is not responsible for unloading. This term may be used for all modes of transport. "Carrier" means any person who, in a contract of carriage, undertakes to perform or to procure the performance of transport by rail, road, air, sea, inland waterway, or by a combination of such modes. If the buyer nominates a person other than a carrier to receive the goods, the seller is deemed to have fulfilled his obligation to deliver the goods when they are delivered to that person". (EMCEE)*

## **A.3. FAS (Free Alongside Ship)**

*"In these transactions, the buyer bears all the transportation costs and the risk of loss of goods. FAS requires the shipper/seller to clear goods for export, which is a reversal from past practices. Companies selling on these terms will ordinarily use their freight forwarder to clear the goods for export. "Delivery" is accomplished when the goods are turned over to the Buyers Forwarder for insurance and transportation". (FTO)*

*"The seller delivers when the goods are placed alongside the vessel at the named port of shipment. This means that the buyer has to bear all costs and risks of loss of or damage to the goods from that moment. The FAS term requires the seller to clear the goods for export. However, if the parties wish the buyer to clear the goods for export, this should be made clear by adding explicit wording to this effect in the contract of sale. This term can only be used for sea or inland waterway transport". (EMCEE)*

## **A.4. FOB (Free On Board)**

*"FOB means that the shipper/seller uses his freight forwarder to move the merchandise to the port or designated point of origin. Though frequently used to describe inland movement of cargo, FOB specifically refers to ocean or inland waterway transportation of goods. "Delivery"*

*is accomplished when the shipper/seller releases the goods to the buyer's forwarder. The buyer's responsibility for insurance and transportation begins at the same moment". (FTO)*

*"The seller delivers when the goods pass the ship's rail at the named port of shipment. This means that the buyer has to bear all costs and risks of loss of or damage to the goods from that point. The FOB term requires the seller to clear the goods for export. This term can only be used for sea or inland waterway transport. If the parties do not intend to deliver the goods across the ship's rail, the FCA term should be used". (EMCEE)*

### **A.5. CFR (Cost and Freight)**

*"This term formerly known as CNF (C&F) defines two distinct and separate responsibilities, one is dealing with the actual cost of merchandise 'C' and the other 'F' refers to the freight charges to a predetermined destination point. It is the shipper/seller's responsibility to get goods from their door to the port of destination. 'Delivery' is accomplished at this time. It is the buyer's responsibility to cover insurance from the port of origin or port of shipment to buyer's door. Given that the shipper is responsible for transportation, the shipper also chooses the forwarder". (FTO)*

*"The seller delivers when the goods pass the ship's rail in the port of shipment. The seller must pay the costs and freight necessary to bring the goods to the named port of destination but the risk of loss of or damage to the goods, as well as any other costs due to events occurring after the time of delivery, are transferred from the seller to the buyer. The CFR term requires the seller to clear the goods for export. This term can only be used for sea or inland waterway transport. If the parties do not intend to deliver the goods across the ship's rail, the CPT term should be used". (EMCEE)*

### **A.6. CIF (Cost, Insurance and Freight)**

*"This arrangement similar to CFR, but instead of the buyer insuring the goods for the maritime phase of the voyage, the shipper/seller will insure the merchandise. In this arrangement, the seller usually chooses the forwarder. "Delivery" as above, is accomplished at the port of destination". (FTO)*

*"The seller delivers when the goods pass the ship's rail in the port of shipment. The seller must pay the costs and freight necessary to bring the goods to the named port of destination but the risk of loss of or damage to the goods, as well as any other costs due to events occurring after the time of delivery, are transferred from the seller to the buyer. However, in CIF the seller also has to procure marine insurance against the buyer's risk of loss of or damage to the goods during carriage. Consequently, the seller contracts for insurance and pays the insurance premium. The buyer should note that under the CIF term the seller is required to obtain insurance only on minimum cover. Should the buyer wish to have the protection of greater cover, he would either needs to agree as much expressly with the seller or to make his own extra insurance arrangements. The CFR term requires the seller to clear the goods for export. This term can only be used for sea or inland waterway transport. If the parties do not intend to deliver the goods across the ship's rail, the CIP term should be used". (EMCEE).*

### **A.7. CPT (Carriage Paid To)**

*"In CPT transactions the shipper/seller has the same obligations found with CIF, with the addition that the seller has to buy cargo insurance, naming the buyer as the insured while the goods are in transit". (FTO)*

*"The seller delivers the goods to the carrier nominated by him but the seller must in addition pay the cost of carriage necessary to bring the goods to the named destination. This means that the buyer bears all risks and any other costs occurring after the goods have been so delivered. "Carrier" means any person who, in a contract of carriage, undertakes to perform or to procure the performance of transport by rail, road, air, sea, inland waterway, or by a combination of such modes. If subsequent carriers are used for the carriage to the agreed destination, the risk passes when the goods have been delivered to the first carrier. The CPT term requires the seller to clear the goods for export. This term may be used for all modes of transport". (EMCEE)*

### **A.8. CIP (Carriage and Insurance Paid To)**

*"This term is primarily used for multimodal transport. Because it relies on the carrier's insurance, the shipper/seller is only required to purchase minimum coverage. When this particular agreement is in force, Freight Forwarders often act in effect, as carriers. The buyer's insurance is effective when the goods are turned over to the Forwarder". (FTO)*

*"The seller delivers the goods to the carrier nominated by him but the seller must in addition pay the cost of carriage necessary to bring the goods to the named destination. This means that the buyer bears all risks and any other costs occurring after the goods have been so delivered. However, in CIP the seller also has to procure insurance against the buyer's risk of loss of or damage to the goods during the carriage. Consequently, the seller contracts for insurance and pays the insurance premium. The buyer should note that under the CIP term the seller is required to obtain insurance only on minimum cover. Should the buyer wish to have the protection of greater cover, he would either need to do so expressly with the seller or to make his own extra insurance arrangements. "Carrier" means any person who, in a contract of carriage, undertakes to perform or to procure the performance of transport by rail, road, air, sea, inland waterway, or by a combination of such modes. If subsequent carriers are used for the carriage to the agreed destination, the risk passes when the goods have been delivered to the first carrier. The CIP term requires the seller to clear the goods for export. This term may be used for all modes of transport". (EMCEE)*

### **A.9. DAF (Delivered At Frontier) - Substituted in Incoterms 2010**

*"The seller's responsibility is to hire a forwarder to take goods to a named frontier, which is usually a border crossing point, and clear them for export. 'Delivery' occurs at this time. The buyer's responsibility is to arrange with their forwarder for the pick up of the goods after they are cleared for export, carry them across the border, clear them for importation and effect delivery. In most cases, the buyer's forwarder handles the task of accepting the goods at the border across the foreign soil". (FTO)*

*"The seller delivers when the goods are placed at the disposal of the buyer on the arriving means of transport not unloaded, cleared for export, but not cleared for import at the named point and place at the frontier, but before the customs border of the adjoining country. The term 'frontier' may be used for any frontier including that of the country of export. Therefore, it is of vital importance that the frontier in question be defined precisely by always naming the point and place in the term. However, if the parties wish the seller to be responsible for the unloading of the goods from the arriving means of transport and to bear the risks and costs of unloading, this should be made clear by adding explicit wording to this effect in the contract of sale. This term may be used for all modes of transport when the goods are to be delivered at a land frontier. When a delivery is to take place in the port of destination, on board a vessel, or on the quay (wharf), the DES or DEQ terms should be used". (EMCEE)*

### **A.10 DES (Delivered Ex Ship) - Substituted in Incoterms 2010**

*"In this type of transaction, it is the seller's responsibility to get the goods to the port of destination or to engage the forwarder to move cargo to the port of destination uncleared. 'Delivery' occurs at this time. Any destination charges that occur after the ship is docked are the buyer's responsibility". (FTO)*

*"The seller delivers when the goods are placed at the disposal of the buyer on board the ship not cleared for import at the named port of destination. The seller has to bear all the costs and risks involved in bringing the goods to the named port of destination before discharging. If the parties wish the seller to be responsible for the unloading of the goods from the arriving means of transport and to bear the risks and costs of discharging the goods, then the DEQ term should be used. This term can only be used when the goods are to be delivered by sea or inland waterway or multimodal transport on a vessel in the port of destination". (EMCEE)*

### **A.11. DEQ (Delivered Ex Quay)- Substituted in Incoterms 2010**

*"In this arrangement, the buyer/consignee is responsible for duties and charges and the seller is responsible for delivering the goods to the quay, wharf or port of destination. In a reversal of previous practice, the buyer must also arrange for customs clearance". (FTO)*

*"The seller delivers when the goods are placed at the disposal of the buyer not cleared for import on the quay (wharf) at the named port of destination. The seller has to bear all the costs and risks involved in bringing the goods to the named port of destination and discharging the goods on the quay (wharf). The DEQ term requires the buyer to clear the goods for import and to pay for all formalities, duties, taxes, and any other charges upon import. If the parties wish to include in the seller's obligations all or part of the costs payable upon import of the goods, this should be made clear by adding explicit wording to this effect in the contract of sale. This term can only be used when the goods are to be delivered by sea or inland waterway or multimodal transport on discharging from a vessel onto the quay (wharf) in the port of destination. However, if the parties wish to include in the seller's obligations the risks and costs of the handling of the goods from the quay (wharf) to another place (warehouse, terminal, transport station, etc.) in or outside the port, the DDU or DDP terms should be used". (EMCEE)*

### **A.12. DDU (Delivered Duty Unpaid)- Substituted in Incoterms 2010**

*"This arrangement is basically the same as with DDP, except for the fact that the buyer is responsible for the duty, fees and taxes". (FTO)*

*"The seller delivers the goods to the buyer, not cleared for import, and not unloaded from any arriving means of transport at the named place of destination. The seller has to bear all the costs and risks involved in bringing the goods thereto, other than, where applicable, any 'duty' (which term includes the responsibility for and the risks of the carrying out of customs formalities, and the payment of formalities, customs duties, taxes, and other charges) for import in the country of destination. Such 'duty' has to be borne by the buyer as well as any costs and risks caused by his failure to clear the goods for import in time. However, if the parties wish the seller to carry out customs formalities and bear the costs and risks resulting therefrom, as well as some of the costs payable upon import of the goods, this should be made clear by adding explicit wording to this effect in the contract of sale. This term may be used for all modes of transport, but when delivery is to take place in the port of destination on board the vessel or on the quay (wharf), the DES or DEQ terms should be used". (EMCEE)*

### **A.13. DDP (Delivered Duty Paid)**

*"DDP terms tend to be used in intermodal or courier-type shipments. Whereby, the shipper/seller is responsible for dealing with all the tasks involved in moving goods from the manufacturing plant to the buyer/consignee's door. It is the shipper/seller's responsibility to insure the goods and absorb all costs and risks including the payment of duty and fees". (FTO)*  
*"The seller delivers the goods to the buyer, cleared for import, and not unloaded from any arriving means of transport at the named place of destination. The seller has to bear all the costs and risks involved in bringing the goods thereto including, where applicable, any 'duty' (which term includes the responsibility for and the risks of the carrying out of customs formalities, and the payment of formalities, customs duties, taxes, and other charges) for import in the country of destination.*

*While the EXW term represents the minimum obligation for the seller, DDP represents the Maximum Obligation for the Seller. This term should not be used if the seller is unable directly or indirectly to obtain the import license. However, if the parties wish to exclude from the seller's obligations some of the costs payable upon import of the goods (such as value-added tax: VAT), this should be made clear by adding explicit wording to this effect in the contract of sale. If the parties wish the buyer to bear all risks and costs of the import, the DDU term should be used. This term may be used for all modes of transport, but when delivery is to take place in the port of destination on board the vessel or on the quay (wharf), the DES or DEQ terms should be used". (EMCEE)*

### **A.14. DAT (Delivered at Terminal) - Incoterms 2010**

The term applies to any modality. *"Seller delivers when the goods, once unloaded from the arriving means of transport, are placed at the disposal of the buyer at a named terminal and at the named port or place of destination. 'Terminal' includes includes quays, warehouses, container yard or road, rail or air terminal". [...] Both parties should agree the terminal and if possible a point within the terminal at which point the risks will transfer from the seller to the buyer of the goods". (F1)*  
*"The seller is responsible for the costs and risks to bring the goods to the point specified in the contract. [...] The seller is responsible for the export clearance procedures and the importer is responsible to clear the goods for import, arrange import customs formalities, pay import duty". (F1)*

### **A.15. DAP (Delivered at Place) - Incoterms 2010**

The term applies to any modality. *"The seller delivers the goods when they are placed at the disposal of the buyer on the arriving means of transport ready for unloading at the named place of destination." (F1)*

*"Seller bears the responsibility and risks to deliver the goods to the named place. The seller is required to clear the goods for export. [...] Importer is responsible for effecting customs clearance and paying any customs duties." (F1)*

### **A.16. Summary Tables and Chart for Buyer/Seller Responsibilities**

Table D and E summarize the increasing responsibilities of the seller under each contractual term (Incoterms 2000, from EXW to DDP).

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**Table D– Responsibility for Performing the Listed Service – S (Seller) B (Buyer)**

| Service/Event          | EXW | FCA | FAS | FOB | CFR | CIF | CPT | CIP | DAF | DES | DEQ | DDU | DDP |
|------------------------|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| Export Pack            | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Mark and Label         | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Export Clearance*      | B   | S   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Arrange Insurance      | B   | B   | B   | B   | B   | S   | B   | S   | S   | S   | S   | S   | S   |
| Nominate Main Carrier  | B   | B   | B   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Nominate Exp. Forw.    | B   | B   | B   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Arrange Pre-Carriage   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Load Pre-Carrier       | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Unload Pre-Carrier     | B   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Load Main Carrier      | B   | B   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Stow Main Carrier      | B   | B   | B   | B   | B   | B   | B   | B   | S   | S   | S   | S   | S   |
| Unload Main Carrier    | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | S   | S   |
| Nominate On-Carrier    | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | S   |
| Arrange On-Carrier     | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | S   |
| Nominate Import Broker | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | S   | S   |
| Load On-Carrier        | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | S   |
| Import Clearance *     | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | B   | S   |
| Pay Destination DTF**  | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | B   | S   |
| Unload From On-Carrier | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   |

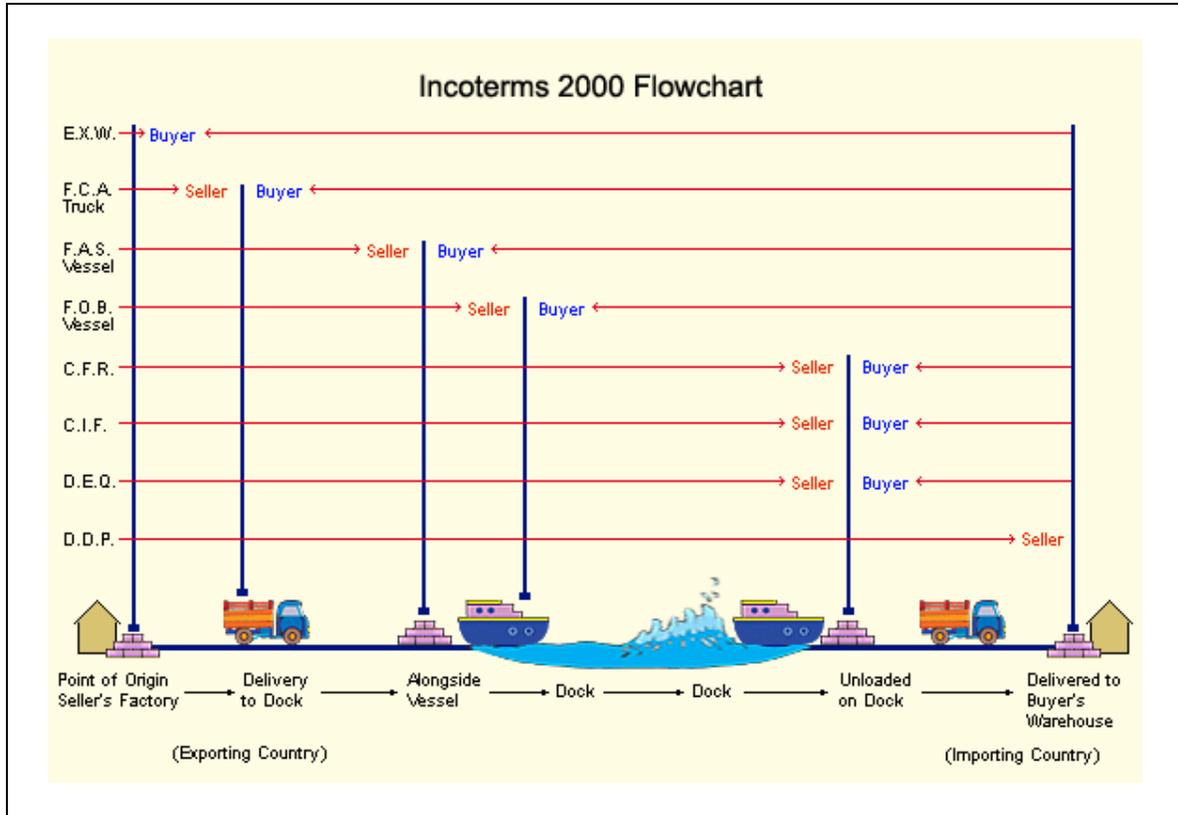
**Table E – Responsibility for Preparing the Documents**

| Documents             | EXW | FCA | FAS | FOB | CFR | CIF | CPT | CIP | DAF | DES | DEQ | DDU | DDP |
|-----------------------|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| Commercial Invoice    | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Packing List          | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Export Declaration    | B   | S   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Certificate of Origin | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Pre-carriage BoL**    | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Export License        | B   | S   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Other Governmental*   | B   | S   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Main Carriage BoL**   | B   | B   | B   | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Dock Receipt          | B   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   | S   |
| Insurance Certificate | B   | B   | B   | B   | B   | S   | B   | S   | S   | S   | S   | S   | S   |
| Import License        | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | B   | S   |
| On-Carriage BoL**     | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | S   |
| Entry Documents       | B   | B   | B   | B   | B   | B   | B   | B   | B   | B   | S   | B   | S   |

Source: EMCEE, [http://www.emceecom.com/customer\\_information.html](http://www.emceecom.com/customer_information.html). (\*) EPA and FDA; (\*\*) Bill of Lading. Published with permission by EMCEE

The following chart illustrates the borders of traders' responsibilities under various contractual terms (International Chamber of Commerce, Incoterms 2000).

**Chart 1 – Selected Incoterms 2000 – Borders of Responsibility**



Source: International Chamber of Commerce

## Part III - Proposals and Recommendations

### 1. Trading arms in Delivery Duty Paid (DDP) terms

Berkol, Schütz, and Wéry<sup>160</sup> have proposed that sellers/exporters of arms should assume responsibility for the arms they ship until they reach the point of destination. Presently, the prevailing types of contracts<sup>161</sup> in import/export transactions assign the responsibility of paying the import duties to the buyer/importer, who also insures the goods, and chooses the carrier that transports the goods from the borders of the exporting country to the borders of the importing country (CIF terms).<sup>162</sup> Here the exporter has no responsibilities for the actual delivery of the goods to the stated destination.

Berkol and colleagues proposed that the arms exporters should trade under CIF terms in order to highlight that the exporter of arms should bear the obligations implied in the CIF terms. The substance of the proposal is clear and may lead to a path of important changes. The reference to CIF terms, however, could lead to confusion because those terms apply to maritime transport only, despite being often and erroneously used in shipping documents other than for maritime transport.

Contracting arms shipments in DDP terms (Delivery Duty Paid, with Named Place of Destination) may be more correct and more effective than in CIF terms. DDP terms mean that *“the seller delivers the goods to the buyer, cleared for import, and not unloaded from any arriving means of transport at the named place of destination. The seller has to bear all the costs and risks involved in bringing the goods thereto including, where applicable, any ‘duty’ (which term includes the responsibility for and the risks of the carrying out of customs formalities, and the payment of formalities, customs duties, taxes, and other charges) for import in the country of destination. While the EXW [Ex-Works] term represents the minimum obligation for the seller, DDP represents the Maximum Obligation for the Seller. This term should not be used if the seller is unable directly or indirectly to obtain the import license”*.<sup>163</sup>

In effect, if the seller and the buyer trade in DDP terms, the exporters/sellers bear the responsibility to make sure that the arms reach the destination stated in the shipping documents and are consigned to the importer as stated in the End Use Certificate or to representatives of the importer at the port, airport, or other “ports” of entry. The proposal of trading commercial sales of arms in DDP terms cannot be

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<sup>160</sup> See: Berkol, I., *Traceability of Small Arms and Light Weapons, Contribution to the United Nations Conference on the Illicit Trade in Small Arms and Light Weapons in All Its Aspects (with the collaboration of F.Schütz and M. Wéry)*. GRIP, July 2001; Berkol, I., M. Wéry, *Technical and Institutional Aspects of an International SALW Tracing Instrument*. Presentation to the Group of Governmental Experts on the Tracing of SALW. GRIP, Geneva, 4 July 2002 ((original in French).

<sup>161</sup> See Annex A above for a complete treatment of the matter.

<sup>162</sup> CIF (Cost, Insurance and Freight) terms mean that “the seller delivers when the goods pass the ship’s rail in the port of shipment. The seller must pay the costs and freight necessary to bring the goods to the named port of destination but the risk of loss of or damage to the goods, as well as any other costs due to events occurring after the time of delivery, are transferred from the seller to the buyer”.

<sup>163</sup> See Appendix 1 for reference.

part of the provisions of an ATT because it is not in the power of States to dictate to private companies the contractual terms of their international activities. However, the proposal to trade arms in DDP terms may be part of ATT recommendations for best practices and of a dialogue with arms manufacturers and exporters aiming to establish an industry Code of Conduct. No matter how difficult it might be to induce sellers and buyers to abandon the present practices,<sup>164</sup> the adoption of DDP terms in arms trade contracts may lead to a series of important and positive changes. Statistical practices should change accordingly.

## **2. Registration of transport service providers**

Under an ATT, States should require (1) the registration of transport service providers operating within their territory and engaged in transport of conventional arms (as already required by some States); (2) the licensing or authorization of each proposed transport service provision activity; (3) applicants for import and export licenses or authorizations to disclose to the relevant national authorities, prior to the international transfer taking place, the names and address of transport service providers (freight forwarders and carriers) involved in the transfer; the registration and flag of any vehicle, aircraft or vessel involved in the international transportation of the items; the route/s to be used and planned stopovers in the international transportation of the items.

Transport service providers should maintain comprehensive and verifiable documentation, including cargo manifests, airway bills, bills of lading and invoices, which at a minimum should contain details of the export authorization, the consignee/consignor, end-user and the relevant customs tariff codes identifying each movement of the items; compliance with existing national legislation or international agreements relating to the transport of weapons by air, land or sea.

## **3. Reporting methods and monitoring activities**

### ***3.1. Recommendations to States in the U.N. talks on the ATT***

Under the final Arms Trade Treaty (ATT), States Parties should adhere to the U.N. Statistical Division's recommendations and report their foreign trade according to the provisions of the General Trade System, which includes arms transfers and monitoring of transfers throughout free trade zones and similar entities.

Countries that already use the Special Trade System for reporting their foreign trade but want otherwise to ratify the ATT should at least apply the provisions of the Relaxed Special Trade System and so include arms trade in their foreign trade statistics.

State Parties to the ATT should also specify which method they use for Partner Country attribution and, ideally, provide information according to at least two of the

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<sup>164</sup> Transferring the costs of insurance, transport, and importing duties to the seller could prove to be difficult, but these costs could be included in the arms prices and the choice of the insurer and of the carrier could be on mutual agreement terms.

three Partner country attribution's methods: "*Country of origin and Country of consumption*;" "*Country of consignment and country of final destination*;" "*Country of purchase and Country of sale*."

### **3.2. Make Public States Reports to the ATT**

State Parties to the ATT should make public their annual reports to the Implementation Support Unit, and design their reports to contain detailed information along the lines of Italy's Law 185/1990 (See Section 6.4.1 above)

### **3.3. Transparency at the 10-digit level of specification**

The United Nations and States Parties to the ATT should make publicly available the data on arms transfers at the Harmonized System 10-digit level of specification, on the model of the U.S. Customs data.

### **3.4. European Union, abolition of the secret country codes**

European Union Member States that ratify the ATT should improve the accuracy and information base of their international arms transfers and trade for intra-trade, in particular when they involve Member States whose economic territory includes free trade zones and similar entities. European Union States Parties to the ATT should avoid the practice of suppressing data from publication by requesting special alphanumeric codes for arms transfers and using the "secret country code" for arms transfers with trade partners.

### **3.5. Barter trade and gratuity terms**

States Parties to the ATT should include in their arms trade reports and statistics specific information on arms transfers agreed on barter trade and gratuity terms, as well as offsets agreements that include transfers of military-related technologies and machineries.

### **3.6. Transit and Trans-shipment**

States that ratify the ATT should engage in a monitoring program for arms in transit, trans-shipment and re-transfers.

### **3.7. Monitoring of FTZs**

States that ratify the ATT should engage in efforts to set international standards and rules for international arms transfers that involve items entering or leaving free trade zones and similar entities. They should also engage in efforts to set international

rules aimed at defining which commercial and industrial processes may be allowed in free trade zones when conventional arms are involved.

### **3.8. Internal Flows**

Every significant international movement of conventional arms – as defined in this report - contributes to changes in the military environment and balance of the area where the movement is directed. Making more transparent international transfers of military equipment and internal security weapons and munitions (which should be one of the goals of the ATT) means also a better knowledge of what equipment is available in a certain area or region. If "internal flows" (to troops, warehouses, depots, military bases, etc. located in other countries) are not reported, there will be a significant distortion of the assessment of the military balance of a certain area or region. Several countries already and explicitly record as exports (or authorization to permanent exports) equipment sent abroad for the use of their troops, allies, or multinational missions.

Chicago and Antwerp, February 2012

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