



CENTRALIZED COMPLIANCE

How and Why the Private Sector Centralizes its Compliance Efforts

Facilitator: Asha Menon
External Presenter: Carol West
Secretary, International Federation of Customs Brokers Associations (IFCBA)

20 June 2017

OUTLINE

- What is compliance?
- Who's in charge of compliance?
- What drives compliance?
- What is centralized compliance?
- Does centralized compliance work?
- What is the effect of centralized compliance on trade facilitation?

WHAT IS COMPLIANCE?

Compliance is “conformity in fulfilling official requirements”, in other words, following the rules. A simple concept in theory, but a little harder to apply in our ever evolving, fast paced world.

WHO’S IN CHARGE OF COMPLIANCE?

In business, compliance managers are referred to as trade champions. They work with senior management to integrate compliance into strategic planning. They are often tasked with promoting company strategies which emphasize the importance of developing and facilitating a robust compliance program and then implementing that strategy. A robust compliance program is one where everyone has responsibility for compliance.

WHAT IS CENTRALIZED COMPLIANCE?

A key element of centralized compliance is that one function retains direct control over all compliance-related activities and execution of controls. This is a common structure in highly regulated sectors, and especially in multi-national companies and large enterprises.

WHAT ABOUT DECENTRALIZED BUSINESS MODELS?

Companies that are decentralized consist of a series of loosely affiliated subsidiary businesses or divisions that ultimately report to a parent corporation or headquarters. Each subsidiary or division is structured as a separate profit and loss center and is usually permitted to do business as it sees fit, as long as it meets its financial objectives. This may lead to decentralized compliance within a company, with each function responsible for its own compliance program. In the realm of trade compliance, however, a corporate import-export program is only as strong as its weakest link.

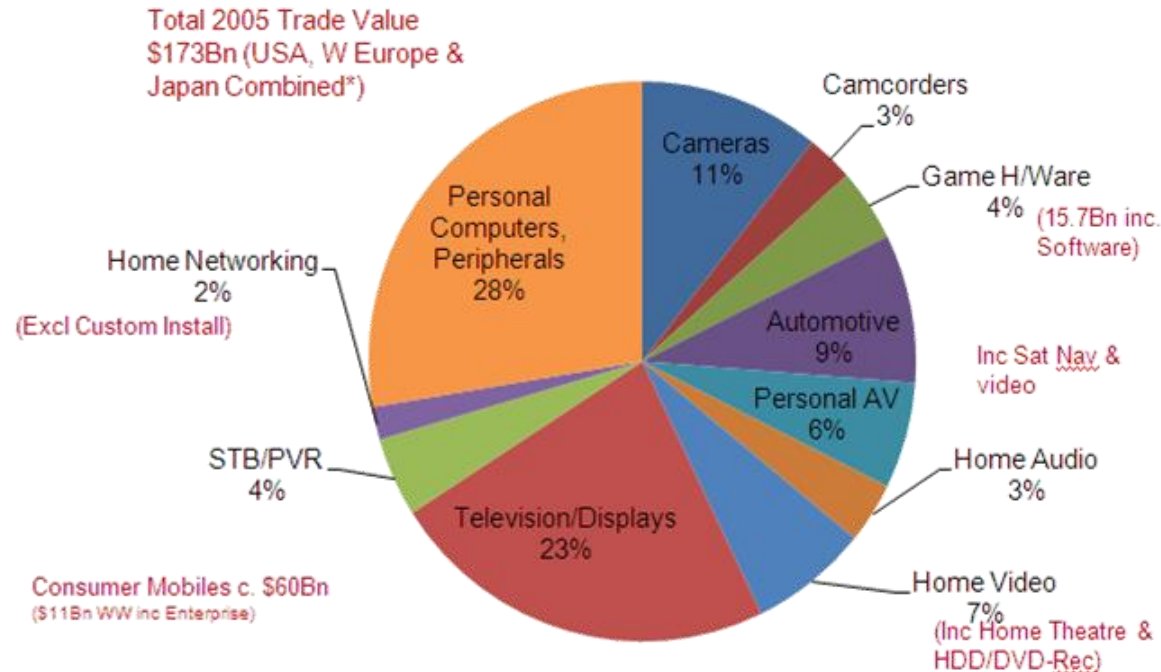
WHERE SHOULD THE COMPLIANCE FUNCTION RESIDE?

- Should it be part of sales, accounting, shipping, purchasing, customer service?
- Should it be with traffic, logistics, legal, regulatory affairs?
- When deciding where to place trade compliance responsibility and staff within a corporation, you need to consider the structure of the organization.
- Look at the diversity in the following sectors as examples to illustrate the complexity and challenges of implementing an effective trade compliance program.

Consumer Electronics

Source: U&S Digital Consumer Electronics Service

CE Hardware Market*: Key Segment Breakouts



Product classification of convergent devices: Tablets versus phones

Classification – end-use vs function - entertainment/ICT device/medical

Software giving rise to additional functions

Varied product testing regs & reqs – NTB

Valuation for products with short lifecycle

Certifying origin for components and sub-assembly

Valuation & Definition for Free-of-Charge samples

Market demand in CE means :

- Retailers have to make sure that they have the right product on the shelf the right week .
- CE now includes a vast array of electronics which require a somewhat different supply chain. They are increasingly becoming fashion items (e.g., iPod, mobile phone), with much shorter shelf/product life than traditionally associated with CE goods.
- They therefore require faster move-through and improved inventory management, demanding more support from cross-border trade facilitation than previously.

Aviation Production and Sustainment

Climbing the value chain

Component manufacturing, the industry gateway



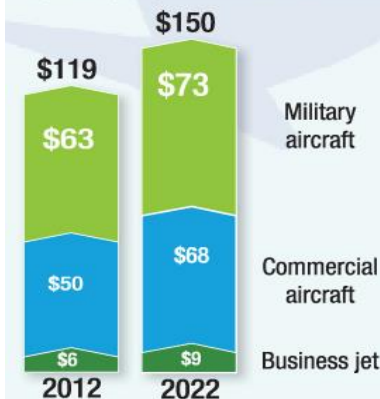
Availability, cost and customer service

Synchronized procurement and manufacturing

Maintenance, repair and overhaul

Inventory optimization and analytics

Maintenance, Repair & Overhaul (MRO)
A growing segment of the value chain, follows trends in new consumer markets



MRO Spending
2012 \$US Bil



MRO Market Share Shifts East
(Commercial)

Automotive MFG & AAM



Conditions:

Highly complex and multi-stakeholder operations.

JIT business processes,

Highly competitive market conditions

Regular crisis management situations – product recall, Sendai tsunami .

Affecting Factors:

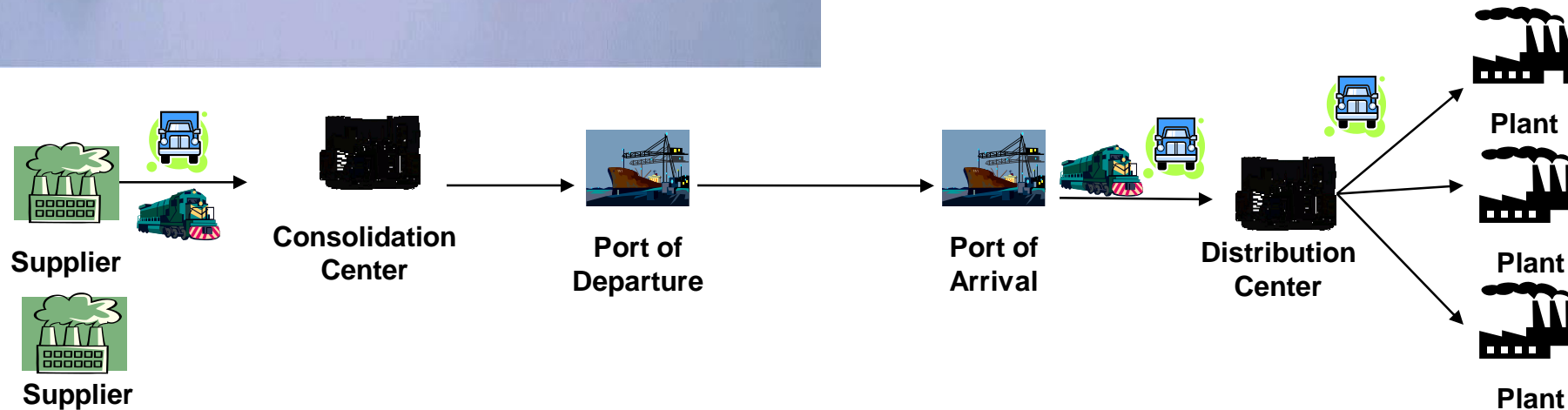
Valuation & overly complex procedures to return external packing

Traceability of End-use-relief “for” mfg

Multiple agency interaction

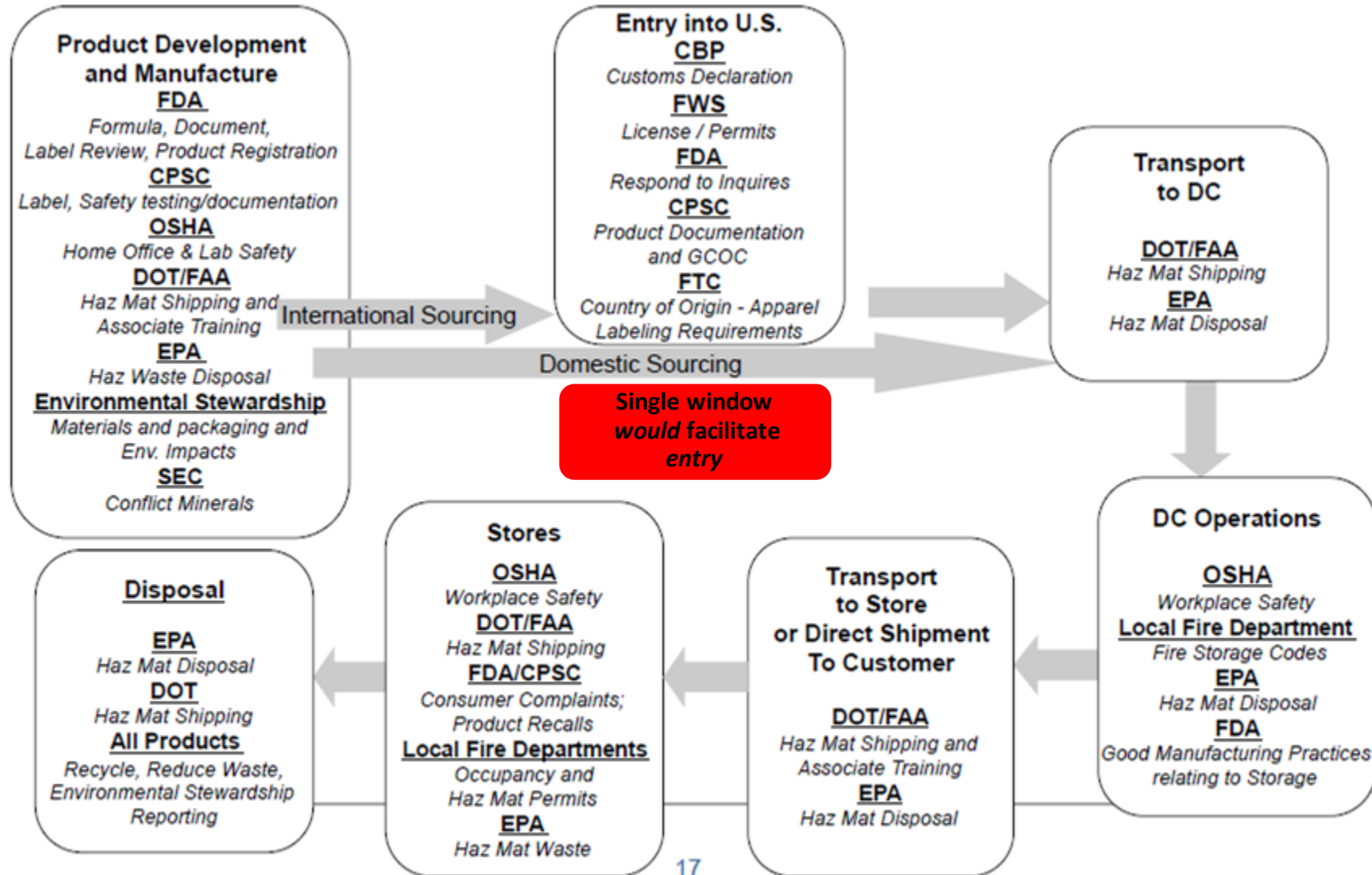
FTAs – automotive as a protected sector

FTZ conditions



Retail

Compliance and Environmental Stewardship is required
Throughout the Product Life Cycle



COMPLIANCE: HOW BUSINESS BENEFITS (The Basics)

- Avoidance of penalties is the most obvious “benefit” – they can be expensive! Still, it may be argued by some that the cost of compliance is greater than a one-time penalty, which can result in a mentality of “catch me if you can!”
- Compliance must go beyond penalty avoidance: a compliance strategy protects from profit margin erosion. When a transaction is correct, unexpected costs are minimized and landed cost calculations remain true.
- Errors or miscalculations found during self-audit or quality assurance checks by the importer may result in additional duty payable. The same errors found during a Customs audit will result in penalties and may affect an importer’s overall compliance record or status as a trusted trader.

CHOOSING TO BE COMPLIANT

- Traders want to be compliant - they want efficiency and predictability at the border and beyond, and compliance with Customs requirements is the best way to achieve this.
- The burden of compliance is a shared one, with businesses implementing compliance strategies, and Customs administrations investing in processes around post clearance audit that are transparent and fair.
- Audits cost money – dedicating time and people for a successful outcome is necessary.

CHOOSING TO BE COMPLIANT ... cont'd

- Reputation is important – an intangible asset for business. Poor audit outcomes may result in a poor risk profile which may affect current and future business opportunities.
- A record of poor compliance can negatively affect predictability throughout the supply chain, which is especially critical to “just in time” inventory operations.
- Poor performance on post-clearance audit may also result in delayed clearance/release of goods if Customs feel there is increased risk and a need to examine goods before they enter the country. This may result in additional costs and lost business.

CHOOSING TO BE COMPLIANT: SELF-AUDITS

- Business should also implement “self audits”, where feasible. A self audit can identify a changed condition that impacts valuation or origin, a clerical error, or a misapplication of a tariff treatment that can provide the opportunity for correction, and even limits the exposure to the error.
- Self audits can demonstrate that a firm is employing due diligence, and that the firm is ethical in its intent and the mistake is an honest one, and not malicious, or intentional – this changes the conversation in the event of a Customs audit.
- Self audits should be scheduled regularly, selecting a number of entries that statistically provides a good sampling and can be viewed with a critical eye. The company auditor must assume nothing, and use all of the information available, the same as a Customs officer would.

TOOLS FOR COMPLIANCE: A COMPLIANCE MANUAL

- A compliance manual outlines how decisions were reached, in terms of valuation, classification, and origin. This demonstrates that the importer has measures in place to ensure that the accounting information is accurate from the source data.
- Compliance manuals should be maintained for both imports and exports.
- Remember: a sound compliance program doesn't happen overnight and doesn't manage itself. It takes hard work, dedication and commitment to ensure it remains viable.

TOOLS FOR COMPLIANCE: A COMPLIANCE MANUAL

...cont'd

- In addition to a compliance manual, business should establish a procedure manual, or a “how to guide” to ensure compliance is achieved. It should contain checklists or flowcharts for employees that describe the processes that must be followed so that everyone is on the same page.
- A commitment to training and knowledge transfer is essential, to ensure compliance expertise is always available.
- This is easier to achieve in a centralized environment.

Sample of a Compliance Manual Table of Contents

- | | |
|---|---|
| 1. Notice of Penalty Assessment Procedure | 8. When Customs Requests Documentation |
| 2. Originating Goods Returned Process | 9. Special Import Measures Act (SIMA) |
| 3. Detailed Adjustment Statements (DAS) Procedure | 10. Trade Compliance Verification Audits (Customs and Self Audits) |
| 4. Maintenance of Records (what, how long, disposal methods) | 11. Tariff Rate Quotas (TRQ) |
| 5. FTA/PTA Certificates and Policy | 12. Voluntary Entries |
| 6. Post Entry Adjustments | 13. Tariff Classification Opinions (Customs rulings, customs broker opinions) |
| 7. Repair/Alteration – for originating goods, or goods under warranty | 14. Valuation methodology |
| | 15. Taxation Information & Policy |

TOOLS FOR COMPLIANCE: A COMPLIANCE TOOLKIT

Compliance managers will review business practices and examine specific elements. These might include recommendations and good practices relating to:

- Duty/Tariff Exposure
- Brand Degradation Risk
- Free Trade Agreement Eligibility
- Valuation/Taxation Implications
- Intellectual Property/Patent Protection
- Liability Exposure

HOW CUSTOMS CAN HELP WITH COMPLIANCE

In order to assist trade in being compliant, there are tools that customs can offer. These might include:

- providing Advance Rulings;
- publishing Advance Rulings;
- providing access to their Trade Verification Manuals;
- providing a list of their Verification Priorities; and
- publishing policies and keeping them up to date (example – HS tariff changes, 2017) regarding tariff classification, valuation, and origin determination.
- joint training

A GOOD PRACTICE: THE CANADA BORDER SERVICES AGENCY'S TRADE VERIFICATION MANUAL

- The CBSA (Canada Border Services Agency), upon request, will provide trade with a copy of their Trade Verification Manual (TVM). The TVM provides detailed procedures, guidelines and templates for CBSA's use when conducting verifications
- The TVM includes:
 - verification and reporting standards;
 - standards for conducting verifications;
 - how to plan and execute a verification; and
 - templates for communication.

CBSA's TRADE COMPLIANCE VERIFICATIONS

The CBSA manages compliance with tariff classification, valuation, and origin by using two types of post-release verifications:

- Random Verifications
- Verification Priorities

Random Verifications: designed to measure compliance rates and revenue loss and the results may be used for many purposes, including:

- risk assessment
- revenue assessment
- promoting voluntary compliance

Verification Priorities: Targeted verification priorities are determined through a risk-based, evergreen process, meaning that new targets are added throughout the year. Verification priorities may also be carried over from previous years.

CBSA's TRADE VERIFICATION PRIORITIES

Twice each year, CBSA publishes its trade verification priorities. This year, some of what they are looking at include:

- Curling Irons (Round 3)
- Spectacle Lenses (Round 2)
- Furniture for Non-domestic purposes
- Seaweed (Round 3)
- Dextrins and Other Modified Starches (Round 3)
- Disposable and Protective Gloves (Round 3)
- Batteries (Round 2)
- Footwear (\$30 or more per pair) (Round 2)

CBSA's TRADE VERIFICATION PRIORITIES ... cont'd

For compliance with valuation, CBSA are looking at:

- Apparel (Round 2)
- Preparations and Pastrycooks' Products

And for origin:

- T-Shirts (Round 2)
- Jewelry

CBSA's TRADE VERIFICATION PRIORITIES ... cont'd

At the end of a verification, CBSA provides additional information to the public. For example, the following was issued after a tariff verification of fresh cut flowers:

- The risk is that specific fresh cut flowers may be misclassified as “other” fresh cut flowers under tariff item 0603.19.00 which attracts a duty rate of 6%.
- Flowers specifically named in the Customs Tariff should be classified under their respective tariff items, which attract duty rates ranging from 8% to 16%
- Additional revenue is still expected from self-adjustments.
- Results confirm that many flowers specifically named in the Customs Tariff were misclassified as “other” fresh cut flowers.

THERE IS STILL ROOM FOR IMPROVEMENT...

CBSA's TRADE VERIFICATION OUTCOMES

- After a verification, corrections must be made, sometimes going back as far as four years.
- Corrections must be made within specific time frames, very costly to business and often revenue neutral.
- Incorrect declarations of tariff, value, or origin may result in penalties.
- Penalty amounts are based on whether the importer had “Reason to Believe” that the declaration was incorrect.
- Penalties range from \$150 up to \$250,000 in cases of repetitive errors that are not corrected within a specific time frame.
- Belief among trade that penalties are punitive, and not corrective (as stated by CBSA).

CUSTOMS BROKERS – PARTNERS IN COMPLIANCE

- A survey conducted by American Shipper found that importers who use a customs broker are more likely to use programs that minimize duty exposure.
- Those who don't use a customs broker may be unaware of these programs.
- What else might these importers not be aware of - the importance of compliance, and how to implement effective compliance strategies?

AN APPROACH TO BUILDING A COMPLIANCE STRATEGY

- Importers look to customs brokers as trusted advisors with experience in mitigating risk and promoting compliance.
- Clients expect customs brokers to manage much more than their importing/exporting business.
- Customs brokers share their compliance expertise with their clients to ensure that they have the necessary tools in place to support compliance and that the consequences of non-compliance are understood.

THE CUSTOMS BROKER AS AN ALLY IN COMPLIANCE STRATEGY

- Customs brokers can directly promote trade facilitation through knowledge, transparency and accountability. Their expertise is critical to implement risk management methodologies.
- Once companies determine or gauge their risk, protocols to mitigate risk can be developed and implemented based on the level of risk.
- Risk management is a component of trade.
- Risk management and trade facilitation strategies can be adopted by any company and once understood can provide the basis for a robust compliance program. In this context, risk management has a natural linkage with activities.

THE CUSTOMS BROKER AS AN ALLY IN COMPLIANCE STRATEGY ... cont'd

- While the importer is an expert in their business, a customs broker is an expert in theirs. A customs broker should be an integral part of a firm's overall compliance strategy, from the initial classification of goods all the way to an audit.
- A customs broker can be the first line of defense in being compliant and maintaining compliance. They are a partner in the supply chain and provide expertise and advice. A customs broker can ensure an importer's compliance by:
 - providing advice on tariff classification, value for duty, and any other relevant federal requirements;
 - ensuring that the importer understands their obligations and liabilities;
 - educating about penalties and the true cost of non-compliance; and
 - providing advice concerning refunds, drawbacks, and remissions.

THE CUSTOMS BROKER AS AN ALLY IN COMPLIANCE STRATEGY ... cont'd

- appealing Customs decisions on tariff, value, or origin;
- providing advice and assistance pertaining to penalties;
- advising the requirements of Other Government Departments;
- assisting in the development of compliance program manuals;
- performing an audit and identifying potential weaknesses in the compliance program;

THE CUSTOMS BROKER AS AN ALLY IN COMPLIANCE STRATEGY ... *cont'd*

- developing and/or maintaining a database using SKU (Stock Keeping Unit, usually included in a bar-code) level detail in relation to tariff classification;
- providing notification of changes to Customs policies that may impact the client;
- providing advice on security related programs or audit existing programs of the client; and
- providing or suggesting compliance training for staff.

MUTUALLY BENEFICIAL OUTCOMES OF A COMMITMENT TO COMPLIANCE: TEPE

Transparency: Uniformity within countries (multiple ports), of common procedures/training and execution

Efficiency: Shorter cycle times/clearance time, coordinated border management – single interaction with multiple agencies

Predictability: Operational and legislative

Engagement: Account based management, and effective consultative mechanisms

CUSTOMS AND BUSINESS – WORKING TOGETHER

- We encourage heads of Customs administrations to engage at an early stage with the trade community to build compliance programmes.
- Customs administrations do not exist in isolation but rather in an economic and political context with an ability to respond to fluctuating and unpredictable economic and market demands and changes.
- Customs and trade are partners in the protection of society and prosperity. Mutual engagement is a necessary pathway to successful development of compliance tools.
- Customs administrations around the world are working on facilitating trade, while at the same time maintaining a strong compliance posture.
- Centralized, consistent compliance strategies in both Customs administrations and the private sector can have a very positive impact on trade facilitation.

WHAT IS THE RESULT OF EFFECTIVE COMPLIANCE?

- Processing of shipments in a consistent, predictable, fast, efficient and cost-effective manner because they are considered legal, safe and compliant.
- Mutually beneficial and sustainable relationship between Customs and trade to support border integrity.
- Optimal conditions to make positive decisions on investment and sustainable growth.

THANK YOU

Carol West

cwest@ifcba.org

+1 623 562 3543