

Chapter 4. Customs and Border Protection: Expectations for Corporate Compliance

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4:1. Introduction

The privilege of importing into the United States has always been dependent on compliance with the laws enacted by Congress and the rules and regulations established by Customs and other federal agencies. The First Congress in 1789 began the process on July 4 with the Tariff Act of 1789 authorizing the collection of duties on imported goods. The fifth Act of Congress shortly thereafter established a Customs authority and the ports of entry. The Supreme Court affirmed “the power of Congress to determine what articles of merchandise may be imported into this country and the terms upon which a right to import may be exercised” over 100 years ago. [Buttfield v. Stranahan, 192 U.S. 470, 493 \(1904\)](#).

For more than 200 years after that first Customs Act, importers of merchandise into the U.S. were required to provide full and truthful information regarding the products they imported, but the application of all Customs laws and regulations to those shipments was exercised solely by the Customs authorities (although subject to judicial review). This division of obligations was dramatically restructured in 1993 with the enactment of the Customs Modernization Act. [Pub. L. No. 103-182, Title VI, signed December 8, 1993](#).

This Act provided for a “shared responsibility” between importers and the Customs authorities. Importers now must not only provide accurate and complete information on imports, but also use “reasonable care” to apply the applicable rules and regulations when submitting that information to Customs. Importers are now obliged to learn, understand, and apply the Customs laws and regulations to their Customs activities in the same way that a taxpayer is required to learn, understand, and apply the applicable tax laws when preparing a tax return for the Internal Revenue Service. The final word on how these rules and regulations are to be interpreted of course remains with Customs (although still subject to judicial review).

U.S. Customs and Border Protection (CBP) (formerly the U.S. Customs Service before its reorganization into the Department of Homeland Security in March 2003) has been very clear on the nature of actions and activities required of importers to meet this "reasonable care" obligation. While specific actions may vary depending upon the size of the company, the quantity and nature of the imported products, and the potential risks as viewed by CBP, all importers are expected to have formal written procedures governing their import process, including a method to verify their proper use and to incorporate updates as necessary. Internal controls are expected, both for day-to-day activities and the overall system, to ensure its continued viability. Owners, officers, and

directors are expected to understand these obligations and provide clear support for company personnel engaged in these activities.

On the traditional commercial side, importers are expected to have appropriate knowledge about their suppliers, the products being imported, and the origin of those goods. Sufficient procedures, including the employment of outside experts as necessary, to ensure correct classification, valuation, and marking for all products, together with an understanding of any applicable regulations or restrictions imposed by other government agencies, are expected. Following September 11, 2001, CBP has developed a range of programs concerned with homeland security, including the Container Security Initiative (CSI), Advance Cargo Declaration Requirements, Importer Security Filing (ISF), Free and Secure Trade (FAST), and the Customs-Trade Partnership Against Terrorism (C-TPAT). Although some of these programs are primarily the responsibility of the shipper--not the importer--others directly involve the importer, and importers must understand how all of the programs affect them and their role in maintaining the security of the United States.

CBP has made the basic actions required quite clear, but left it up to companies in the import business to determine how to perform these functions. Importing companies may differ on what internal department or section should have primary responsibility; on how other departments or offices are to be consulted and coordinated; on whether full-time Customs compliance personnel are required, or the responsibilities can be distributed to various employees on a part-time basis; and on whether to combine or split the responsibility for cargo security and commercial compliance. CBP recognizes that there are multiple processes by which compliance can be reached and that these will differ from company to company and industry to industry.

There are, nevertheless, some common threads and minimum standards. Some of CBP's expectations have been developed from observing the solutions devised by individual importers. Where approaches, systems, and arrangements have been demonstrated to produce high compliance levels, CBP begins to find "best practices" with regard to particular issues or industries.

In response to these Customs obligations, many companies, and generally at least some in each major industry, have established full-time Customs compliance departments, with one or multiple employees, and sometimes with a licensed Customs house broker brought on staff in-house. To an extent, at least for major importers, this type of organization has become expected by CBP. Companies that choose to organize their responsibilities differently, particularly those distributing responsibility on a part-time basis across multiple departments, face the burden of demonstrating to CBP that their system works as well as the full-time departments of other companies to ensure compliance with regard to that company's activities.

4:2. Best practices in commercial compliance

During the last two decades, CBP has developed extensive materials in the commercial compliance area regarding expectations for corporate activities. One of these is a document entitled "Best Practices of Compliant Companies," which outlines ten basic areas of expected activity. This is currently available on the CBP website on the page covering the Importer Self-Assessment Program, and is also reproduced as Appendix 1-B in this volume.

These practices apply to all companies, large or small, although specific implementation may differ. They suggest the degree of involvement expected from every company engaged in international trade in ensuring that its obligations as citizen, taxpayer, and importer are met.

1. The first activity listed in these best practices for a company is to have management's commitment to Customs compliance. This involves both a formal statement of corporate policy and action from the board of directors assigning both authority and responsibility to the Customs group.

2. The second practice is to state compliance and cost goals. This requires that a company identify and analyze relevant risks and develop goals to manage the risks. This necessitates a review of corporate Customs activities, determination of risk areas and consideration of how they should be managed, and methods to control weaknesses in a timely manner.

3. A third practice, emphasized at all levels, is the development of formal policies to ensure that management's goals and objectives are met. This includes formal written procedures on "how to" conduct the company's Customs activities, and internal controls to ensure that the procedures are followed. It also requires verification of the effectiveness of those policies and ongoing practices to make updates, changes, and corrections as needed.

4. The fourth best practice is to establish training programs to ensure that employees receive appropriate training and guidance on the nature and requirements of their responsibilities. Companies must identify the positions in various departments that will have information and input necessary to the Customs function and ensure that they are properly trained and incorporated in the process. Advanced training, including outside seminars and programs, for the core Customs group is also essential.

5. Internal controls involve both day-to-day processes--such as post-entry review of broker-created documents and filings--and activities intended to assess the performance quality of the internal controls themselves. Audits, both internal and external, are necessary to review Customs operations and ensure that the corporate policies are implemented and to take corrective action as needed.

6. The sixth listed practice is to create a Customs compliance group. For some companies, this may necessitate one or more full-time job positions dedicated exclusively to overseeing the Customs operations of the company. For other companies, the functions may be distributed among several individuals on a part-time basis, provided they are given the time and support necessary to meet the compliance responsibilities, have access to all areas of the company related to Customs, and provide a sufficient level of responsibility and access to ensure company-wide compliance. The Customs compliance group is responsible for ensuring open communication channels in all areas that may be involved in CBP processes, as well as establishing the control activities and self-testing processes to verify the internal control system, update policies and procedures as necessary, and provide necessary information to management to make informed decisions in the Customs area.

7. The next practice is to ensure access to executives for needed resources. The Customs group must be visible to top-level management, perhaps by being attached to the tax or legal department or division. Sales-oriented executives must be made aware of how the Customs process impacts their supply chain and affects their ability to conduct operations.

8. The eighth practice is to develop compliance requirements for suppliers. This process may well be tied to supply chain security as discussed below. For commercial compliance, it is

important to develop the necessary language for contracts, purchase agreements, and instructions to ensure the suppliers understand marking requirements, invoice details, the necessity of accurate documents, and activities necessary to ensure compliance with special requirements, such as the North American Free Trade Agreement (NAFTA) or other Trade Agreements, the Generalized System of Preferences (GSP), or other government agency requirements. Expectations by Customs will naturally differ for companies that have only one or a few suppliers, with whom the companies should be highly familiar; and those companies, such as mass merchandisers, which buy from hundreds of locations. Even in those situations, however, minimum standards and requirements to ensure compliance must be implemented.

9. The next best practice discussed is establishment of a record-keeping program. There are minimum record-keeping requirements established by regulation, both for specific records and specific pieces of information and for general support of claims to CBP. A best practice record system will extend beyond this minimum to form a complete audit trail, from production control to payment to CBP entry, with the ability to provide supporting documentation in a timely manner.

10. The final general best practice listed is to partner with CBP. This involves not only continued awareness of CBP activities and procedures, but also active participation in voluntary CBP programs, including security-related processes such as C-TPAT, CSI, and FAST, and commercial programs such as the Importer Self Assessment (ISA) and the developing Automated Commercial Environment.

Specific best practices tend to follow the above general best practices list with regard to written procedures, internal controls for monitoring feedback, assignment of individual responsibility, and management oversight. Specific subject-related issues are then added. For example, for valuation, best practices include the company's access to and knowledge of the U.S. Customs Valuation Encyclopedia and binding rulings on value; the use of accounting system links to Customs entry numbers; procedures to deal with specific issues such as freight and insurance deductions, assists, additional payments, and visa purchases; and proper information and records for sales commissions, royalties, packing costs, and proceeds of subsequent resales.

For classification, in addition to the basic best practices that include written procedures, internal controls, assigned responsibility, and management involvement, best practices include knowledge and use of binding rulings; consultation with CBP import specialists and/or private consultants; ensuring complete and sufficient merchandise description by vendors on invoices; training staff for classification of merchandise; maintenance of a database of classifications for the company's product line and the use of classification numbers on invoices; and the involvement of purchasing and/or engineering personnel in the classification of new items or parts. Similar specific practices apply for special programs (e.g., GSP, NAFTA, and U.S. goods returned), marking, quantity, other agency compliance, and other applicable issues.

Another source of information on CBP's expectations for importers in addition to the best practices list is contained in the extensive materials prepared for the Focused Assessment program. The Focused Assessments have replaced Compliance Assessments as the formal process in which a Customs audit team evaluates the compliance level of importers. A Focused Assessment is not an enforcement audit or a program intended to discover wrong doing, but an evaluation of a company's ability to comply with Customs requirements. CBP's stated goal is to maximize the number of importers who perform at high-compliance levels, thus presenting low risk of Customs

violations. This allows CBP to focus its efforts on noncompliant companies.

The complete and lengthy set of Focused Assessment materials, including the actual checklists used by CBP in conducting the review, is available on the CBP Web site at www.cbp.gov.

4:3. Best practices in cargo security

Following the events of September 11, 2001, the security of the United States has become the primary mission of CBP. The consolidation of border agencies such as the Border Patrol, the Animal and Plant Health Inspection Service, and the border inspection personnel of the Immigration and Naturalization Service has given CBP many tools to go with this responsibility. Programs include passenger screening, border enforcement, and document review for individuals. For commercial shipments, the primary concern is the potential for the introduction of weapons of mass destruction or other terrorist-related resources.

Previous cargo security activity by CBP largely addressed smuggling, primarily of drugs. This involved programs such as the Business Anti-Smuggling Coalition, a voluntary program whose members reviewed their entire process of manufacturing and shipping merchandise to reduce, if not eliminate, product vulnerability to narcotics smuggling. These reviews of packing and shipping practices, and the exchange of ideas among CBP and the import community, allowed importers to take both responsibility and specific action to stop narcotic traffickers from using legitimate business shipments to smuggle contraband. The expansion of these programs to combat possible terrorist infiltration of legitimate business shipments draws on past experience, including voluntary participation, use of "best practices," and extensive cooperation between CBP and the business community.

The primary partnership program developed by CBP for control of supply chain security is the Customs-Trade Partnership Against Terrorism (C-TPAT). This voluntary program is open to importers, brokers, carriers, warehouses, ports and terminal operators, third party logistics suppliers (3PLs) and consolidators, and, with certain limitations, foreign suppliers. It requires a formal commitment by the entity applying to the program, and includes a review of all supply chain activities and cooperation with CBP to improve security levels.

Since its initiation of C-TPAT, CBP has strengthened and expanded requirements for participation and transformed minimum security guidelines for most participants into minimum security criteria by category of member. Detailed information on the application process, security criteria, company profile requirements, and validation procedures are set forth on the CBP website. CBP has periodically published "Best Practices" catalogs listing specific procedures and holds regular conferences for participants.

C-TPAT is, of course, not the only supply chain security program. Many are mandatory, including the Importer Security Filing and Advance Cargo Declaration, which require the importer and carrier, respectively, to report cargo information for review prior to shipment of merchandise, and the Container Security Initiative, which monitors shipping containers in foreign ports prior to movement to the US. Others are voluntary, like C-TPAT, the Free and Secure Trade (FAST)

program administered with the Canadian Border Security Administration for land border shipments, and newly developed programs for Mexican border movements.

CBP has indicated that companies that do not participate in C-TPAT are nevertheless expected to be aware of and take appropriate actions with regard to their supply chains. One such indication is the inclusion of a Supply Chain Questionnaire as part of a Focused Assessment for any company not participating in C-TPAT. The Questionnaire seeks information on corporate actions relating to business partner security, container security, physical access controls, personnel security, procedural security, security training and threat awareness, physical security, and information technology security.

Early in the program, Customs outlined general "best practices" for supply chain security, including C-TPAT members. Unsurprisingly, many of the same practices found in the commercial enforcement area are, with appropriate modification, also applicable in cargo security. Although these specific guidelines, summarized below, are no longer on the C-TPAT webpage, they remain relevant for all importers whether or not they participate in C-TPAT.

1. The primary best practice is securing executive management participation. This includes awareness of the programs and the reasons for participation and formal expression of the company's commitment to security procedures both for purposes of national security and for the benefit of the company.

2. The second best practice is for management to assign responsibility for participation to a specific individual or position and ensure that adequate support is provided. This entails not only the manpower and resources needed to conduct reviews, evaluate risks, and prepare required documents, but, in addition, ensuring that the affected personnel, departments, and service providers are informed of the program's importance to the company and the necessity of full cooperation. One issue for companies to consider is the extent to which the company's C-TPAT operations must be coordinated with, if not run by, the personnel responsible for commercial compliance.

3. A third best practice is to ensure that the company's response to CBP's initial and any follow-up supply chain questionnaires is comprehensive (physical security, personnel security, process security, data security); is fully evaluated to identify risk concerns and areas of needed improvement; and results in formal, written policies with specific procedures and appropriate internal controls to ensure their implementation.

4. Cargo security is a continuing and ongoing concern, and the company's responses must include continual awareness of new issues and new programs, as well as regular updating based on changes in the supply chain and weaknesses discovered in the company's procedures.

Many of CBP's other major cargo security programs are directed primarily at carriers and shippers, rather than importers. These include the requirements for advance electronic filing of cargo declarations, with different deadlines depending upon the mode of transportation; the CSI, in which program U.S. CBP personnel are physically located at major foreign container shipping locations, conducting preloading reviews in cooperation with the local authorities to identify suspect shipments prior to their being laden for export; and FAST, a program for land border shipments that allows expedited clearance for products when all of the parties in the supply chain are C-TPAT qualified and truckers have appropriate identification filings with CBP. Importer C-TPAT participants who have properly conducted a supply chain review would necessarily be aware

of these programs, including the necessity for timely and complete information on products to be provided by their suppliers and the responsibility of carriers to properly supervise shipments. This knowledge will aid importers in developing smoother supply chain logistics.

5. CBP considers C-TPAT participation by importers by itself to be a "best practice." CBP's recognition of the importance of supply chain security has caused CBP to require C-TPAT participation (although the program itself remains voluntary) before importers are considered eligible for certain other programs, including commercial compliance related programs such as the ISA and cargo security programs such as FAST.

4:4. What does Customs and Border Protection expect?

The "reasonable care" standard required of importers has been developed over the last two decades to the point where CBP has established specific norms and guidelines expected of importers. These expectations begin with corporate management-level involvement in, knowledge regarding, and understanding of the importance and extent of Customs matters; and extend to the need for written policies and procedures, assigned responsibility, internal controls, personnel training, record keeping, and involvement with suppliers as well as CBP. A clear allocation of responsibility to a Customs compliance group--although the size and nature of the group will differ depending upon the size and nature of the importer--is necessary. CBP has indicated that "reasonable care" means full involvement by a company -- making good faith efforts to ensure compliance and establishing responsibility within the company for the Customs function. Each importer must, within these expectations, address these issues as best fits the company organization.

Numerous resources are available, including the referenced materials from CBP, as well as materials produced by law firms, consultants, and Customs brokers.

In addition to the CBP Web site www.cbp.gov, see the links on the American Bar Association Customs Law Committee site at <http://apps.americanbar.org/dch/committee.cfm?com=IC712000> and related links on the American Association of Exporters and Importers site www.aaei.org.

What is essential is for corporate management to recognize its obligations and ensure the establishment of the necessary policies, procedures, and controls expected by CBP. Failure to do so may subject a company to increased scrutiny by CBP, resulting in delayed shipments, additional costs, and possible enforcement actions. Incorporation of Customs responsibilities into related areas, such as corporate controls over financial reporting, may also be necessary to ensure compliance with the Sarbanes-Oxley Act and other legal requirements.

The author has written a series of articles on Customs compliance issues exploring these themes, which have been published in Thomson/West's CORPORATE COUNSEL'S INTERNATIONAL ADVISER beginning in 1997. Most of these articles can be accessed on the author's Web site at www.swbakerlaw.com.