



**The Institute of Brazilian Business  
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**The Minerva Program**

***U.S. Customs Trade Compliance and  
Risk Management Process:  
A Model for Brazilian Customs Modernization***

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*“Customs Administrations play a vital role in the growth of international trade and the development of the global marketplace. The efficiency and effectiveness of Customs procedures can significantly influence the economic competitiveness of nations.*

*In a highly competitive world environment, international trade and investment will flow toward efficient, supportive and facilitative locations. At the same time it will rapidly ebb away from locations, which are perceived by business as bureaucratic and synonymous with high costs.*

*Customs systems and processes must not be allowed to serve or be perceived as a barrier to international trade and growth.*

*Modern production and delivery systems, linked with the dramatic potential of new forms of electronic commerce, make swift and predictable Customs clearance an important prerequisite for national prosperity.”*

**World Customs Organization – WCO**

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## **Introduction**

The Globalization process, leading to an extraordinary increase in the international flow of people, goods, capital and information, changed radically the role of the government in the last decade of the 20<sup>th</sup> century. Government performance review has pushed up toward reform and modernization. The governance is more and more a strategic issue that must be dealt by all the nations.

In this scenario, with the increasingly importance of the international trade, Customs Organizations play a key role. Customs procedures have a powerful impact on the economic competitiveness, and the modernization of its procedures must be a target for any country. A modern efficient Customs operation can contribute to domestic priorities, facilitate trade, and address complex international issues. Customs should not jeopardize the prosperity of the nation by driving away business and investment.

So, Customs Organizations, in this new environment, must be more effective in the protection of the economy, but, at the same time, must act in order to encourage the economic growth. And, in order to achieve these two apparently contradictory objectives, one of the most important tools, is the Trade Compliance and Risk Management Process.

In this Final Paper, after discussing some aspects of globalization and its consequences in governance and in Customs activities, we will briefly describe the U.S. Customs Trade Compliance and Risk Management Process. Our goal is to pose a possible model for the same process in Brazilian Customs. However, it is important to say that each country has its specific characteristics and that must be taken that into consideration in the implementation of a Trade Compliance and Risk Management Process.

In order to have a better understanding of this Final Paper and its goal, it will be useful make a brief overview in the structure of this final paper, summarizing the content of each chapter.

In the first chapter, we will say some words about the Globalization Process, its definitions and different aspects. The focus will be some economic consequences of globalization and its influences in the role of the government. This discussion will proceed in the second chapter, speaking more specifically about the changes in the roles and the importance of the Customs Organization in this new scenario.

In the third chapter, knowing what are the new challenges of the Customs Organizations, we will discuss the need of a modernization process in Customs. In the forth chapter point out that a Trade Compliance and a Risk Management Process are the best tools to achieve success in facing this new challenges.

In the fifth chapter, the theme will be the U.S. Customs Modernization Process. We will do a brief overview in this process, and, in the sixth chapter, describe with more details the Trade Compliance and Risk Management Process of the U.S. Customs, the core of that modernization process. This description will be completed in the seventh chapter where we will see some practical cases.

In the conclusion, we will try to summarize the main ideas of the paper and briefly discuss the need of an introduction of a strong, uniform and general Trade Compliance and Risk Management Process in Brazilian Customs.

## **First Chapter**

### **The Phenomenon of Globalization**

One of the most important phenomena of the modern world is Globalization. Globalization is one of the central concepts in current analysis of the economy and society. The term was first used more than 40 years ago, and, in the early 1990s, the term was little used. By 2000, no speech was complete without it – even if those who used the term agreed on little more than the fact “that we now all live in one world”.

So what does Globalization mean? Most often, the term is synonymous with the extraordinary expansion of the global market place, and increasing interrelationship of individual and countries lives and futures, including politics and economics issues. Also there is a perception, and often a reality, of globally integration of communication (as telephony, Internet; airline networks), culture (as literature, movies, popular and classical music), entertainment (as sports and television), and economics (trade, capital flows, integrated production). However, globalization is much more than that. It is an ideology that defines basic expectations about the roles and behaviors of individuals and institutions.

At the core of the globalization movement, the communication revolution has strongly developed over the last decade: a lightning-fast communication, especially the Internet, meaning the speeding up of communications. In fact, many communications improvements have been taking place over the last century, but the contemporary speed of change, the enlargement of capacity for information transmission and the proliferation of communications media have not been experienced before.

In an economic perspective, globalization is viewed as a process that can lead to a fully internationally integrates markets, with free movement of goods, services, labor and capital. Thus a single market in inputs and outputs and full national treatment for foreign investors (and nationals working overseas) so that, economically speaking,

there are no foreigners. It can be “the borderless world”, radical progress and modernity, and of life beyond the limits of the traditional nation-state.

So, what we perceive is a “liberalization revolution”, a freeing up of markets and reduction in the role of government in terms of ownership and control over production of goods and services, with a process going to a free movement of goods, services, labor and capital. It’s true that the globalization has been significantly retarded by the combined impact of autarkic-protectionist trade policies in many developing countries (though a considerable number of these are now being liberalized), and discriminatory trade barriers (tariffs, quotas and VER - Voluntary Export Restraints) rose against their products in developed countries.

But the process continues as has been manifested in successive rounds of multilateral and regional trade liberalization. In the world, the economic integration, within the framework of Free Trade Agreements or Customs Unions, has been a major force in reform, and international liberalization has resulted in booming trade volumes, as we can see in Tables 1, and 2.

**Table 1 – Comparison between the growth of Total GDP and Total Imports of the world, in 1990, 1995 and 2000 (considering 1990 equal to 100).** - We can see that, during the last decade, the percentage of growth of the international trade (88%) is bigger than the percentage of growth of Gross Domestic Production (25%) in the world. This fact shows how international trade is growing exponentially with the globalization process.

<b>Years</b>	<b>Total GDP in the World (1990 = 100)</b>	<b>Total Imports in the World (1990 = 100)</b>
<b>1990</b>	<b>100</b>	<b>100</b>
<b>1995</b>	<b>107</b>	<b>147</b>
<b>2000</b>	<b>125</b>	<b>188</b>

*Note: Data from World Trade Organization Internet Site*

**Table 2 – The Amount of Exports and Imports in the World and some selected regions, in the years 1980, 1990, and 2000 (in billion dollars).** – In this table, we can see how the international trade increased throughout the world, imports as well as exports, between 1980 and 2000, in absolute numbers.

Regions	Exports (US\$ billion)			Imports (US\$ billion)		
	1980	1990	2000	1980	1990	2000
World Total	2,035	3,442	6,364	2,075	3,542	6,669
North America	294	522	1,058	320	641	1,504
Latin America	110	147	359	123	130	388
Western Europe	816	1,637	2,441	926	1,700	2,567
Asia and Oceania	324	792	1,828	351	762	1,661

*Note: Data from World Trade Organization Internet Site. The differences between imports and exports in the World exist in the site and, probably, are due to errors in data collection. Anyway, they are useful to give an idea of the great increase.*

**Table 3 – Percentage of Growth in Exports and Imports, in the World and some selected regions, between 1980-2000.** – Observing the percentage of growth in the international trade between 1980 and 2000, we can foresee the challenges the Customs Organizations will face in this new millennium to contribute to the development of the nations.

Regions	Growth in Exports (%)	Growth in Imports (%)
	1980-2000	1980-2000
World Total	212.73	221.40
North America	259.86	370.00
Latin America	226.36	215.45
Western Europe	199.14	117.21
Asia and Oceania	464.20	373.22

*Note: Based in data from World Trade Organization Internet Site.*



More than the increase of international trade, the economic globalization happens on capital movements. That also influences the trade, for example, in the role of the multinational companies, moving towards internationally integrated production in some fields. And we have also the, maybe the most truly global market – in the sense of globally integrated systems and complete economic integration – resulting in instant mobility of capital and globally uniform prices: the financial markets.

The broad picture is clear: world trade in goods and services, foreign direct investment and increased financial flows all suggest growing interdependence, and this interdependence affects all the society. And the government is not out of that environment, on the contrary is on the frontline.

## **Second Chapter**

### **The Globalization and the New Role of Customs**

There are several specific ways in which the globalization is having profound implications for the way in which business is transacted and the way government is organized and structured. All these ways have cumulated into a fundamental transformation of governance, a transformation that poses substantial challenges for public institutions and how we manage them. And, it's important to say, there are good reasons to believe that a reversal in this tendency is highly unlikely, though not impossible.

The performance of any Government, it's to say, its effectiveness, efficiency, responsiveness and accountability, depends on facing all this changes in the environment and preparing to the future. Globalization defines the agenda for governance in the early twenty-first century. It's a challenge for government, not only to devise new strategies for managing public programs effectively in a globalize policy world, but also to build the capacity for doing so.

National economies are, also, more and more interconnected, as customs duty rates are dropping worldwide and as the cross-border information flows is increasing, whatever the policy-makers want it or not. For example, there is growing trade over the Internet, because electronically driven commerce – the e-commerce. And, the cost to industry of government processing is becoming an issue of greater concern to government, international organizations, and business.

On the other hand, all this process of freedom of movement has also contributed to increase the rate of many security problems for a nation. As the barriers to commerce come down, it becomes more difficult to stop traffic in goods, or services, organized crime, terrorism, immigration, fraud, contraband, smuggling, and intellectual property rights violations, all crimes related with the Customs Organizations.

Customs organizations throughout the world hold a unique a position within a country's government and within the international community. Customs is often the first contact foreign businesses and travelers have with the government. A satisfactory encounter with customs can encourage continued commercial activities. Therefore, Customs, as an agency positioned on a country's international borders, looking both inward and outward, is facing a challenge of working protect the national economy while help to encourage dynamic solid economic growth.

Customs administrations have always had to meet the challenges of rapid smooth and secure processing of goods clearance operations. Now more than ever before, one of the key goals of Customs is to reconcile the facilitation and control of trade, whilst protection our society. Customs is currently faced with two major challenges: processing the expedient growth in legitimate trade and combating an array of threats to our national security.

Thus, globalization affects Customs activities with the increasingly demand of government, importers, exporters, brokers, travelers, carriers and the society for higher revenue, faster service, more reliable information, better statistics, increased protection of economy, environmental and agriculture controls, and improved enforcement performance. At the same time, with the explosive growth of international trade, in terms of volume and complexity, travels, and tourism, there are additional pressure on the customs organization, budgets and staffing, so that is putting the capabilities of all customs services to the test.

In its most simple terms, we can say that the goal of customs is to ensure that all imports and exports comply with laws and regulations. In other words, Customs must, with a comprehensive, responsive, and timely action, create responsive knowledge management capability in order to increase compliance with the laws of a nation at its borders. In Table 4, there is a summary of the main customs functions.

**Table 4 – The main functions of the Customs Organization in the globalize world are the following.** – To better serve the nations, the Customs Organizations must be efficient and effectiveness in dealing with these functions.

<b>The Main Roles of the Customs Organizations</b>
<b>Assess and collect all appropriate duties, taxes, fees and penalties due on the foreign trade, protecting the government revenue.</b>
<b>Facilitate legitimate trade, travel and tourism.</b>
<b>Interdict and seize trafficking in narcotics, other contraband, and smuggling.</b>
<b>Combat intellectual property rights violations, frauds, and money laundering.</b>
<b>Enforce the protection of environment, health and public safety.</b>
<b>Promote a uniform and transparent system for Customs Organizations.</b>
<b>Processing persons, baggage, cargo and mail according with the laws and regulations.</b>
<b>Collecting accurate import and export data for compilation of international trade statistics.</b>

### Third Chapter

#### The Need for Modernization of Customs Services

The Modernization of the Customs Services is the way to achieve excellence in Customs procedures, in order to face this new scenario on the World economy. Taking account of the lessons of the past and the realities of the present, the governments must shape the future of the Customs.

In this modernization process, the automation plays a very important role. Many countries, including United States and Brazil have already developed automated systems in the import and export procedures, as noted in Table 5. We will talk about the U.S. Customs automated systems in a following chapter.

**Table 5 – The Main Automated Systems in Import and Export Procedures in United States and in Brazil.** – In this table, we can note that both countries, United States and Brazil are working on the automation of their international trade procedures. The main difference is that Brazil doesn't have a Passengers System.

	United States	Brazil
<b>Imports</b>	Automated Commercial System - ACS (since 1984), and Automated Commercial Environment - ACE (since 1998, is in process of replacing the ACS)	Siscomex - Foreign Trade Automated System – Imports (since 1997), and Mantra – Manifest Cargo and Inbound System (since 1995)
<b>Exports</b>	Automated Export System (AES)	Siscomex - Foreign Trade Automated System – Exports (since 1994)
<b>Passengers</b>	Automated Passenger Inspection System (APIS)	-

But, more than simply automated of the procedures, the path Customs must follow is its use to increase reliance on the use of intelligence as a tool for greater selectivity in the inspections and audits. Automation will have very significant benefits for Customs, as the administration of the future will rely on accurate and timely information in order to carry out its function, with more accurate and timely statistical information.

Many Customs administrations are also embarking on a new era of performance measurement as a way of guiding the effectiveness of their initiatives and efforts that will increase the demands for risk assessment skills. They are introducing management audit as a means of quantifying the movement of goods and travelers to aid the allocating resources and to measure results. Total Quality Management philosophy and practices will play a pivotal role in Customs managerial practices in the years ahead.

In this new philosophy, developing industry partnerships is another target. It means that Customs must remove barriers to get closer to their customers. Customs administrations have to change the way they conduct business, taking the position that importers and exporters are customers and must be treated as partners, not adversaries. Not only improving service to customers is a major challenge, but also to improve importers, exporters, brokers and carriers compliance.

A Prior Disclosure Program, for example, can stimulate the compliance, because makes the participants of the foreign trade work together with the Customs Service. The goal is higher compliance, it is to say, to have a permanent process where the trade entities establish procedures or evaluate existing procedures to maximize trade compliance.

Partnerships are important not only with the importers, exporters, brokers, and carriers, but also with other government agencies and closer co-operation between Customs administrations themselves. The World Customs Organization – WCO stimulates this dialogue, exchange and sharing of information between Customs officers

throughout the world. For a closer relationship it's essential the acceptance and implementation of international customs standards on value, classification origin, and procedures.

So, as technology plays an increasing role in the Customs procedures, the adequate management of that information becomes of critical importance. It is currently necessary to assist the Customs data management, in order to change the face of Customs enforcement with the emphasis on flexible, risk based and targeted operations accentuated intelligence as the principal weapon to identify fraud and smuggling and the effective deployment of limited human and technological capital. As Customs administrations seek to maintain and increase their efficiency and effectiveness, risk management, which allows for better targeting their resources towards those areas where most warrant attention.

By using the principles of risk management, based in a process of trade compliance, Customs administrations will be able to demonstrate ensure the best available outcomes for the country within the constraints of the resources they are given. The importance of risk management is in using strategic intelligence to support the effective achievement of organizational objectives. In the enforcement context, strategic intelligence will provide Customs Administrations with a timely insight of current and emerging trends, threats to public safety and avenues for change to policies, strategies and legislation.

**Fourth Chapter**  
**Risk Management as the main tool for**  
**Modernization of Customs**

Risk is the key word. We experience risk is a common part of daily life. There is uncertainty in almost all aspects of day-to-day living. Risk is characterized by the fact that is partially unknown, increases with lack of knowledge, changes with time but is manageable. Managing these risks is a natural reaction to minimize the level of potential harm that comes with not knowing what the future might hold. In Customs, we can define risk as the degree of exposure to the chance of non-compliance, which would result in loss or injury to trade, industry, or the public.

Risk Management is equally common, since we have an instinct to reduce potential problems and take advantage of opportunities and the Customs' employees in the daily work practice it. The challenge is to practice it in a more uniform, systematic, and disciplined manner.

This new environment that Customs Services are now facing must point that there is no sense at all in use the finite technological and human capital to perform limited inspections and reviews on all the imports, for example. The fact is that we can perceive, based on our own experiences, that some importers and some imports present a much more significant risk than others, therefore, it's clearly more effective to perform extensive, thorough reviews on a smaller percentage of imports.

So it is wrong to think that all importers, and therefore all imports, are some how deficient and result in a loss of revenue or present a threat to the government and public. Customs has accepted the fact that many importers have an act of complying with import laws and do not present a risk that justifies a significant allocation of resources. Customs administrations must focus on what presents the greatest risk of



loss to the government and public. This logic leads to performing a risk analysis or risk assessment to determine who and what merits attention. To contend with new reality, Customs has to turn to the principles of risk management. Risk management can, with the help of new technologies, facilitate enforce in a dynamic new era of global trade.

Though the Customs Risk Management process, we constantly analyze information to determine what merits attention. Customs can consciously dedicates more resources to some areas and less to others. Whether an importer's cargo is inspected at the port, or supporting documentation is reviewed afterwards, all findings of compliance as well as violations are recorded and analysed within the Risk Management Process. This process segregates the significant violations and focuses human capital on the most serious problems. Customs can systematically diminish its oversight of compliant companies and dedicate more resources to non-compliant companies.

Risk Management is a logical response to committing limited human capital to ever-increasing foreign trade and tourism, with consequences in a higher number of arriving passengers, cargo, and conveyances. It uses the principles of statistics to assist in identifying targets having the highest likelihood of success based upon a commitment of resources to examine or inspect.

Risk management is a method of managing that concentrates on identifying and controlling events that have the potential to cause significant problems. In Customs trade terms, it means identifying those imports that represent the greatest risk of non-compliance so that we can focus our resources in those areas. The Risk Management process is repeated continuously. Each time new data is added, and the analysis and actions are refined. Each data collection cycle is more focused and more effective than the one that preceded it. Available data guides today's decisions. Data collected today becomes tomorrow's starting point for risk management.

The key to effective risk management lies in the data. It is not only crucial that the initial data be complete, accurate, and timely, but that the results of our actions – both

positive and negative – be captured, recorded, and fed back into the process. Without tracking and reporting our efforts, the risk management wheel goes flat, the process stalls, and we never make forward progress. A good risk management process recognizes the results of your efforts. If a process requires that you only write down your “hits” and not your “misses”, then that process never tells the complete picture of the work performed at each location.

The purpose of risk management is to reduce the gap between the things that we know and those we don't know. A Risk Management Program then must increase the knowledge about some subject, and with this knowledge reduce the uncertainty in the procedures, and change behavior and actions. The use of the risk management allows us to operate and make decisions more efficiently and effectively. But, to be truly effective, the Customs Risk Management Process needs to be practiced throughout the Service. If it is uniform, systematic, and applied in disciplined manners, the process will work for everyone.

In order to understand better how a Risk Management Process works, we will try to summarize the United States Modernization Process and, more specifically, the Trade Compliance and Risk Management Process.

## Fifth Chapter

### The U.S. Customs Modernization Process

Originating in the 1789, the U.S. Customs is the oldest Federal agency with in the executive branch of U.S. government. And it was also, for nearly 125 years, until the income tax was implemented during the First World War, the main source of revenue for the federal government and, even now, it is one of the more important agencies in collecting revenue to finance the government expenditures.

U.S. Customs, regarding national security, is at the forefront of efforts to protect the United States from smuggling, contraband, terrorism, drug trade, trafficking of weapons, and strategic materials, or adulterated food, and unregulated medicines. It plays also a vital role in the combating economic crimes including intellectual piracy, money laundering, and commodity dumping. On a typical day, the U.S. Customs examines a huge amount of passengers, aircraft, truck, containers, vehicles, and vessels, as showed below in Table 6.

**Table 6 – A Day in the Life of the U.S. Customs Service** – Above we have the amount of inspections and examinations on a typical day in U.S. Customs, in October, 2000.

Item	Quantity
Passengers	1.3 million, approximately
Aircraft	2,661
Trucks and Containers	60,196
Vehicles	348,205
Vessels	522
Entries	59,055

*Note: Data from U.S. Customs Service Internet Site.*

So the U.S. Customs Service mission is diverse, with many functions. In order to face all this challenging functions, keeping in mind that it must not jeopardize the legal trade and tourism, the U.S. Congress, in 1993, approved the Customs Modernization Act – as a part of the North American Free Trade Agreement (NAFTA). This act, known as “Mod Act” established a broad and simple goal: to develop an organizational structure that would enable the U.S. Customs Service and its employees to make their maximum contribution to the development and protection of the U.S. economy.

It was concluded that the scope of mission challenges facing the Customs Service, it would be necessary to transform Customs’ culture to one focusing on People, Processes and Partnerships. The new culture would characterize by: improving the skills and the action of the employees; managing essential core processes; serving the legitimate needs of Customs’ many customers as the focus of the organization’s process management efforts; and forming partnerships as a means of meeting improving Customs’ mission performance.

In others words, U.S. Customs decided to redefine its core processes, moving to a risk management approach centered on these processes. Customs must identify its customers and their needs, developing methods for defining customers’ needs as process goals and stimulating the their compliance. And it must, finally, improve its workforce through an elevated Human Capital Management program.

But to manage to do that, the automation of procedures is vital. Not only with technological tools to proceed more profound and less intrusive inspections and examinations of cargo and passengers, but also with automated systems. In the first point, the U.S. Customs is provided with a great quantity of equipment, such as Body Scanners, Radiographic and Reflective Energy Imaging Systems, in the most important ports, airports and road offices.

The U.S. Customs Service develops, and is still developing, also, the automation of all the procedures within the process of import, export, cargo and passengers. The

main goals are to reduce costs and bureaucracy for importers, exporters, carriers and brokers, increasing their compliance, and to maximize Customs' actions, creating a data bank reliable to implement the Risk Management Process. In the Table 7, we have a summary of the most significant systems.

**Table 7 – The main U.S. Customs Automated Systems** – In this table, we have some commentaries about the main automated systems in the U.S. Customs.

<b>Systems</b>	<b>Commentaries</b>
<b>Automated Commercial System (ACS)</b>	<b>ACS is the old Import processing system of U.S. Customs, with more than 17 years old. The Automated Commercial Environment System (ACE) is replacing it.</b>
<b>Automated Commercial Environment (ACE)</b>	<b>The implementation of ACE, in substitution of the ACS, is introducing major efficiencies in the way both Customs Inspectors and the trade address the arrival of merchandise, providing significant benefits to Customs field operations personnel, the importing community, and most importantly, the U.S. economy. The goal is paperless imports in all modes: air, sea, road, railroad.</b>
<b>Automated Export System (AES)</b>	<b>AES related information from exporters and is used to identify violators of export laws. AES facilitates quick and efficient exporting by eliminating inaccurate information, filling our paper forms and duplication reporting.</b>
<b>Automated Passenger Inspection System (APIS)</b>	<b>The APIS is used by the U.S. Customs to obtain traveler information prior to the arrival of the aircraft. It's a strong tool for the Risk Management in the airports. It's a joint operation between Customs and air transport community, and almost 80% of the air carriers are participating of this system.</b>

Another very significant program that U.S. Customs Service is sponsoring, in order to increase the partnership with other Customs Administrations, is the G7

Initiative. Since 1996, the G7, Group of Seven Developed Countries – U.S.A., Canada, Japan, Germany, United Kingdom, France, and Italy - is working to standardize the data required by Customs to develop a common electronic message structure. Today, although the import and export processes are similar in these countries, different information and reporting formats are required by each Customs.

The main idea is to standardize the electronic message structures, using the UN-EDIFACT standard (United Nations Electronic Data Interchange for Administration, Commerce and Transport), allowing the Customs Services of each of these countries to cross the information of imports and exports between them.

## **Sixth Chapter**

### **The U.S. Customs Risk Management and Trade Compliance Process**

The U.S. Customs Service has established a Risk Management Process to best allocate available resources to our priorities. Operating this way is a necessity for U.S. Customs, because, with limited resources and dynamic growth in trade, the number of potential violations will continue to out pace the number of Customs employees. This greater volume combined with increased trade complexity makes our deployment of resources vitally important.

Increase in land, sea, and air traffic entering the U.S. is steadily increasing and outpacing the growth of Customs resources. With approximately 20,000 personnel located at more than 300 ports of entry, and, annually, more than 480 million passengers and close to \$1 trillion in imports cross U.S. borders, Customs has reorganized to establish a system focused enforcement utilizing methodologies geared to maximizing port effectiveness and integrating core operational processes.

To confront these changes, Customs established a Trade Compliance and Risk Management Process. In the imports, for example, this includes every activity related to trade from pre-import analysis through cargo arrival, examination, release, investigation, revenue collection, liquidation, and archiving of trade data. There is a changing on the focus from transactions to accounts; it's to say, not in the import itself, a focus in industries and a compliance measurement and assessment action, and a continuous feedback process. Focusing in the account, not in the imports, and using the risk management, the U.S. Customs can use more efficiently its resources.

This is the genesis of the U.S. Customs Service Risk Management Process for trade. The U.S. Customs Risk Management Process for trade consists of four key steps, which we will analyze briefly:

- 1) Collect Data and Information
- 2) Analyze and Assess Risk
- 3) Prescribe Action
- 4) Track and Report

### **1<sup>st</sup> Step - Collect Data and Information**

Proper risk management requires a systematic approach to collecting data. Risks cannot be assessed or managed until data is collected and the risks can be identified and described. The collection methods must be statistically valid. If the data is sound, it serves as a strong foundation for accurate analysis, but if that data is faulty, it can seriously undermine our ability to obtain positive results.

The collection of data and information related to the Trade Compliance Process is the first step in the Customs Risk management process. Through the collection of data, Customs can begin to identify which importers are most likely to be non-compliant and the probable nature of their non-compliance. Proper use of this knowledge will assist in effectively distribution of the resources. Through this collection, Customs is able to establish base lines, comprehend its universe of trade imports and maintain a historical perspective of trade patterns.

In others words, in this first step, Customs is attempting to identify any potential risk in the Trade Compliance Process, isolating it. The key to risk identification is to systematically review the entire process. Risks cannot be assessed or managed until they are identified and described in an understandable way.

Customs has several mechanisms in place to identify risks in the importation of trade. The Compliance Measurement and Compliance Assessment of the traders, importers, and brokers, as a part of the Integrated Trade Measurement System is the center of this first step. In order to efficiently measure and assess the compliance, it is important to use the Account Management, based in national criteria.



## **2<sup>nd</sup> Step - Analyze and Assess Risk**

The next step is to analyze the data and determine the likelihood of non-compliance. After collecting the data, the next step is to analyze the data and determine the likelihood of non-compliance. Analyzing historical data and trends, and applying definitions of significance and materiality, allow Customs to narrow its focus on areas of the greatest potential risk, and for that employee specialization of knowledge and experience are very important.

After this analysis, some level of risk can be assessed. This part of the Risk Management process has evolved rapidly within the last year and the Customs Risk Management Team is working to increase the sophistication and accuracy of Customs risk assessment. Customs also knows the compliance rate for various industries, specific commodities, and certain importers. Analyzing these historical data and trends, and applying definitions of significance and materiality, allow Customs to narrow its focus on two areas of the greatest potential risk.

The components of the Analyze and Assess Risk step include:

### ***a) Automatic Tools:***

Automated tools are in place to help you analyze data and assess risk. These tools can identify trends and lessons from past experiences, as well as point out high-risk areas and payoffs. Use of analytical tools to determine the areas of greatest risk, and the scope of the problem in those areas.

More than that, automated tools allow employees to identify and assess potential compliance problem areas, it is to say, to identify major players in the alleged problem area. This includes importers, manufacturers, brokers, countries and ports. Some of the tools also allow users to perform verifications or reviews of specific transactions within the problem area.

Above there are some others benefits of the use of automated tools to support the Risk Management Process:

- Establishment of cargo compliance and discrepancy rates - It helps to identify trade compliance risk areas and to assess the effectiveness of cargo exam targeting;
- Generation of trend analyses – It provides an overview of the activity for passengers, commodities, importers, brokers, manufacturers, shippers and countries, that allows Customs to invest more time to potential violations;

***b) Definitions of Significance and Materiality :***

Acknowledging that all violations were not of equal importance must narrow the focus of Customs. Customs must developed significance definitions for violations discovered while examining and reviewing transactions and materiality definitions. Once data points to a compliance problem, Customs conducts further analysis to determine the scope or magnitude of the problem.

Facts taken into consideration include, but are not limited to:

- Number of ports impacted;
- Value and volume represented;
- Portion of industry impacted;
- Laws and regulations that may be violated;
- Commercial issues involved, entries impacted, loss of revenue;
- If the non-compliance represents a possible pattern of non-compliance.

In this subject, we have two main steps: Compliance Measurement Significance Definitions and Compliance Assessment Materiality Definitions:

- Compliance Measurement Significance Definitions – All violations, no matter their seriousness, discovered during a cargo examination or entry summary review are recorded and addressed appropriately. Then definitions are applied which measure the violation’s “significance”.
- Compliance Assessment Materiality Definitions – Compliance Assessment include the use of statistical testing of transactions to determine if importers have internal control systems that produce accurate and complete Customs information. Based upon the results of the testing of these individual transactions, a compliance rate is computed for each of the major areas covered. Compliance rates are also computed to measure the number of times sampled transactions are correct. If any compliance rate is below 95 percent, the cause and effect of the poor compliance is analyzed to determine what plausible corrective action is necessary for the importer to achieve compliance.

***c) Compliance Risk Categories:***

After the step of identification of significance and materiality, we got the definition of the Compliance Risk Categories. For each, one there will be a specific action of the Customs:

- High compliance, Good Internal Control Systems – Low Risk, therefore minimal Compliance Measurement exams – The importer passed the assessment with above a 95 percent compliance result, and also demonstrated reasonable care in administering its business practices. This company poses low risk to achieving trade compliance goals.
- High Compliance, Suspect Internal Control System – Moderate Risk, and average number of Compliance Measurement exams – The importer passed the assessment above a 95 percent compliance result, however,

did not demonstrate reasonable care in administering its business practices. This company poses moderate risk to achieving trade compliance goals.

- Low Compliance – High Risk and a significant number of Compliance Measurement exams – The importer failed the assessment, with a score below 95 percent, and did not show reasonable care in administering its business practices. This company poses high risk to achieving trade compliance goals.

***d) Enforcement Evaluation Team:***

The Enforcement Evaluation Team is a group that has as a mission to ensure uniformity of enforcement actions across ports, and to ensure Customs' enforcement resources have the greatest effect. The Impact Levels (high, medium and low impact) are used to guide Customs enforcement decisions.

***e) Account Management Evaluation:***

An Account profile is created. It allows the Account manager to begin narrowing his or her focus with the company to address crucial compliance problem. It's mostly used when there is no Compliance Assessment. Without a Compliance Assessment, a specific Compliance Risk Category is not assigned, but by creating and analyzing an Account Profile, areas where the Customs and the account (importer, for example) should focus resources become apparent.

**3<sup>rd</sup> Step - Prescribe Action**

Data collection and analysis alone do not constitute a fully developed risk management system. After you have collected the necessary data, and the risk analysis is complete, action may be needed to reduce risk and to increase compliance. Once a

potential risk has been identified and analyzed, it is time to design the appropriate action and dedicate necessary resources.

Some remedies must be implemented to reduce risk and increase compliance, but it's imperative to say that Customs designs these performance measures linked to national goals and objectives. And in developing measures, comprehensive indicators, those that show a ratio of expected results to actual results, are preferred, as opposed to indicators that only show work completed.

Prescribing action involves two distinct actions:

- Identifying the cause of the risk, such as an importer's lack of knowledge, complex trade laws, or willful disregard for importer laws and regulation;
- Designing an action and assigning resources to address that risk or selecting and implementing an appropriate response. This step requires two distinct actions: identifying the cause of the risk, such as an importer's lack of knowledge, complex trade laws, or willful disregard for import laws; and designing an action and assigning resources to address that risk.

Over the last few years, Customs has developed a variety of tools to actively address high-risk areas. These tools span a range of activities from instituting laws and regulations creating a voluntary compliance system to aggressive enforcement to address some of the most grievous non-compliance. Involvement of skilled personnel and managers that control the resources is crucial here. Each of these tools feeds into the overall Customs mission to maximize trade compliance through a balanced program of Informed Compliance, and Enforcement Compliance (targeted enforcement actions). Within the Trade Compliance Process, these are the primary and complementary components. However, Informed Compliance and Enforced Compliance must be used together. The coordination of these efforts is crucial.

Informed, voluntary compliance is the preferable approach to trade compliance. But, when determining which approach to take, the nature, scope and impact of non-compliance are evaluated in the context of the involved account's overall compliance history. Informed compliance actions, such as intervention, education and counseling of the account are employed by Customs to address instances of non-compliance when an account has demonstrated a failure to apply reasonable care. Informed Compliance is a prescribed action in the Risk Management Process that is a win-win situation. Educating importers increases voluntary compliance and this allows us to release the goods in a timely manner.

Enforcement actions such as seizure and investigation are reserved for those instances of violations, fraud, or repetitive violations that could not be solved through informed compliance. Some examples of Enforced Compliance are investigation, seizure, arrest, penalty and exclusion from some Customs Programs.

It is important to point out that, sometimes, the traditional Customs responses to a non-compliance situation are not the best. In these cases, the Enforcement Evaluation Teams can act to make an early determination of the nature, extent and impact of instances of non-compliance; select the Customs response best suited to remedy the problem; and follow-up on that action to ensure the non-compliance problem is solved. It is the function of the Enforcement Evaluation Teams to ensure that significant discrepancies and possible violations are treated uniformly on a national and account-wide basis.

#### **4<sup>th</sup> Step - Track and Report**

All the results of the remedies, informed or enforced compliance, are compiled and reported back into the Trade Compliance and Risk Management Process for monitoring the account and for future action. Ensuring that actions are implemented and reporting their results are critical to the cycle of identifying and eliminating future risk. So, after you have implemented a prescribed action, results must be tracked and

documented. This process ensures that successes can be repeated and that personal knowledge becomes shared knowledge.

It is vital to stress out that this feedback can occur at any of the described steps, not only in this last one. All the information and knowledge gained in the process are fed back into it, causing a change in a risk priority, leading to new Compliance Measurement and Assessment, new accounts analyzed and new remedies recommended. Risk is never absolutely known and changes with time. Therefore, results and experiences must be continuously fed back into the process to increase knowledge and better predict future risk.

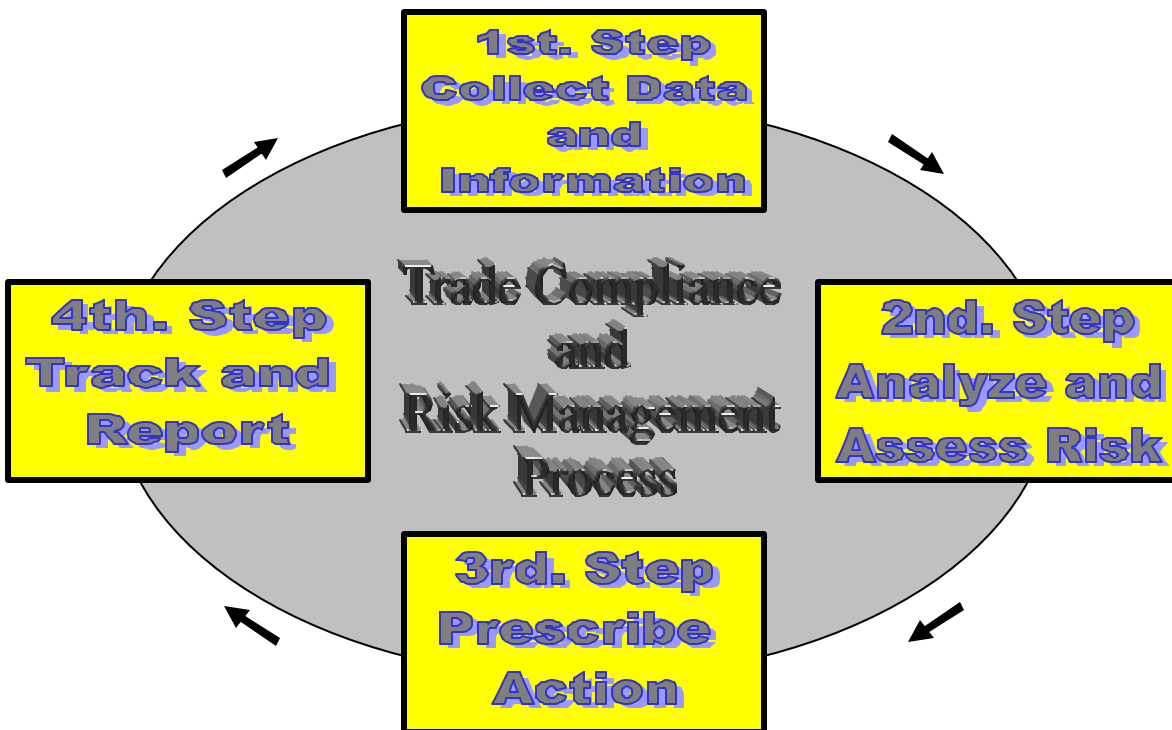
Above there are some of the several reporting mechanisms that Customs employs in this step:

- Trade Compliance and Enforcement Plan – It is the annual plan for the Trade Compliance and Risk Management process. It must have an effective evaluation by the end.
- Report to Congress on Trade Compliance – The Customs Modernization Act requires this report, which purpose is to provide an objective assessment and measurement of compliance with United States trade laws and regulations. It is very useful not only for the U.S. Congress but also for the U.S. Customs itself.
- Account Management – Account managers must track their accounts' compliance progress to ensure compliance problems are resolved, measuring the account's progress. Account Managers meet regularly with their accounts to ensure implementation of Account Actions Plans and track compliance progress. These meetings are important to share some information about the successes and the failures of the accounts.

- Follow-up Verifications – They are conducted to determine if the corrective actions were fully implemented and effective in correcting the deficiencies identified during the Compliance Assessment. Compliance Assessment Teams conduct follow-up verifications with companies to ensure Compliance Improvement Plans were effectively implemented.

As we can see in the Figure 1, these plans and reports have to be done, in order to give for the Trade Compliance and Risk Management process a strong mechanism of feedback, that will allow make it be a dynamic process. An agenda with formal meetings and reviews, where experiences can be openly shared and discussed, provides an opportunity for all the Customs employees and the accounts to find the optimum approach to a certain problem, improving the compliance and reducing the risk.

**Figure 1 – The U.S. Customs Trade Compliance and Risk Management Process –**  
This figure can be useful to give an overview of this process, including the importance of the feedback.





## **The Goals of U.S. Customs**

The main goals that the U.S. Customs wants to achieve with the Trade Compliance and Risk Management Process are:

- Achieve 90 % of overall trade compliance;
- Achieve 95 % of compliance in primary focus industries;
- Maintain collection of at least 99 % of the revenue;
- Reduce cargo release cycle time for compliant imports;
- Increase customer satisfaction;
- Reduce cost per transaction.

**Seventh Chapter –**  
**Practical Cases in the U.S. Customs Experience**

In the tables below, we will describe two extremely diverse practical examples of the U.S. Customs Trade Compliance and Risk Management Process. The first one is an experience in a specific port (Los Angeles/Long Beach), with a specific group of imports and with a great enforcement action. The second is a national experience in the airports, with the passengers, generating a great rationality in the use of the resources.

**Table 8 – Trade Compliance and Risk Management Process in Los Angeles, California** – This table will be an example of the use of this process in defense of the Intellectual Property Rights, specifically in Los Angeles/Long Beach, which is the primary port of entry for shipments from the Far East.

Steps	Brief Description
Step 1 – Collect Data and Information	Using the Automated Systems, there was a strong process of data collection in the imports, in order to search where was the greater risk.
Step 2 – Analyze and Assess Risk	It was verified that there was a great necessity of an action to combat the imports, especially from the Asia (Far East), of counterfeit intellectual property rights merchandises.
Step 3 – Prescribe Action	This area became a high priority in the inspections, examinations, and reviews. During this process it was found counterfeit trademark merchandise. After some investigation, Agents discovered that the suspect shipper had imported this kind of merchandise for 2 years. The suspect was arrested.
Step 4 – Track and Report	The U.S. Customs to feedback the process reported all the process of that operation.

**Table 9 – Trade Compliance and Risk Management Process in Passengers Programs.** – It was a national program The Automated Passenger Inspection System (APIS) is a very strong instrument that U.S. Customs can use to select the passengers that will be inspected in the airports.

Steps	Brief Description
Step 1 – Collect Data and Information	Using the Automated Passenger Inspection System (APIS) and many other sources of information, the data from the passengers were collected, in order to search identify the greater risk.
Step 2 – Analyze and Assess Risk	The analysis of the information collected allowed the Customs to determine which were the more risky airports, flights and group of passengers. Also the methods of these groups and the effectiveness of the Customs’ actions were analyzed.
Step 3 – Prescribe Action	With this information, U.S. Customs trained the its employees (interview and searches techniques), targeted airports, flights and groups and reviewed the actions to combat then and performed them. With this program the personal search efficiency increased from 5%, in the first three-quarters of 1999, to almost 14%, in the first three-quarters of 2000.
Step 4 – Track and Report	All the experience was reported with the positive “hits” and the negative “misses”, and the process was fed back.

These examples show how a Trade Compliance and Risk Management Process can be a useful instrument to give the Customs Services more power in their activities. Again we must point out that it’s a dynamic process, and that the feedback is not only need but also indispensable.

## **Conclusion**

In the new millennium, the increase of numbers and scope of challenges that the Customs Organizations throughout the world face will continue. National government need to recognize that by investing in modernizing and reforming their Customs Administrations there will be a short-term payoff in revenue collection and a long-term one in national prosperity. Modernizing and reforming is a changing process, changing with the world, seeking to achieve further gains in efficiency and effectiveness.

The Trade Compliance and Risk Management Process, as a core tool for that modernization, can and must be used by Customs Administrations, in order to achieve the excellence with speedy processing and higher security in foreign trade. This process must be done with the complete involvement of all the participants of the international trade process, since the Customs' managers and employees, until the importers, exporters and brokers.

More than that, to be effective, this process must be formal, universal, systematic, and applied in a disciplined manner. And, since risk is never absolutely known, and because risk can change over time, results and experience must be fed back into the process to narrow the knowledge gap and better predict future risk.

Brazil is a country inserted in the globalization process and, as it happens with many other countries, seek to improve the international trade, in order to achieve economic growth and development. That's why the process of modernization of the Brazilian Customs Service must be a priority for Brazilian Government. And this modernization is happening, all the procedures of export and import are automated, and a great part of the cargo procedures. But, it's indispensable that the introduction of a formal, universal, and systematic Trade Compliance and Risk Management Process, as said in the last paragraph.

Of course there are many other aspects that must be improved in order to give to the Trade Compliance and Risk Management Process the plenty possibility of success. One of the most important is the elimination of antiquated, archaic and intrusive Customs control. There are the difficulties caused by archaic legislation that must be reviewed or substituted in order to reflect new priorities and methods of carrying out the Customs function.

Another point is the human capital policies. It's recommended to have strong recruitment policies, training services and performance evaluation systems. In this point, a special attention must be given to development Customs Expertise. The increase in the demand for new skills will lead to the increase in the need for training staff to do new jobs and retraining staff to do jobs differently.

The professional know-how of the employees is a key to a successful modernization of the Customs. As Customs places greater reliance on post-release audits, audit skills are going to be required. Expertise in classification, value, origin, inspection, and enforcement is needed as more administrations become knowledge based, information management skills will be increasingly in demand. Computer knowledge is already essential for Customs officers, because information technology became a part of the day-to-day operation, with the computer-based systems. These skills will need to be incisive and effective to ensure proper compliance.

The integrity of the organization and the individual Customs offices is a very important variable and Customs administrations must act in order to avoid and punish the corruption. The Automation Process and the Trade Compliance and Risk Management Process act strongly in that direction, as well as the education and commitment policies. All these policies must act together. That's the path that not only Brazilian Customs but also all the Customs organization throughout the world must seek to improve its activities.

There are many policies that the Governments can do to enable Customs Services to act towards a greater contribution to the economic growth. But, maybe, the most important lesson that not only Customs but also the whole government agencies have to follow is to become a learning organization. Once you have the capacity to learn, adapt, change, and grow, all the challenges can be faced.

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