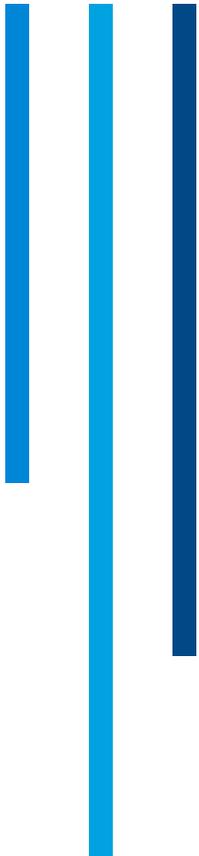




GET READY FOR A FOCUSED ASSESSMENT

WHY FOCUSED ASSESSMENTS ARE INCREASING,
AND HOW YOU CAN PREPARE

WHITE PAPER



C.H. ROBINSON
ACCELERATE YOUR ADVANTAGE®



IN BRIEF

As U.S. Customs and Border Protection (CBP) steps up enforcement of customs regulatory compliance, more companies are facing customs audits. In this white paper, importers can learn what increases their risk of undergoing a Focused Assessment and how they can prepare an audit team to successfully face such an event. By doing so, importers can create necessary procedures or augment their current ones to improve their overall compliance program.

CONTENTS

Why CBP's enforcement is increasing	3
Is your company a likely target?	6
How to prepare for a Focused Assessment	8
What to do during a Focused Assessment	11
The aftermath of a Focused Assessment	13
Next steps	14

International trade is an uncertain business. As such, importers can expect to encounter one particular outcome—a Focused Assessment—at some point.

WHY CBP'S ENFORCEMENT IS INCREASING

General compliance issues tend to dominate many importers' trade agendas. Relatively few companies put much effort into preparing for a CBP Focused Assessment.

Yet, the penalties for trade-related transgressions can be severe, depending on the seriousness of the infraction. Even problems that appear to be relatively minor can attract significant penalties.

For example, CBP imposes fines of up to \$10,000 per entry for recordkeeping infractions. Non-financial costs, such as shipment delays, the diversion of staff resources to correct problems, and in rare instances, the loss of trade privileges, can be detrimental to an importer's business.

CBP maintains two penalty provisions—the loss of revenue provision and a non-loss of revenue provision. Each provision has three degrees of culpability that are predicated upon whether the violations that occurred are deemed as negligent, gross negligent, or fraudulent. Compliance errors that result in the loss of revenue to the U.S. government are penalized based upon a percentage of the loss of revenue, in correlation with the importer's degree of culpability. Even inaccuracies that do not pose a loss of revenue to the U.S. government, such as statistical errors or omissions, can potentially result in the administering of severe penalties to the importer. Inaccuracies that do not pose a loss of revenue incur culpable penalties based on a percentage of the entered value of the goods.

The typical import duty in America is estimated to be 1.2 percent; a penalty of 1/2 that amount can be imposed for basic-negligent mistakes, to as high as 8 percent for a fraudulent infraction. Non-revenue infractions—infractions that do not affect the revenue the government would have received—begin at 5 percent and go to as high as 80 percent of the entered value of the goods, based upon the

degree of culpability. Since CBP invariably begins with the maximum penalties for wrongful filings, the actual fine can be quite substantial.

For example, CBP could potentially deem a statistical error, such as incorrectly claiming the relationship¹ during the entry, as gross negligence. This could result in a non-loss of revenue penalty of 20 percent of the entered value of the shipment. Infractions in the negligence category are relatively simple mistakes, but gross negligence errors are those that the importer should have detected in a post-entry review or some other process. But this distinction poses a conundrum for importers, because CBP generally believes that every mistake should be discovered via an entry audit or an internal control. As a result, fines tend to start at around 40 percent for gross negligence infractions—a figure subject to mitigation. Fraud represents a knowing violation, and CBP must prove that the importer is guilty of this serious offense.

Regardless of the severity of the infraction, it is becoming increasingly likely that an importer will end up under CBP's microscope. Although there was previously a mandate to complete a Focused Assessment on the top 5,000 U.S. importers, they are not the only importers at risk of undergoing this enforcement activity. Quite recently, with the advent of the Informed Compliance Letters, CBP has stated that companies which are not part of the top 5000 importers in the United States are at risk for increased compliance scrutiny, based upon several risk factors (see Figure 1 on page 5) potentially present in their import program.

As if these various penalties are not sufficient encouragement for companies to prepare for a Focused Assessment, importers should also consider the shock factor. Until an enterprise is selected for and actually experiences a CBP enforcement action, it cannot anticipate every eventuality. The best safeguard against surprises is to be as well prepared as possible.

Certainly, trade operations that are in compliance are less likely to incur costly penalties if audited, but there is another upside to a Focused Assessment, as well. When importers apply discipline to trade compliance and introduce ways to streamline related processes, they usually reap significant supply chain efficiencies.

When importers apply discipline to trade compliance and introduce ways to streamline related processes, they usually reap significant supply chain efficiencies.

In a recent issue of CBP's Import Trade Trends Report, former Assistant Commissioner of CBP Daniel Baldwin relates the experience of two members of the Agency's Importer Self-Assessment (ISA) Program. Baldwin said, "Most notably, their ISA participation expedited shipments at the ports, literally saving the companies days during the clearance process. Another benefit was better communications with CBP, which facilitates the movement of goods."²

FIGURE 1: Common pitfalls of importing

The following list provides guidance to the most common import compliance pitfalls for importers. Expect penalties if you misinterpret or fail to comply with these various requirements.

- 1. Manufacturing assists**
Items supplied directly or indirectly and free of charge or at a reduced cost for use in connection with the merchandise. Examples are materials, components, tools, molds, and engineering/design work.
- 2. Additions to price paid or payable**
Royalties/licensing agreements, packaging, indirect payments and proceeds of subsequent sales.
- 3. Non-dutiable costs**
Various costs that are not subject to duty payments; for example, deduction of freight and insurance charges.
- 4. Country of origin**
Determination and marking requirements.
- 5. Classification**
Inaccurate product classification.
- 6. Free trade agreements**
Wrong or inaccurate interpretation of these agreements.
- 7. Chapters 98 & 99 classifications**
Items imported under both Chapter 98 and Chapter 99 generally have defined provisions or special requirements that must be met.
- 8. Related Party transactions**
The price paid for a good when the buyer and seller are related parties; for example, a transfer price arrangement where the participants are part of the same organization.
- 9. Recordkeeping**
You are responsible for keeping trade transaction records for five years. The corporate guidelines must be followed, and CBP will audit for consistency and compliance.
- 10. Anti-dumping & Countervailing Duties**
Reviewing your products to see if they are applicable to a scope order.
- 11. Quantity verifications**
Ensuring that the quantity received is the same as reported at the time of entry. Discrepancies that are discovered need to be addressed in a Post-Summary Correction.
- 12. Selling commissions**
Commissions paid to a foreign "person" related to a foreign vendor or working on behalf of and for the benefit of the foreign vendor need to be addressed as an addition to the price paid or payable.

CBP is more favorably disposed toward enterprises that demonstrate reasonable care and due diligence, and that have made a genuine effort to comply with all the regulations. Conscientious companies may find that CBP officials will recognize their efforts, ultimately resulting in greater leniency.

IS YOUR COMPANY A LIKELY TARGET?

There were approximately 196,925 domestic importers in 2015.³ Some of them will have a Focused Assessment completed by CBP; just how many depends on CBP's priorities, selection practices, and available resources.

Roughly 5,000 entities in the U.S. account for about 80 percent of the total value of imports, so by virtue of their size, and as mentioned above, these operators are high on the CBP's list of likely candidates for further scrutiny.

But enterprises that are not members of this select group should not rest easy. CBP also created a sub-group of importers that, by virtue of their behavior patterns, are deemed to be potential lawbreakers. These enterprises may or may not be in the top 5,000 group.

There are a number of characteristics that can lead to a company being tagged in this way. For instance, CBP may have analyzed an importer's trade statistics and detected a high incidence of anti-dumping actions. This type of importer category represents a game-changing departure from CBP's practice by widening the agency's compliance net. Thus, importers need to have a deep understanding of their trade compliance statistical profiles. Third-party compliance service providers with the ability to create and analyze these profiles can help companies to stay off the CBP's audit list by discovering areas of noncompliance and offering assistance in proactively implementing corrective actions.

Even if your organization does not appear in any of these lists, there is no guarantee that you will not be flagged for a Focused Assessment. There are numerous ways in which an importer can attract the attention of CBP officials. For example, organizations that make recurring filing mistakes—or perhaps even a single bad entry—can warrant a quick review through a Request for Information (CBP-28) or a Notice of Action (CBP-29). Depending

Third-party compliance service providers with the ability to create and analyze trade compliance statistical profiles can help companies to be compliant.

upon the outcome of CBP's review of the importer's responses, investigative enforcement could proceed in several different directions. These may include a Quick Response Audit, an Informed Compliance Letter, or a Focused Assessment, all of which place a greater degree of scrutiny on an importer's compliance program.

Importers should remember that CBP puts significant effort into identifying every opportunity for recovering payments from the trade community. In particular, CBP watches for anti-dumping and countervailing duties, application of free trade programs, and transactions between related parties (to name a few). These are likely to uncover infractions and therefore, to result in higher revenue recoveries.

If you receive a letter from CBP that your organization has been targeted for an assessment, it does not necessarily mean that a wide-ranging audit is imminent. You may be the subject of an inspection that is not as comprehensive as a full Focused Assessment. Quick Response Audits (QRA), for instance, have a narrower focus than a complete evaluation of a company's import compliance activities.

The sobering news is that once you receive a formal notice, the clock is ticking; it is probably only a matter of time before you will be audited. Based on past experience, the probability that you will have to undergo a full audit increases considerably when a CBP official calls and asks pointed questions, such as where you keep your import records and who in your organization is in charge of compliance. The important takeaway: don't fall into a false sense of security because you have not received a notice already. When it does come, time is of the essence.

What should you do when you finally receive the news that CBP is going to pay you a visit? First, don't panic. Second, spread the word by issuing a memo to all relevant interests that an audit has been confirmed. Make sure that you alert external providers, such as customhouse brokers, for assistance.

CBP statistics⁴ that outline its financial role

In fiscal year 2016, CBP:

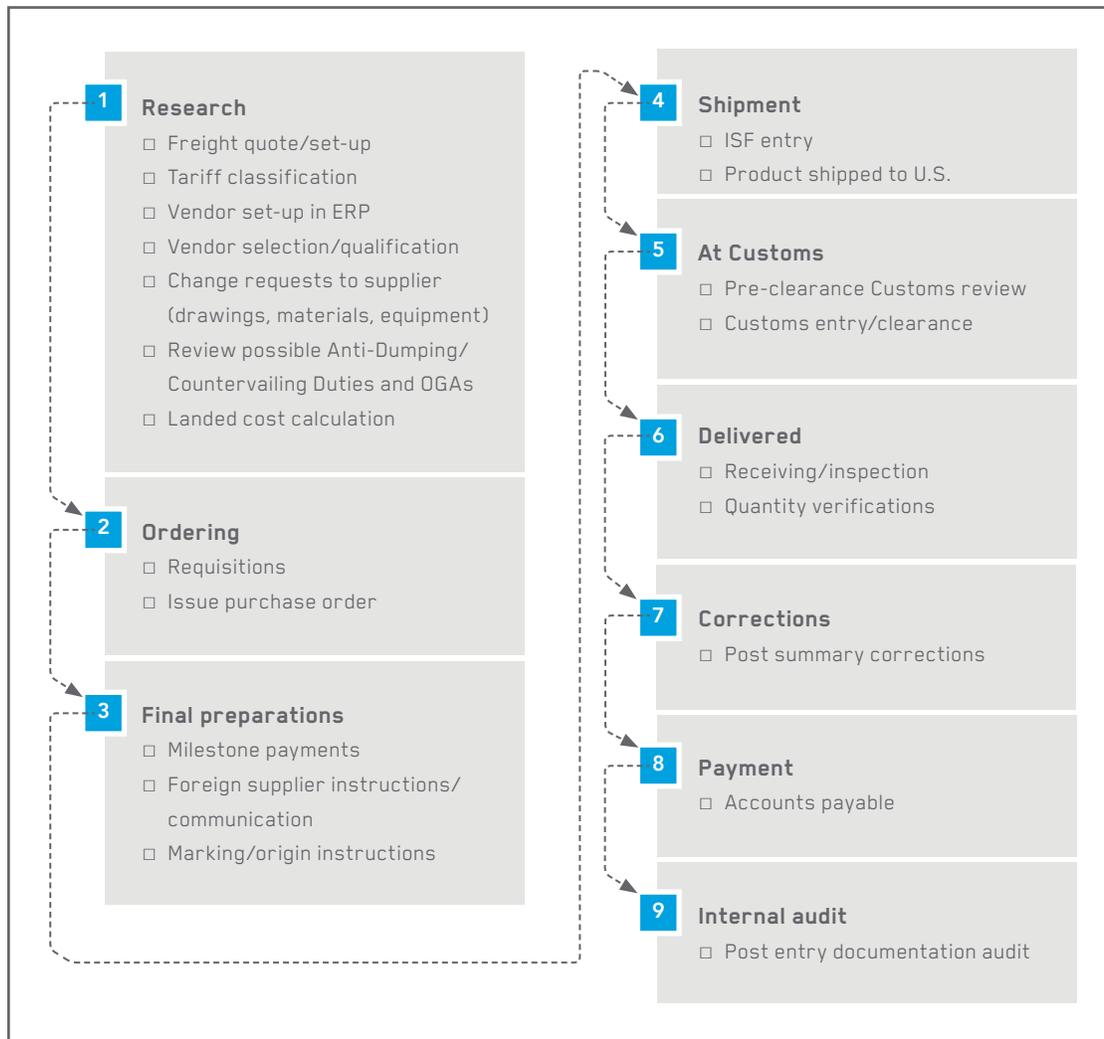
- Processed about \$2.28 trillion of entered value
- Collected \$40.1 billion in duties, taxes, and fees
- Processed 32.6 million entries
- Refunded duties of \$948 million through the duty drawback program.⁵

HOW TO PREPARE FOR A FOCUSED ASSESSMENT

When a major enforcement agency such as the Internal Revenue Service decides to audit a company, the organization goes on red alert and forms a project team to meet the unexpected challenge. A CBP audit should elicit the same response, since the financial repercussions can be just as grave as with any other agency with a finance-oriented enforcement mandate.

The makeup of the internal CBP audit team will differ according to the nature and size of the company's business. A good way to establish who should be involved—and to gain a better understanding of your trade operations at the same time—is to create a flow chart of an import transaction. Mapping each step—from the time a purchase order is opened to the point of payment to the foreign vendor—is a great way to define the parties that will need to participate in the Focused Assessment.

FIGURE 2: Example of trade transaction flow chart



As part of your audit response team, recruit key individuals from these or like groups assuming your company possesses them:

- **Trade Compliance.** They will be on the front line during the Focused Assessment.
- **Supply Chain/Logistics.** They have a wealth of knowledge and information about the company's trade business.
- **Procurement.** This is the go-to department for information on corporate purchasing activities.
- **Finance and Accounting.** Finance staff make decisions about how the company buys from trading partners and have detailed knowledge of financial flows.
- **Legal.** Don't wait to bring in Legal until it is too late. Again, if this were a tax audit, involving legal experts would be expected. Get your internal legal department on board, and consider contracting external trade compliance resources. This decision depends to a large extent on your risk profile. For example, importing textiles from multiple countries with the benefit of various free trade agreements is comparatively risky from a Focused Assessment standpoint. External legal resources might not be necessary if your import operations are relatively small and straightforward.
- **Production.** They interact with vendors and customers, and have valuable information on the company's international operations.

In addition to these internal experts, you should recruit specialists from outside where appropriate. Obvious candidates include trade-related service contractors, such as customs agents and brokers, freight forwarders, and third party logistics service providers.

As you assemble the team, think about areas of vulnerability that need to be addressed before the audit day arrives. Figure 2 (page 8) shows an effective tool you can use to help identify gaps in your compliance practices.

As a team, you can conduct a quick health check. Gather data on the total entered value for one or a few foreign vendors. Compare that value to the amount your company actually paid that vendor

for the same purchase orders. Many times, this simple exercise will uncover an issue with the validity of entered value. In addition, such issues as post summary corrections, after-the-entry deductions to price, and agreements on reconciling overages, shortages, and damages with vendors may be revealed.

It is easy to overlook discrepancies in import dealings, particularly with relatively complex international purchases involving multiple parties. But these oversights will come back to haunt you during a Focused Assessment.

For example, imagine that your company imported 500 cartons of sweaters from Asia. Ten cartons were damaged while in transit, so the purchasing and accounting departments arranged to short pay the shipment. But this happened during a peak buying time, and neither department got around to informing the company's compliance people or its customs brokers that the adjustment had been made. As a result, that particular entry was not amended to reflect the new payment. This is an infraction that will surface during a Focused Assessment and in all likelihood, incur a penalty.

When assessing your vulnerability to a Focused Assessment, also keep in mind that many areas of trade compliance can be in direct conflict with other areas of corporate oversight. For example, companies engaged in related party transactions normally apply a transfer price which was established to obtain the best tax situation across many jurisdictions. However, the process of determining transfer pricing is done in contradiction with the requirements of CBP. Specifically, on the tax side of the business, transfer pricing is based on a year's reconciliation of total transactions; CBP expects pricing to be based on a transaction by transaction basis.

The preparations described above may seem daunting. To help you determine whether your organization may be prone to this or other risks, review the list of important infractions that generally present themselves during a Focused Assessment (see Figure 1 on page 5).

In addition, as you prepare for a Focused Assessment, gather and use external sources of information on compliance requirements.

- **CBP A1A List.** Specifies what documents an importer should have in its files. Auditors will want to see complete documents, so review your files well before the appointed day.
- **CBP's Focused Assessment Handbook.** The playbook for customs audits. The 600-plus pages in the handbook can be a dry read, but the information is invaluable; it basically lays out the CBP's game plan for carrying out an audit.
- **The Import Compliance Manual.** Many companies neglect this document, which describes the import procedures they should be following. Companies that do not have written policies and procedures will most likely need to develop one as part of their Compliance Improvement Program (CIP) in the post-Focused Assessment.
- **Local and national trade associations.** These organizations are a rich source of information, such as training materials and case studies of organizations that have gone through a Focused Assessment.

Many of these information sources are available on the CBP website (www.cbp.gov), which provides a wealth of advice on compliance and trade regulations. Many official websites are lackluster, but CBP's is one of the exceptions. The site is easy to navigate, offers useful information, and is extremely comprehensive.

WHAT TO DO DURING A FOCUSED ASSESSMENT

As mentioned, unless your company has been through a customs audit, the actual process is something of an unknown variable for the organization. Even so, you can take steps to make the process go smoothly.

Bear in mind that in all likelihood, CBP is better prepared than you are; the agency has worked hard to compile all the information it needs for the audit. In fact, by the time the actual day arrives, the visiting CBP officials will likely be very knowledgeable already about your importing process, as well as the risks that your company poses to CBP.

An obvious requirement is that you have all relevant documentation on hand. Make sure that key staff members are available for the duration of the audit. It might be necessary to arrange for replacements should certain staff members be unavailable. However, past experience shows that such is the importance of this event that managers are advised to make attendance mandatory for essential personnel.

When CBP arrives, be cooperative. Don't handicap your performance unnecessarily by being offensive or flip. At the same time, avoid overpromising. If there is no need to offer some elaborate solution to an issue that requires a lot of resources on your part, then don't go that route. Remember, you will be held accountable for any responses you promise to provide. It is better to have an honest and frank conversation about what the CBP officers want, and to perform the minimum amount of work required to meet their requirements.

Know your numbers. This might seem like obvious advice, but CBP will expect you to be intimately familiar with all the statistics that relate to your business. Two sources to use as reference points include the Importer Trade Activity (ITRAC) data, which provides statistics for importers and their legal representatives, and CBP's Automated Commercial Environment (ACE) database.⁶

Hold CBP accountable for its commitments. Insist on a timeline for their responses, and make it clear that you expect them to adhere to agreed-upon deadlines. CBP failing to deliver on its promises can disrupt your business. This is not an easy conversation to have with the agency, but it is perfectly valid. View it as good business practice. If you are using an external advisor, this is an ideal time to call on their resources; it is often easier for a third party to have these discussions with CBP.

Finally, don't get flustered if the audit does not appear to go well. You will have learned some important lessons that benefit the business and make you a savvier importer.

THE AFTERMATH OF A FOCUSED ASSESSMENT

What takeaways are there from a CBP Focused Assessment?

Obviously, these will differ from company to company, but here are some insights that any organization can benefit from:

- Consider joining an industry and/or government program, such as the Importer Self-Assessment (ISA) Program. There are benefits to doing so, not the least of which is reducing the probability that you will be the subject of future Focused Assessments. Moreover, you are likely to be better prepared as a program participant and recoup some of the costs by avoiding penalties.
- Review your compliance training programs, and consider introducing periodic mock audits. A convenient option might be to engage an outside professional consulting service with relevant experience in carrying out mock audits for your organization.
- Review internal and external standard operating procedures to ensure flaws do not put your operations at risk.
- Build broad support for a compliance effort within the organization from senior management and down through the ranks.
- Create incentives for being compliant with trade regulations and practices. Establish procedures for continuously reviewing your records and practices, and taking corrective action where necessary.
- Choose a service provider such as a customhouse broker that has in depth expertise and helps you to stay compliant, not just complete a transaction. The provider should be there when needed, not only when a government agency is knocking on your door.

Correcting mistakes

Even your best efforts to comply can fail for many reasons, so review your trade processes on a regular basis. As you identify errors, fix them, and make sure that they will not recur.

Be proactive when an error is detected. The severity and duration of the error might require a Prior Disclosure, rather than a Post Summary Correction. Entering into a Prior Disclosure is not to be taken lightly. It is strongly recommended that your organization acquire a trade attorney or, at the very least, that you run all activity associated with the Prior Disclosure through your legal counsel. Generally, you will need to determine the extent of the infraction over a five-year period, outline the infraction in full, and include details of the corrective action you have implemented. CBP will expect immediate payment where duties were not paid or underpaid, plus all interest accrued.

NEXT STEPS

In the next few years, increasing trade volumes will put more pressure on the regulatory agencies that monitor the flow of goods. Furthermore, new regulations add another layer of complexity to these international movements.

In the future, importers can expect to be pushed toward joining self-assessment regimes and partnership programs. For example, there could possibly be an initiative by CBP to entice importers to join the Importer Self-Assessment Program and the Centers of Excellence and Expertise. By participating in these programs, an importer becomes a more active participant in ensuring compliance with U.S. import regulations and therefore will pose an acceptable risk in CBP's purview. When an organization poses an acceptable risk to CBP, there is less likelihood of CBP enforcement activity. This results in measurable return on investment, both monetarily and in hours spent fixing issues.

Our information is compiled from a number of sources that to the best of our knowledge are accurate and correct. It is always the intent of our company to present accurate information. C.H. Robinson accepts no liability or responsibility for the information published herein. Where questions arise, please review the various CBP publications on this topic or contact local customs counsel if necessary.

For a wealth of advice on compliance and trade regulations, visit CBP's comprehensive and useful site, www.cbp.gov

END NOTES

1. According to 19 CFR 152.102(g), "Related persons" means: (1) members of the same family, including brothers and sisters (whether by whole or half blood), spouse, ancestors, and lineal descendants; (2) any officer or director of an organization, and that organization; (3) an officer or director of an organization and an officer or director of another organization, if each individual also is an officer or director in the other organization; (4) partners; (5) employer and employee; (6) any person directly or indirectly owning, controlling, or holding with power to vote, five percent or more of the outstanding voting stock or shares of any organization, and that organization; (7) two or more persons directly or indirectly controlling, controlled by, or under common control with, any person.
2. U.S. Customs and Border Protection, "Import Trade Trends: Fiscal Year 2012, Year-end Report," January 2014.
3. Department of Commerce, "Profile of U.S. Importing and Exporting Companies: 2014-2015."
4. Unless otherwise noted, all statistics in this sidebar were found in U.S. Customs and Border Protection, "Performance and Accountability Report: Fiscal Year 2016."
5. Data provided to C.H. Robinson upon request by U.S. Customs and Border Protection, September 20, 2017.
6. U.S. Customs and Border Protection, Automated Commercial Environment database, <https://www.cbp.gov/trade/automated>.

ABOUT US

At C.H. Robinson, [we see things differently](#). We believe in accelerating global trade to drive the world's economy. Using the strengths of our people, processes, and technology, we help our customers work smarter, not harder. As one of the world's largest third party logistics providers (3PL), we provide a broad portfolio of logistics services, fresh produce sourcing, and managed services through our global network. In addition, the company, our Foundation, and our employees contribute annually to a variety of organizations.

For more information, resources, and our blogs, visit www.chrobinson.com.



C.H. ROBINSON
ACCELERATE YOUR ADVANTAGE®