Government Audits: Avoiding the Pitfalls that Trigger a Regulatory Audit

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Customs Audits: Avoiding Pitfalls

➢ The “New CBP”

– Renewed Emphasis on Trade Enforcement and Compliance

– New Tools

• Centers for Excellence and Expertise (CEE’s or Centers)

• Trade Facilitation and Trade Enforcement Act of 2015

• Trade Enforcement Task Force (within CBP’s Office of Trade)
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- 1993 Mod Act Vision Realized
  - Transformation from entry-by-entry review to Importer “Account based” review
  - CEEs allow easier comparison of importer activity with similar industry participants
  - Industry Centers and “Account based” structure facilitates efficient targeting and use of CBP Compliance and Enforcement resources
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Priority Trade Issues

Priority Trade Issues (PTIs) represent high-risk areas that can cause significant revenue loss, harm the U.S. economy, or threaten the health and safety of the American people. They drive risk-informed investment of CBP resources and enforcement and facilitation efforts, including the selection of audit candidates, special enforcement operations, outreach, and regulatory initiatives.

Current Priority Trade Initiatives:
- Antidumping and Countervailing Duty (AD/CVD)
- Import Safety
- Intellectual Property Rights
- Textiles/Wearing Apparel
- Trade Agreements

Comprehensive trade enforcement efforts in these areas continue to protect the U.S. from risk of significant revenue loss, economic risk to U.S. industry, and health and safety concerns.

In April, one Import Specialist from each Center for Excellence and Expertise (CEE), collectively known as the Antidumping and Countervailing Duty (AD/CVD) Centralization Team, (ACT) were detailed to the Antidumping/Counter Vailing Duty Division within the Office of International Trade (OT). The ACT is a “virtual” team; each of the members continues to work from their regular port location.

ACT facilitates the centralization of compilation of information relative to CPB’s carrying out Commerce’s liquidation and other instructions that previously was done by all ports, thus eliminating redundancy of work. This new approach to oversight is intended to increase the accuracy of the AD/CVD liquidation process, and frees up resources for AD/CVD and other trade enforcement.
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AD/CVD Enforcement Updates

AD/CVD Update
- April/May 2016
- March 2016
- February 2016
- January 2016
- December 2015
- November 2015
- October 2015
- September 2015
- July 2015
- June 2015
- April 2015
- February 2015
- January 2015
- December 2014

Commodity-Specific Outreach
- Information on AD/CVD Orders on Aluminum Extrusions
  - NIS Presentation for Aluminum Extrusions Webinar
  - Department of Commerce Scope Rulings on Aluminum Extrusions

CBP Penalizes Wire Hanger Importers

CBP imposed $3.9 million in civil penalties on three importers for evading the antidumping duty order on wire hangers from China. CBP found that these importers failed to properly report the imports as subject to antidumping and failed to pay the antidumping duties. This resulted in a potential loss of revenue of $3.4 million in antidumping duties. CBP found the importers to be negligent of making false statements and false invoicing. CBP is continuing its enforcement of the antidumping duty orders on wire hangers from China. Vietnam and Taiwan, etc. This is an update on AD/CVD.

Audit of Antidumping Duties

CBP’s Regulatory Audit division completed an audit and found an importer underpaid antidumping duties of $5.6 million as the company claimed an antidumping rate of 71.71 percent instead of the actual 128.32 percent. The company was referred for audit based on concerns about the company importing xanthan gum from China without paying the correct duties.

During FY 2015, U.S. Customs and Border Protection, CBP, assessed penalties under 19 U.S.C. §1592 for fraud, gross negligence, or negligence for AD/CVD violations exceeding $51 million. The penalties are based on the goods subject to the duty and are assessed on specific imports of commodities such as aluminum extrusions, bedroom furniture, clad steel, citric acid and sodium chloride, laminated woven sack, large diameter pipe, pencils, petroleum coke, tires, and wood flooring.

Significant Regulatory Audit Findings

CBP’s Regulatory Audit discovered a loss of revenue of $36 million during an audit of importers from China. The findings resulted in $32.4 million of AD duties on shipments, resulting in $32.4 million of AD duties, along with finding errors resulting in an additional $15 million in penalties. CBP is seeking recovery of the penalty amount from the importers.

AD/CVD Enforcement Updates

Selected Fiscal Year 2014 Highlights

- CBP collected $508.5 million in AD/CVD cash deposits, a 12 percent increase from FY 2013.

- CBP conducted 78 audits of importers of AD/CVD commodities with AD/CVD discrepancies of $24.6 million. CBP collected $8.5 million. Commodities involved in the audits include aluminum extrusions, bearings, candles, nails, lock washers, pencils, plastic bags, ribbons, shrimp, solar cells, steel pipe, tires, tissue paper, wooden bedroom furniture, and wood flooring.

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From 2008 to 2010 RA completed 1,053 General Audits
- Recommended collection of $154.2 million in additional revenue to CBP.
- OIG-12-117, September 2012
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➤ Types of Audits & Reviews
  – Focused Assessments
  – Quick Response Audits (QRAs) (*risk or referral based*)
    • Subject matter specific
      – ADD / CVD & IPR (trademarks and copyright)
      – Value, Classification (single issue)
      – NAFTA, GSP, SFTA, Chapter 98
      – Commercial Fraud
  – Audit Surveys
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Focused Assessments

- “Risk” based approach in selecting candidates
- Multiple factors considered, including
  - Size & import activity (value/volume) (10 Million+)
  - Complexity in import activity (HTS variety)
  - Preferences, Free Trade, Special Provisions (SPI, CH98)
  - Priority Trade Issues (i.e., ADD/CVD, IPR)
  - Referrals from other government agencies

Audit Plan is developed for each new fiscal year beginning October 1
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- Quick Response Audits (QRA)
  - Single-issue audits have a narrow focus
    - I.e., Valuation – related party, Classification; AD/CVD compliance; IPR or FTA
    - Limited objective as opposed to the complete evaluation of a company's Customs and Border Protection (CBP) activities in a Focused Assessment
    - Generated primarily from referrals from Import Specialists (CEEs) on compliance issues (CF-28s) or Prior Disclosure
    - Focus is on compliance and revenue collection
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CBP’s Audit Survey Program

- Though similar to audit risk assessment procedures, surveys do not constitute an “audit” in accordance with Government Auditing Standards.

- Allows CBP to quickly and efficiently obtain onsite information about import activities relative to a specific trade area or issue without committing substantial time and resources required by a full audit.

- Allows RA to assign resources to only risk based companies for audit, increasing efficiencies for both CBP and the trade community in facilitating legitimate trade.

- Lack of preparation can result in an expansion full-blown audit or other enforcement action.
U. S. Customs and Border Protection
Office of International Trade
Regulatory Audit
Questionnaire

Introduction

The questionnaire allows us to obtain information about organizational structure and processes and procedures related to U.S. Customs and Border Protection (CBP) transactions.

Please respond to all questions completely and comprehensively. The information you provide will help us gain an understanding of processes and procedures and identify the individuals that are responsible for implementing the processes and procedures and the types of documentation available for review.

Answering the questionnaire affords operations pertaining to CBP activities.

Section 2: Classification/Anti-dumping duties and countervailing duties (ADCVD)

2.1 What position and person is assigned responsibility for accurate reporting of merchandise classifications and ADCVD to CBP?

2.2 What tools are used to aid in the classification process and the determination of any ADCVD?

2.3 Do you rely on Customs Brokers, attorneys, in-house experts, or outside consultants to classify your merchandise under HTSUS and/or make the determination if merchandise is subject to ADCVD?

2.4 What types of records are maintained to support the classifications and/or ADCVD of imported merchandise (mill certificates, CAD / engineering drawings, schematics, product catalogs, product samples, etc.)?
2.5 What type(s) of information, if any, does your purchasing department, legal department, engineers and others departments provide to ensure proper classification and determination of possible ADCVD implications of imported merchandise?

2.6 Are classifications and ADCVD determinations maintained in a database?
   a. If so, how often is the database reviewed and updated?
   b. Is the database provided to the Customs Broker(s)?
   c. Please provide a copy of the database in Microsoft Excel or Access format.

2.7 Are Customs Broker(s) required to have advanced company approval to make classification changes? If so, how is advance approval communicated?

2.8 How is the classification of new merchandise handled?
   a. Who is responsible for ensuring that new merchandise is properly classified?
   b. How does the Customs Broker process new merchandise or merchandise that has not yet been added to the company’s classification database?

2.9 Does the company conduct periodic review of entries to verify that correct classifications are used? If so, what is the frequency of these reviews?

a. Purchase of Foreign Merchandise, such as:
   i. Purchase Order(s); and
   ii. Purchase / Sales Confirmations;

b. Evidence of Import Activity, such as:
   i. CBP-3461 (Entry/Immediate Delivery);
   ii. CBP-7501 (Entry Summary);
   iii. Commercial Invoice(s);
   iv. Packing List(s);
   v. Transportation documents such as bill of lading complete from the declared country of origin;

c. Evidence to support the declared classification, such as CAD / engineering drawings, prints or pictures of the imported merchandise, physical samples, the end use of the
Core Risk Areas

- **Merchandise Classification**
  - Focused Assessment teams often find “basket” provisions or “parts of” provisions incorrectly used rather than the applicable specific tariff

- **Special Trade Programs & 9801 and 9802**
  - importers unable to support claims for special trade programs
  - Don’t verify the foreign manufacturer or producer can support the claim
  - Don’t properly monitor use of special trade programs; cannot provide evidence of origin, qualifying value content, or proof the imports were wholly produced or a product of

- **Recordkeeping**
  - Unable to produce (a)(1)(A) records or
  - accounting and financial records that support the value and quantities
Core Risk Areas

➢ Valuation
  – Related-Party Transactions (TV untested or supported)
  – Payment records don’t match invoices
  – Supplemental payments or year end adjustments unreported
  – Standard cost reconciliation to actual costs unreported
  – Assists unreported
  – Royalty and licensing fee payments to third parties unreported
  – Interest payments to vendors are non-qualifying
  – Commissions are unreported and unsupported
  – Undocumented CIF costs
  – Non-transaction value goods (samples, repairs and returns)
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ACTION STEPS TO DEVELOPING A CUSTOMS COMPLIANCE PROGRAM

– Identify Customs programs you use
– Identify persons knowledgeable about products and programs
– Assemble compliance working group
– Review regulations and legal requirements
– Determine what records must be maintained and/or procedures that must be followed
– Flow-chart company import & payment process
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- Conduct a “Risk Assessment”
  - Evaluate & test processes and import transactions
    - Are they accurate?
    - Is process reliable?
    - Do they produce repeatable results?
    - Is testing broad enough to cover the full gambit of import transactions
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➢ Become an ACE Portal User

  – Download and review importer activity Reports

  – “Mine” data for information
    • Exporters/manufacturers
    • Values
    • Related party indicators
    • Tariff classifications
    • Special duty / trade preferences
    • Unknown Brokers and/or filers
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- Identify risks and compliance goals
  - Sample entry and financial transactions
  - Identify errors and root cause
  - Share results with effected groups
  - Determine how errors can be reduced/eliminated
  - Develop procedures that “reasonably ensure” compliance goals and objectives are met.

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➤ Internal Controls: What does Customs want to see?

– Management committed to compliance with customs requirements
– Written program or process with assigned responsibilities
– Distribution of important Customs related information to affected company employees and Customs brokers.
– Periodic checks to verify accuracy.
– Regular training for key employees.
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- What activities should customs internal controls cover?
  - Classification
  - Valuation
  - Quantity
  - Special classifications and duty preferences
  - Broker Management
  - AD/CVD compliance?
  - IPR process?
  - Country of Origin?
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How To Prepare Internal Controls

– Keep it simple!
– Don’t reinvent the Wheel
– Say what you are going to do & do what you say!
– Test and verify to make sure you have done what you said you were going to do!
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- Internal Controls: Valuation
  - Learn how and where vendor payments are recorded to G/L;
  - A/P, finance, responsible for reporting to Customs Department
    - Key & or new suppliers/ vendors
    - monthly or quarterly vendor payment reports
    - Check payments against Customs invoices
    - Research discrepancies
  - Is there a royalty account?
  - Is there an R&D or NRE Account?
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Study:
- Customs FA Questionnaire and Guidelines
  [https://www.cbp.gov/trade/programs-administration/audits/focused-assessment](https://www.cbp.gov/trade/programs-administration/audits/focused-assessment)
- Model Internal Controls Manual
- Consult experts & peers for ideas

FOCUSED ASSESSMENT
PRE-ASSESSMENT SURVEY-QUESTIONNAIRE

The purpose of this document is to obtain information from the importer about its import operations over compliance with CBP laws and regulations. The contents of the PASQ will be tailored based on the auditors’ analysis of the importer’s import activity and the audit team’s initial assessment of the potential risks for each of the audit areas that were identified in the PAR. Auditors may adopt or modify this document as needed or may develop alternate formats. Auditors may also request copies of documentation in conjunction with the PASQ.

INSTRUCTIONS TO THE IMPORTER FOR COMPLETING THE PASQ

Please respond to all questions. The information you provide will assist us in focusing on the specific risks relative to your imported merchandise and processes/procedures used to mitigate the risk of being noncompliant with CBP laws and regulations. In addition, your responses will help us to identify the individuals that are responsible for performing the procedures and the types of documentation that will be available for us to review.

The audit team will review your responses and prepare supplemental questions that will be discussed with your personnel to further our understanding of your processes and procedures. This PASQ file is a word document that may be filled in with your responses and returned to the auditors either as a word or portable document format (pdf) file. We request that your complete response be provided to us by [insert date] so we may prepare our questions prior to the Entrance Conference.

POINT OF CONTACT INFORMATION

Name(s) of the person(s) preparing the form.

If there are multiple preparers, you may identify a single person that can be contacted to obtain clarification of the responses.

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## Focused Assessment Program Table of Contents

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CBP Best Practices Guidelines

https://www.cbp.gov/document/forms/best-practices-compliant-companies

1. Have management’s commitment. — *(Control Environment)*
   Demonstrates management’s commitment to compliance.
   - Establish a statement of corporate policy that addresses Customs and Border Protection (CBP) matters.
   - Solicit a statement from the Board of Directors that assigns authority and responsibility to the Customs group.

2. State compliance and cost goals. — *(Risk Assessment)*
   Identify and analyze relevant risk and develop internal goals to manage the risk.
   - Conduct post-entry reviews and compare these against established goals.
   - Determine how risk areas should be managed.
   - Resolve control weaknesses in a timely manner.

3. Develop formal policies. — *(Control Activities)*
   Develop, implement and/or modify formal policies and procedures to ensure that management’s goals and objectives are met.
   - Verify the accuracy of the Internal Control Manual to ensure processes and procedures achieve prescribed goals and objectives.
   - Modify controls that are ineffective or inefficient and report to management.
   - Define accountability and controls in job descriptions.

4. Establish training programs. — *(Information & Communication)*
   Ensure that employees receive appropriate training and guidance to effectively discharge their responsibilities.
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• Final Thoughts
  – Start small
  – Don’t try to get everything in the first time around
  – Remember the 80/20 rule
  – It is easy to overlook something, have your process reviewed by 3rd party who can bring a fresh perspective and/or broader experience