

Two Bottom-Line Basics for Succeeding at Global Trade

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Discussions of global trade become more sophisticated with each and every article published. Amidst all the remedies offered for managing the complexity associated with each new regulation, two basic principles may be all firms need to succeed in global trade: honesty and automation. They will not only lead to success in compliance but to improving the bottom line.

Today, the "bottom line" tends to dominate business concerns. Companies want to know how they will profit—or "what's in it for them"—in very specific terms. Firms rarely take into account the economic impact of honesty in their business dealings. This is a serious mistake. Honesty is an important business principle overall, but there are practical economic reasons why firms should place more emphasis on integrity in their endeavors, especially when it comes to supply chain partners and compliance.

"When in doubt, tell the truth" is not easy advice to follow. Consider, for example, the complex challenge automotive manufacturers face when specifying country of origin for import purposes. Generally speaking, the country of origin is the location where the last major manufacturing stage occurred in production (in legal terms, "last substantial transformation"). There are two methods for determining substantial transformation, for NAFTA and non-NAFTA countries. In addition to overall regulations, Customs also issues interpretive rulings relating to country-of-origin determinations. Thus, automotive companies, which manufacture parts all over the world and transform them into products, face formidable difficulties in determining country of origin at the time of import entry.

Import Compliance

The U.S. Customs Modernization Act shifted the legal responsibility for Customs compliance activities to importers. Customs continues to provide the global trading community all the information it needs to be compliant, but the act shifted Customs' focus to improving levels of voluntary compliance.

The shift from border inspections to "post-entry compliance reviews" requires importers to establish internal controls and well-documented procedures. Customs then uses intelligence analysis and risk assessment techniques to target compliance improvement programs within specific industry sectors, as it is not practical to examine every import and export transaction. Customs audits then confirm the integrity of the information supplied.

If Customs determines that an importer is fulfilling its legal responsibilities and possesses adequate systems to assure future compliance, it will likely not target that firm in the future. If Customs determines that a company is not in compliance or does not have adequate internal systems, inspections will occur more frequently and penalties may be issued. Increased scrutiny translates to greater corporate costs. Thus, if a firm is honest in its self-assessments and diligent in implementing systems to ensure compliance with Customs regulations, a company can save a lot of time and money.

Export Compliance

Export compliance consists of two major activities: screening supply chain participants against denied-party lists (DPLs) to detect individuals and organizations with potential terrorism-related ties and classifying and screening goods to identify products that have been restricted for exportation for a variety of reasons. Companies must be diligent in assuring that their product classification schema and DPLs are up to date. And, because DPL screenings may generate only approximations,

it is critical for firms to have proper procedures in place that can later serve as proof that they made every reasonable effort to comply.

In this post-911 age, the penalties for export violations such as exporting without filing the proper export declaration, exporting without obtaining the proper licenses or not abiding by the license provisions, or exporting to prohibited parties can be substantial. Civil penalties can be either \$250,000 or an amount that is twice the value of the improper transaction. Criminal violations can result in \$1 million penalties, imprisonment of 20 years or both.

Two recent settlement agreements illustrate how costly missteps can be:

- Dresser Italia S.R.L. agreed to pay a civil penalty of \$820,000 for allegedly exporting to Libya and Iran without authorization.
- Cerac Inc. agreed to pay a civil penalty of \$297,000 for allegedly exporting to an organization that was on the Entity List without the required licenses and making false or misleading statements on Shipper Export Declarations concerning authority to export.

New ACE System

So far, the Automated Commercial Environment (ACE) clearance component has not revolutionized the import process as expected. If anything, it has led to a trend toward relaxing compliance editing rules. Without immediate notification of problems during the clearance process, critical, potential, honest, and do-not-care errors can go undetected until the time of a Customs audit.

ACE, which shifts more of the compliance burden to importers, underscores the need for quality internal compliance verification procedures. A simple clerical mistake may create mistrust and jeopardize a company's future import clearance status, setting it up for more frequent and comprehensive Customs scrutiny. Both translate to increased costs.

C-TPAT

The Customs-Trade Partnership Against Terrorism (C-TPAT) is a program designed to secure the global supply chain. C-TPAT partners, who participate voluntarily, are rewarded for their involvement with reduced inspections at the port of arrival and expedited processing at the border. There could be no better return on program investment. Dishonesty would eliminate such preferential treatment, causing significant economic impact that would have a ripple effect throughout the supply chain.

10 + 2

The 10+2 security program under consideration by U.S. Customs and Border Patrol will require importers to collect additional information about containers coming into the United States. Timeliness and availability of required information mandate major adjustments to importers' processes, as the proposed regulation will shift additional security responsibilities to importers. It may not be easy to catch inaccuracies originating from agents in foreign countries in a timely manner, but, as a minimum, an honest effort must be demonstrated. Clearly, failure to discharge the responsibilities envisioned under 10+2 could increase Customs scrutiny.

Financial Supply Chain

As the marketplace becomes more global, distance and other factors create conditions where fraudulent activity can thrive, causing growing economic problems for the trading community. Most often, fraud occurs with financial instruments such as letters of credit and it can involve large sums of money. Careful reconciliation of financial and compliance data is paramount to accommodate

honest participants of the financial supply chain and to separate the others.

Audits and security protection programs are expensive to implement. All global supply chain participants eventually bear the costs when fraud necessitates the adoption of more preventive measures. Sophisticated computer systems enhance protection and make it possible to stay compliant. Overall, a firm's bottom line will be positively affected by using a preemptive compliance tool.

IMPORTANCE OF BEING COMPUTERIZED

Part of the inhumanity of the computer is that, once it is competently programmed and working smoothly, it is completely honest.

- Isaac Asimov

Computerized data analysis provides many benefits in preventing and detecting logistics, compliance and financial problems. A full 100 percent of transaction data can be verified and done in less time than manual procedures allow. Automation also yields improved business intelligence, as the aggregated information often provides insights that can lead to process improvements.

The automotive companies mentioned earlier can solve the dilemma related to determining country of origin with a real-time, collaborative compliance and "smart-parts"-based warehousing system. It not only keeps track of country of origin but also is completely honest in doing so.

Import Compliance

As discussed earlier, post-entry compliance reviews require importers to establish adequate internal controls and well-documented procedures. Implementing a computerized global trade management system demonstrates to Customs an importer's ability to adhere to compliance regulations. Possessing such a system also confirms the integrity of all the information supplied. The return on investment manifests itself in fewer inspections and audits and smoother movement through Customs.

Reliability of Computer-Processed Data

Generally accepted government auditing standards require that computer-processed data be valid and reliable when those data are significant to auditors' findings. Typically, the data universes and sampling items used for focused assessments include the Customs entry log, purchase orders, vendor master general ledger (GL), invoice line detail, chart of accounts, foreign purchases journal, accounts payable or GL expense file for imported merchandise, accounts payable with GL reference, cash disbursements, wire transfers, letters of credit and inventory records as well as the flow of information across multiple computer systems. Investing in a computerized system that offers a high level of integration, automation and centralized data warehousing (integrity and easy access) will result in considerable savings if a firm should be the subject of a focused assessment.

Firms should recognize that a major "red flag" that may trigger a compliance audit is either the absence of a computer system or reliance on an inadequate computer system. Customs recognizes that it is practically impossible for firms to comply with the many and diverse rules governing trade relying on a manual system based on spreadsheets.

There is no doubt that a Web-based system, especially one coupled to a centralized data warehouse, promotes real-time collaboration between supply chain and financial chain participants. However, collaboration comes with a price; the price is data reliability. Importers, who ultimately hold all responsibility for all compliance issues, must rely on the integrity of a foreign manufacturer or other entity that operates without similar responsibility.

A robust, fully automated, exception-driven system with rich functionality, sophisticated business rules and verified compliance content can minimize user interference and minimize—or at least alert the proper parties of—human-infused errors, both honest and fraudulent. Owning such a system demonstrates an intent to be compliant, which quickly translates to a return on investment.

Export Compliance

Out of necessity, DPL screenings rely on “fuzzy” logic algorithms to detect potential entries in multiple lists. These result in “false positives,” which necessitate user intervention. To reduce the volume of data that require personal attention and to accommodate large volumes of transaction, firms can implement functionality that allows marking of false-positive entries, batch processing and automated delta screenings. Such features save time and money.

Likewise, automating the export license determination process offers economic benefit in terms of saving time and demonstrating sophisticated internal processes. There is another advantage, too. The Bureau of Industry and Security, Department of Commerce, will employ a “Great Weight Mitigation”—equal to a reduction of 25 percent—in administrative penalty cases where an exporter can demonstrate an “effective compliance program” is in place.

New ACE System

From a technical standpoint, the new ACE clearance component offers the same proprietary format used by U.S. Customs since the inception of the Automated Broker Interface (ABI) with minor added conveniences derived from years of experience using the old system. Notably, it does not use Customs declaration message (CUSDEC), the format approved and successfully used by G7 and other countries worldwide for electronic data interchange (EDI) between trading partners.

The trend to relax compliance editing rules places the burden on importers and compliance software vendors since preventable issues should be detected and resolved before they escalate into non-compliance problems. More robust functionality and in-depth content must be maintained, and automation simplifies both requirements.

10+2

Every container coming into the United States generates data to be processed, assessed and acted upon. Even with some level of profiling to separate low-risk shipments, the volume of information sought and the timeline for its reporting will mandate the use of computerized systems. The cost will be money well spent in order to be compliant with 10+2 and its anticipated tight time frames.

Financial Supply Chain

Ever-evolving global trading practices together with highly adjustable manufacturing processes and “on-demand” deliveries require fast reaction to purchase order modifications that, in turn, trigger changes to related commercial, financial and transportation documents, especially letters of credit or open accounts and corresponding vendor payments. Affirmation of rules issued by various government agencies, collaboration with supply chain participants and fraud prevention techniques require access to multiple databases and sophisticated algorithms to analyze rich content. In this environment, automatic reconciliation of financial and compliance data is mandatory.

Compliance and security are hot topics now. The environment continues to intensify with regulators demanding intelligence as well as scrutiny. As organizations deal with a magnitude of new regulations, they need to know which ones impact them and what practices are based. Data retention and retrieval will play major roles. The best-positioned firms will be those with “a

defensible compliance strategy.”

A computer system alone cannot assure adherence to all the trade, financial and compliance regulations that govern global trade management today. Yet, with today’s level of complexity and the sheer volume of information being exchanged it simply is not possible to be compliant without one.

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