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INTERNATIONAL TRADE: IMPROVING THE DUTY COLLECTION/ PAYMENT PROCESS



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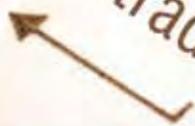


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EXECUTIVE SUMMARY

THIS ISSUE PAPER IS DESIGNED TO ASSIST COUNTRIES and international businesses in improving their processes for Customs duty collection and payment. Modernized duty and tax practices can provide a faster and more efficient system for releasing imports from Customs control. Obtaining this result is particularly important for those businesses that depend upon “just-in-time” production systems. This will improve their commercial efficiency and their ability to compete in the world marketplace. For Customs, improving these processes will speed the collection of revenues, make their transaction more accurate and compliant with laws and regulations, improve border law enforcement for detecting illegal goods, and help remove opportunities for corruption.

This paper provides an overview of the collection process and contains recommendations for Customs reform that encourage countries to:

1. Conduct a comprehensive environmental assessment that addresses the political climate, state of economy, dependency on duties to pay for governmental appropriations, dependency on international trade, professional Customs workforce, level of cooperation among the various border agencies, automation, and international trade processes;
2. Decide on a reform plan, based on the country’s collection process, its public-private sector trade agency/organization relationship, and its scope (conservative, full spectrum, or combination approach); and
3. Develop that plan with involvement and participation of all relevant parties including the trade sector, Customs organization, and experts in the duty collection and planning processes; and identify and develop metrics (performance measures) relative to changes being implemented. Knowing the effect of the reform and gauging improvement is important to holding the gains.

DISCUSSION

Trade-related inefficiencies impose significant additional costs on a country’s imports and exports and seriously diminish its ability to compete in the global economy. Additionally, confusion and corruption at the borders usually hurt the country’s legitimate trade community because of unfair competition from firms that do not comply with the rules.

The use of information provided and implementation of actions recommended in this paper will facilitate international trade, improve the duty collection process, and strengthen international trade security. Adoption of these proposals will also standardize the process of international trade and improve government interface with companies and countries involved in the trade process and, therefore, contribute to the economies of developing countries. Case studies illustrating these points are presented in a later section entitled, “Case Studies in Duty Payment System Reform.”

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THE DUTY COLLECTION PAYMENT PROCESS

The traditional approach to duty and tax collection by Customs is based on manual, transaction-by-transaction processing of each Customs entry or declaration. In developed economies, Customs has developed more advanced processes for collection of taxes, fees, and duties that employ electronic collection, post-entry collection, importer accounts, and surety-guaranteed systems. This paper is intended to assist those countries and international traders that want and need to improve international trading practices and duty collection payment systems.

ALL NATIONS HAVE THE OPPORTUNITY TO INCREASE PROSPERITY by participating more efficiently and effectively in international trade. An efficient and reliable Customs operation along with adequate collection of Customs duties, fees, and taxes is a critical part of that activity. Essential elements of the duty collection/payment process include commodity classification, commodity value, duty computation, origin determination, duty payment, and collection.

Nations involved in international trade collect a variety of "payments" including processing fees for passengers, cargo, and conveyances; tariff duties on commodities; value-added taxes (VAT); and fees related to special programs such as anti-dumping and countervailing duties.

The most significant payments in terms of amount collected and impact on international trade involve duties and value-added taxes assessed on merchandise imported by land vehicles (usually trucks), sea-going vessels with cargo (containerized or bulk), and aircraft. Significant opportunities for improving duty collection/payment on merchandise and commodities exist in many countries through modernization of Customs practices.

The following steps precede the modern collection process:

- First, the importer or agent presents a declaration or entry to Customs describing the goods and the price paid.
- Customs reviews the declaration and classifies the merchandise using the WCO Harmonized Tariff Schedule as a basis.
- Based on the classification, Customs determines the duty owed using the World Trade Organization system for assessing value.
- Customs applies the rules for determining value-added tax or other fees or taxes.
- Customs calculates the total of these assessments.

Alternatively, the importer or his agent may be required or permitted to make these calculations, in which case Customs would verify the totals to determine their accuracy.

Computing the duty due on imported merchandise begins by classification using the Harmonized Tariff Schedules (HTS) of the particular country. This determines the rate

Significant opportunities for improving duty collection/payment on merchandise and commodities exist in many countries through modernization of Customs practices

of duty. Classification is determined by the description of the merchandise on the invoice and summarized on a “formal entry summary.” The value indicated on the invoice is usually the amount paid by the importer to the overseas seller for the merchandise. The amount of duty due is determined by a simple process of multiplying the rate of duty times the value and, if applicable, adding specific duty rates by weights or other measures.

Payment of duty is made via the submission of a declaration or similar form/data, usually along with the invoice. Many countries require duty to be paid before the merchandise is released into the commerce of the importing country, with the goods being held at the border or in a Customs facility. At the extreme, the delay is so odious that it constitutes a non-tariff trade barrier. Other Customs administrations expedite the flow of cargo by requiring duty to be paid after the release of the merchandise, usually within a set time



period (e.g., 10 days). Some countries have halted direct collections by Customs, relying instead on banks to collect duty payments.

To ensure duty is paid, the importer often deposits a bond. In these instances, the revenue is protected by the utilization of a surety bonding system that guarantees full payment of financial obligations upon the completion of administrative requirements. A bond and security system works to the advantage of both the importer and Customs in that Customs is assured that the revenue is protected and the importer may be assured of predictability, facilitation, and release. The importer or agent will be assessed a nominal fee for the bond by the surety. Bonds may cover a specific shipment or be for a specific period of time, for example, one year.

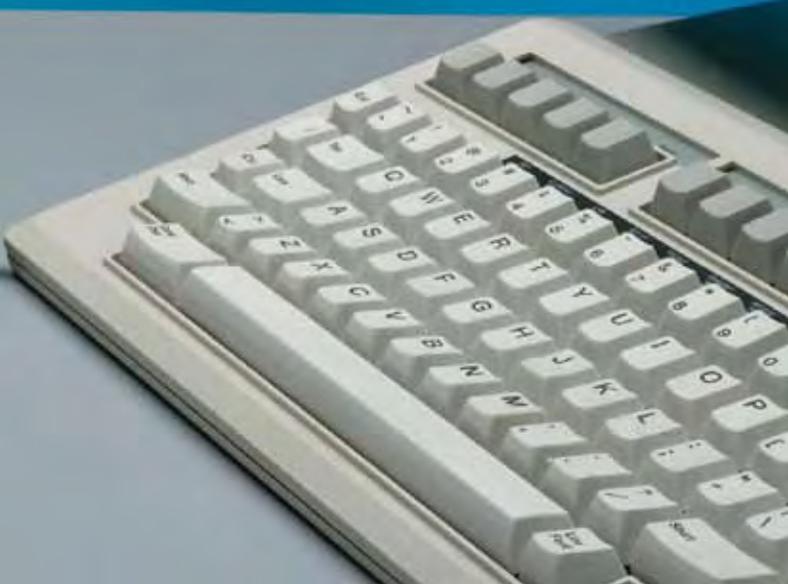
Separation of cargo release from payment is significant to border formalities as it will not only reduce the border clearance cycle time for repeat, low-risk, highly compliant importers and shippers, but the resulting reduction in port congestion also can speed the effective border clearance of all entering goods and people. This approach also allows the Customs agency to focus its scrutiny and inspection on high-risk shipments, increasing the detection of customs fraud and smuggling attempts. Of course, some commodities such as those covered by quota or a special program may require that duty and release of merchandise be done at the same time.

Until recently, most countries collected the duty/payment via the submission of a check with the entry summary for each and every importation. Most countries employ a sizable state employee workforce to process imported merchandise. This includes:

- Inspectors at the ports of entry to verify the merchandise description and to quantify and determine the admissibility of the merchandise based on the health and safety laws of the importing country;
- Experts in classification to verify classification, value, and the amount of duty to be collected;
- Entry processing personnel to collect the entries, separate the checks, and forward the checks for deposition;
- Financial personnel to effect deposit and prepare input into the country's financial system; and
- Auditors to review internal agency records and trade community records to ensure compliance with all laws, accurate duty computation and payment, and detection of fraud.



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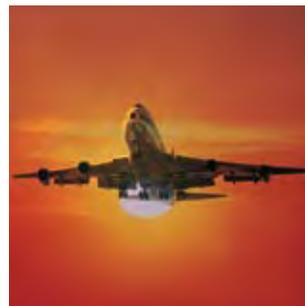


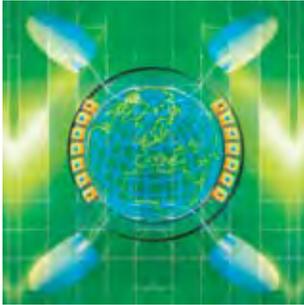
APPROACHES AND STRATEGIES

Steps that are intended to ensure collection of the revenue and prevent loss or theft of funds may also serve to hinder rather than facilitate trade and may not be necessary to ensure integrity under a modernized system of revenue collection.

STEPS FOR IMPROVING DUTY COLLECTION must address key areas including integrity, duty payment insurance, electronic payment of duty, periodic duty payment, entry accountability, and government partnership with the trade. Key elements of improving the duty collection processes are as follows:

- **Integrity.** A country's intentions regarding accurate duty collection and effecting improvements to the process depend heavily on the integrity of the country's border control and duty collection personnel, the soundness of the processes involved, and the existence (or lack of) safeguards in the border systems to prohibit fraud and theft. Effective recruitment, adequate compensation, a code of conduct, performance incentives, professionalism and pride, built-in system safeguards, investigation of alleged integrity violations, and prompt and effective employee discipline all serve to enhance integrity.
- **Duty Payment Bond.** The payment of duty can be assured via the use of a surety or insurance instrument, usually referred to as a bond. This bond is acquired by the importer via the use of an insuring entity/surety. It guarantees that the importer will pay the duty due and conform to all other importing requirements. The bond provides the basis for releasing merchandise before the duty is paid, thereby expediting the movement of the cargo.
- **Electronic Payment of Duty.** Duty can be paid via electronic funds transfer. This involves the importer or Customs broker submitting the duty payment from a financial institution or from the importer's financial entity directly to a bank designated by the government agency responsible for duty collection, usually the country's Customs organization. This is not only more efficient, but it also helps to provide integrity safeguards as human intervention is minimized.
- **Periodic Duty Payment.** Efforts to reduce the cost of collecting duty often include exploring methods for consolidating payments. The importer, usually through a Customs broker or agent, submits one payment for all of the merchandise entered into a country, usually for a period of one month. For example, if an importer would have paid duty on 1,000 separate shipments with 1,000 checks during a one-month period and that duty would have totaled \$2 million, one payment in the amount of \$2 million may be paid at the end of the month.
- **Entry Accountability.** Using periodic duty payment and electronic payment of duty does not absolve the importer of responsibility for accounting for every entry of merchandise. The periodic duty payment should be accompanied by a listing of all entries for which payment is due. Such a listing is necessary to account for all the





Movement of merchandise may also be expedited by strengthening the “international supply chain”

Supply chain security can go hand in hand with improving trade compliance and efficiency

merchandise and to determine the exact date of entry. Some countries, such as Canada, are moving to a post-entry audit approach in lieu of accounting for every entry.

■ **Partnership with the Trade.** Most international trading organizations (such as importers, brokers/agents, and freight forwarders) are motivated to comply with the importing country laws and pay the duty owed. Duty is regarded by most trading organizations as a legitimate “cost of doing business.” Failure to comply with a country’s laws can delay or deny the entry of the commodity, causing far more loss of revenue than paying the duty. Accordingly, the importing country can often achieve mutually beneficial relationships and trading practices through assisting the trading organizations by:

- Jointly reviewing the trading organizations’ internal processes for conforming to Customs and related laws;
- Providing training to the trading organizations’ personnel involved in preparing and submitting entry documentation and payment;
- Providing feedback to the trading organization and providing an opportunity to correct errors in submissions, in lieu of taking punitive actions; and/or
- Expediting the movement of the participating “trusted” trade organization’s merchandise.

Such assistance may be provided directly to the trading organization or to its Customs broker, as appropriate. Failure to provide a fair and equitable system may cause other Customs violations such as misclassification, undervaluation, and smuggling.

Movement of merchandise may also be expedited by strengthening the “international supply chain.” This protects the integrity of the merchandise shipment from time of manufacture in the foreign country until its delivery to the ultimate consignee (usually the importer). Supply chain security can go hand in hand with improving trade compliance and efficiency. Measures that developing countries may follow for creating secure, compliant, and efficient supply chains that will meet the expectations and requirements of the U.S. and other major trading nations are contained in a document entitled, “International Supply Chain Security: Its Impact on Developing Countries,” prepared by Michael H. Lane for the USAID FASTrade Project and posted on the Project Web site.

■ **Training.** Effective operation of current collection/payment systems and the implementation of change require that the importing country’s workforce be competent and knowledgeable. This can be achieved only with the availability of a full curriculum of appropriate technical courses and its delivery to field officers involved with the Customs duty collection and clearance processes.

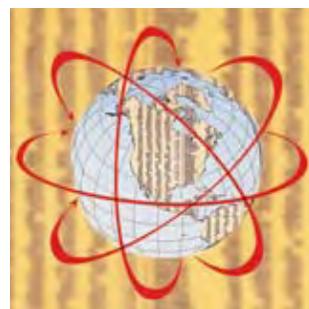
RECOMMENDED ACTIONS

SPECIFIC ACTIONS FOR DEVELOPING AND IMPLEMENTING THE KEY ELEMENTS

outlined above include conducting an environmental assessment, deciding on an appropriate approach, conducting requisite planning, and implementing performance measures. These actions are discussed below.

- **Conduct an Assessment of the Customs Environment.** An environmental assessment is necessary to determine the current state of the importing country's collection systems and key factors that must be considered in improving those systems. The questions to be asked regarding the environment follow closely with the basic elements of the importing process and the key features of an expedited process, as described above and summarized below.
- **Decide on the Scope.** A systematic analysis must be made of the important factors in the environment, the current state of the country's collection process, and the customs-trade relationship. The key elements of alternative improved collection approaches also must be systematically analyzed and compared. No simple or universal approach can be prescribed for this discussion. Although the information gleaned from the sections above will be invaluable, for the final analysis, an evaluative approach must be pursued and a plan prepared that is appropriate for the individual country. Examples of key premises for such plans include:
 - a) *Conservative Approach.* The country's total Customs environment and capabilities do not lend themselves to innovative collection/payment approaches. The emphasis in the short term, therefore, should be on implementation of safeguards to prevent theft, enhance integrity, and promote an improved relationship with the trade as well as on improving the quality of entry submissions and providing training of Customs personnel to better assist the trade.
 - b) *Full Spectrum of Innovations.* With a firm base in automation and a good partnership with the trade, the country's Customs organization is an increasing participant in international trade. Such a country may be ripe for significant improvements including periodic duty collection, electronic duty payment, extensive training of the trade regarding their internal duty-related processes, and the use of post-entry audit approaches.
 - c) *The Middle Ground.* The country's Customs organization has many of the requisite elements needed to modernize payment and collection. Such a country may benefit from both short-term and long-term improvement approaches building upon elements of both a) and b) above.
- **Develop a Plan.** The following parties should be involved in developing a plan based on information gained from the environmental assessment:
 - **The country's key managers of its duty collection process**, including those involved in port operations, trade outreach, finance, and legal affairs. Each of these managers

An assessment of the Customs Environment is necessary to determine the current state of the importing country's collection systems and key factors that must be considered in improving those systems



represents a key facet of the duty collection/payment process that must be encompassed in an effective plan;

- **Key participants from the trade sector** who represent the greatest volume of trade and pay the largest amount of duty. Care should be exercised, however, to involve the smaller players, who may have different trade processing and payment challenges and should not be overlooked; and
- **Experts in the field of international trade facilitation** and duty collection/payment should be used to support this joint effort and facilitate team formation, strategic and tactical planning, conducting of planning sessions, preparing action plans, assisting in implementation, and monitoring progress. The World Customs Organization (WCO), the Customs Services' of industrialized countries, and other international donor organizations may all be of assistance to this joint planning and implementation effort.

■ **Institutionalize Performance Measures/Metrics.** The benefits of cross border trade liberalization and improved duty collection are generally accepted. But it is good for a country that is implementing improved collection procedures to be able to measure the success of its own efforts. To the extent feasible, before and after processes should be documented and performance measures for new procedures should be developed, addressing such variables as costs of operation and amounts collected before and after the improvements are implemented and efficiencies that may be derived from a facilitated trade process. The measures should be continued indefinitely so that the gains realized from the reforms are maintained.



CASE STUDIES IN DUTY PAYMENT SYSTEM REFORM

Successful international initiatives can serve as case studies and models for improving international trade and duty collection. No single case can demonstrate all of the approaches outlined above. Hence, the summaries below contain many cases for which additional information Web sites are shown, in the event that further information is desired.

INDONESIA

During the March 22–April 2, 2004, International Civil Aviation Organization (ICAO) Facilitation Division Conference in Cairo, Indonesia presented, “Trade Initiatives for Trade Facilitation in Indonesia.” Indonesia’s plans include modernization of automation to eliminate unnecessary intervention of Customs officer(s) during the clearance process, enforcement measures, importers registration, improved intelligence, comprehensive measures for combating smuggling, and new release procedures for importers with high compliance and outstanding reputation, as well as many other measures that collectively incorporate most of the elements and recommendations provided in this paper. More information is available at: http://www.icao.int/icao/en/atb/fal/fall2/documentation/fall2ip015_en.pdf.

SOUTHEAST EUROPEAN COUNTRIES

In a collaborative effort among Albania, Bulgaria, Bosnia, Croatia, Macedonia, Moldova, Romania, and Serbia and Montenegro (Yugoslavia), and with the support of the World Bank and the United States, these countries are implementing a wide spectrum of initiatives to facilitate the movement of trade across their shared and exterior borders, including the single payment window. The Web site, www.ttfse.org, provides extensive, valuable information on this cooperative program.

LAOS

As part of a broad spectrum of efforts to improve its financial infrastructure, Laos is developing simplified and computerized customs declaration procedures. These include streamlining tariff nomenclature and customs valuation procedures, Customs training and manuals, and production of trade statistics. Such efforts help enhance the public sector’s economic performance. More information is available at: www.undlao.org.

JAMAICA

In early 2001, with funding assistance from the World Bank, Jamaica began efforts to improve Customs duty collection and clearance procedures, including extensive automation, partnership with Customs brokers, streamlined duty payment and cargo release, and other initiatives. Additional information is available at: http://www1.worldbank.org/publicsector/egov/jamaica_customs.htm.

Indonesia is implementing measures that collectively incorporate most of the elements and recommendations provided in this paper

Southeast European countries are implementing a wide spectrum of initiatives to facilitate the movement of trade across their shared and exterior borders

Laos is developing simplified and computerized Customs declaration procedures

Jamaica is implementing efforts to improve Customs duty collection and clearance procedures

The Philippines Customs Bureau has developed an on-line system to process clearance of imports, payment of duty, and delivery of release orders

Poland has modernized its Customs processes to ensure effective control and fraud detection while at the same time facilitating the free movement of goods

PHILIPPINES

Using an “off-the-shelf” customs application package as the main building block, the Philippines Customs Bureau has developed an on-line system to process clearance of imports, payment of duty, and delivery of release orders for shipments to leave the docks. The new on-line system has lessened the cost of trade for businesses, reduced opportunities for fraud, and helped the Bureau to maximize revenue collection. Additional information is available at: <http://www1.worldbank.org/publicsector/egov/philippinecustomscs.htm>

POLAND

To meet the challenge of European Union (EU) accession, Poland has modernized its Customs processes to ensure effective control and fraud detection while at the same time facilitating the free movement of goods. The Integrated Duty and Tax System was developed, which includes budget accounting, tax clearing, and declaration processing with validation and risk analysis, data warehouse, and a Customs government gateway. Benefits include reduction of processing time from 15 to 2 minutes, error reduction, freeing up of staff to focus on core functions, increased responsiveness to changing circumstances, and compliance with EU accession requirements. More information is available under ID=14864 at: <http://www.microsoft.com/resources/casestudies/CaseStudy.asp?CaseStudyID=14864>

CONCLUSION

Trade-related inefficiencies impose significant additional costs on countries' imports and exports and can seriously diminish their ability to compete in the global economy. The improvement of duty collection processes can facilitate and increase economic development and international trade, enhance duty collection, and improve international trade security.



Methods to collect duty payments entry by entry are inefficient and time consuming and, therefore, costly to the trading community and a hindrance to economic development. This paper recommends a sound approach for reforming a country's duty collection process in a way that is appropriate to its political and economic environment and border processing infrastructure, as well as to its dependence on international trade.



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