



USAID
FROM THE AMERICAN PEOPLE

TAPRII
TECHNICAL ASSISTANCE
FOR POLICY REFORM

CUSTOMS POST-CLEARANCE AUDIT MANUAL

June 2006

This publication was produced for review by the United States Agency for International Development. It was prepared by the USAID-funded TAPRII project.

CUSTOMS POST-CLEARANCE AUDIT MANUAL

TECHNICAL ASSISTANCE FOR POLICY REFORM II

CONTRACT NUMBER: 263-C-00-05-00063-00

BEARINGPOINT, INC.

USAID/EGYPT POLICY AND PRIVATE SECTOR OFFICE

JUNE 2006

AUTHOR: ALAN MORLEY

SO 16

DISCLAIMER:

The author's views expressed in this publication do not necessarily reflect the views of the United States Agency for International Development or the United States Government.

CONTENTS

Chapter 1:	INTRODUCTION.....	1
Chapter 2:	PURPOSE AND ORGANIZATION OF ENTERPRISES.....	3
Chapter 3:	PRIMARY RECORDS MAINTAINED BY AN ECONOMIC ENTERPRISE	6
Chapter 4:	SUBSIDIARY RECORDS KEPT BY AN ENTERPRISE.....	8
Chapter 5:	STAGE 1 – PRE-VISIT PLANNING.....	10
Chapter 6:	STAGE 2 – INITIAL INTERVIEW WITH THE IMPORTER.....	12
Chapter 7:	STAGE 3 – CUSTOMS AUDIT PROCEDURES	14
Chapter 8:	STAGE 4 – CREDIBILITY CHECKS.....	26
Chapter 9:	STAGE 5 – COMPLETION OF THE AUDIT VISIT.....	28

CHAPTER 1: INTRODUCTION

1. Customs Post-Clearance Audits

1.1 The assessment of customs payments on importations is based upon the Customs import declaration that the importer submits at the time of importation. The declaration is verified and, based upon selection criteria, Customs officers may examine the imported goods prior to release, but there are some elements of the import declaration that cannot be adequately verified at the time of importation. For this reason, audits may be conducted at some time after the importation of the goods to verify the accuracy of the Customs import declaration. During these audit visits various control techniques are used to determine the accuracy of the declarations. This manual describes a number of such techniques and their application in the post-clearance audit of Customs declarations.

2. Legal Authority for Customs Post-Clearance Audits

2.1 The legal authority for the conduct by the Customs Authority of post-clearance audits is _____ *(to be completed upon passage of appropriate amendments to the Customs Law and/or the Executive Regulations of the Customs Law to establish the legal authority for the conduct by the Customs Authority of Post-Clearance Audits)*

3. The Purpose of Audit Visits.

3.1 Visits are made to importers to verify the accuracy of their Customs import declarations. The importer's expectation of such a visit has preventive and deterrent effects. The preventive effect is the extent to which control visits prevent importers from under-declaring their liability at the time of import declaration. The deterrent effect is the extent to which importers decide not to avoid or evade Customs requirements, because they are aware of audit/control activity and fear detection.

3.2 Within a scheme of post-clearance audit control, audit activities should be directed to areas of the greatest revenue or potential revenue risk. It is not expected that all aspects of an importer's import activities will be covered on every visit. However, almost every import activity represents a potential duty and/or tax risk. There is a consequent need for checks to be planned across the totality of an importer's import activities over a series of visits.

3.3 The post-importation audit control program, which is drafted and approved in advance for the following year or quarter, should allocate the available person-years of direct staff effort to the selective audit control of the current importer population. The basis for selection should be the apparent revenue risk of the individual importer, and the frequency and duration of the visits should be determined by the degree of difficulty and risk perceived.

3.4 The manner in which audit is exercised must be perceived generally as fair and reasonable.

4. Conclusion.

As it is not always possible (or desirable), to verify the correctness of all the import transactions and activities of an enterprise on each visit, the need will be recognized for a proper systematic method of recording what has taken place. Over a period of time all the import activities can be covered, and the records of the visits will help in establishing which area of the enterprise is most likely to require further checks. In this way audit visits are set up as part of a continuing system that becomes more effective as time goes on. It will allow management to be more selective in the allocation of resources.

CHAPTER 2: PURPOSE AND ORGANIZATION OF ENTERPRISES

1. Purpose of an Enterprise.

1.1 The purpose for starting an economic enterprise is, generally, to earn profits. The earning of profits distinguishes an economic enterprise from a charitable organization, and from certain other organizations such as Clubs and Societies, which, although they may often make profits, are not set up for that sole purpose. Clubs and Societies are generally set up to further the interests of their members. They often provide social amenities, or act as a non-profit making umbrella organization.

1.2 An economic enterprise often comes into existence because an entrepreneur has the vision to recognize an unfulfilled need in society. It can also be the result of a special skill or knowledge possessed by the entrepreneur or, as a result of concentrated training, as is the case with the professions, e.g. architects, lawyers, etc.

1.3 There is one additional element necessary before an enterprise can become viable, and that is capital. The amount of capital necessary to commence an enterprise varies considerably, and it can be said that, in the case of the professions, much of the required capital has already been invested in the years of study and training that is necessary. Manufacture or trading in goods requires a considerable amount of capital for the purchase of machinery and raw materials and/or for stock for resale.

1.4 Capital used to invest in an enterprise is known, with justification, as "risk capital". Enterprises can fail as well as succeed. Persons investing in an enterprise need to be aware of the risks that are involved. A successful entrepreneur is required, over a period of time, to give a satisfactory return on the capital invested. If the enterprise can make no more profit than would be achieved by depositing the capital in savings the risk is not justified. It is of course possible for an enterprise to operate at a lower than usual profit on capital invested, for a period when the enterprise is being developed, or when expansion is taking place, provided that the long-term prospects are for a greater return.

2. Organization of an Enterprise.

2.1 It can be accepted that all enterprises, of whatever size, must have some form of organization. In general an efficiently organized enterprise will give a higher return than a badly organized enterprise. The wider the range of activities and the larger the turnover, the greater is the need for an efficient organization. Large concerns will go to considerable lengths to ensure that this is achieved.

2.2 However, it must not be forgotten that even a small enterprise will need some sort of organization, even if this merely means the allocation of responsibilities to various family members.

2.3 The features of an organization generally include a formal structure that is often hierarchical, a variety of systems to cope with the operation of the business, and a considerable element of delegation, with the co-related reporting and feedback systems. Structures of organizations may be varied to meet the particular requirements of the business, but there are many areas where the basic structures are similar.

2.4 The more complicated the structure of an organization, the more likely it is that a model or description will be set out in a formal manner so that the requirements, once they are determined, are known to all members of management.

3. Risk Areas in Enterprises.

3.1 There are certain areas within enterprises that have a higher risk factor than others. Most enterprises will have identified these and made special arrangements to reduce those risks. The risks arise in areas that can usually be identified, such as cash handling, stock control, lowly paid employees, etc.

3.2 In a well-organized enterprise these risk areas will, normally, be the focus of a greater number of management checks. Specific responsibilities will be allocated. This principle is well illustrated by the practice of allowing only family members to handle cash in family-owned enterprises.

3.3 Where goods that are attractive to members of staff are held in stock, it is often the case that unannounced searches are made by the enterprise. It is also common to allow employees to purchase such goods at a reduced price - this is intended to discourage petty theft, and to make employment in such enterprises more desirable.

4. Delegation of Responsibilities.

4.1 Except in the smallest enterprises, generally there will be some delegation of responsibilities. Examination of a large enterprise will reveal the manner in which such delegation may take place. Normally this will be done by the segregation of integral parts of the enterprise. Typically, these will include:

- a management team (or Board of Directors);
- a purchase department;

- a sales department;
- a production or manufacturing department;
- a personnel department;
- a transport section;
- a customer relations section; and etc.

4.2 These sections or departments may be further sub-divided where the enterprise is very large or where management considers it to be necessary.

4.3 The effect of this division of responsibilities is that a system of record keeping, and reporting is essential if management are to keep proper control of the enterprise. Delegation does not mean the abdication of responsibility by management.

5. Conclusion.

5.1 Enterprises are complicated organizations whose aim is to make profits or, at the very least, to give a satisfactory return on the capital that has been invested. This cannot be achieved without a formal allocation of responsibilities, a considerable amount of record keeping, and a system that is understood and recognized by all staff.

5.2 Customs officials who have responsibility for audit are required to recognize these realities and to be able to make use of them in their work. Enterprises that attempt to pretend to auditors that they do not keep records or who deny any form of organization should be treated with suspicion. The audit visit should be structured carefully to ascertain the reasons for this deception. It should be noted as well that provisions of the Customs Law and Executive Regulations require an enterprise to maintain records of imports and exports. Failure to present documents required for Customs Control may entail administrative sanctions.

CHAPTER 3: PRIMARY RECORDS MAINTAINED BY AN ECONOMIC ENTERPRISE

1. General.

1.1 The general nature of importations has the effect of bringing a very wide range of types and sizes of enterprise within the Customs field. This means that Customs Post-Clearance Auditors will be required to become familiar with a wide range of accounting systems and other enterprise records.

1.2 It is a function of Customs Auditors to make themselves familiar with these various systems, and the best tutor is experience. A common misconception is that there is some loss of face and authority if a Customs Auditor has to ask an entrepreneur to explain how the accounting system works. This is not the case. It is increasingly common with the advent of computerised systems for an Auditor, Accountant or other person unfamiliar with the systems of a particular business to spend the first period of time being shown how the system works. In fact it is easy to lose credibility with the staff of the enterprise if an attitude of "I know it all" is taken.

1.3 With the gradual change to International Accounting Standards it will be found that, in most enterprises of medium size, double entry bookkeeping is the usual practice, although many enterprises will also be using special systems of their own. If any system is encountered that is new to the Customs Auditor, he should ask for guidance from the staff of the enterprise or ask for any available literature.

1.4 In smaller registered enterprises, cashbook accounting is becoming increasingly common. However it is unlikely that the accounts of smaller enterprises will prove to be a problem to Customs Auditors. In these cases the main problem is likely to be a lack of records.

1.5 The main problems are likely to arise in large enterprises. In such enterprises computerised systems are common or there are specialized records and accounting systems that have been developed. However, in these cases, accounts staff are often accustomed to explaining how their systems work, as other people within the enterprise require to obtain information but will not be technically expert in computers or specialist systems.

1.6 The essential feature in all proper accounting systems is of course the existence of an audit trail. If any enterprise is found to have an accounting system from which an audit trail is absent, the facts should be reported for consideration of a further detailed examination of the business. Many systems that involve computers are not fully self-contained but merely record data and produce hard copy print-outs which then form the normal accounting books (e.g. invoices listed to produce a day-book).

1.7 All audit work on the financial records of the registered enterprise is designed to test whether the import declarations made by the enterprise are correct. No detailed requirements are set out as to the form of further checks. The results of special selective checks and the examination of the business premises, stocks and materials will indicate these. Any factor that comes to the attention of the Customs Auditor that indicates a possible irregularity in the import affairs of the enterprise will also indicate what further checks should be undertaken.

1.8 The attention of Customs Auditors is drawn to the subsidiary records of the enterprise. These are difficult to falsify but they are an integral part of the running of any enterprise.

1.9 Customs Auditors will encounter a number of enterprises that have special methods of maintaining records. Where a small range of specialized goods is traded it is common for sales invoices to merely list code numbers. Such invoices are meaningless to anyone outside the trade. In such cases the enterprise should be required to provide an interpretation of the coded items. This should normally cause no problem. In other cases the specialized nature of enterprises will have necessitated the development of specialized procedures. In such cases the Customs Auditor should ensure that any information that is gathered, that would be of use to another Customs Auditor visiting an importing enterprise in a similar trade, is permanently recorded.

1.10 Customs Auditors should take note of the circumstances under which certain records are required under Egyptian Law to be kept by an enterprise.

CHAPTER 4: SUBSIDIARY RECORDS KEPT BY AN ENTERPRISE

1. Introduction.

1.1 There is a general tendency to think of the records of an enterprise as consisting of financial records and the associated financial documents. These records are of course very important and form the basis of a verification of the Customs value of imported goods.

1.2 However, from the viewpoint of the Customs Auditors involved in an audit, the various supplementary records that are necessary for the operation of a viable enterprise are of equal importance. In fact they are the foundation on which all of the operations of the enterprise are based.

1.3 Another factor that increases the importance of supplementary records is that, because of their volume and as subordinate staff prepare them, it is extremely difficult for them to be falsified. In fact, even if the financial records have been falsified to reflect an incorrect valuation of imported goods, the supplementary records can be used to prove or disprove the accuracy of the financial records.

1.4 The essential factor to be borne in mind concerning supplementary records is that, although they relate to different aspects of the enterprise, they are all related to each other. As such they can be used to establish the credibility of the financial records.

2. Types of Subsidiary Records.

2.1 There are two main types of subsidiary record.

- The first are the **STOCK RECORDS**.
- The second are the operational control records such as **DELIVERY NOTES, ORDER FORMS, PRODUCTION RECORDS, TRANSPORT RECORDS**, etc.

3. Use of Subsidiary Records for Customs Post-Importation Audit.

3.1 Subsidiary records are the working documents of the enterprise. They should all support each other and the information that they contain should have a direct relevance to the activities of the enterprise.

3.2 During verification visits, Customs Auditors should take the opportunity to examine all of the available supplementary records. They should attempt to test whether the information that these records contain confirms that in other records, particularly the financial records.

3.3 As an example, if a manufacturer buys electric motors to incorporate in the machines that he makes and one motor goes into each machine, there should be a direct relationship between the number of motors purchased and the number of machines manufactured. In the clothing industry there is often a direct connection between garments made and purchased components such as zips and buttons. This can be a critical element in verifying the accuracy of Customs declarations made by an importer of goods under the Temporary Import for Processing regime.

3.4 Whenever an inconsistency is found in the subsidiary records, the matter should be fully investigated in a discrete manner. There is usually no offence directly relating to the subsidiary records but inconsistencies can often reveal errors in the financial records.

4. Conclusion.

4.1 It is not possible to give precise directions on how Customs Auditors should proceed in their examination of supplementary records. Experience will be the best tutor. However the examination of these records is closely related to the use of "credibility". Together they will give the diligent Customs Auditor a good basis on which to carry out the audit procedures

CHAPTER 5: STAGE 1 – PRE-VISIT PLANNING

1. Factual information concerning the importer.

1.1 When an enterprise has been selected for an audit visit it is essential that all available internal information is gathered and read thoroughly by the Customs Auditor. Current information comes from reports on the importer's imports and exports, reports on the importer's payments of duties and taxes, and copies of the importer's import declarations. This information can be used for visit selection, assessments, allocation of resources, and legal procedures, e.g. enforcement. Out of date information can cause legal problems and embarrassment to Customs Auditors and the Egyptian Customs Authority. All correspondence in the importer's file should be read as well as any report of a previous audit visit.

1.2 The record of compliance of the enterprise in respect of the preparation of Customs import declarations and making payments of Customs duties, taxes and fees should be noted. As well the Customs Auditor should take into account the enterprise's record of compliance for other taxes. The more information a Customs Auditor can gather before the audit visit the better prepared he will be.

2. Arranging the Audit Visit.

2.1 Unless it is felt unwise to warn the enterprise of the forthcoming visit, for example if fraud is suspected, it is preferable to make an appointment and ensure that the person in charge of the enterprise is available.

2.2 The Customs Auditor must also ensure that all of the accounting records will be available during the audit visit. The Customs Auditor's request for the records to be available may include the following:

- expense records and receipts;
- bank records;
- purchase/sale invoices;
- import and export documents;
- inventory records;
- annual accounts, such as profit and loss statements;
- balance sheet; and
- any other records which may be unique to the enterprise.

3. Final Preparations.

3.1 In preparing to call on the importer, the Customs Auditor should be fully prepared for all contingencies. The Customs Auditor should take:

- credentials to prove he/she is an authorised Customs official and has been instructed to make the visit;
- a copy of relevant file information concerning the importer/transporter of goods;
- copies of applicable Customs Laws, Decrees and Orders; and
- any guidance notes and public notices to advise the importer.

CHAPTER 6: STAGE 2 – INITIAL INTERVIEW WITH THE IMPORTER

1. General.

1.1 The procedure adopted on visits will vary according to various factors, including the size of the enterprise, the frequency of visits, the complication of the accounting system, the volume of records kept, and the revenue reputation of the registered enterprise. However there are certain basic procedures that should always be carried out and the order in which they are carried out is important.

2. Initial Interview.

2.1 On commencing an audit visit the Customs Auditor should contact a person in authority (director, partner, manager, proprietor, etc. as appropriate). This first contact is of great importance as it establishes the seriousness of the matter, gives the Customs Auditor a status link with the top management, and provides a reliable source of information concerning the business.

2.2 This person should be asked to confirm that the information concerning the business held in official records is still correct (or give details of any changes).

2.3 The interview with the importer must be thorough and it is important not to assume anything. Although some questions may appear obvious it is essential that the importer confirm all details.

2.4 The Customs Auditor should ask if the enterprise has any problems concerning import or export processes. He should always help the importer with genuine problems but should not attempt to answer hypothetical questions. He must not be drawn into discussion concerning the rights or wrongs of Customs requirements. He should not give answers to questions if he is not certain of the correct answer but should always arrange to give the importer an answer in due course, either by telephone or, preferably, by letter.

2.5 The entrepreneur should be asked to identify the person who has been given the responsibility for completion of import declarations, and whether authority for that has been given in writing.

2.6 It is not essential that the person first seen accompanies the Customs Auditor for the whole of the visit but the initial interview is important.

2.7 A suggested format of the initial interview, although not exhaustive, is set out below:

(i) Enterprise:

- who owns the enterprise;
- are there any other premises;
- what are the names/TINs of any associated enterprises;
- how many employees;

(ii) Activities:

- what are the trading activities;
- what type of goods/works/services does it provide;
- what are the main purchases/expenses;
- what are the main capital assets;
- who are the main suppliers; and
- are there any major customers and who are they?

(iii) Accounts:

- what sort of accounting records are maintained;
- who prepares the accounting records;
- who prepares/signs the import declarations;
- who are the external audit/controllers;
- how many bank accounts are kept;

CHAPTER 7: STAGE 3 – CUSTOMS AUDIT PROCEDURES

1. General.

1.1 This chapter sets out the basic checks that should be made by the Customs Auditor to test the validity of certain types of Customs declarations.

1.2 Customs Post-Clearance Audit is not intended to be a full financial audit. It is not the place of the Customs Auditor to ensure that the enterprise has met the demands of International Accounting Standards. Audit is intended to ensure that the enterprise makes correct declarations to Customs and pays the correct amount of duty and taxes on imported goods. It is not possible to check all of the records of an enterprise for accuracy as is sometimes done in a financial audit. Selective checks need to be made to the extent necessary to ensure that the figures on the Customs declarations are based on the records of the enterprise.

1.3 It is easy for audit visits to become pointless checking exercises. Nevertheless there is a need to carry out some basic checks although these should, initially, be on a selective basis.

2. Reasons for Selective Checking.

2.1 In modern production systems it is unusual for mechanical checks to be made on 100% of the manufactured items. Such methods are wasteful of resources, uneconomic and achieve very little. Valuable resources are better deployed on more productive work.

2.2 It is not always necessary in the conduct of an audit to attempt to make a full check of every entry in the import and export declarations of an enterprise. The auditor should begin by making percentage checks of any type of entry. If these are correct no further checking of these types of entry will normally be necessary. However, if the selective checking reveals significant numbers of errors the checking must be extended.

2.3 It is necessary to find out if the errors cause any loss of duty or taxes. If the duty or tax loss can be isolated and calculated precisely or if it extends over a longer period a special assessment will need to be made.

2.4 At the stage in the audit visit when the Customs Auditor has completed the basic checks he should consider the value of extending his audit to more in-depth checks, further credibility checks and into carrying out one or more special selective enquiries.

2.5 If the enterprise furnishes inadequate books and records the Customs Auditor will also need to extend his audit to in-depth checks, further credibility checks and more selective enquiries. Inadequate books and records are indicative of transactions and other matters being suppressed and he will need to keep this in mind as he extends his audit.

2.6 A record of the basic checks carried out and the results should be made in the visit report of the Customs Auditor.

3. Subsidiary Records.

3.1 As subsidiary records are the working documents of the enterprise, they should all support each other, and the information that they contain should have a direct relevance to the outputs of the enterprise.

3.2 During audit visits Customs Auditors should take the opportunity to examine the available subsidiary records and make an attempt to test whether the information that they contain seems to confirm what is held in the other records, and in particular the financial records.

3.3 Whenever an inconsistency is found in the subsidiary records the matter should be fully investigated in a discrete manner.

3.4 It is not possible to give precise directions on how Customs Auditors should proceed in the examination of subsidiary records. These records will vary from enterprise to enterprise and it will be for the Customs Auditor to decide the manner in which they should be checked to best advantage. Experience will be the best tutor. Nevertheless the examination of the subsidiary records is closely related to credibility. (These are considered in the next chapter.) Together they will give the diligent Customs Auditor a good basis on which to carry out the audit procedure.

4. Determination of Customs Value

4.1 Pursuant to Article 22 of the Customs Law and Article 14 of the Executive Regulations of the Customs Law, determination of the Customs value of imported goods is based upon the price paid or payable on the sale of the goods for export to Egypt. Pursuant to Article 23 of the Customs Law, the importer shall submit the purchase contract or commercial invoice documenting the sale of the goods to the importer to identify the price paid or payable for the goods.

4.2 The first objective of a post-clearance audit of the Customs value presented on an import declaration is to confirm if the price paid or payable shown on the purchase contract or commercial invoice attached to the import declaration can be corroborated by the financial records and subsidiary records of the importer. This corroboration can be made in one or more of the following ways:

- Comparison of the invoice value to the importer's payment or expense records – do the records reflect a payment to the vendor in the amount shown on the invoice?
- Comparison of the invoice value to the bank transaction records for the importer's bank account – do the records reflect a credit to the vendor in the amount shown on the invoice?
- Comparison of the invoice value to relevant entries in the importer's accounting records for the cost of goods sold or the cost of goods manufactured.
- Comparison of the invoice value to relevant entries in the importer's profit tax declarations with respect to the cost of goods sold or the cost of goods manufactured.

4.3 The second objective of a post-clearance audit of the Customs value of imported goods is to determine

- if the importer has made any royalty payments that should be incorporated into the Customs value, or
- if the importer has provided any input materials or other support to the exporter in the production of the imported goods, the value of which has not been reflected in the commercial invoice for the imported goods.

This determination is made through an examination of the financial records of the enterprise for payments (either to the exporter or to others) for royalty rights or for input materials, engineering costs, etc. that might pertain to the imported goods.

4.4 Preparation of a Risk Assessment Sheet

In a number of countries with well-developed customs systems, the Customs Auditor who reviews the importer's customs value declaration prepares a risk assessment sheet. The mentioned areas are the areas where incorrect information could be declared which would result in revenue losses. Applying this assessment method, the officer, based on the information that he has on a number of factors that relate to the process of importation (importer, exporting country, specific feature of the product, etc), shall identify the risks of incorrect or incomplete declaration. Based on the risk factors identified by the Customs Authority, those importations that have higher risk indicators will require further examination.

RISK ASSESSMENT SHEET

	Risk areas	Risk assessment				
		Low	Medium	High	Very high	
		(1)	(2)	(3)	Not very serious (4)	Very serious (5)
1.	Undervaluation (reliable invoice)					
2.	Situations without sales					
3.	Further sale					
4.	Packaging transactions/split deliveries					
5.	Discounts					
6.	Financial agreement (indirect payment)					
7.	Averaging					
8.	Deposits - partial payment					
9.	Loans - previous transactions					
10.	Exchange rate					
11.	Use of the local currency in the declaration					
12.	Purchase/sale brokerage fees					
13.	Brokerage fees					
14.	Services - advertisement, guarantee payment					
15.	Supplementary goods and services					
16.	Testing and examination fees					
17.	Packaging fees					
18.	Equipment expenses, etc					
19.	Trademark fees, etc.					
20.	Transportation and insurance					
	LOADING					
	TOTAL					

4.5 How to use the Risk Assessment Sheet

Where no risks are identified, the sheet is not filled in. Where the level of the risk is low, "1" shall be completed. In case of medium risk level, "2" is completed. Where the risk level is high, "3" is completed. A very high level of risk shall be divided into 2 levels: serious and very serious. If "4" is completed for 2 and more areas, that means that the importation shall be subject to further close examination. Total amount shows the priorities of the review of the importation and the requirement for a close examination.

4.6 Verification of Declarations Assessed under Method 1:

Examine the customs value details declaration.

Confirm that the person who signed the declaration has the appropriate authorities. If no, then a new customs value details declaration shall be obtained from the legitimate importer. Check if all columns in the customs value details declaration are appropriately completed. Check the accuracy of the value shown in the customs value details declarations and other relevant documents and how accurately it is reflected in the SAD.

Verify the fact of the sale of goods in the country of export. The fact of the sale of the imported goods may be verified through the relevant contracts, commercial invoices, purchase invoices, etc. Where there was no sale, the determination of customs value of the goods by method 1 is impossible.

Identify that the importation of the assessed goods is based on the following conditions. If yes, then no sale transaction took place:

- The buyer and the seller are the same legal entity,
- Goods are imported by brokers on behalf of the supplier, no facts of sale are indicated,
- Goods are imported on conditions other than their sale,
- Goods are sold under a lease or a rent contract,
- The sale transaction includes a compensation, a trade-in or a mutual trade arrangement,
- Other conditions, when goods remain under the supplier's ownership.

Identify if some goods were sold in transit, before they were imported.

Indicate the parties of the transaction: the buyer and the seller:

Was any third party involved in the transaction – a purchase or a sales broker? The third party may be the main party of the transaction. Instead of establishing legal relations between the buying and the selling parties, the broker can buy the goods from the seller and resale them to the buyer. In such circumstances the broker shall be deemed as the seller.

The importer may be the owner of the assessed goods. If a person other than the buyer makes importation, then it is possible that the sale agreement is not taken as a relevant sale transaction used for customs valuation purposes.

Identify if a sale for export to Egypt has really taken place. Identify if there are other official or non-official agreements or other arrangements besides the primary sale agreement. Other arrangements may appear as a result of services provided in relation with goods and their value may be included in the customs value.

There may be the following examples of the buyer's payments and/or undertakings under the mentioned supplementary agreements, contracts and arrangements:

- Supply of articles, components, parts and materials registered with the imported goods,
- Stamping, sealing and checking,
- Design, decoration, plans,
- Transfers between the companies against management, advertisement, research and development assessment costs,
- Concluding activities and processing,
- Trademark use and license fees,
- Sale brokerage fees, brokerage fees.

Verification of the declared customs value:

- Review the importer's records for all the details of the sale transaction: from ordering to making the final payments.
- Check payment details, the amount paid, the date and the form of payment, to whom the payment was made.
- Make sure that all the invoices for the concerned goods were included in the customs value.
- Examine all the records related to the goods concerned, check if there are still amounts to be paid to the supplier,
- Check if terms of supply declared at the moment of importation comply with the terms mentioned in the invoice.
- Make sure that transportation and insurance costs are included in the customs value, where they are not indicated in the accompanying invoices.
- Verify the accuracy of conversion of the amount shown in foreign currency into the currency of the importing country.
- Make sure that the deductions are acceptable and accurately calculated.
- Review all the correspondence related to the given transaction.

Identify any amounts that shall be paid to a third party. Obtain the details on the amounts paid and the reasons of payment. Obtain the copies of those documents that present the details of the reasons of payment.

4.7 Verification of Declarations Assessed under Methods 2 or 3

Make sure that valuation under Method 1 was impossible. Where a customs value details declaration has been submitted with the import declaration, verify if the importer had all the appropriate information to fill in. Where methods 2 or 3 are approved, the following steps shall be taken.

Make sure, by the comparison of features and/or physical examination, that assessed goods are similar or identical to the goods assessed under Method 1. Indicate any differences.

Confirm that the declared customs values are based on the customs values of similar or identical goods exported within the timeframes established in the relevant Articles of the Executive Regulations of the Customs Law.

Confirm the need for any adjustments, taking into account differences in quantities or trade levels, and obtain detailed information on the principles on which the calculation is based. If possible, similar or identical goods shall be sold taking into account the quantitative and trade level similarity of the goods to the assessed goods. In the absence of these conditions the sale of similar or identical goods may be taken as a basis if:

- trade level is the same, but quantity is different,
- trade level is different, but quantity is the same,
- trade level and quantity are different,

Verify the accuracy of costs declared as international transportation and insurance costs and the accuracy of differences in these costs.

Identify the need for other verifications, taking into account the differences in transportation and other associated costs between the imported goods and goods similar or identical to them in the country of export, and obtain detailed information on the purposes of these costs and the method of their calculation.

4.8 Verification of Declarations Assessed under Method 4

Make sure that the valuation under Methods 1, 2 and 3 was impossible. Where method 4 is acceptable, the following steps shall be taken.

Make sure whether the person who signed the customs value declaration has the appropriate authority. Confirm the compliance of information presented in the customs value declaration with information presented in subsidiary records.

Confirm the sale actually has taken place: check the invoice, sale contract and other payment documents.

Check if the imported goods were sold to the persons who:

- are not related to the sellers,
- didn't supply, directly or indirectly, free or at a smaller price the goods and services which will be used for production and sale for export of goods subject to importation under Paragraph 1b of Article 8 of the WTO Customs Valuation Agreement.

4.9 Unit price

Verify the price paid by the in-country buyer by checking the importer's correspondence, sale and payment documents, copies of sales register, sale invoices and profit certificates presented to tax authorities.

Make sure that the unit price was calculated correctly:

- If there is one fact of sale of imported goods or goods similar or identical to them, for which customs value will be determined, its price per unit shall be calculated based on that one sale.
- If there are more facts of sale, then the price per unit will be calculated based on the sale of the imported goods or goods similar or identical to them on the first commercial level, which includes the biggest quantity of units sold for a common price.
- Trade level is not taken into account while determining the price per unit, which means that goods may be sold to a wholesale trader, distributor or a retailer.

Confirm that imported goods or goods similar or identical to them were sold within the same or almost the same period of time or within 90 days before the importation of the assessed goods.

Confirm that a sufficient number of units were sold. Sufficient number shall be determined based on a specific case, subject to the conditions of importation and market processes, as well as the marketing situation in the country of import. E.g., the price per unit for which the biggest quantity of goods is sold, can be deemed acceptable if the number of goods sold within the same or almost the same period of time constitutes only a small part of general sales of this product. Therefore, these sales can be used to determine the price per unit if the price for which they are sold is compatible with the usual selling price of the goods.

Confirm that basing on the sale transaction of processed goods after the importation is justified if:

- after processing the imported goods change their identity, and Method 4 is usually not applied,
- value added after processing can be easily determined, although the identity of the imported goods is different, and the application of Method 4 for can be grounded,
- Further sale of the processed goods shall take place within a specific period of time after the moment of importation of the assessed goods (e.g., within 180 days).

The importer shall indicate in writing the application of this method.

4.10 Deductions

Confirm that information on the amount of the brokerage fee, profit or overall costs are normally obtained in the country of import based on the sale of goods belonging to the same group or category. This amount can be presented as a range of amounts, which is considered to be an “ordinary” amount, as it is obviously perceived. The ordinary amount can be calculated, e.g. by simple averaging or by a dominantly repeated amount.

Find if the assessed goods were sold with a brokerage fee in the importing country. The application of the deduction made for the profit or overall costs is generally optional for those transactions that do not include brokerage fees.

Confirm that other deductions, e.g. transportation costs in the importing country, customs duties and taxes and transportation fees paid abroad, are calculated correctly.

Make sure that costs of further processing are calculated correctly.

4.11 Verification of Declarations Assessed under Method 5

Make sure that the valuation under Methods 1, 2, 3 or 4 was impossible (if the importer suggests changing the order of application of methods 4 and 5, then method 5 should precede method 4). Where the application of method 5 is appropriate, the following steps shall be taken.

Confirm that the importer is ready to provide Customs with documents necessary for further checks with respect to his expenses. If Customs considers the provided information insufficient, then method 5 cannot be applied. Confirm that the value or the price declared under this method is based on the commercial calculations of the producer and that these calculations are compatible with general accounting principles of the given country. Check if the value of materials used for the production of the imported goods was determined correctly.

Materials used and costs include:

- *Raw materials, e.g. wood, steel, clay, textiles, etc.*
- *Costs of transportation of the raw materials to the production site.*
- *Partially assembled or half-finished products, e.g. integrated circuits.*
- *Components that will be used in the production of the final product.*

Make sure that production and other processing costs on the imported goods are indicated correctly.

Production costs include:

- *Costs of direct and indirect work.*
- *Costs of assembling, when assembly takes place and not production.*
- *Indirect costs, e.g. production management, storage, overtime payment costs, etc.*
- *The amount of the internal tax collected in the exporting country, which is directly applied to the materials or their use. If there is a tax exemption or a refund in case of export, it shall not be included in the customs value.*

Check if costs for containers, which for customs purposes are considered to be parts of the imported goods, are determined correctly. Check if packaging costs, incl. labor and materials used, are determined correctly. Check if the value of supplementary materials and services is calculated correctly and that the seller didn't include it in the selling price. You should know that the value of supplementary materials and services should not be calculated twice. Costs mentioned in Article 14 of the Executive Regulations of the Customs Law shall be included in the customs value if they were not included in the purchase price and were originated by the buyer.

The value of specialized projects, designs, design work, plans and sketches made in the importing country shall be included in the customs value if costs of supplementary materials and services used is covered by the producer.

Check that transportation, insurance and other related costs are calculated correctly.

Check that the amount of the profits and total costs presented is correct.

- *The amount of the profit and total costs shall be determined based on the producer's brand name or the information he provides, except for cases when the figures he presents are not compatible with the figures reflected in the sale of goods of the same category or group.*
- *The amount of the profit and total costs should be taken as a whole. Therefore, if the figure representing the producer's profit is low and total costs are high, then his profit and total costs in total may be incompatible with the figures reflected in the sale of goods of the same category or group.*
- *If the producer states that his profit from the sale of the imported goods is low for some trade-related reasons, then the figures representing his actual profit shall be taken into account, if there are justified reasons for that (e.g. an unexpected decrease of demand) and his price policy complies with the general price policy applied in that particular branch of industry.*

If, apart from the records presented by the producer or on his behalf, other information is used for the determination of calculated value, then Customs shall, upon the producer's request, inform the latter on the source of that information, information used and the calculations made based on that information, pursuant to the provisions of Article 10 of the WTO Customs Valuation Agreement.

4.12 Verification of Declarations Assessed under Method 6

Confirm that the valuation under Methods 1 - 5 was impossible. Find out how the declared value was calculated.

The following examples show how Method 6 can be applied:

- *Where there is no sale of similar goods produced in the country of production of the assessed goods, but instead there is a sale of similar goods produced in some other country, the latter may be used as a ground for customs valuation under method 6, if all other conditions required for method 3 were met.*

- *Where there is no sale the circumstances of which comply with the requirements of method 4 (90 day's period), but there are sale transactions that, for example, took place 100 days before the importation of the assessed goods, the latter may be used as a ground for customs valuation under method 6, if all other conditions required for method 4 were met.*

If previously mentioned methods are applied flexibly, due regard should be given to the principles of valuation, trying to avoid distortions of customs value determined under the selected method.

Confirm that the declared value is not based on any of the prohibited methods specified in the WTO Customs Valuation Agreement. Confirm that all transportation, insurance and other costs alike related to the imported goods were taken due account of. Confirm that all additions (e.g. transaction related expenses, supplied materials) are declared.

5. Temporary Import for Processing

5.1 Pursuant to Article 98 of the Executive Regulations of the Customs Law and Prime Minister's Decree 1635/2002, an importer can be authorized to import goods into Egypt temporarily for the purpose of manufacture into a product that will be exported. Pursuant to Article 139 of the Executive Regulations of the Customs Law, the Investment Guarantees and Incentives Law (Law 8/1997) and the Law on Economic Zones of Special Nature (Law 83/2002), free zones and economic zones of special nature can be established into which non-duty paid foreign goods can be imported for the purpose of sale for export or manufacture into a product that will be exported, or for sale and importation into Egypt.

5.2 The purpose of a post-clearance audit of this regime is to confirm:

- that the imported goods have in fact been used for the authorized manufacturing process or other authorized purpose and not diverted for use in Egypt without proper accounting to Customs.
- that all goods manufactured from the imported goods have been exported, or if diverted for use in Egypt, that such diversions have been properly accounted for to Customs.
- that any scrap or waste from the manufacturing process has been disposed of and not re-sold.

This determination is made through an examination of the financial and production records of the enterprise.

CHAPTER 8: STAGE 4 – CREDIBILITY CHECKS

1. General.

1.1 The examination of the financial and operations records of an enterprise is the main approach to the verification of the accuracy of Customs declarations made by the enterprise. However it is useful to have some indirect methods of being satisfied that Customs declarations are accurate, or of finding indicators to show when this is not the case.

1.2 As well as carrying out checks on the records produced by the importer it is also necessary to look behind these records to test the overall credibility of the enterprise. This does not mean that the Customs Auditor checks the viability of the enterprise but that alternative checking methods are used to substantiate the records produced by the importer.

1.3 In the dictionary "credible" is defined as "worthy of belief; likely; acceptable", and credibility can be a key factor in the examination of the affairs of an enterprise. If all officials having contact with a taxable enterprise considered the "credibility" of the information received concerning the enterprise, the risk of losing duty or tax revenue could be greatly reduced. Information that raised "credibility" doubts would give a valid reason to examine the affairs of that enterprise in greater detail than would otherwise be the case.

1.4 Once the validity of the credibility method has been recognized there is the need for something more than the intuitive checks made by the individual. As Customs Auditors become more experienced in the various technical aspects of verifying the accuracy of Customs declarations, it should be possible for credibility checks to be devised and specified. Where the official information is kept in a computerised system it is possible to build a number of parameters into the files maintained by the Customs Authority on imports and exports made by an enterprise. This will indicate automatically when the credibility of the information is questioned.

1.5 Credibility is also valuable in examining the overall picture of a business when considering selection for control visits and planning the time element that should be allocated. Part of such credibility examination is a comparison between similar trades or occupations and enterprises of similar size together with the consideration of the usual import and export patterns for particular types or levels of business.

1.6 Customs Auditors are encouraged to adopt a method of operation that incorporates "credibility" checks and will allow for immediate further examination of the particular aspect of the enterprise's system that fails a credibility check. The work allocation for audit visits should be arranged so that the checks considered essential are always made. The remainder of the time should not be allocated formally. This will allow time for the follow up of queries relating to credibility.

1.7 The success of the credibility method of audit is dependent to a large extent on the quality of the Customs Auditor. A good quality Customs Auditor will respond to the responsibility given to him and is likely to show a good rate of discovery of underpaid tax. It is not economical to have Customs Auditors performing routine audit checks that will occupy the time available but produce very little extra revenue.

CHAPTER 9: STAGE 5 – COMPLETION OF THE AUDIT VISIT

1. Future Compliance.

At the conclusion of the audit visit it is important that the Customs Auditor is satisfied that the declarations filed by the importer are accurate and consistent with what has been seen and checked on the visit. The Customs Auditor must also be able to make a sound judgement on the likely future compliance of the importer. He will then be able to suggest that time between audit/controls be extended or reduced accordingly based upon his assessment of the results of the current visit.

2. Final Discussion with the Importer.

On completion of the audit visit, all proposed adjustments should be discussed with the importer and/or the qualified representative of the importer. It is extremely important that the importer fully understands the proposed adjustments and the reasons for them. Of course, throughout the visit the Customs Auditor should have good communications with the importer, so that any adjustments should come as no surprise.

3. Final Report.

On completion of all of his actions the Customs Auditor should complete a final report detailing the audit visit and its outcome, and any required assessments of duties, taxes and penalties.

4. Evidence of Fraud or Similar Conduct.

4.1 Where the Customs Auditor becomes aware of evidence of fraud or similar conduct relating to the submission of Customs declarations containing false information or, where the total amount additionally assessed exceeds a prescribed limit, the file should be referred to higher management for a decision on the appropriate course of action.

4.2 The referral should include:

- the visit report, signed by the Customs Auditor and the Customs Auditor's immediate supervisor;
- copies of the bookkeeping documents with evidence of the fraudulent conduct;
- any explanatory comments that might have been made by the management of the enterprise on the subject of the fraudulent conduct;
- final report on the discussion of disagreement between the parties; and

- any evidence supplied by the registered enterprise in defense of the alleged infringement.

4.3 The file should also be referred to the Risk Management Department so that risk selection parameters can be updated (for imports whether by the subject of the audit or by other importers of similar goods).

Technical Assistance for Policy Reform II
BearingPoint, Inc,
8 El Sad El Aali Street, 18th Floor,
Dokki, Giza
Egypt
Country Code: 12311
Phone: +2 02 335 5507
Fax: +2 02 337 7684
Web address: www.usaideconomic.org.eg