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TAPR IQC Egypt  
Technical Assistance to Support Economic Policy Reform

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**Customs Needs Assessment**

**Submitted to:**  
United States Agency for International Development

**Submitted by:**  
Chemonics International Inc.

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## **Executive Summary**

### **Introduction**

The reader will note that the product of the assessment has limited itself to primary focus on the impacts of the changes in the valuation system, automation, and the infrastructure changes needed to accomplish those goals. To broaden those areas of concern prior to implementation of changes called for by WTO/GATT might be counterproductive to the best interests of Customs.

This is the result of the Assessment of Customs Reform activity carried out by USAID through the Technical Assistance for Policy Reform (TAPR) project under the Technical Assistance in Support of Economic Reform (TASER) program. The project is a direct result of a request from The Minister of Finance to the U. S. Agency for International Development.

The Assessment began on June 1, 2001 , and is scheduled to conclude on August 31, 2001 .

Personnel conducting the assessment were:

Harry M. Allison, Team Leader (Training, Compliance, Process) James H. Cassing, Ph.D. (Economics)  
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The assessment used a four-phase development to complete the project in the most effective method. This was:

- Information gathering
- Analysis
- Prioritizing
- Reporting

The assessment team visited a wide range of Customs facilities and reviewed processes, guiding documentation, laws, and policies. The "trade", that is the people representing companies, corporations, and individual importers, exporters, customs brokers, freight forwarders, expeditors, and associations were also met with and enjoined in the process of the assessment. In addition to

the foregoing, a large number of Customs managers and staff were interviewed. A record of the meetings is attached to the report as an appendix.

These discussions and observations were critical to understanding the current situation, constraints to reform, and exploring potential avenues to successful change.

The analysis stage included a comparison between where the Customs process is now, and where it needs to be. The question answered by the analysis phase is how best to reach the goal. Knowledge of the subject matter and the experience of the team brought to light the avenues of approach that might be recommended.

In the prioritization phase those recommendations were balanced against reasonability, potential for success, and the ability of Customs to perform the change. This phase was added after beginning the assessment due to the complexity of the problem to be addressed.

In addressing the resolution of constraints to progress, it is important to not only see and understand the current system, but to understand why it is as it is, in order to understand what needs to be changed and what offers the best potential for success. Changing a process does not alleviate the concern that was a basis for the previous system.

The reporting phase is included in this report, it contains a detailed presentation of each of the areas of concern and recommendations for reform, both immediate and longer term.

Each of the Areas of Concern is documented in this report as a separate chapter. The reader will notice there is some duplication in each report. That is because the experts independently came to the same conclusions from the perspective of their focus subject. This overlap was intentional and reinforces the recommendations for correction.

The recommendations for change are given in two stages; first as those things that can be done immediately to begin the reform, and second as a potential or recommended assistance project to provide the guidance, funding, and advice needed to fully implement the changes. It is the unanimous conclusion of the team that the goal of full compliance with the World Trade Organization/General Agreement on Tariffs and Trade (WTO/GATT) guidelines is accomplishable, as is full automation of the entry process; manifest, declaration compliance databases, and connectivity to other Agencies, within a reasonable time frame. The team strongly believes that implementing these actions will enable the Customs Service to more rapidly process imports and collect customs duties, better identify compliance and non-compliance by importers, and thereby better support Egypt's more rapid economic development.

## **Findings and Discussion**

Finding 1. Customs must take a number of actions before it will be able to implement the valuation of merchandise methodology described in the AGREEMENT ON IMPLEMENTATION OF ARTICLE VII OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994.

Discussion. The change from a market price reference system of value determination to the WTO/GATT value method is a major change in procedure and process requiring a number of skills and knowledge not previously required. It also requires specific changes in law and guidelines to allow the procedure to take place as designed.

This caused two major problems that are related to change. First is the dependence on

The first of these changes is perhaps the most problematic. Customs for years has been accustomed to having the importer present an invoice that stated a value of the merchandise. Customs would compare the value declared with a reference value list and with previous importations to determine the correctness of the value. The reference lists was based on market value or wholesale value, consequently the invoice value or declared value was frequently low. To verify this Customs would require certified commercial invoices, consular certified invoices, bank certified payments, etc. If the determined value was low a penalty was assessed. Understandably, the next importation by an importer would show a higher value. Customs began to depend on the use of legitimized documents as a justification for acceptance. Resultantly, the laws, guidelines and decrees followed in support. This pattern is not unique to Egypt. Most countries that used a similar system had the same results.

documents considered legitimate by Customs, and second, it caused mistrust and confrontation between customs and the trade. Customs felt that the trade could not be trusted to present a real value, and the trade felt they were being forced by customs to inflate values in an arbitrary and capricious manner.

This confrontational pattern of development was one of the reasons why the GATT met to discuss and revise valuation determination. It was found that in today's world of computers, the reference price system had little to do with the actual value of merchandise. It took no account of the ability of the trader to buy at the best price through legitimate international business methods. It tended to level the playing field in favor of the worst buyers. International commerce could not depend on a predetermined cost of customs clearance. From the customs point of view, it was becoming too easy to falsify documents, and values tended to increase over time beyond normal inflation. The system itself was creating a real barrier to commerce.

The resultant GATT transaction value (the primary basis of valuation, or in the absence or transaction value other means of valuation), method was adopted. For most importations the value became the price paid or payable for the merchandise. Simple, direct, and verifiable are the elements of the system. The verification when needed is done from the business records and financial data of the importer, a much more accurate method than the reliance on other documents. This however requires a level of knowledge of business and business records that was hitherto unneeded in customs. It also requires that traders keep their records for a specific time period and in a manner in accordance with the Generally Accepted Accounting Principals of Egypt.

The transition to GATT valuation requires a major training effort and information sharing with the trade. Customs must train employees to use the methods set forth in the GATT rules to determine value, possible adjustments to value, or alternate methods when a transaction value is not applicable, resulting in the use of deductive and computed value when appropriate. Employees must know what business records to ask for and under what circumstances to ask for them. The trade must also know what is expected of them from customs. This training has not been done to the level of competence needed.

The Customs Law, implementing decrees and guidelines must also be changed to reflect the change in process and procedures. Particularly, in the demand that documents presented to customs meet standards of official verification, changes must be made to comply with the agreement.

Finding 2. That Customs must put in place the appropriate infrastructures to apply the WTO/GATT concepts without risking revenue loss that may be at an unacceptable level.

Discussion. Some temporary revenue loss can be expected as the system goes into effect. This loss caused by the difference in collections based on the lower transactional value, should be at an acceptable level and will be overcome by the natural economic results of the system change. As voluntary compliance increases, as shown by the experience of many nations, losses will be fully eliminated.

While voluntary compliance, e.g. importers freely and fully meeting the legal demands of the system of their own volition, is a goal of the transactional value system, it is not automatic. Risk management must be addressed to assure that the unscrupulous persons who are users of the system do not take unfair advantage of it.

The Customs first line of defense of the system is in a well-trained staff handling declarations. These employees, who know when to accept a value, when to question a value, and what verification to seek, is the most valuable asset Customs can have. This can be achieved only through training and proper management guidelines that are in accord with the agreement.

Compliance, based on risk management is the key to developing a system of safe guards that protect the system from abuse. The units of compliance are the research and development section (R&D), the intelligence (commercial) section, and the audit section.

The agreement encourages nations to defend the system through selective verifications and audit. In addition to the well-trained employee handling daily declarations and primary inquiries of value, comes the selective system for examination, verification, and audit.

This may be done in three permissible methods; for cause, randomly, or when there is a high risk of loss or damage. The R&D section functions to continually keep the appropriate level of selectivity in place, targeted to the highest risk, through continual review and application of risk assessment. Intelligence uses all official sources (domestic and international) to develop information of potential violations. Audit is targeted by the three methods also. A final back up to the system is a unit of trained investigators who can carry through on a violation to presentation for administrative penalty or prosecution. While the system of selectivity is much more accurate with an automated compliance database, the infrastructure and a manual system can and should be put in place as soon as possible.

Finding 3. The guidance provided to Customs Officers should be revised to clearly indicate the policy of the Government of Egypt regarding the application of the AGREEMENT ON IMPLEMENTATION OF ARTICLE VII OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994.

Discussion. Customs receives guidance in three separate manners: by law, by direction from higher authority, and by institutional policy. It may seem that the will of the Government is clear in this regard in the fact of Egypt becoming a signatory to the Agreement.

However, Customs is an Institution that functions through the application of specific procedures and processes. In this Egypt is not unique. Internationally, the function of Customs demands this methodology in order to treat merchandise crossing its' borders with fairness and standardization.

The application of the agreement is a major change in the procedures and processes dealing with the valuation of merchandise to those found in the agreement. In the agreement these processes and procedures are very specific. They deal with one of the most basic and important of all Customs functions, which is the treatment of merchandise arriving, transiting, and leaving the nation.

All Customs procedures and processes are founded in law, implementing decrees, and approved guidelines issued by competent authority. If, at any level of that process there is conflicting information, a lack of clear direction, or a failure to provide the authority that Customs needs to act, then the result must be confusion, lack of change, and delay in implementation.

This calls for a concerted effort on the part of each level of Government, from the Ministerial level involved in the drafting and enactment of legislative action, to the issuance of institutional policy, to the various Customs executive and management levels producing specific guidance for implementation, to assure that the final procedures and policies conform to the standards agreed upon.

Finding 4. That commercial importers, exporters, and associated service providers have not been involved in the planning process to a sufficient level to assure willing acceptance of the final product.

Discussion. Those persons dealing with Customs in the processing of merchandise being imported or exported (the trade) must be involved in the process of change. Beyond knowing what is expected of them in the changed procedures, they offer a wealth of knowledge that can be shared with Customs in establishing the information needed for verification of values and the knowledge of business record systems and trade practices considered normal in international trade.

For Customs to reach out to them in the planning stage would be an invitation to the normalization of relations between the trade and Customs that is fundamental to success in creating an environment for voluntary compliance. The trade community must have a clear and full understanding of invoicing requirements for Transaction Value and knowledge of what charges (commissions, freight, etc.) are included or excluded from the dutiable value. In addition, Customs must clearly set forth record keeping requirements for both the importer and agent, if used, for example, the retention of full purchase records (purchase order and payment records, etc.) and the time from entry the records must be retained.

Meetings between Customs and the trade should be ongoing in all Customs locations. Seminars should be held in each location to seek input into the formulation of reasonable policies that are within the options of the agreement. This can be of great value to Customs in deciding reasonable documentation for declaration of value.

Continuing a confrontational attitude between Customs and the trade can only be counterproductive. The relationship does not have to become a "close friends" type connection, but it should become one of mutual respect and professionalism.

This begins with professional intra-personal communications and is considered essential to success.

Finding 5. The present Customs training configuration and methodology of presentation must be revised and strengthened in order to be able to provide the quantity and quality of training that is needed for transition to the new system.

Discussion. Extensive training and retraining of personnel are required in order to meet the skills level needed for application of the new system. The training system used will have to be specialized career specific within the context of the work functions to be performed.

Present systems are based on a rote educational model that requires long-term basic training of a generalized curriculum to produce a "Customs Officer" that can be assigned to any area in customs. Once on the job, the employee begins to learn the parameters of the job function. While this offers some reasonable flexibility in the old work system, where the learning period on the job can be extended, it does not provide the rapid integration to a highly skilled specialized field as required for GATT systems.

Under the GATT systems, skilled specialists are required in the fields of examination of merchandise, classification and valuation of merchandise, accounting and audit, investigation and intelligence, compliance systems analysis, automation, database development and use, liquidation of entries, bonds and sureties, instructor/course development, etc. In training the message should convey that each officer has a degree of independence to make decisions on selectivity, importer record reviews and that their decisions will not be challenged as long as they were carried out with the intent to comply with Customs rules.

In each of those areas supervisors and managers must also be brought to a high level of technical and administrative competence. It is suggested that this can be accomplished in a reasonable time frame by the use of Adult Occupational Training systems based on the task relationship of training objectives to work performance. Trainees receive this training within specialized career fields in order to reduce the time spent in training and to increase the retention of information.

The transition of the training units to the suggested method can be best accomplished in a reasonable period with some international advisory assistance, equipment and publishing procurement.

Finding 6. That the Customs Service should provide more detailed direction to the automation contractors if they are to effectively develop systems and use programs that will bring computers into the workplace as tools to increase efficiency and speed in processes.

Discussion. In order to design and develop the use screens and programs for use in customs, contractors must be told by customs what they want the system to do and what it is to be used for.

Finding 8. That Customs officers individually are not currently authorized to act on their own volition in the release of merchandise, or the acceptance of a declared value for merchandise.

The equipment has a multitude of potential for use, but must be designed to produce the specific function required.

Because of the wide application of automation in Customs, the use requirements must be defined and prioritized. This is normally best done by a committee of Customs subject matter experts, led by a chairperson having the authority to make the level of decisions required for implementation, and the ability to keep the committee focused on the tasks mandated. The committee must have the authority to call upon any subject matter expert within customs, to meet with persons from other agencies to discuss interconnectability, and to meet with the trade to discuss system accessibility.

Executive management must continually review the progress of the committee, changing committee members when required by lack of progress or when progress makes a particular committee member obsolete by accomplishment.

International advisory assistance may be of help in this area also.

Finding 7. That bonds and other sureties currently used in moving goods from and to free trade zones may be a precedent for development of early release of merchandise pending final duty/tax determination.

Discussion. In the WTO/GATT valuation system, a declaration is made by the importer to Customs containing information regarding the merchandise and the transaction which took place to purchase it that is sufficient for Customs to determine the duties/taxes due from the importer. In a normal or usual transaction, no further information may be needed, and the merchandise may be released upon the payment of duties/taxes. This is effectively a final determination of duty/tax for the transaction.

However, if there is serious doubt as to the validity of the declaration, verification or further information may be required; or, if the entry is selected for verification by the selectivity process, then the possibility that the duty/tax may be increased or decreased exists. In this situation the merchandise may be released to the importer while the appropriate duty/tax is being determined. This is called early release of merchandise pending final determination of duty/tax. In early release policy, it is normal to protect the revenue, pending the final determination of the entry. The period of time involved may be from several days to several weeks, depending on the depth of verification that is needed. The idea is to let the importer have his merchandise while a final determination is pending.

In discussion with a number of Customs managers, it was felt that the collection of final duty/taxes would not be a problem as Egyptian law allows for such collections as a priority tax lien against the importer's assets if not paid upon billing.

This may be true and is certainly a lever to assure payment when the trader is an established business or known resident of the community. However, as the system expands in the number of traders doing business with customs, there may come a point in growth of the system that one time importers increase and unscrupulous persons may attempt to defeat the system by using a "ghost" or name change, or fictitious entity to defeat the historical reference of the system.

It is therefore recommended that a system of sureties, supplied by a bank, surety agent, insurance company, or by cash be emplaced to protect the revenue. Such sureties could be single event or time termed for multiple transactions.

As a surety system is in current use for other purposes, then the cost to traders should be minimal and the benefit to customs as an easy method of assurance of collection is obvious.

Discussion. Under the GATT system, officers are not only required to use their judgment in the acceptance of declared value, but must accept the declared value unless there is a reason to doubt

This is a first very positive step to the acceptance of individual use of discretionary authority that is not currently a norm in Egyptian Customs but is a requirement of the GATT system.

it that is sufficient to be articulated in writing to the importer demanding verification.

This is not only a change in philosophy from the old system which demanded a number of certified documents to justify the officers' action, but is an authorized risk on the part of management to trust the judgment of the officer.

The risk is however one of limited potential for loss. Whether the value is accepted with or without documentation, the duty/tax is still collected. The safeguard to the officer's action is found in the random selection system that may override the officer's decision, or by the random audit system that also allows a cross check of the officer's action. The declaration may still be reviewed for correctness by supervisors after the merchandise is released, and officers must be able to articulate their rationale in deciding to accept the declared value or verify the value.

If the officer does not have a reasonable doubt, acceptance is the appropriate action. In the worst case scenario, the duty may be collected on an undervalued import. But if the under valuation is caught by audit or selectivity, then the fine or penalty will be severe and will result in future shipments of the same importer being selected for cause for verification.

The risk of collusion between importer and officer is reduced by the same system, supervisor's review of the transaction, and the selectivity system. This is another reason for increased technical competence of the supervisors and managers.

A well-trained officer exercising his/her authority in the GATT system is not a serious risk to either the revenue or to customs.

This authorization, to accept the best judgment of an officer must be included in the management guidance to officers to allow them to develop the confidence to perform the job function as described.

Finding 9. Examination by-pass can begin immediately on a percentile level by executive order to begin the preparation of selectivity criteria.

Discussion. By Ministerial Order, or Executive Order from the Customs Commissioner to Customs Managers at Ports of Entry (Air and Sea) to begin a by-pass, or pass without examination of 20% of importations of merchandise having no interest to other agencies. They, the Customs Managers would be required to select the importations for by-pass and report back to the issuing executive the criteria used for that selection.

This would be the beginning of selectivity. The Customs Managers will normally select for by-pass those importers that they have had the least problems with. As the duty/tax will still be collected and the document process would not be changed at this time. Potential losses would be minimal and acceptable.

This forces the managers to begin to think about selectivity and to begin to develop selectivity criteria. It also shows employees that merchandise may be by-passed without negative results.

A meeting should be held 30 days after the implementation to discuss the criteria each individual manager used in the selection. At the end of the meeting the by-pass system should be increased to 25%.

As soon as the legal guidelines are emplaced to allow it, document by-pass should begin using the same methodology. By-pass levels should not exceed 25% until the infrastructures of audit and selectivity are in place.

Records of merchandise by-passed should be maintained, as should revenue collections for the same period for comparison uses.

## **Conclusions**

A transition period is always needed to implement the changes of process and procedure having major impact. That transition period at this time would be considered approximately three years.

The recommendations of this project, if followed, may help to substantially reduce that transition time and the institutional impacts caused by the changes.

The current confusion within Customs and to the trade may have a beneficial unintended result. It demonstrates to managers the major scope of the changes required and the need to take the implementation preparation stage seriously. If so a constraint to implementation will be diminished.

Immediate steps that should be taken now:

### **Valuation:**

(See the full context in Chapter 2, Customs Duty Collection and Valuation)

1. Customs identify and supply WCO materials both the English/French version and a translated Arabic version to all officers involved in the valuation process. The materials should include the WCO Valuation Control Handbook (Introduction, Parts I-IV, and Glossary), WCO Compendium of Valuation Decisions, WCO Commercial Fraud Action Plan and any other material that the WCO recommends. This material is available to all WCO members.
2. Immediately begin a dialogue with the Trade Community and start a discussion of valuation problems, and how to address them. Provide the trade community with an education process. Discuss what Customs expects from them and why it is expected under the new procedures. Provide all necessary materials and guidelines about any new forms or expectations for documentary evidence. Start a discussion about need for procedural changes. Importers and exporters need to be a part of the process to effectively make changes both legislative and procedural. Pass all legislative and procedural changes through trade associations for comment.

Discuss the need for assistance from the trade community in training Customs officers on industry sectors, product manufacturing, negotiations, financing, and business practices. In a true open and transparent environment, Customs and the trade work together to promote efficient processes. The training is essential to familiarize Customs officers with international business practices as related to purchasing (purchase orders), letters of credit, payment for goods, transportation, and other elements related to import transactions.

3. Review the Kyoto Guidelines specifically the guidelines incorporated in general Annex Guidelines for Customs Control (Chapter 6), Relationship Between Customs and Third Parties (Chapter 8), Information, Decisions and Rulings Supplied by Customs (Chapter 9), Appeals in Customs Matters (Chapter 10), and Clearance and Other Customs Formalities (Chapter 3). These will be useful in setting up the procedures for Post Audit, Risk Management, Rulings and the Trade Interface Process. The Kyoto Convention guidelines on

Customs Procedures are available for download from the WCO web site and are considered to be the international standards for Customs procedures.

4. Consider sending a working level group to the Customs Department of the Kingdom of Jordan to review their experience and procedures for implementing the Valuation Agreement. Jordan Customs has initiated a process of risk management, profiling and selective release of cargo. At some sites as much as 50% of the cargo is released without additional review or physical inspection. It would be useful to exchange information, ideas, and materials on how to affect cargo release without review or physical inspection based on criteria and risk assessment.
5. Based on the above create a short-term action plan to develop materials, and resources for Customs officers, the trade community and the public sector.
6. Begin to pass without examination 20% of imports that represent transactions of least risk.

Training:

(See the full context in chapter 3, Training, A Solution)

1. Our company is in the process of obtaining a copy of the WCO/CCC Customs Valuation Control Handbook in Arabic. It is recommended that this handbook be re-printed in quantity, and distributed to all employees concerned in the valuation of merchandise.
2. A class be convened at the Customs Institute in Alexandria for 30 selected supervisors of valuation units nationwide. This class should be instructed by Mahmoud M. Abou Alla (X-ray unit), or another person well qualified in GATT valuation, using the handbook mentioned above as a training manual/lesson plan. This course should run for 2 weeks, five days a week, 4 training hours a day. After the first class graduates, additional classes should be taught by attendees of the first class, in their respective area institute. Again the classes should not exceed 30 people, and the handbook should be the manual. Classes should continue until the valuation of importations is complete.
3. Trainees of the classes above, upon their return to the work site, should become mentors for untrained or inexperienced personnel.

There follows in the chapter on training a suggested course outline.

Automation:

(See full context in chapter 5, Customs Automation)

1. Select a senior executive manager reporting at the ministerial level to manage customs automation
2. Create the steering committee to assist the executive manager in prioritization and scheduling
3. Develop the initial implementation schedule of system components
4. Develop a matching training schedule and curriculum, and start training
5. Identify and acquire funds to support initial acquisition, development, and training
6. Acquire funding to support additional programming and testing
7. Acquire and install the initial equipment allocation

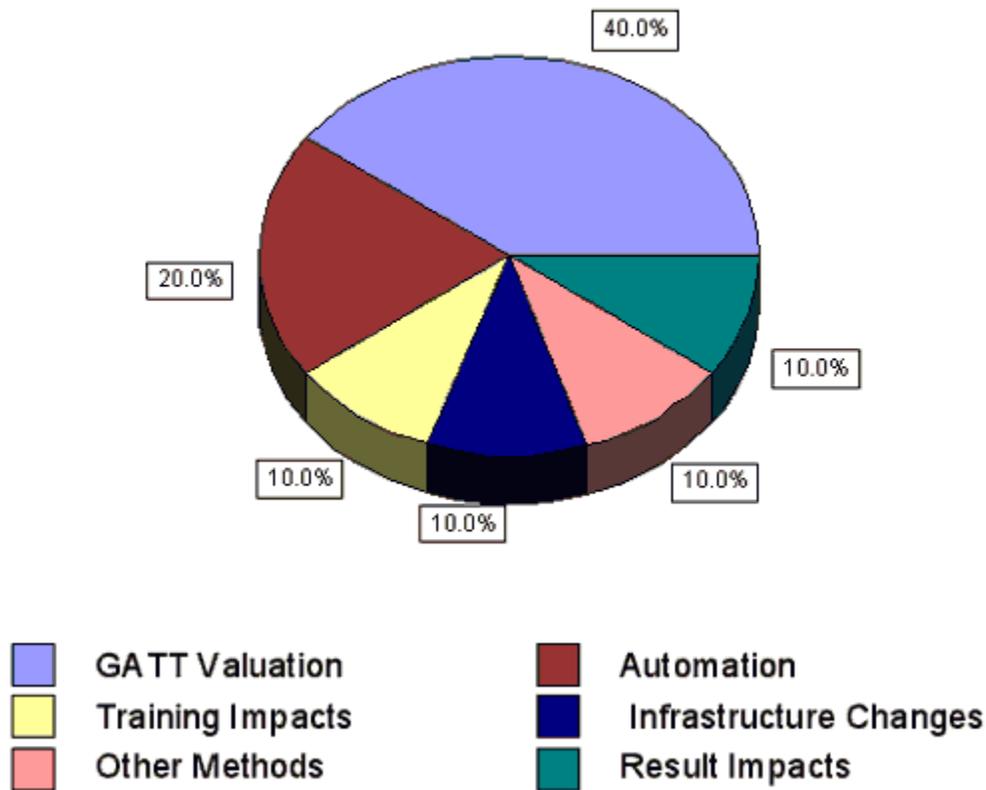
8. Begin the programming recommended here to complete the design
9. Review legislation to permit customs document review discretion

Please see Chapter 7, A Recommended Program of Assistance for Customs Reform for a longer term suggested program of assistance.

### Introduction

The main points of interest of this assessment have been applied to what we consider to be the most pressing issues effecting customs in the foreseeable future to be presently addressed. These are; the application of the GATT agreement valuation procedures, the expansion of automation in Customs, and changes to infrastructures and training caused by the foregoing as well as other modern techniques found successful in other nations that may benefit the organization.

Pie Title  
Percent of Interest



As clearly seen in the pie chart, the impacts of the first subjects drive the rest of the project to a great degree. The reason for this is that the classification and valuation of commercial merchandise entering the country for domestic consumption is the basis of all customs formal duty/tax collections based on *ad valorem* tariff rates. It is truly what customs does in it's functional operations. Everything else in customs is ancillary to this process. It is the heart of the organization

Under the previous " Brussels " Valuation System, duty was applied to a "Customs Value", or value

determined by customs based on market reference or wholesale value. Customs could change the value declared for customs purposes based on past imports or a reference price list. This required some skill and knowledge of the merchandise and use of reference material, but much less knowledge than is required for the proper application of the GATT transactional valuation methods. The consequence of improper application of those techniques are loss of revenue, confusion on the part of importers and customs officers, under valuation, complaints, and fraud. Efficient application will require an absolute knowledge in detail of the GATT agreement, exact application of the principals, an in-depth knowledge of the merchandise and fabrication methods, a more than working knowledge of international commerce, business practices, business relationships, financing, and transportation. Therefore training becomes an important adjunct and long-term consideration to implementation. Customs must be congratulated for making available introductory training to as many employees as they have. However long term training must be considered, as well as on the job restructuring to meet the standard of expertise that will be required for sustainable success.

Revenue loss becomes a serious consideration also as the valuation methodology changes. Even with a well trained specialist reviewing transactional value, the opportunity for false declaration, under value declaration, and fraud are apparent. This is recognized internationally as an acceptable risk that can be controlled through risk management techniques. The point is that the event spins off into a number of directions. Risk management brings forward the topic of compliance, which can offer a number of benefits to Customs in the valuation field, and even into passenger baggage.

The expansion of automation will be needed to meet goals in valuation. The management priorities of Command, Control, and Communications can well be enhanced by computer use. Immediate data recall, criteria based data search, record keeping, and data storage are all easy for computers to do. Computer use by a trained cadre will expand their capability to produce high quality courses. We are sure this will call for more computers, which will call again for training and perhaps some help to assist managers in formulating criteria for unit or program use design.

So, then what we have to this point is an assessment that begins with several points of interest. Addressing those leads to an expansion of those points in order to serve properly that interest. Needed change causes impact to a wide range of the Customs Organization. It also has collateral impact to other parts of the organization that may well benefit from the changes in perspective being incorporated.

Without having gotten ahead of ourselves by pre-designing, it is easy to see the concept of a basic assistance project of three years duration. Many changes have occurred in the international Customs field over the past ten years. As trade practices change and global markets develop, Customs must become more sophisticated, develop new methodologies, and use technology to keep pace.

The standard Custom Mission of collecting and protecting the revenue, enforcing customs and related laws, and protecting developing domestic industry from unfair competition, while true and never changing must be accepted within the context that Customs is an extension of the policy of the Government of Egypt. International trading partnerships and associations are made, not by Customs, but by Government. Tariffs, which determine the duty rates that Customs applies, are not determined by Customs, nor, are the exemptions from duty. Customs is acting on the policy of the Government of Egypt where from it derives its authority, based on its responsibility. So it is with the GATT and other international agreements, trade facilitation, and, meeting the challenge of creating a Customs environment conducive to trade and tourism growth. As with the expansion of points of interest in the assessment, the organization, while meeting the challenges imposed by Government Policy derives benefits from the changes made in the process. More skilled and knowledgeable employees, working in a position calling for the exercise of independent judgement, are a more valuable employee who can be paid accordingly. The environment of automation is a more pleasant work environment attractive to the retention of employees. New methodologies result in bigger, more complex violation cases, resulting in larger penalties and fines being collected. The image of Customs changes, from a suitcase checker, to a sophisticated compliance based organization.

Therefore our interest in this assessment, shaped by the items of interest of the Minister of Finance, known impacts of the Valuation changes effective in Customs on July 1, 2001, the coming of automation, and knowledge of customs operations, we feel that the proper study needed is in the following areas:

- 1.- Economic Projections
2. - The valuation of merchandise in the WTO/WCO GATT system
3. - Training
4. - Compliance
5. - Automation
6. - Warehousing, Free Trade Zones, and Special Schemes for Delayed Duty Collections.
7. - The Customs Organization
8. - A Recommended Assistance Project for Consideration

Effectively this assessment will cover the entire operational base of customs. The recommendations apply to all areas within customs. These are the areas that demand immediate action to avoid confusion, loss of revenue, and severe complaints from the trade and public.

## **Chapter 1**

### **The Economics of Customs Reform**

James Cassing, Ph.D.

#### **Introduction**

The Government of Egypt (GOE) has committed to creating an economic environment conducive to growth in the gross domestic product at an annual rate of around seven percent. (Specifically, the targets are 6.8% by 2002 and 7.6% through 2017.) An important part of the strategy for achieving this ambitious target is policy reform aimed at enhancing international trade and investment. Such a "globalization " strategy is probably well suited to Egypt at this time as the world economy continues to prosper, other nations continue to open their borders to trade, and there is a large pool of international capital seeking productive investments. Also, the new European Association Agreement portends increased trade and investment opportunities.

As the GOE continues to pursue lower barriers to trade, there is a recognition that an important part of creating a trade-friendly environment is to ensure that products can move across the border expeditiously and are treated in a manner compatible with WTO obligations such as the Customs Valuation Agreement. (See, e.g., Trebilcock and Howse [1999] for an extensive discussion of the Agreement.) Indeed, around the world, nations are adopting a transactions cost, or "actual value", customs valuation system and, more generally, are embracing ever-sleeker systems of customs clearance. For example, in the port of Kaoshiang in Taiwan , after implementing a new customs system, it now takes 3.87 hours for shipments to clear customs. In the Mediterranean area, Morocco, Tunisia, and Israel have all recently streamlined their customs clearance and adopted the GATT mandated Customs Valuation Agreement.

As a contracting member of the WTO, the GOE is also obligated to abandon its current Brussels Definition of Value based reference price system of valuation and to adopt the GATT Agreement.

However, as a way of implementing such compliance, the GOE has an opportunity to overhaul the entire customs system in a way that will modernize Customs and create a state-of-the-art customs clearance operation. The nature and implementation of this new system is described at length in the other chapters of this report.

The purpose of this chapter is to recount how, well beyond simply meeting a GATT obligation; the proposed customs reform is likely to bring substantial gains in economic welfare for Egypt . Furthermore, when implemented, the reform will probably lead to increased levels of exports and foreign investment, possibly quite large. Thus, the proposed reforms will keep Egypt squarely in the camp of the global economic community and serve a purpose consistent with the GOE policy of enhancing international trade and investment.

In what follows, we address the sources of potential benefits of the reform proposed and offer some empirical measures of the magnitudes of those benefits. Section 2 addresses the so-called "static benefits" owing to adopting a transaction valuation system and to streamlining clearance. Section 3 explains how exports will be enhanced and provides some estimates of the potential size of export enhancement. Section 4 explores some "dynamic benefits" and addresses the impact on direct foreign investment. Finally, the last section considers Customs' overall role after reform and offers some conclusions.

### **Static Benefits of Customs Reform**

Any customs clearance mechanism consists fundamentally of two components: the "system", or the laws and best practices, and the "system implementation", which is how the system is run *de facto*. The current proposal would change both. Not only would the system begin using the actual valuation method for valuing shipments, but also a fairly complex mechanism for coordinating information and reducing inspections (so-called "risk management", a "post-audit" structure, and so on) would be put into place. The whole operation of Customs would become highly automated and interfaced with other agencies with the aim of greatly facilitating customs clearance and thus reducing the time and other costs currently imposed on importers.

These changes will, in turn, lead to increases in economic efficiency, or "static benefits". Here we will consider the potential benefits of adopting the Valuation Agreement and of implementing the new system separately.

### **The Valuation Agreement**

While much of the economic benefit will be generated by changes in predictability, transparency, uniformity, and accountability - discussed below - a potentially large, but subtle benefit arises simply from moving away from the current reference price system. The issue involves "similarity of product". A problem associated with the Brussels Definition of Value is that it frequently leads to the assignment of value based on a reference price for products that are really very different in value due to quality differences or differences in the costs of production abroad. Thus, if a lower priced import is assigned a higher reference price value, the "effective tariff rate" is in fact higher for this product than for higher priced imports assigned the same reference price. (In fact, the process of assigning a value to imports is not this straightforward in Egypt . Often the final assigned customs valuation of a shipment is somewhere between the declared value and the reference price, depending on some discussions during clearance.)

Specifically, suppose that there are two products on the same tariff line, but that one is produced at a low cost abroad and priced well below the reference price, while the other is actually produced and priced at the reference price. Now the tariff rate relevant to the importer is the "effective tariff rate", or the tax amount paid per unit relative to the actual price. If the reference price is applied to both goods, then the per unit tariff paid will be the tariff rate,  $t$ , times the reference price,  $P_r$ , or  $tP_r$ . And the "effective tariff rate" will be the tariff amount paid divided by the actual price of the good, or  $tP_r/P_j$

where  $P_i$  is the actual price of good  $i$ . But note; if there is a low priced good,  $P_i$ , and a high priced good,  $P_h$ , then the "effective tariff rate" will be higher on the low priced good. That is,

$$t_{PR_h} < t_{PR_i}$$

Furthermore, the effective tariff rate applied to any good whose actual price, or more specifically the true transaction value, is below the reference price will confront a tariff rate higher than was intended. That is,

$$t < t_{P \sim P_j}, \text{ where } P_i < P_r$$

For example, suppose that the high priced good is actually comparable to the reference price,  $P_h = P_r$ , and that the high priced good is twice the price of the low priced good,  $P_h = 2P_i$ . Then, from the formula for the effective tariff rate, the high priced good is taxed at the rate  $t$ , but the low priced good is taxed at a rate twice as high,  $2t$ . Thus, two goods on the same tariff line of 20% could see one taxed at 20% and the other effectively taxed at 40%.

### Economic Efficiency

Aside from giving the appearance of unfairness, more seriously the reference price system creates increased dispersion in the effective tariff structure and this reduces economic efficiency. Although a technical term, economic efficiency can be thought of as the Egyptian pound amount of money that Egyptian consumers and producers would net be willing to pay to alter various policy constraints. While no payments would actually be made, the measure is useful as a guide to the costs or benefits from policy changes. The net gains or losses for consumers are measured in "consumer surplus" and for producers in "producer surplus". Using the standard welfare measure of consumer and producer surplus, this is illustrated in Figure 1 on the following page. Shown are the import demand schedules for a low and a high price good in the same tariff category with the same reference price applied. We assume that  $P_h = P_r$  and, of course,  $P_i < P_h$ . If goods were taxed at actual value, then the tariff

inclusive price of the goods would be  $(1+t)P_h$  and  $(1+t)P_i$ . The efficiency loss owing to the tariff - or, "deadweight loss" - is given by the triangles labeled "a" and "b". (As is well known, of course, while raising revenue, most taxes including tariffs impose some economic efficiency losses.)

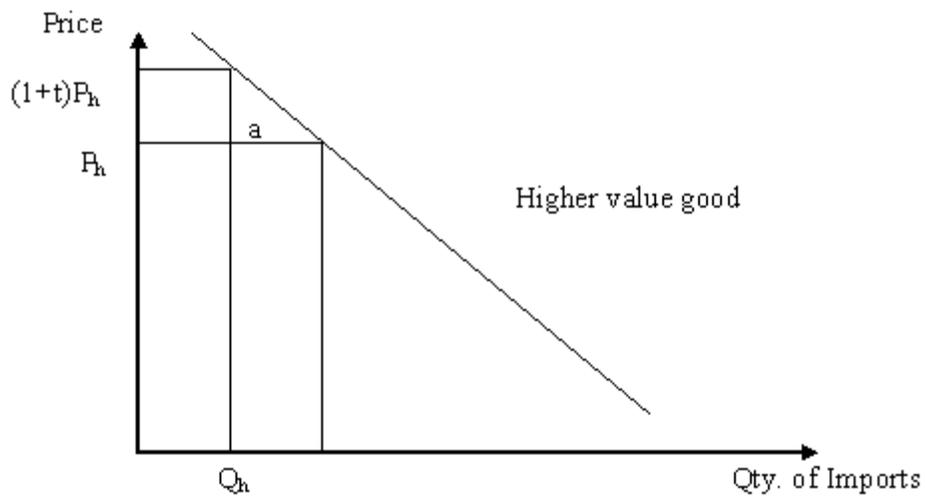
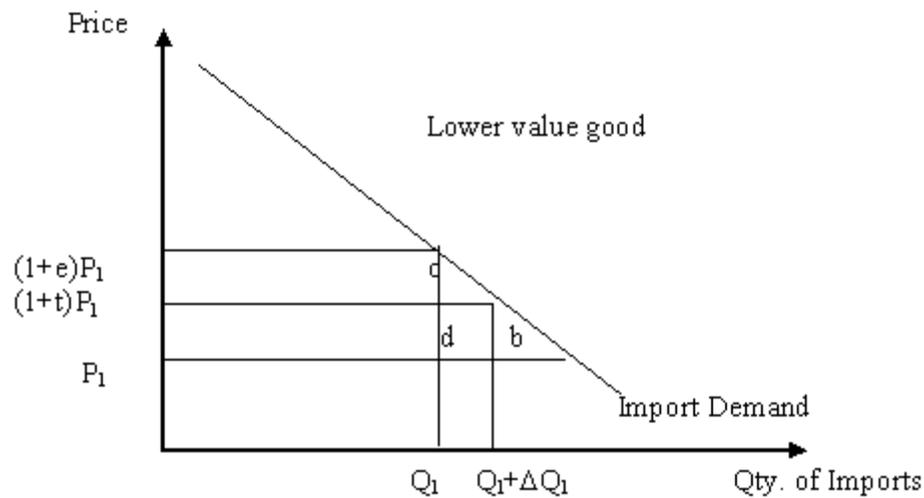
Now if the reference price is used to value the low price good, then the importer confronts the effective rate of  $t_{P \sim P_i} > t$ . In this case the effective tariff inclusive price now rises to  $P_e > (1+t)P_i$ . Thus, the efficiency loss rises by the additional area labeled c and d in Figure 1.

Mathematically, after some rearrangement of terms, this increased efficiency or "welfare" loss is given by,

$$D W = (t + 0.5e)P_i D Q$$

where  $D$  denotes "a change in",  $e = t_{P \sim P_i}$ , is the effective tariff rate, and  $Q$  denotes the level of imports for the good.

**Figure 1**



For example, if  $t = 0.2$ , or 20%, and  $P_h = 2P_l$  (The high price good is twice the price of the low price good.), then the effective tariff rate for the low price good is 40%, that is,  $e = 0.4$ . Thus, the reference price system has doubled the tariff on the low price good. Now, if we assume a unitary price elasticity of import demand, this will lead to about a 17% decline in imports of the lower price good. Using the welfare expression above, this means that welfare will decrease by about 7% of the value of those imports in the absence of the reference price system. Thus, in this example, if the value of shipments were LE 10 million, then moving to the Valuation Agreement would lead to a LE 700,000 increase in economic efficiency.

More generally, for all goods  $i$  subjected to some reference price and for all commodities  $j$  in the same tariff line, the gains from adopting the Valuation Agreement relative to the current system are given by,

$$DW = \sum_j S_j (t_j + 0.5e_j) (\text{Dvalue of shipments of good } i)$$

where  $e_i$  denotes the effective tariff rate,  $t_j$  is the actual tariff for products on tariff line  $j$ , and  $S$  represents the summation operator.

### **Empirical Estimates**

As a practical matter, while the above argument is correct and the gain from moving to the Valuation Agreement must be positive on account of the "similarity of product" issue, actually measuring the gain precisely requires detailed knowledge of the dispersion of actual transaction values of products in a given tariff line that are subjected to some higher reference price valuation. There is anecdotal evidence that this is a problem under current Customs practices [DEPRA, 2000a], and it is easy to verify that there is dispersion of actual transaction values in most tariff lines (For example, the problem has been documented to arise in Egypt even for seemingly relatively homogeneous products such as lumber [DEPRA 2000a].). But the overall effects have never been calculated.

Nonetheless, we can get a first approximation of the magnitude of the potential gain for Egypt of this one aspect of reform by making a few assumptions that are not unreasonable. Suppose that the dispersion of actual transaction values within each Harmonized System (HS) tariff line in Egypt is the same and, on average, represents a 50% price differential. (Note that this is the midpoint between the case of the lowest actual price being half the highest in the line, as in the example above, and the case of no differential in true prices due to quality or cost differences at all.) Taking the average trade weighted import tariff in Egypt,  $t$ , to be 20% [DEPRA, 2000b], this means that the average effective tariff rate,  $e$ , would be 30%. (This administrative markup of 10% in the invoice unit value appears to be a reasonable assumption for low priced goods.) Finally, assume that the price elasticity of import demand is  $-1.85$  [DEPRA, 2000b]. Then, the change in the value of shipments owing to adopting the GATT Valuation Agreement would be 15.4% and, using the welfare expression developed above, the change in welfare would be 5.39% of the value of imports. This represents an efficiency gain for Egypt from adopting the Valuation Agreement on account only of the "similarity of product" issue of LE 3.2 billion, or nearly 3/4% of GDP per year. While this estimate is surely not precise, the welfare effect will nonetheless be positive and the estimate does suggest that under reasonable assumptions the effect could be quite large. (Indeed, the estimate would be substantially larger if we used the World Bank unweighted average import tariff for Egypt of 28%.)

To put this in perspective, this is equivalent to the efficiency gain that would be generated by a nearly 43% cut in tariffs. Thus, Egyptians would realize a significant increase in real incomes.

## Revenue Effects

One concern of the GOE is that customs reform, as with tariff reform, might result in reduced customs revenue. (In Egypt customs revenue account of 12.4% of total government revenues and about 20.9% of tax revenues [Ministry of Finance, 1998].) In the case of moving away from the reference price system, this might occur due to the lower effective tariff rate applied to many goods. However, the actual changes in revenue could be positive or negative depending on the import demand elasticities. If these elasticities are on balance sufficiently greater in absolute value than unity, then tariff revenues will go up when the effective tariffs come down because the level of imports will increase by enough to offset the effect of lower taxes. A recent study [DEPRA, 2000b] estimated that the average import demand elasticity in Egypt was indeed greater than unity -- -1.85 - and found that revenue effects were likely to be small due to tariff reductions of the magnitude involved here. Tariff revenue is likely to remain about the same on account of adopting the Customs Valuation Agreement.

Furthermore, to the extent that adopting the Valuation Agreement and implementing other reforms discussed in this Report lower transactions costs of importing, the level of imports and compliance are likely to increase and so revenues will increase as well.

## Implementation

As a practical matter, the benefits from customs reform are undoubtedly going to be generated substantially from a reconfiguration of the operational aspects of Customs necessitated by the movement to the transaction valuation methodology. Indeed, much of the impetus for adopting the proposed reform resides in lowering the costs to business of importing products and so effectively lowering an administrative non-tariff barrier to trade.

Any coherent customs system strives to provide importers with predictability, transparency, uniformity, and accountability. Essentially, Customs needs to be assured that importers are not representing their merchandise falsely, and importers need to be assured that they are being treated as they expected to be when they consummated a business deal in the first place.

The current implementation of the customs system has some deficiencies in this respect, as is recorded in other chapters of this report and in DEPRA [1996, 1998] and World Bank [1999]. (Tohamy [1998] critically assesses the overall Egyptian tax administration, including customs, and transaction costs.) Without a more centralized and automated system, importers have been confronted with uncertainty and a lack of uniformity across time and place of customs procedures [DEPRA, 2000a]. Although no one is to blame, the current system makes it very hard to implement an even-handed customs treatment. And this raises the costs to importers and so serves as an implicit tax on imports. These costs are borne by importers in the form of port delays, uncertainty as to treatment, and the necessity of holding excessively large inventories due to the possibility of input supply disruptions at the ports [DEPRA, 1996; World Bank, 2000a].

While it is difficult to quantify the trade-inhibiting effects of costly customs compliance, survey data indicates that clearing customs in Egypt acts as an implicit tax on imports equivalent to 10% to 90% relative to firms usual business models [DEPRA, 1996]. Konan and Maskus [1997] estimate the above normal compliance costs to be 15% - 20%. The World Bank [2000b] estimates the tariff equivalent cost of customs clearance, licensing, and inspection procedures to be 15% and the tariff equivalent costs of quality control to be 5% - 50%. While Law 106-2000 and the "one stop shop" may help to alleviate this implicit tax, the proposed reforms would go further. For example, currently some food importers report that in Egypt it can take 30 days for actual clearance time and the appeals process can take as much as 5-6 months. One significant food importer indicated that the best they could obtain was 21 days for clearance after several years of learning and working the system. (The experience of this same importer in most other countries is that it normally takes from 1 - 7 days to clear product.) Also, there are paperwork concerns. In Egypt, customs clearance involves about

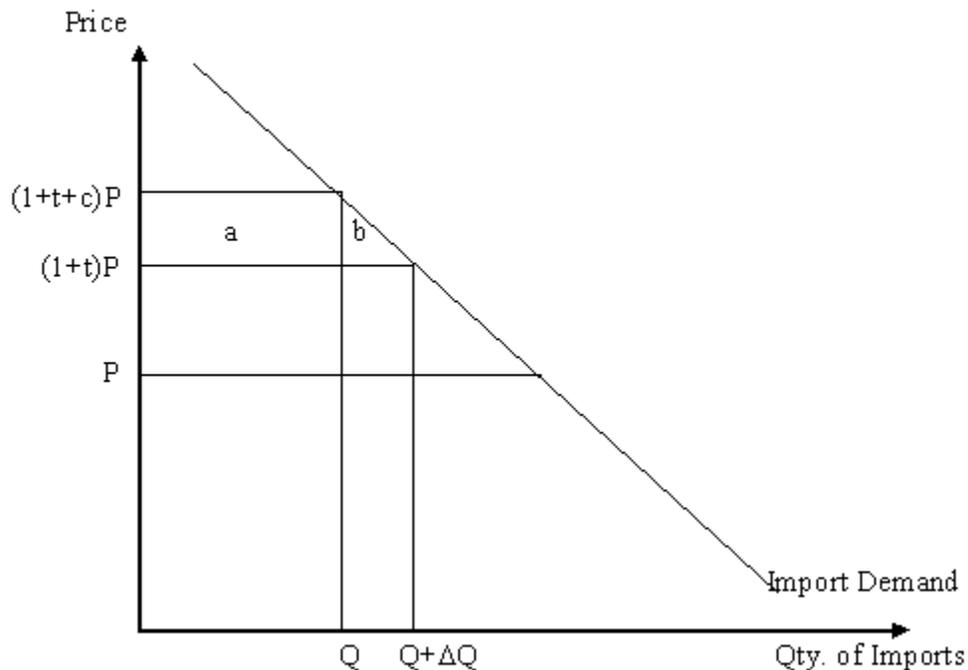
\$600,000 of product per official per year. In Singapore , that number is \$666,000,000 of product per official. One estimate is that clearance time at Egyptian ports takes two to three times as long as any other Mediterranean port [World Bank, 1996].

In contrast, developed and developing countries alike have found that more automated systems using modern risk management techniques have greatly facilitated trade by reducing the customs compliance costs imposed on importers. For example, after a reform begun in the 1980s, the U.S. now moves cargo rapidly through ports, inspecting only 1% - 3% of shipments, while achieving a high compliance rate with trade laws and a 99% revenue collection rate. Taiwan has adopted a new system and inspects fewer than 40% of ships (randomly) with shipments clearing customs in 3.87 hours on average. Jordan inspects about 30% - 50% of shipments. In South America , fewer than 20% of shipments are inspected due to some modern risk management techniques, and the international norm is less than 5% customs inspection. Thus, the reconfiguration of Customs to embody more automation and some modern risk management techniques could greatly lower the business costs, including especially time delays and input supply disruptions, of importing.

### Economic Efficiency

Once again, if the administrative costs of importing can be reduced, then this will effectively reduce a barrier to trade and bring economic efficiency gains to Egypt . Analytically, these gains are illustrated in Figure 2 shown on the following page. The diagram shows the import demand schedule for some good, with  $t$  representing the tariff rate and  $c$  the tax equivalent of customs compliance. If the costs of compliance in terms of delays and so forth could be brought to zero (Impossible, of course, but they can be brought down.), then economic efficiency would increase by an amount given by areas  $a$  and  $b$ .

**Figure 2**



Mathematically, this increase in welfare is given by,

$$DW = c(PQ + 0.5PDQ)$$

where, as before, Q denotes the level of imports.

Of course, if the compliance costs c can only be reduced not eliminated, then only a fraction of this gain will obtain.

### **Empirical Estimates**

As a rough approximation of the magnitude of efficiency gains, we can use the above welfare expression along with some Egyptian data. Using the DEPRA [1996] business survey data, suppose that the tax equivalent of customs compliance costs is 20%. (This cost tends to be higher for food products and lower for manufactures. It is consistent with the study by Konan and Maskus [1997] and the World Bank [2000].) Again, as above, take the import price elasticity of demand to be -1.85. Then, using the welfare expression, the gain from customs reform that eliminates all of the "above business model" compliance costs would be LE 14.4 billion, or about 3.6% of GDP. Again, this is probably an upper-bound estimate as it would be unrealistic to believe that all compliance costs could be eliminated. Nonetheless, the effect is positive and the assumptions used to derive the estimate are not unrealistic.

### **The Impact of Customs Reform on Exports and Employment**

While Egypt has no export taxes and few non-essential restraints on exports, customs reform can nonetheless augment exports significantly in two ways. First, there is a direct effect to the extent that exporters rely on imported inputs. If the effective tariff rate on inputs is lowered due to eliminating the "similarity of product" problem, then these inputs will become cheaper for exporters. Furthermore, if the compliance costs of importing, especially time delays, can be reduced, export producers will see their cost decline and can become more competitive in world markets. This effect could be substantial. In a survey of exporters [DEPRA, 1999], businesses in Egypt reported tariffs on imported inputs and compliance costs to be the single biggest constraint on exports, ahead of things like export procedures or absence of export credit.

Second, and much more subtle but just as real, there is an indirect effect of import impediments on exports. Roughly, any tax - implicit or explicit - on imports changes relative prices in an economy and effectively lowers the relative price of exports and non-traded goods compared with protected import-competing goods. Thus, while not an explicit tax on exports, import-impediments nonetheless implicitly tax exports and reduce the incentive to produce these goods. (This is part of the so-called "anti-export bias" inherent in the Egyptian import tariff structure.) Consequently, impediments to imports, like the "similarity of product" effective tariffs or high compliance costs, mimic an export tax and so discourage exporting. (See, e.g., Greenaway [1989], Wells and Evans [1989], and Clements and Sjaastad [1984].)

Together, these two effects can have a powerful impact on the level of export activity in Egypt. Exporters who are not in a position to absorb the increased costs of the implicit export tax will be priced out of international markets. This is one explanation of why Egypt can export goods like petroleum products, tourism, certain agricultural products, and the Suez Canal, which can absorb the tax, but not non-traditional exports like light machinery and appliances, which cannot.

### **Empirical Estimates**

The effect of impediments to imports discussed in this report could be quite high and so the benefits of customs reform could equally be large. Concerning the direct effect of increased costs of imported intermediate goods for exporters, Egyptian exporters on average import 45.36% of their inputs [DEPRA, 1998]. And, since intermediate good tariffs are not very

high in Egypt yet they are the main complaint of exporters, it is reasonable to assume that it is the reference price system and the compliance costs that are to blame. (Indeed, many of the explicit input tariffs can be rebated to exporters.)

Suppose, as a rough approximation, that we take the tax equivalent of the compliance costs to be 20% above the "usual business model" based on survey results and the Konan-Maskus [1997] study. Also, add to this the 10% tariff equivalent increase in the average import tariff due to the "effective tariff" argument. (We take the average trade weighted tariff again to be 20%). Then, the total net effect of customs reform, which eliminated these costs, would be equivalent to reducing a 30% import tariff to zero.

Now a study of the incidence of import tariffs on exports in Egypt has shown that a reduction in the implicit import tariff by this magnitude - assuming that the explicit tariffs remain in place -- would be equivalent to eliminating a 16.7% implicit export tax [DEPRA, 1998]. Suppose that the export supply elasticity is unity for Egypt. (In fact, it is probably much higher for nontraditional exports.) Then, when the proposed reforms are fully implemented, they should result in an increase in exports of nearly 17%. And, if employment patterns do not change, this would imply an increase in employment of 17% in the export sector. (Of course, there will be an expansion of imports and so a contraction of production in the protected import-competing sector. But, if the transition time to the new customs system is several years, there need be no unemployment as natural attrition of labor in this sector will render involuntary separations unnecessary [DEPRA, 2000a].)

### **Dynamic Benefits, Investment, and Growth**

While the benefits of the proposed reform discussed above are quite large, there are likely to be substantially larger benefits which are very hard to quantify - so-called "dynamic benefits". An advantage of a customs clearance system that incorporates increased predictability, transparency, uniformity, and accountability, is that the business community responds positively to the decreased uncertainty. This response by traders and investors can be quite large.

While there is no way of being certain of the positive impact on foreign investment, if imported intermediate inputs are taken to be around 40% for the whole economy [DEPRA, 1998], then a reduction in the importing business costs associated with the current system of 30% as posited above would lead to cost reductions for foreign direct investment on the order of 8%. According to DEPRA (2000b), a 1 % change in tariffs leads to a \$63.3 million change in foreign direct investment in Egypt. So, to the extent that these cost reductions mirror tariff changes, the increase in foreign direct investment due to the imported inputs cost savings would be about \$506.4 million per. In fact, this is likely to be a very conservative estimate since the experience of other countries has been that as investment discovers a country, the investment process is enhanced [Roberts and Tybout, 1997]. Also, notice that since compliance costs act as an implicit tariff, free trade zones, duty drawback, and so on, could not achieve this result.

Furthermore, note that the compliance cost reduction is likely to result in "better" investment. Currently, most of the foreign direct investment - and much of the domestic investment as well - is flowing into import-competing industries that are protected by high explicit and implicit trade barriers. Such investment tends to be in comparative disadvantage, lower productivity industries that need the protection for survival. More alarming, when foreign-owned firms repatriate their profits abroad, they send artificially large profits that have been protected by trade barriers and so actually create an artificially enhanced drain on foreign exchange reserves [DEPRA, 2000a]. When the non-tariff trade barrier of compliance costs is lowered, investment will be redirected to the export and non-traded goods industries and out of the import-competing industries in approximately equal amounts. Thus, Egypt will gain both more investment and employment due to the cost reductions and "better", more productive investment.

Another way to assess the gain of reform is in terms of the marginal effective tax rate (METR) on real capital investment in Egypt. Suppose that we take the after-tax rate of return to be 9.25% in order to attract investors. (This was the nominal deposit rate of Egyptian banks in September 2000.) Then, Kheir-El-Din, Fawzy, and Rafaat [2000] calculate that a marginal joint stock investment in the manufacturing sector needs to earn a before-tax rate of return of 16.45% in order to invest. The

number when omitting indirect taxes - tariffs, sales, and stamps - is 12.47%. Now, reference prices and compliance costs work like an indirect tax from the point of view of an investor. If this implicit tax is taken to be 30%, as above, and if 40% of new investors' inputs are to be imported, then this works like an additional 12% tax on capital investment and, using the Kheir-El-Din, et al, methodology, would necessitate about a 2% additional before-tax rate of return to induce new investment. Thus, Customs reform would lower the required before-tax rate of return and consequently induce more investment, both domestic and foreign.

Any new investment, of course, will translate into higher rates of growth and employment for Egypt. Since real growth tends to compound, even modest increases in new investment could contribute substantially to the GOE growth targets between now and 2017 as posited in "Vision 2017".

### **Other Costs and Benefits of Implementing the Proposed Reforms**

The benefits described above are both real and large. Beyond this, many of the proposed changes in Customs need to be made anyway in order to meet WTO obligations and thus a benefit of such changes is to showcase the GOE as WTO compliant.

However, it would be unfair to dismiss the substantial costs inherent in the proposed reforms. As is documented in this report, there is the need for substantial training, automation, and administrative reconfiguration. The experience of other countries - the U.S. Taiwan , Singapore , etc. - has been that in the short-run the system encountered high costs of implementation and modest benefits in terms of facilitating trade. However, trade law compliance and revenue collection responded fairly rapidly, and in the longer run the benefits described above accrued.

Also, there are bound to be intangible benefits from the reform which accrue to the personnel of Customs and to the GOE. The reform will equip Customs with state-of-the-art techniques and skills. Professionalism will be enhanced and the whole customs process will begin to engender mutual respect between importers and Customs agents. This has been the experience in other countries and should be the same for Egypt . For example, after the United States reformed Customs and adopted the Valuation Agreement, there was a dramatic decrease in appeals to the courts from administrative determination of valuation [ Jackson , 1997].

### **Conclusions**

In order to conform to WTO obligations, the GOE needs to adopt the Customs Valuation Code. This is not a trivial undertaking as all of Customs will be reconfigured if it is to be done properly. But this is an opportunity. As the report makes clear, there is a path toward automating and streamlining Customs in a way that can confront the challenge and at the same time reinforce the GOE's goal of facilitating international trade and investment.

While there will be costs incurred, the benefits to the economy would appear to be large. Also, the personnel of Customs should benefit from increased skills and knowledge that Egyptian Customs is state-of-the-art. Administratively, Customs would retain its role in clearance and data collection.

References used in this chapter are found at the end of this report.

## Chapter 2

### Customs Duty Collection and Valuation Irina Swift

#### Background

Customs authorities play a significant role in the area of international trade. The efficiency of Customs processes can promote additional investment, as more trade will flow into a country that has an efficient process for moving goods including raw materials and capital goods into the economy. However, if the movement of goods through Customs and other agencies is viewed to be costly and inefficient, trade and investment partners often migrate to markets that are perceived to exist in a more business friendly region. Since the mission of Customs is to collect revenue and enforce the import laws of the nation, Customs impact on the economic health of a country is not often well understood even among Customs officers.

Many nations promote efficient and cost effective operations so as not to have Customs viewed as a non-tariff barrier to international trade and growth. Those countries have modernized their Customs Services by working with trade partners to create more efficient processes through legislation and practice and by developing automated tools to facilitate the movement of goods. Both the WTO and the WCO encourage Customs services to incorporate modern business practices and tools into their operational plans and to implement new philosophies for Customs management and trade interface.

The Government of Egypt is a member of the World Trade Organization (WTO) and the World Customs Organization (WCO). On June 30, 1995, Egypt became a contracting party to the WTO Agreement on Customs Valuation (GATT Valuation Agreement) and invoked paragraph 1 of Article 20 of the Agreement to delay application of its provisions for a period of five years from the date of entry of June 30, 1995 and thereby was scheduled to apply the provisions of the Agreement by June 30, 2000. Prior to that date the Government of Egypt requested an additional extension and received one year to prepare the legislation and necessary procedural reform to implement. The law was amended by legislative action as Law 160/2000 to provide for the Agreement and Ministerial Decree 765/2001 published on June 25, 2001 implemented the Agreement on July 1, 2001 .

The Government of Egypt is also a contracting party to the Harmonized System Convention and has used the Harmonized System to classify goods since it was officially adopted by Presidential Decree 38/1994 of February 13, 1994 .

The implementation of the Valuation Agreement can be viewed as an opportunity to initiate reform, to reorient the commercial cargo process, and to further develop and modernize the Customs Department. The Value Agreement alters the methodology of valuation of imports entering Egypt. The primary basis for valuation of goods for Customs purposes is the transaction value of imported goods i.e. the price actually paid or payable for the imported goods sold for export to the country of importation adjusted in accordance with the provisions of Article 8 of the Valuation Agreement. The Agreement specifies six methods of valuation but before a Customs official can reject the transaction value and apply another method of valuation in strict sequential order he must first determine that transaction value may not exist for the imported good, provide the importer with an opportunity supply additional information, and only when that information is not provided or does not substantiate the invoice price as reflecting the price paid or payable move to apply the next method of valuation.

The World Customs Organization provides guidelines for the implementation of the Valuation Agreement. The WCO recommends that Customs authorities alter their organization in order to cope with the Valuation System by creating the legal authorities within their laws and regulations, providing

an organizational structure that supports post-clearance audit, intelligence gathering, risk assessment, expertise on the Valuation Agreement and international trade, and that structured training on the Agreement be provided to all parties involved in the process. It is anticipated that when this process matures, a paperless electronic environment can be considered and that Customs Authorities will have the foundation to process shipments electronically and still maintain a level of confidence that the transactions are accurately declared and appropriate revenue is collected.

The WCO Valuation Control Handbook states "The GATT Valuation System necessitates the active involvement of both importers and Customs in the valuation process. It presupposes that a process of consultation take place between Customs and the importers to ensure that the value determined is accurate." It encourages the use of automated systems to provide efficiency to the process and the creation a historical database that can be used for analysis, risk management, and identification of candidates for further review or for post audit.

It is due to these factors that Customs is encouraged to consider reorienting its commercial cargo strategy. The Valuation Agreement does not only impact on how Customs values merchandise but re-defines how Customs officers will perform their work and interact with the trade. In the current process there is limited capability for trade interaction on the part of valuation personnel.

The Agreement necessitates: that importers have full information of the Customs laws and regulations and only then can they fulfill their obligation to provide Customs with full and accurate information about the circumstances of the transaction; and that Customs officials have a knowledge of the legal framework and the expertise to examine and verify all the relevant facts of the importation.

The greater degree of interaction between Customs and the trade will encourage the building of relationships based on trust, and an environment that hopefully will promote confidence that specific trade information provided to Customs officers to help them verify the invoice price of the goods will be held in strict confidence within the law and not shared with others except by legal authority.

The Agreement encourages groups to be developed within specific industry sectors, and necessitates that an orderly rotation policy be developed that does not disrupt the expertise within the group. It encourages Customs to promote in-house or outside training and provide resources to help officers maintain their level of expertise. It encourages the use and development of automated systems to help officers do their work with modern tools. It encourages officers working with like commodities to meet periodically to discuss mutual problems and have the ability to communicate via efficient electronic means to gather information from their colleagues or outside sources. It encourages a greater degree of decision making at a lower level of authority. It encourages importers to seek the advice and guidance of Customs authorities prior to importing new products. It encourages a system of rulings be implemented binding on both Customs and the importer. It encourages Customs to use information resident in the declaration system to perform trade analysis and identify patterns, areas of concern, risk, compliant importers and transactions that can be given expedited release procedures. It encourages the ability to verify invoice data, review importer records, provide preliminary release, and the develop risk management and post audit capabilities. In effect the Customs Value Agreement necessitates a reorientation of the working environment and an opportunity for modernization and reform.

### **Review of Current Determination Process (June 2001)**

Customs receives the declaration that either has been transmitted and printed or presented for keying of data from a coding sheet. If another government agency such as Agriculture, Health, or GOIEC (General Organization of Import Export Control) is involved in the import of goods process, that other agency must provide a release or conditional release for Customs release processing to be initiated. The electronic data is first reconciled with the documents and then the file is presented to the specialized Customs officers for review and designation. Groups of officers dedicated to specific industry sectors review the declaration and associated documents. This is a good foundation to further develop expertise to promote full implementation of the Agreement. The officer reviews the file to ascertain that all documents including any required other agency releases are present, that the

information on the declaration reflects the invoice, that a packing list is present, and that the provided Harmonized System tariff item number is accurate.

During the review we witnessed in June 2001, using the valuation guidelines based on the Brussels Definition of Value, the officer checked the value against the value database using the harmonized system item number to search the database. If the officer does not locate a product on the database that conforms to the similarity of specifications of the product before him, there may be a process of consultation that will occur between the estimator and his superiors. It is this process of checking values against a database to identify a market price that will require change and additional expertise in product knowledge. The Valuation Agreement speaks to valuation of the goods based on the price actually paid or payable, and not based on a market value.

Draft guidelines addressing this change have been written and distributed to the workforce. Based on the translation received, the guidelines seem to rely more on price information before Customs and on properly notarized documents than on providing an environment for verification of the circumstances of sale. There have been forms created to allow for the importer to provide additional information, but time period (15 days) for providing the information on related party transactions seems unusually short considering that the importer may have to contact his foreign supplier to provide Customs with the information.

It is understood that during the transitional phase there must be time to develop a new methodology for working within the principles of the Agreement, and it is hoped that as the process of invoice value verification matures, there will be less reliance placed on pricing information before Customs or on consular invoices or certificates of origin which seem to be required for every shipment. It may be worthwhile to visit other nations in the region to see how they have implemented the Value Agreement and learn from their experience and work together to discuss methodologies and exchanges of material that have been found to be useful. In today's electronic age, documents have less meaning. Often commerce is initiated without documents. With computer equipment and software, consular stamps or certificates of origin can be altered and falsified as easily as invoices. This is the essence of expertise development. The process moves from a reliance on documents to a reliance on trade knowledge.

Additionally all cargo is designated for examination and is examined in the presence of the importer or his agent and the duty, fees, and taxes paid prior to release. Once payment is made the cargo is free to move. Should there be a difference of opinion between the Customs officer and the importer, the importer has the option of paying the additional duty or posting a bank guarantee for the difference and filing an appeal. Since the Agreement provides that if additional verification is needed by Customs the goods should be released under guarantee to the importer, this process may need to be altered as complex transactions may require additional time to verify or audit. This is an area that needs to be reviewed for additional legislative action.

In the current process, every transaction seems to be treated with the same level of scrutiny. The only selective processing that occurs is the designation of the percentage of the shipment that is to be examined. It is as if every transaction is a first occurrence with no previous documented or available historical record. There is no structured methodology of risk assessment or selective processing. It appears to be a time consuming process with no apparent objective or quantifiable methodology to assess overall results. This is also a factor that may actually degrade the work performance of the officer. When there is no specific identified risk regarding the exam or review of documents, the officer may perform his work in a rote fashion and could easily overlook a significant factor.

Customs services that have initiated selective inspections have found that a greater number of discrepant findings accrue based on the number of exams performed. When exam and/or review are required based on a specific concern, officers are more likely to take the time to review the transaction with a greater level of scrutiny. Selective inspections and risk management methodologies are modern Customs tools used to grant benefits to compliant importers, provide for more efficient movement of goods, and for the development of annual enforcement plans to promote compliance.

## **Trade Perspective on Duty Determination Process**

The team interviewed trade participants during the process of developing information. The interviews were conducted both with import export associations and with individual importers. The perception of the trade community regarding Customs was one of lack of trust and lack of confidence in Customs to properly perform their functions in the duty determination process. Although this is a trade perception and may be inaccurate, it is troubling. Many members of the trade stated: that most customs officers were not well informed about the classification and valuation of goods; that standardization and uniformity did not exist; and information was difficult to identify and locate for both Customs officers and trade participants.

When one major trade association requested training on the new methodology to be used to value goods under the Agreement, they told us they received a book. The law and implementing decree was not passed through them for comment. Although not required, it is normal for countries to discuss major changes with their client community. In many countries when a major change in procedures is to occur, the trade community becomes an active participant in that change and even helps to promote it.

When asked about specific portions of the Agreement, there was concern about Customs audit capabilities and additional time allowed to verify the transaction. One importer expressed his concern by discussing his understanding of how Customs had conducted previous "audits" often involving the seizure of books, computers, and all business records preventing firms from doing any work. There seems to be little understanding on the part of the importers as to the meaning of post clearance audit or invoice verification.

Importers also voiced deep concerns about the ability of Customs officers to delay the final duty determination process, as envisioned by the Agreement, in cases of complex issues or the need to further verify additional documentation. Importers felt they would rather know the duty and tax amount during the release process and not be surprised with additional payment due after they sold their goods. While in many countries it is considered a benefit and a right to move goods from Customs custody under surety during the verification process, the local trade community viewed this practice with great apprehension.

There was also concern about the time factor allowed for providing additional information to Customs. The implementing decree allows 15 days from the request to provide additional supporting information. This is a very short time period. There can be complex issues that would require additional time but there seems to be no provision for extensions to be granted. It may be that Customs authorities are not totally familiar with the process of producing substantiating documents of the type envisioned by the Agreement. Fifteen days may appear appropriate based on previous experience, but may not be adequate under the Value Agreement.

Importers also expressed concern about whether Customs had in fact restructured their organization to support the changes needed to properly implement the Agreement. Once again since the trade community received little information on what the new Agreement necessitated, it is normal for them to be concerned as to whether Customs authorities were in fact prepared to implement on July 1.

The basic consensus of the trade community was that no matter what the Agreement called for little if anything would change within Customs. This is the perspective of the trade community and in order to change this perspective there needs to be a major public information campaign and education of the trade.

There were several discussions about invoices. Most Customs officers stated that 90% of the invoices indicated under valuation of the invoiced goods, the domestic producers we interviewed seemed to hold a similar view, but the trade associations felt that 90% were accurate and only 10% were in fact undervalued. This is also a matter of perception. There appears to be no objective or quantifiable data on this issue. Since Customs applied a system of valuation based on Brussels Definition of Value, no invoiced value that indicated a value lower than the right market reference price was usually accepted. In that system there was little need to verify the accuracy of the invoice price, thus lower negotiated prices would seem to fall into under valuation of goods category. However, it is possible that not only were the invoice values understated but also in fact the goods misdescribed on the invoice to provide for a lower tariff rate and a lower value.

One party expressed direct knowledge of misdescription of goods and alteration of the invoices to receive a more favorable duty rate and value from Customs. Another party stated that although he receives quantify discounts for his goods, Customs officers value his goods at the same value as competitors that buy in smaller quantities and he had no reason to believe anything would change under the new Agreement.

Confidentiality also was an issue. Importers did not appear to trust Customs authorities not to disclose confidential business information outside of the work environment even though there were laws to preclude this from happening and punishment for the disclosing officer. Importers had no direct knowledge that anyone had ever been punished for disclosing information. This is another area that may require some additional legislative action within the Customs Law. Even though there are current laws governing the conduct of civilian employees of the Government of Egypt and the disclosure of confidential information, there may be need to address this issue separately as part of the Customs Law particularly since this is an important component of the Agreement.

Generally all importers agreed that the work environment and salaries of Customs officers were a major factor that created many difficulties and that officers could not properly do their work under those conditions. Communication was either non-existent or sporadic, work areas were noisy, and personnel had few materials, resources, or tools to improve their expertise and function in a professional manner that is a necessary component in a modern Customs Department.

#### Development of a Long-Term Infrastructure for Full Implementation of GATT Valuation Agreement

The following considerations are provided as options to help develop new methodologies to promote a foundation more conducive towards implementing the Valuation Agreement. Many of the suggestions can be considered as separate and discreet options and developed on as needed basis either within the total organization or as model pilot initiatives at specific sites to serve as proof of concept before considering them for acceptance within the organization. Certain areas such as the building of expertise, post-audit functions and risk management have been expanded both because of the interest expressed by persons interviewed and because they are recommended by the WCO as basic building blocks in the implementation of the Agreement. These areas are long-term initiatives that will require both automation and outside support.

#### **Development of Resources and Tools**

In order to move towards the full implementation of the Agreement, Customs officers will require the appropriate reference materials and tools to do their work. There is an identified need to further develop a central reference or library area at each site for Customs officers to access and review reference materials. General references such as the Valuation Agreement, Implementing Decree, and guidelines must be made available to all officers. Additional WCO valuation material such as the Compendium of Valuation Rulings, WCO Valuation Control Handbook (specifically designed for developing countries implementing the Agreement), WCO Value Course, WCO Commercial Fraud Action Plan (Essential Elements for the Control of Fraud Under the WTO/GATT Valuation Agreement), the Harmonized Tariff, the Explanatory notes to the Harmonized Tariff, WCO classification rulings, the applicable Rules of Origin, rulings provided to importers, appeal decisions, and written standard operating procedures on the processing and release of commercial cargo should be available in this reference area. Specific industry related publications, trade publications, and materials should be identified and procured. Personnel should have full access to this material and be allowed to extract, copy or borrow material that is specific to their assigned area. WCO materials need to be translated into Arabic and made available in both the Arabic and English/French version. This is an area that may require assistance from donors particularly in translation and printing costs.

Until such time as computers are assigned to individuals, a certain number can be made available to perform research and communicate with counterparts. They can also be housed at the reference site. Materials that are available in an electronic format can be loaded into the computer for officers to review and copy. The trade should also be encouraged to use such a site.

It appeared that general material was difficult to locate and request. Some reference material may have been appropriated by Customs officers for their own use and not returned. This is common in areas where reference materials are rare and therefore quickly appropriated by senior personnel for their exclusive use.

Automated tools need to be developed to allow individual officers to research the specifics of previous transactions and trade trends to make educated decisions about the shipment undergoing processing. As more computers are made available to individuals, much of the material can be made available on-line and up-to-date information disseminated through the Customs network. Email is an important aspect of communication in modern Customs services. Information, instructions, requests, and general communication move electronically to individual officers and everyone becomes aware and has the same information either about procedures or concerns on specific shipments.

All managers and officers involved the classification and valuation of merchandise should have access to computers and computer training to use basic programs and email. Electronic communication is also less intrusive to the work process. Currently telephones ring continuously, intruding on a manager's time and ability to concentrate. As computers become available, information and inquiries either from inside or outside should be encouraged to be sent electronically. It encourages the use of a more efficient method of communication with requests and responses available for review. It provides greater flexibility within the work environment. A manager or Customs officer can have time to consider the response and research it before responding. This provides for a more efficient and quieter work environment.

Training from outside sectors should be encouraged. The trade community and domestic industry can provide valuable assistance in product knowledge. The banking and accounting sectors are excellent sources of determining audit trails for payment and product financing. Visits to manufacturing plants, processing facilities, warehouses, distribution centers, and common carriers can provide invaluable information about how products are made, financed, bought, and shipped.

General and specialized joint seminars for Customs and the trade can be considered. Often there is a misconception among the trade community on how goods are classified or valued. To bring together Customs officer and the trade community in a seminar environment and provide either a general or industry specific course on product classification or valuation would benefit both parties and it would create a greater atmosphere of trust. Currently there seems to be a perception among traders and the business community that Customs officers are not applying the Harmonized System properly nor according to trade interview will they apply the Valuation Agreement properly. Joint training could alter that perception and promote more trade interface. Not only should clearing agents attend, but also importers should be encouraged to send representatives involved in the import process. The same process should be put in place for other Customs functions. It provides a common understanding of the rules in an open and transparent environment. Customs and the trade should be encouraged to do their work together and receive their information from the same sources.

### **Development of Expertise\_**

One option is to give consideration to promote the development of a working level commodity expert with responsibility for a finer industry sector focus and greater exposure to the trade. In major developed countries teams dedicated to specific industry sectors work under the direction of a team leader and develop expertise within the sector. As specific industry groups are already in place, it would be useful to consider developing those officers into commodity experts that have the necessary background and product knowledge to be able to easily detect either non-compliance or fraudulent practices.

Another option that some countries employ is to create a group of national commodity experts that: provide information; identify resources; initiate trade seminars; and serve as a central place of consultation to both Customs officers and the trade community. A system of orderly rotation must exist so as not to disrupt the efficiency of the process and the expertise needed to properly classify and verify the value of the merchandise.

In order to implement properly the Value Agreement there needs to be a different level of specialization and expertise than was necessary under the system of valuation based on Brussels Definition of Value when values were researched and identified as reflecting market prices. Such values were used in valuation of goods and not the price paid or payable by the importer. As this system is no longer applicable under the Value Agreement consideration can be given to reeducation and realignment of the workforce.

The Valuation Agreement necessitates the active involvement of the importer in the process. Although the clearing agent plays a significant role in the processing of the goods, he is not the knowledgeable party about the specific transaction. The importer or buyer of the goods is the knowledgeable and responsible party. The importer needs to be part of the process. He needs to be educated or have member of his staff educated in what documents, records, and books are to be kept and made available to Customs on request; that Customs has the authority to review those records, books, financial arrangements, and even the specifics of what happens to the imported goods. Visits to plants and processing sites should be encouraged. Importers should be encouraged to educate Customs officers about their business environment and Customs in turn needs to educate the importer about the Customs environment. To make this process efficient and less time consuming, only those officers dedicated to processing goods in specific industry sectors would visit importers' premises.

Any information learned about the transaction or use of the goods must be subject to the confidentiality laws of the GOE and the Agreement. If the importer can trust the officers to not disclose proprietary trade information to outside sources, he will be more willing to educate them about his business practices and product line. This is envisioned as a long-term process that requires confidence building in both areas.

Customs authorities can also promote the development of expertise by allocating funds for training, for resource material, for seminars, and for meetings at the working level with other Customs Services to discuss mutual problems. A degree of independent decision-making comes with expertise. Managers can be encouraged to manage the process and not the task.

Customs authorities can work towards creating better process for internal record keeping were results of examination of goods and review of documents whether in an electronic or paper format be kept in an orderly and accessible manner and available in a timely fashion to other officers, managers, auditors, or parties involved in the appeals process. Only then can risk management and post audit techniques be properly applied. There will be a need to have a historical record and baseline in order to properly assess risk.

### **Development of a Binding Rulings Process**

One area to be considered is an efficient and published binding ruling process. It is understood that there is a process that allows for importers to receive rulings from Customs authorities. Apparently it does not appear to be binding on either party. In fact if an importer receives an unfavorable ruling there may be no current methodology to even know that such a ruling exists particularly if he brings his goods through another port. Rulings should be binding on both parties. They should be published and made available to all sites processing cargo. Once computers become available to the majority of the workforce, rulings can be made available on-line. However, a database of rulings can be developed in the current system. It would allow for rulings to be numbered and abstracts entered into the automated system by importer name. This would allow the customs officer processing an importer's shipment to review if a ruling was made on a specific product. Rulings can cover HS classification, origin determination, method of valuation, or any number of Customs processes. By deleting specific importer information, and describing the issues only, rulings should also be made available to the trade which may alter the current view about lack of uniformity and standardization in applying HS, origin or value determinations.

If the imported product is the same as described on the ruling, Customs officers would be obligated to use the ruling even if they disagreed with it. If an error on the part of Customs was discovered, Customs could only change the ruling to be effective after a specific notification period. Clear

guidelines on such issues would have to be published and followed. If Customs has all the facts and makes an incorrect determination, Customs should not have the ability to change the ruling without proper notification and only for future imports. Importers have priced and sold their goods based on a ruling that was issued and should not be requested to pay additional revenue. However, if the importer has in fact misrepresented the product or issue, the ruling cannot be considered to be binding for the product or issue before Customs.

By deleting specific importer information, and describing the issues only, rulings should also be made available to the trade which may alter the current view about lack of uniformity and standardization in applying HS, origin or value determinations.

Many Customs services publish their binding rulings, appeal decisions, court decisions, and make them available on-line for anyone to review. The United States, Australia, the European Union, and many other nations have web sites that include rulings available for review and download either to the public or to members. These are designed to eliminate the keeping of manual records, to promote uniformity and provide information to a wide audience including other governments. The WCO publishes tariff rulings and makes them available for review. All of these can be used as tools and can help to provide formats for the binding ruling process.

### **Development of Analysis and Research Capability**

Another possibility or option is to develop a group dedicated to analysis and research of trade sectors, importer and commodity histories, and processes. This group would need to have good research and computer skills. They would work closely with estimators to develop trends based on historical data and evaluate risks associated with specific commodities or traders. They could help develop criteria for selective processing, identify candidates for the post audit, become a repository of commercial intelligence, and develop management information. If the estimator needed information about specific risk associated with a commodity, an industry sector, or an importer, the analyst could perform internal and external research to provide that level of information.

For this process to be effective there would be a need to develop an on-line historical database on the results of physical examination and documents review. While a database development process occurs, input of this level of information from current paper documents could begin using an off-the-shelf software database such as MS ACCESS. This type of action could help develop the specifications for creating an on-line tool that would be part of the declaration process. It could be a proof-of-concept. This type of approach has been used and found to be efficient in the development of both lookout criteria and selective processing. However, to be an effective participant in the cargo process, such a group must be part of that process and have significant interaction with personnel dedicated to duty determination. Analyst positions could be filled from both inside and outside the current Customs staff. In the future as more computers become available to the general workforce, this group could help educate the workforce in the use of software and research tools.

### **Development of Conditional Release Capabilities\_**

Some goods declarations are more complex than others and require a longer period of time to verify the circumstances of sale. In some cases there is a requirement to consult with the importer either on the specific transaction or to audit the books and records of the importer on multiple transactions. This process necessitates that the cargo be released to the importer under a guarantee or surety obligation which provides that if any additional duties or taxes accrue after the review of the transaction documents or financing arrangement, the Customs Authorities have a guarantee of payment. This procedure also necessitates that a reasonable and specific time period be established to finalize the action and allow the importer to have an opportunity to protest or appeal the action.

All of these actions must have clear and specific guidelines as to the obligations of Customs and the importer to produce books and records, and of Customs to finalize the action within a specific period. The business and trade community cannot function without having clear and legal guidelines. They need to have predictability and a clear understanding when final action occurs and Customs cannot

re-open the declaration to assess additional revenue due to an error on the part of either party. The same rules are to apply to the importer seeking a refund. At end of the time period the action is final and closed. The only option available to re-open the process would if there was some evidence of fraudulent practices. Article 13 of the Value Agreement anticipates a process of conditional release be in place to allow Customs authorities to verify the circumstances of the transaction.

### **Development of Confidential Procedures**

The Value Agreement specifies a greater level of involvement of the importer in the Customs valuation process. It provides a great degree of latitude for Customs to access and review proprietary business records and information to verify the price paid or payable. For the importer to provide that level of information and for Customs to properly perform the verification process, the importer must be secure that all information provided to the officer will be kept in strict confidence and not released to outside parties or other government agencies without his consent or only as part of a specific judicial proceeding.

There may be a need to review the current procedures and possibly initiate legislative action to further define the responsibilities of Customs officers in handling proprietary business records. It is possible that there are confidentiality guidelines in place for government personnel handling anti-dumping investigations. Those officers deal with very sensitive business information and those guidelines could be studied and possibly incorporated into the Customs confidentiality regulations. Clear guidelines must be established and adhered to by both parties. The obligations of providing information to Customs must be clearly defined and the Customs Authority's responsibility to keep the information confidential and secure must also be well defined within the Customs regulations. This is an essential component of the Agreement and covered within the Agreement under Article 10.

### **Development of a Post-Clearance Audit Process**

The area of post clearance audit was expanded and further defined because of questions that were asked by Customs officials during the interview process.

The Value Agreement provides for release of cargo and in some instances for final determination of value to occur after the release of the goods. In cases of complex issues there is a need for specific audit expertise. It is suggested that a group of audit personnel be developed. It is often effective to have a commodity expert assigned to the audit group when they perform an audit in the area of expertise of the estimator. This is additional reason to develop expertise within commodity sector. An auditor is an expert in reviewing records and audit trails but will have no classification and little valuation expertise. This expertise needs to be part of the audit process. Only such a joint effort can properly evaluate the importer's compliance level.

In the broadest sense, post-clearance audits are reviews of the records and accounts of an entity, private or public, by an independent authority, and to verify that they conform to generally accepted accounting principles.

Many entities also have their own audit staffs, which conduct internal audits to determine whether funds and assets are accounted for, and properly managed.

As used by Customs authorities, post audits are financial examinations of the books and records of importers to reconcile their accounts with the information contained in customs declarations and with the goods themselves. Customs post audits may be conducted on other international trade participants for similar reasons. As an example of one such reason is to reconcile the financial records of privately owned customs warehouses with the inventory of goods stored therein and customs records of the goods.

Post audits allow Customs authorities to check importations and importers for compliance with the

laws and regulations after release of the goods to the importer. Consequently, such audits are referred to as post-clearance audits or simply post-audits.

### **Increased Use of Customs Post Clearance Audits**

The use and practice of post clearance audits by Customs authorities has grown considerably in recent years for several reasons: emphasis on trade facilitation has led to increasingly rapid clearance times; increase in the complexity and volume of importations has created a need for post release review; and in some countries the number of Customs officers has failed to keep pace with the increase in international trade due to economic, political, and social factors.

Post clearance audits allow a check of importers accounts, not just of individual importations, and they are understood to be a more efficient method of verifying compliance with customs laws than review and clearance of individual importations. However, it is not intended that this process completely replace document and physical checks done at the time of importation.

### **What Post Audits are Not**

There are sometimes misunderstandings about post audits that need to be clarified:

- Post audits should not be confused with internal audits to reconcile accounts kept by Custom: officers on funds, property, and assets handled or owned by Customs authorities. *Custom,, Post audits serve a wholly different purpose from customs internal audits; thus they arE conducted by separate staffs not under the same managerial direction.*
- Post audits are not criminal investigations of fraud or violation of financial laws. Crimina investigations are conducted to investigate suspected violations of the law or regulations. Pos audits are conducted to determine whether financial records can be reconciled with custom: records. If an audit reveals a suspected violation of law, the matter is turned over to crimina investigators for action. Occasionally, criminal investigators will call on assistance frorr auditors to audit the accounts of suspected violators and obtain information in connection witY an investigation.
- Some Customs officers who check declared value and classification information upor importation are concerned that auditors are checking on the quality of their work. This is no the intent of the audit. The nature of auditors' work gives them more time and opportunity to obtain and evaluate information that is normally not available at the time **of processing of the import declaration.**

### **Foundations of Post Audit**

Post audit programs and procedures are likely to be unsuccessful without several underlying preconditions.

### **Legal Authorities**

The laws of most nations require importers and other relevant participants in international trade to maintain books, records, and accounts of their importations, as well as the authority of Custom: administrations or related ministries to specify by regulations the documents that fall into the category. The laws also give Customs administrations authority to demand the presentation of those books and records to Customs for examination, or allow Customs officers to examine them at the premises of the importer. Further authority is usually given for government authorities, to conduct ce search of premises for books and records relating to customs matters.

Since post audits are not likely to be useful if their results are not implemented and additional revenue collected, most nations allow customs authorities to collect duties, taxes, and penalties on past importations due as the result of an audit. Sometimes these amounts can be collected from the importer's pledge or security given by the importer, but in other instances Customs authorities are authorized to pursue court or other actions to compel payment of these amounts.

Finally, the law of most nations contains a legal presumption that an unresolved discrepancy between the importer's books and records and the goods and information as declared to Customs is a debt either due from the importer to Customs or a debt from Customs to the importer. The audit report needs not show precisely when or where the discrepancy occurred, only that the information could not be reconciled. As an example, if an audit discloses that the customs value of imported goods was 1,500 c.u. (currency unit), and the declared value 1,000 c.u., the importer owes duty to Customs or an additional 500 c.u., which Customs may legally collect. Similarly, if the Customs value was 1,000 c.u., and the declared value was 1,500 c.u., Customs owes the importer a refund on 500 c.u. of declared value.

### **Generally Accepted Accounting Principles**

Generally Accepted Accounting Principles refers to the recognized consensus or substantial authoritative support within a country at a particular time as to (1) which economic resources and obligations should be recorded as assets and liabilities, (2) which changes in assets and liabilities should be recorded, (3) how the assets and liabilities and their changes should be measured, (4) what information should be disclosed, and (5) which financial statements should be prepared.

The standards may be broad guidelines of general application as well as detailed practices and procedures. The GAAP is usually formulated and approved by independent *boards* or commissions; not by governments, but legislatures and governments may require compliance with GAAP by certain entities and in certain situations. *Each* nation usually has its own GAAP, but they are often very similar to one another because (1) business practices between nations are very similar and (2) there is a *body of* International Accounting Standards which influences, although it does not dictate, the GAAP of individual nations.

The GAAP are important to provide transparent records that will assist investors in calculating the risk of investing in an enterprise, and assist banks in deciding whether to provide a loan to an enterprise. They also assist the enterprise to determine whether it has achieved its profit goals.

The GAAP also provide standards and practices against which independent auditors can evaluate the maintenance of books and records, whether for investment, banking, tax, customs, or other purposes. Therefore, the GAAP serves as a basis for the conduct of such audits by Customs authorities.

### **Recruitment and Training**

In most countries, auditing is a profession, with a professional association that conducts examinations confers credentials, and maintains professional standards.

Most auditors who conduct customs post audits are recruited from other government ministries, from private firms or directly as entry-level personnel from universities. Many of them already have the necessary education and professional credentials. However, they may have no particular knowledge of customs laws, import transactions, the Customs operational environment, or the specific goal of customs audits. Customs authorities may need to conduct training to familiarize audit personnel with Customs laws and procedures.

### **Planning Audits**

Customs authorities usually maintain a listing or record of all major importers for planning purposes. The record may include basic business and corporate information such as its charter, officers, and business address; past audit reports; any criminal investigation reports; and any other information that would be relevant to the risk represented by the importer or goods and the need for Customs to

perform a post audit. Some audit organizations also conduct routine interviews with importers to assess their overall compliance with basic accounting standards as an additional risk factor to be considered.

From this record, identified Customs priorities, and information provided by officers, the Audit Unit may prepare an annual or periodic schedule of audits to be performed. The audit plan may be updated as needed to address changes in audit priorities stemming from new information. The audit plan usually indicates the objectives (e.g. to verify the valuation or quantity of goods imported) and the scope (e.g. the number or dates of importation of transactions to be verified) of the audit.

## **Audit Process**

Prior to initiating the audit, the auditor interviews other customs officers that may have recent information about the importer. The auditor also sends an official letter to the importer announcing the planned audit, when the auditors will arrive at the importer's premises, and the scope and objectives of the audit. Audits are not performed without advance notice to the importer. Post-clearance audit places great emphasis on the professionalism in the conduct of a review and examination of the audit candidate's books and records. From pre-audit planning to completion, it is essential to maintain communications and co-ordination with the audit candidate and with other interest parties in Customs. A report should be produced to ensure that all findings and other relevant issues are fully shared and discussed.

*To further define the Customs post-audit process, the following 7 points were taken directly from Kyoto Convention Annex Chapter 6 Part 7.2.15*

1. **Pre-audit survey:** the first step in the audit process is to assess and evaluate the strength and weaknesses within the commercial system of the audit candidate. The survey can include gathering data regarding: corporate organization and structure, commodity information, methods of payments, value of commodities, costs associated with commodities, detailed product-cost information/submissions for analysis, related-party transactions and record-keeping systems. This type of information is commercially sensitive and should be treated as confidential by Customs.
2. **Initial importer contact:** before carrying out a routine compliance audit, Customs should contact the audit candidate to request detailed information on the types of records and documentation needed. These may include: commercial invoices, shipping records, purchase orders, delivery notes, accounts, records, contracts, royalty and marketing agreements, inventory records, journals ledgers, chart of accounts, business correspondence, and records of payments.
3. **Initial Audit conference:** The initial meeting should be attended by the auditor and the audit team, representatives of other Customs areas as needed, and representatives of the auditee (accountants, legal staff, assigned customs liaison person). The auditor will discuss the scope and objectives of the audit.
4. **Audit Questionnaire:** Companies may be asked to fill out a questionnaire to obtain information about their structure, related party transactions, commodities, methods of payment, valuation, manufacturing costs, sourcing and supply. In related party transactions, the foreign parent company may also be asked to complete a questionnaire focusing on information regarding the relationship between the auditee and its parent company. Completion of such a questionnaire by the foreign parent would be voluntary.

5. **Internal corporate review:** Customs should encourage the audit candidate to carry out a preliminary self-evaluation, review and analysis of its operation in relation to the audit.
6. **Audit co-ordination:** The auditee should be kept fully informed of any potential findings unless there is reason to suspect fraud. In cases of suspected fraud, the team will need to co-ordinate with the appropriate enforcement unit. Customs can make any information available to other tax/revenue agencies in accordance with national laws, and confidentiality.
7. **Exit Conference:** A formal meeting should be held with the auditee to present the findings and provide an opportunity for the auditee to give any explanations needed to assist in the preparation of the final report.

### **Conduct of Audits**

The audit generally begins with information contained in customs declarations, such as the invoice price; added costs such as freight, insurance, assists, etc.; and quantity of goods imported. Prices and costs are traced forward into payment and bank records to verify the amounts actually paid, and further into accounting records to verify that those amounts have actually been deducted from assets of the importer. They are also traced backwards through purchase records to see how the prices were determined and negotiated with sellers and obligated against the importer's assets as accounts payable. Special attention is paid to determine dutiable costs and charges not included in the invoice, such as payments made to third parties in connection with an importation.

Goods information is traced into merchandise accounting records to verify that quantities declared are actually recorded as receipts into inventory, and also to verify that the declared or invoiced description of the goods is the same as that of the goods actually imported and received by the importer. Special attention is paid to excess, short shipped, and damaged goods to verify that these exceptions from the declared quantities are also accurately recorded in inventory records, and determine whether these discrepancies occurred (1) before or after importation and (2) before or after receipt at the importer's premises.

If information disclosed during the audit indicates a need for further audit, the audit objectives or scope may be expanded. Any information indicating possible criminal activity is reported to Customs criminal investigators for their action. Any information concerning criminal activity is revealed to the importer only by criminal investigators, according to requirements of the law, not by the auditor.

All significant documents, audit work, and findings are recorded in audit working papers, which are prepared according to professional audit standards. These working papers serve the basis for a written report of the audit.

### **Conclusion and Follow-Up of Audit**

Upon conclusion of audit work, the auditor conducts a closeout interview in which the tentative audit findings are reported to the importer. The importer is given an opportunity to reconcile any accounts or information that the auditor could not reconcile, or to provide any information rebutting the tentative findings of the auditor. Information from the importer is considered in the final report of the audit.

After conclusion of the audit work, the auditor prepares a written report that is reviewed by Customs audit management. In some countries an independent peer review is conducted by other auditors who did not participate in the audit. These reviews usually are done on the basis of the audit working papers and conformance with professional audit standards. The final report of audit is issued to the importer under the signature or authority of Customs audit management, rather than that of the auditor who conducted the actual audit work.

If the audit reveals actual discrepancies in the value or quantity of goods, these findings are reported to Customs officials responsible for collecting or refunding duties and taxes or for issuing penalties, as prescribed by the law and regulations.

### **Development of a Risk Management Strategy\_**

The area of risk management has been expanded because of the interests expressed by managers and the Minister of Finance. Because of the interest, the scope has been expanded to cover all Customs functions not just the duty determination process. A great deal of the methodology discussed below is based on Kyoto Convention General Annex Guidelines, Chapter 6, Part 6.

Risk management has become an essential business process for both the public and private sector. Many Customs Services have undertaken some form of risk management because they have found it inefficient and non-productive to process each commercial transaction with the same level of scrutiny. There is also a business need to expedite the declaration and release process so that the goods will enter the commerce as quickly as possible. Most business communities have undertaken efforts together with Customs authorities to promote expedited release of their merchandise so that it can enter quickly into the production process. With expedited release procedures, the commercial sector does not need to keep a costly inventory at their premises. However, this type of business practice requires that the goods are processed and released from Customs on a timely and predictable schedule.

In many countries importers and industry sectors have worked with Customs to identify some sort of methodology that Customs can use to maintain a level of comfort on the compliance of the goods before them. The risk management process can promote expedited release of compliant goods.

There is always an element of risk in facilitating the movement of goods and persons. However the extent of the controls should be in proportion to the assessed level of risk. Customs administrations determine risk factors based on their national priorities and in-depth analysis of the trade data.

In managing risk a balance must be struck between costs and benefits. It is not cost effective both for Customs and the national economy to treat all risks equally. It is expensive for importers to have their goods detained or examined and this cost is always passed to the domestic consumer. This factor also impedes investment and economic opportunity. Importers require a great degree in predictability both in revenue to be paid and release times. It is the best method for pricing their goods or predicting production times. Even domestic producers import raw materials and capital goods. A good risk management system based on compliance data and close contact with importers makes good economic sense.

The risk management process requires that a risk context be established identifying national priorities, within those priorities there should be risk identification, a risk analysis and assessment, a methodology to address the risk and a method to monitor and review the whole process by periodically measuring compliance.

### **Establish the Customs Priorities**

There is a need to develop a strategic national plan that will address major issues such as valuation, classification, public health, social issues, and trade agreements. This is done by studying and analyzing national trade data. Who are the major importers and what do they import or export? Which importers are the major revenue producers, what is their compliance history, where do they import, and what are their business practices? Are there small importers that import goods that may be of national concern? How will the issues be addressed? Many Customs authorities have

developed a compliance measurement methodology to identify a baseline and work from that baseline to develop a plan to raise the level over a multi-year period with yearly goals. After a period of time those goals may need to be adjusted. It may be that they were unrealistic or that the plan to improve compliance was deficient and needs to be changed.

Operational plans should be developed as to how to attain specific goals. This part will require training both the workforce and the trade community. Those trade sectors that have been determined to need additional scrutiny will require additional resources. There will be a greater need to work with them to develop their level of knowledge of Customs laws. The workforce must be educated to understand that not all declarations require the same level of scrutiny. Small unique shipments that may never occur again should be processed as quickly as possible on the best available information and not take up the time and effort of the workforce which should concentrate on major importers and trade areas and their compliance level. This is a major culture change since small unique shipments always seem to be more time consuming than large repeat commercial shipments. But in most cases those shipments do not represent any recurring revenue loss risk or overall threat to the national economy. They are one-time occurrences. They should be treated as such.

Tactical plans are usually local plans to deal with certain aspects of the trade or specific importers that may require greater resources. The local workforce is most familiar with the specific portion of the trade that files declarations through their port and should address any problems or issues directly with the trade. They can develop their own plan within the scope of the national plan to address compliance at their port. They can determine which movements require greater controls.

### **Addressing Risk through Profiling, Selectivity and Targeting**

Risk profiling is the means by which Customs puts risk management into practice. It replaces general examination of documents and goods with a planned and targeted working method, making maximum use of Customs expertise and resources. Once risk areas are defined such as specific trade sectors, or traders, or trade agreements, those areas can be selected through selective processing based on the risk indicator to determine the level of compliance. Previous history can provide a risk profile that can be updated as needed and an action plan undertaken to minimize the risk. This can be maintained in either a paper or electronic mode. This document will also provide a record and allow Customs officers to evaluate the effectiveness of the risk profile and the remedial action. The nature of risk is dynamic. It changes as the nature of the business changes. Regular review procedures should be in place and feedback received from the workforce as to the effectiveness of the profile/criteria record.

### **Compliance Measurement**

Many Customs administrations have instituted a baseline measurement system to establish the level of compliance throughout the trade. Compliance measurement is a phrase understood to mean that statistically valid random sampling techniques are used to determine the degree to which traders, carriers, imported goods, etc conform to Customs rules and procedures. When properly designed compliance measurement provides objective and statistically valid results. Compliance measurement can be used as a diagnostic tool to identify areas of non-compliance within the trade. Compliance measurement should be used together with risk assessment, profiling and targeting procedures. Used correctly compliance measurement and targeting can provide the necessary balance to focus resources effectively in areas of concern to Customs. Initial results of compliance measurement can provide important information to enhance the risk assessment process. It can also provide Customs a basis to assess its own performance for revenue protection and to help develop and improve efficiency and effectiveness to improve compliance. It can also help Customs determine trade trends and need for resources.

In countries where examination occurs on a selective basis, the methodology used is to analyze the total number of tariff lines for each 4 or 6 digit HS and to identify a statistically accurate sampling and place a random statistical indicator against each 4 or 6 digit line. When the line is generated for review - the whole process should be reviewed for accuracy and information as to whether or not any violations occurred and that information input into the system. At the end of a three/six/nine/twelve month period this information can be analyzed for a baseline measure of overall compliance. Once the data is available it can be sorted and analyzed to develop an overall compliance improvement plan for those areas that are deficient. However, since the current environment requires examination and review of all documents, there is only a need to input the results of those physical examinations and document review into some sort of database and assess those results after a period of 3 to 6 months to develop a strategy to promote compliance.

The same type of measures can be used in trade sectors, for carriers, for warehouses, free zones, and any other portion of the trade.

### Priority Focus

Using the risk management program, Customs should identify the priority areas to focus their resource. One approach is to consider that in some countries 10% of the traders account for over 80% of the imports and exports. By focusing on the top 5-10% of these highest volume traders or commodities, Customs can ensure that those entities which have the most significant impact on the national economy are being reviewed most effectively and that their level of compliance does not fall below the determined acceptable level.

The areas of compliance measurement may include:

Documentary issues-such as proper classification and valuation by traders

Procedural issues-such as the goods declaration process, transit, free zone Revenue

Issues-timely and accurate payments, securities

Transport Issues-accurate quantity reporting, accurate description of goods on transport

documents, accurate container quantities and identification numbers Specific Concerns-

compliance by tariff number or range of tariff numbers, public health and safety issues,

intellectual property rights, compliance with trade agreements, country of origin, high revenue

commodities and selected traders.

### The Measurement Process

Customs gathers data from many sources both internal and external through manual and automated means. With the data (import and export records) and systemic analysis of large traders or commodities Customs can make reasonable, informed conclusions about the compliance rates of many entities. The compliance rates can be determined for each step of the transaction process for imports-from the manifest to the goods declaration to the collections of duties and taxes. The automated system can be developed to support compliance review through a scientific approach for accurate data collection, analysis and projections. Compliance rates can also be effectively measured without automation.

Some of the processes identified for compliance verification would be

Goods declaration process

Trader compliance

Transit compliance

Free zone or warehouse compliance

Manifest and transport document compliance

## Transporter compliance

### Factors to be considered for goods declaration compliance

Evidence of documentation to support accurate goods declaration Do the quantities declared match what is contained

Does the declared country of origin match the markings and documents Does the declared description of the goods match the actual goods

### For Importers found to have a compliance rate of less than the tolerance level

Inform the importer and discuss the problem and determine remedial action

Establish targets/criteria for the identified areas of non-compliance

Conduct subsequent measurements to ensure that the importer has corrected the problem

Conduct more review and examinations

Issues fines or penalties if appropriate

## Use of Compliance Measurement Results within Customs Control

The use of statistically accurate compliance measurement results can be used in various ways:

To define any revenue gap-what revenue we collected-what we should have collected

Prevent widespread commercial fraud-determine risk in all areas

Assess performance of major key industries

Assess performance by major importers and exporters

Increase commercial compliance

Accurately measure international trade

The results of these measurements can help direct resources effectively. In determining compliance rates for individual importers, those found to have high compliance rates may have their goods examined less frequently and have predictable release times. Those with low compliance rates will have their goods examined more often with documented reasons.

Compliance review for commodities traders, and industries provide information to promote selective criteria used to target high-risk transactions as well as the overall effectiveness of an administrations' risk management program. In addition they contribute significantly toward determining trends and issues relating to specific industry sectors. The result should be that focused, up to the minute analytical information is available to assist Customs officers in their daily activities and that Customs understands the trade environment in which it works.

## **Development of a Trade Relations Office\_**

The implementation of the Value Agreement is a major change for both Customs and the trade. It necessitates a partnership between Customs and the Trade. One option is to develop a group responsible for educating and interfacing with the trade on a broad level particularly during the transitional period, which could take several years. A Trade Relations office would be responsible for providing information to the trade, clearing up misunderstandings between Customs officers and trade participants, encouraging the development of productive dialogues between Customs officers and trade participants and acting as a neutral party to the process.

Such an office is not to be considered as a problem resolution desk for trade complaints about a specific problem but rather an office that could promote uniformity, transparency, and predictability to the trade. It would be the function of this office to promote trade participation with Customs on new initiatives to reform or correct inefficient procedures, to help develop productive dialogues between the trade and Customs, to educate the trade on Customs processes, and to help promote a professional relationship between Customs and the trade.

Several countries have established an office of Trade Ombudsman who is viewed as a neutral party and an advocate. The chief of such an office is often selected on the basis of a reputation of neutrality and advocacy. Such a person could come from the trade environment or from the judicial sector. This type of office could prove invaluable during a difficult transitional period when major new procedures are being implemented and both parties are uncertain of the obligations and requirements of the new process. If such an option is considered there could be satellite locations in each major port working with the main office. Customs officers could rotate in and out of such an office as staff members and gain additional experience in dealing with the trade community. This type of arrangement could further promote the transparency indicated in Article 12 of the Agreement.

There are many methodologies to educate the trade community on complex or new issues. One is to develop a strategy of providing informational material to the trade sector. There are over 70 such publications available to the trade community. They are available for downloading from the US Customs web site at [www.customs.gov](http://www.customs.gov). Other Customs services also have similar information on their web sites.

### **Development of a Problem Resolution or Help Group**

As a separate option to consider is a problem resolution, inquiry, or help group to work with importers particularly small importers who do not have the same access to Customs officials as major corporations. A import and export guide can be developed to describe all the steps of the process, the forms needed, the information or other government agency releases required, how to initiate the process and what is required of the trader. Any minor problems or complaints can be sent to such a group to research and address. This could help promote a more uniform and efficient process and become a resource for importers to use for help. There does not appear to be such a process in place.

This type of group has proved to be very helpful during major changes or transitions from one type of environment to another. It precludes the need for constant access to the workforce and promotes uniformity among importers. It is also beneficial from a public relations point of view and promotes the spirit of Article 12 of the Agreement. This type of group can function as part of the Trade Relations office if one was established or as a separate group. Based on conversations with importers and with many Customs officers it appears this would be a beneficial development.

### **DEVELOPMENT OF THE APPEALS PROCESS-ARTICLE 11**

Ministerial Decree 787/2000 provides executive guidelines for appealing Customs Decisions to arbitration boards that shall be presided by a judicial authority and allow the participation of the importer or his representative. This is a change from the old procedures. What is not included in this procedure is the ability to appeal a Customs decision after the goods are released if some omission or mistake in fact on the part of Customs is detected or perceived after release. Article 2 of the Decree states that arbitration shall not be permitted except concerning goods within Customs custody. However, once the application is filed and accepted and the goods sampled or reviewed the importer can move them under guarantee.

Many countries allow a period as long or possibly longer than 90 days after final action by Customs to enter an appeal to a Customs decision. This allows the importer to review the decision, acquire additional information possibly from foreign sources, review previous Customs decisions on similar cases that are normally available to the public for review, and provide the necessary framework for the appeal process. There is usually a method whereby an importer can file directly with a court to have his case heard and forego the expense of an administrative process should he so desire. This may be true in cases where the importer feels he has a better chance if he takes his case directly to court rather than incur the costs and time factors involved in the administrative process.

Also the Decree speaks only to goods and not to any other process that may be subject to a dispute with Customs. In most countries the appeal process is generic and allows any party affected by a Customs decision or omission to file an appeal. This could include importers, exporters, brokers, agents, and the traveling public.

It may be worthwhile to review the legislation of other Customs services and some of the standards contained in the Kyoto Guidelines and decide whether or not there need to be changes in legislation. Also this seems like an excellent matter to discuss with the trade and a multi-disciplined group. No matter what the final decision, some sort of plain language publication initiated by Customs describing step-by-step procedures may prove to be useful. Additionally, in the spirit of transparency the background information on the issue and the rationale for the decision and the final outcome could be published.

If a decision was made to support Customs not on the legal aspects of the issue but because the importer could not substantiate the facts than this would differ from a decision to support the Customs decision because of the merits of case and may prove to be useful information. If such decisions were published then interested parties could learn about the specific determination concerning classification, origin, or value decisions as well as the necessity of providing substantiating information to the appeal process. This not only promotes transparency but also leads to a valuable education process for both the trade community and other interested Customs officers.

### **Conclusions on Interim Findings and Solutions**

The suggestions or considerations for creating an infrastructure for the implementation of the Valuation Agreement are based on the suggestions and building blocks promoted by the WCO. This methodology has proved to be an effective in many Customs Services and many of the above procedures have become international standards. It is understood that it may take several years to fully implement many of these changes. It may also require outside assistance and funding in developing expertise, providing materials, tools, computer hardware and software, a risk management process and strategy, post audit capabilities, as well as legal and trade interface initiatives. The US Customs Service and other international entities have provided overviews and training on the new approaches and techniques. Although the overviews did provide information and training to Customs officers, there is still a need for additional assistance in developing and implementing some of these procedural changes.

It may be useful for working level personnel to visit other countries that are in the process of making these changes. One neighbor, the Kingdom of Jordan , implemented the Agreement in April 2000 and has initiated many changes. They are currently using criteria based selectivity and only physically examine 30 to 50% of their shipments. They have created a risk management group and planning to deploy a post audit group. Their process is in the formative stage, but there has been a beginning and a new philosophy evolving promoted by the government's desire to enter the world of e-commerce, e-government, and e-customs. There are other customs services in the region in various stages of change and their processes could be reviewed to see if they would be applicable to Egypt 's Customs environment. There could also be an exchange of materials, information, and regulations for review and possible adoption. This too promotes efficiency since if a neighbor already implemented or formulated a process or regulation, why not consider it, alter it for your use, and incorporate it.

The first step in the process would be to determine a plan of action and review the suggestions for possible incorporation into that plan. The development of resources and materials and expertise is a long-term process. It may be useful to consider taking a specific group dedicated to an industry sector and starting this process with that group. Once the process is developed and proves useful, it can be deployed to other groups.

The trade interface process can also be developed along the same lines. New procedures and regulations can be published in booklets explaining them in plain language. The attached US Customs trade compliance publications can be used for guidance. Other countries have used them and copied many of them and distributed them to the trade. The Republic of Uganda has worked very effectively in this area and has published even within a small budget many publications and provided them to the trade. Uganda Revenue Authority/Customs has initiated trade outreach, is a vocal member of the WCO, and has adopted manual selectivity, risk management, and post audit. Some of these

are only nascent programs, but there is a beginning with little if any outside assistance.

It is not the intent to compare one Customs Service with another, but only to indicate that many developing countries that are also very dependent on Customs revenue collections have initiated some of these procedures to promote efficiencies, modernize their Customs process, and achieve compliance with Article VII of GATT/ WTO Customs Value Agreement.

### **Recommended Action for Initial Phase of Implementation of the Agreement**

After almost one month of processing under the Valuation Agreement, there appears to be a great deal of confusion and apprehension on the part of the trade community. Those major importers who have the resources and knowledge demand their rights under the provisions of the Agreement, but most are either ignorant about the Agreement, need their goods processed quickly, or do not wish to earn the displeasure of the Authorities and merely go along with whatever is asked of them and appear to pay duty on something other than a price paid or payable.

Also many of the questions asked by senior level Customs valuation personnel identify a need for additional training and a greater understanding of the principles of the Agreement. Thus, the confusion of the trade is understandable. Customs has not provided any information to them about new procedures or new forms or made any attempt to provide written instructions on what is expected. Since this issue was a major portion of the request for the extension to implement the Agreement, it is troubling.

The Agreement is intended to speed processing, but Customs appears to have taken the view that verification of documents is necessary for almost every shipment and the process of cargo release is taking longer. Customs also requires a new form from the importer for which they have provided no instructions on how to fill it out. Customs also seems to require written contracts that normally do not exist other than for long term commitments. It does not appear that Customs is working within the spirit of the Agreement or possibly not even within the principals. The current internal guidelines and the implementing decree both contain language that appears inconsistent with the Agreement.

During a previous review in March 2000 about Customs ability to implement the Valuation Agreement, it was determined that the need for an extension was appropriate. Certain recommendations were included in that study that addressed the need to educate the trade community, reorient the internal structure of the Valuation directorate, provide material and guidelines to the trade, and train officers in the Agreement. It was also envisioned that this transition would begin prior to the actual implementation date. Few if any of the recommendations were addressed or implemented. In fact it may be that the recommendations were never reviewed.

It is recommended that as quickly as possible:

1. Customs identify and supply WCO materials both the English/French version and a translated Arabic version to all officers involved in the valuation process. The materials should include the WCO Valuation Control Handbook (Introduction, Parts I-IV, and Glossary), WCO Compendium of Valuation Decisions, WCO Commercial Fraud Action Plan and any other material that the WCO recommends. This material is available to all WCO members.
2. Immediately begin a dialogue with the Trade Community and start a discussion of valuation problems, and how to address them. Provide the trade community with an education process. Discuss what Customs expects from them and why it is expected under the new procedures. Provide all necessary materials and guidelines about any new forms or expectations for documentary evidence. Start a discussion about need for procedural changes. Importers and exporters need to be a part of the process to effectively make changes both legislative and procedural. Pass all legislative and procedural changes through trade associations for comment. Discuss the need for training of Customs officers by the trade community on industry sectors, product manufacturing, negotiations, financing, and business practices. In a true open and transparent environment, Customs and the trade work together to promote efficient processes.
3. Review the Kyoto Guidelines specifically the guidelines incorporated in general

Annex Guidelines for Customs Control (Chapter 6), Relationship Between Customs and Third Parties (Chapter 8), Information, Decisions and Rulings Supplied by Customs (Chapter 9), Appeals in Customs Matters (Chapter 10), and Clearance and Other Customs Formalities (Chapter 3). These will be useful in setting up the procedures for Post Audit, Risk Management, Rulings and the Trade Interface Process. The Kyoto Convention guidelines on Customs Procedures are available for download from the WCO web site and are considered to be the international standards for Customs procedures.

4. Consider sending a working level group to the Customs Department of the Kingdom of Jordan to review their experience and procedures for implementing the Valuation Agreement. Jordan Customs has initiated a process of risk management, profiling and selective release of [cargo](#). at some sites as much as 50% of the cargo is released without additional review or physical inspection. It would be useful to exchange information, ideas, and materials on how to affect cargo release without review or physical inspection based on criteria and risk assessment.
5. Based on the above create a short-term action plan to develop materials, and resources for Customs officers, the trade community and the public sector.

It is anticipated that if the above steps are initiated that it will provide for a smoother implementation process and a better working relationship between Customs and the trade community. There is need for a great deal of work in building such a relationship. But, without such a relationship, the success of implementing the Agreement within a reasonable period of time is questionable.

## **Chapter 3**

### **Training, A Solution**

Harry M. Allison

#### **Intoduction**

During the reading of this entire document you will have heard the term "training" many times. The reason is that every change has a training impact. I think it is an important thing for all managers and executive to know, so that they will think of those training impacts as they plan a change. Too often, training is an afterthought, not budgeted for in the original proposal.

The development of training as it applies to the field of Customs, has been an attempt to fill in a gap that exists between academic education and practical application. The processes and procedures used in Customs are very specific, yet are designed to be used by persons with an understanding of their intent and having sound judgment in their application. This requires knowledge of the theoretical concept of the pattern of operations in Customs, the laws and regulations governing Customs operations, and a familiarization with the guidance authorities available to the officer. It also requires

that the officer function in a practical environment, applying that knowledge in the form of skill and judgment to a real situation.

Prior to the development of Customs Training Programs, the officer who was new to the position had to attempt to learn the job through practice, asking questions, and close supervision. After several years in the position, the officer had learned what to do in specific situations, but not why, nor, how to apply judgment to an unusual event.

Basic, or formation, training was designed to provide the employee with the basic concepts and knowledge needed to perform the function. In those designs, several of the questions that needed to be answered were; how long do we keep the employee off the job in training, and how much academics can we expect the employee to retain if they are not put into practice within a reasonable time frame? Both concerns are legitimate to training. First, because the people hired to do the job are not extras, they were hired because they were needed to accomplish the mission. Second, because of a known training principal. That is, if training is not put into practice within a reasonable time frame, it is forgotten.

Two additional training concepts become significant in the basic or formation training. First is the concept proven by experience that there is a specific, major difference between Adult Occupational Training and Education. While there are many differences, the one we are concerned here with is the fact that training relies on being able to relate a skill or concept to an educational skill already learned, i.e. math, or a previous life experience, i.e. personal communications. The question is, did the new employee have enough experience to relate to the skills to be learned? In Colombia it was decided to approach it as an education program through a two-year academic program. In Russia they use a four-year degree program. In the USA , a number of approaches were tried to see which worked best. One was to have the employee complete a correspondence course prior to attending training. This did not turn out to not be practical, nor was any advantage seen to other methodologies. Another program sought to have the employee attend training after six months on the job. This was found to be good for the training relationship to experience, but it was found to be not a good solution because of the waste of manpower by having unskilled personnel. Also, because of the development of some very bad work habits by trying to do things they were not prepared for. By default, the basic or formation training of employees as they come into the workforce or very soon thereafter, became the standard that has worked very successfully. The personnel designing courses being very aware of the training concepts discussed, and practicing them in all courses derived that success. Basic courses are basic. They concern items of fundamental skill development, in areas that will receive the reinforcement of practical usage on the job. They leave advanced concepts to courses designed for introduction later in the career life of the employee. Short courses of advance concepts and specific advanced processes are given after the employee has been selected for a specific detail or job that calls for those skills. Examples of these are intensified enforcement projects, contraband enforcement teams, senior inspector school, and instructor training.

Therein lies the gap. There is the need that training must address; the gap between training and full, practical proficiency. How quickly can the supervisor rely on the employee to be able to function on the job with minimal direct supervision?

Training impacts occur whenever a new concept, or a new process is introduced. Training impacts occur when new employees are hired, need to be refreshed or updated, are moved to a different position, grow to an advanced level, or are promoted. Because in each of the scenarios just described, an employee has to learn new skill in job performance.

Many Customs Services worldwide have found that functional training can best be effective if it is related to the career progression of the employee. It can be spaced to be received at times when an employee can relate to it, and when the employee will most need it. That way course can be shortened and the employee returns to training at various intervals for more advanced and refresher training.

In this regard another concept to be considered is on-the-job training. It is used to supplement basic training. It helps the employee learn to do the job properly while he/she gains experience. The best

on-the-job training programs have been shown to be those that were the most simple. It need not be a formal program. A mentor is assigned to work with the new employee. The mentor is selected from available experienced personnel on site. The mentor's function is to help the trainee understand the functions of the job, coach the employee into the practical aspects of the position, answer questions, and generally help to teach the job to the trainee. This is a hands on, "show me" situation that accelerates the employees learning the job.

The most successful mentors have been shown to follow this format of instruction:

- Explanation of the job being performed, "This is what we are doing..."
- Demonstration of the technique, "Watch me...."
- Rationale, "This is why we do it this way...."
- Application, "You try it..."
- Correct, "No, this way..."
- Clarify, "in answer to your question..."
- Repetition, "Try it again..."
- Reinforcement, " Now you're getting it..."
- Praise, "You are doing fine, I think you have it"
- Practice, "Fine, now do a few alone"
- Withdrawal, "You can do it alone now, call me if you have a problem"
- Certification, "I'm satisfied that you can perform this function"

When we assessed training we asked this question: Is it able to produce the training needed, in the quantity and quality needed as the Customs Authority moves into a new era?

The training Directorate and the Customs Institutes have done a truly marvelous job in training the numbers of people they have in preparation for GATT value implementation. I can think of no criticism connected to them in our assessment.

We looked at training from the criteria of:

- Trainees (Number per class, pre-requisites, testing, career field, etc.)
- Training Environment (facilities, classrooms, trainee comfort, and space)
- Training Materials (Manuals, Books, Handouts, etc.)
- 
- Instructor Development (Qualification, Selection, Experience, Training as an Instructor)
- Lesson Plans (an instructor's guide to presentations)

- Instructor Methodology (how is it being presented)
- Task Relationship (material presented to actual job performance)
- Training Aids Availability (Projectors, Graphics, Computers, Chalk Boards, Easels, etc.)
- Practical Exercises and Class Interactions (Relationship to material)
- Modular Interface of Courses (Like or related material presented in succession)
- Course Development (Order of presentations, updating, continuity, coverage of subject matter, completeness, length, etc.)
- Training Needs (Number/type of courses to be run during a given year, for X number of trainees)

In our assessment of the training needs that will face the organization during the next three year period, if full implementation of recommended changes are approved, the training workload of the Institutes will at least triple. While the Institute management and staff are doing a very good job, we feel that this may be an area where assistance may be meaningful and of value.

Every one of the criteria listed above could be enhanced by the use of Adult Occupational Training Programs in place of current Academic (Educational) Courses. This means designing courses around the position function. Each task performed on the job becomes a training subject, prioritized by the result of negative performance, the frequency of use, the guidance available to the employee, and difficulty. For example, for an Inspector in a passenger baggage situation would need to know:

- How to speak, read, and write (met by pre-requisite education requirement)
- Basic Mathematics (met by pre-requisite requirement)
- Ability to understand basic guidelines and to follow them (Pre-requisite, but tested during training in practical exercises).
- Customs and the Pattern of Customs Operations. . Customs Laws, Regulations and Policy.
- Carrier Operations.
- Passenger Manifests.
- Controlling Passenger flow to Customs.
- Aircraft visit to look for smuggling indicators.
- Internal Conspiracy with Airport Personnel.
- Passenger Declarations.\*
- Passenger Exemptions.\*
- Classification and Valuation of Goods.\*

- Collection of Duty/Taxes
- Interview Techniques.\*
- Observational Techniques.\*
- Search and Seizure.\*
- Penalties and Fines. Criminal Proceedings. Report writing.\*
- Testifying in Court Proceedings.

*\* Indicates a practical exercise is related to the subject.*

Each of these classes makes up a module, in this case, the Passenger Baggage Module for Inspector/Examiners. This may be one of several modules in a Formation/Basic course for Inspector/Examiners. Other modules in the same course may be Air Cargo, Seaport Operations, etc. Some subjects may be complex enough or relating to multiple modules to become a single module in themselves, for example, Law, or Classification and Valuation. Modules are joined to become courses. Individual courses become a Curriculum. The use of modules allows the training organization to oversee the presentation of the material. A senior course developer/instructor is assigned as module leader responsible for assuring that Instructors are using Approved Lesson Plans, that training aids and materials are available for the module, and that testing is accomplished. Tests are designed for each module at the time they are run, by use of a computer test bank. Final testing is done at the end of the course.

Courses are designed from the bottom up. First by determining what skills and knowledge are needed to perform a specific function. These are translated into training objectives. A block of time, or blocks of time is allocated to a particular lesson that is required to meet a training objective. In adult education, based on ideal attention span, that period is usually 50 minutes. Lessons are linked into modules by commonality of use or, by logical sequence. In a like method modules are linked together to become courses.

Instructors must also develop in the system. Some Universities are now offering Customs as a part of their Business Administration courses, but few offer more than one or two courses. Customs therefore remains a topic learned by experience. It follows that it must then be Customs personnel who teach Customs. A good Instructor must be first an experienced Customs Officer. Through the use of an Instructor Training course the candidate is taught the basic principals of instruction, is given the knowledge of the use of lesson plans, the use of training aids, and is asked to prepare and deliver a number of presentations of increasing duration. They are graded on their ability to follow instructions, delivery, and the accuracy of the information they present. On completion, they are qualify to become Instructor Trainees and assigned to a program.

Once in the system, they learn by experience under the supervision of a senior instructor and a Module leader. In their first year on-the-job training period they are gradually given increased independence and more responsibility for the lesson development/presentation, aids, and materials that are used in the programs. They will then move forward as Instructor, Course Developer/Instructor (Module Leader), and Senior Course Developer/Instructor (Course Leader).

It is recommended that all Instructors return to a field assignment for at least 30 days every two years. This can be as a vacation relief, or to temporarily fill a vacant position, or as an extra, for the purpose of keeping field acuity.

That is our recommendation, that the training system move from its present form to a system of Adult Occupational Training, as described above. We will go into more later as to the specific recommendations for assistance, which we hope would be attained soon, based on the impact of the implementation of the Articles of the GATT agreement.

An immediate recommendation based on the impact of GATT valuation would be the retraining of all current personnel (including Supervisors) dealing with the valuation of goods through a specialized refresher course of four to six weeks duration. Revision of the formation or basic course to 12 weeks duration. Specialized courses, particularly commodity seminars, expositions, and computer usage, would also be recommended. This is important because the level of knowledge required to make decisions under the Agreement is a quantum leap from previous systems. The trade must also be trained to understand what information Customs will be asking for, and how the record keeping requirements will change for them. For Customs to assist in this training will open a door to a good working relationship.

The new system for valuation calls for an understanding of a very specialized vocabulary used in international commerce. Customs Officers and the Trade must use that vocabulary correctly alike, so

that the verification of a declared value may take place when called for. Confusion in terminology can result in either not getting the information needed, or getting the wrong information. Training therefore must address that issue. For example it would not be unusual to see a Training Objective for a Valuation Module for an Import Specialist to list:

### **TRAINING OBJECTIVE 1 – Import Specialist Basic Training Course**

By the end of this course Trainees will be able to define, know the use of, and be able to discuss the terms and vocabulary used in Valuation. These are:

#### **ASSISTS**

apportionment of assists  
assist definition  
components which are destroyed, scrapped, or lost  
consumed in the production  
costs of acquiring assists  
depreciation of assists  
directly or indirectly  
drawback on assists  
engineering, development, artwork, design work . . . necessary for the production  
equipment  
free of charge or at a reduced cost  
inspection services  
management services, salaries  
materials, components, parts, and similar items incorporated in the imported  
merchandise  
offsetting overpayment of duties  
payment to seller  
proration of assists  
supplied by the buyer  
testing costs  
tools, dies, molds, and similar items used in the production  
transportation costs  
use in connection with the production or the sale for export  
value of assists, i.e., cost of acquisition or cost of production

#### **BUYING COMMISSIONS**

bona fide buying commissions  
commissions paid to agent for acquiring assists  
control over agent  
deducting buying commissions  
dutiable as part of the price actually paid or payable  
factors to consider  
identity of seller  
totality of circumstances

#### **CANCELLATION PAYMENTS**

contract termination fee  
goods not imported  
liquidated damages and/or penalties  
minimum quantity cancellation charges

#### **COMPUTED**

assists

cost of fabrication  
election by importer between computed and deductive value  
elements of computed value  
merchandise of the same class or kind  
profit and general expenses  
severance pay

### **CONDITIONS OR CONSIDERATION FOR WHICH A**

transaction value inapplicable

### **CONFIDENTIALITY**

### **CONSIGNMENTS**

transaction value inapplicable  
transaction value of identical or similar merchandise

### **COUNTERTRADE**

price actually paid or payable

### **CURRENCY CONVERSION**

computed value  
formulas used in determining the price actually paid or payable  
price actually paid or payable

### **DEDUCTIVE**

deduction for commissions  
deduction for usual profits and general expenses  
duties currently payable  
election by importer between deductive and computed value  
related party transactions  
resale in Egypt  
sales to unrelated persons  
similar merchandise  
superdeductive value  
transportation costs

### **DEFECTIVE MERCHANDISE**

allowance in price  
defective parts returned to Egypt  
defective merchandise imported  
in-transit damage to imported goods  
price renegotiation  
subsequently imported merchandise discounted  
warranty provisions

### **DIRECT COSTS OF PROCESSING**

direct costs of processing operations

## **DISCOUNTS**

early payment discount  
price actually paid or payable  
quantity discounts  
renegotiation of price

## **DUTIABLE**

### **DUTIES AND TAXES**

currently payable  
deduction from transaction value  
identified separately requirement  
offsetting overpayment of duties

### **FOREIGN TRADE ZONES**

assists  
design and development costs  
merchandise processing fee  
valuation

### **FORMULAS**

pre-determined formula agreed to between parties  
currency conversion  
price actually paid or payable  
provisional price  
sufficient information available to determine price actually paid or payable

### **GENERALLY ACCEPTED ACCOUNTING PRINCIPLES**

computed value  
interest expense  
rejection of accounting system  
repairs  
start-up costs  
zero-value assists

### **INDIRECT PAYMENTS**

advertising expenses  
compensation for assists as indirect payments  
part of the price actually paid or payable as an indirect payment  
reduction in purchase price for settlement of a debt

### **INSURANCE COSTS**

deduction for cost of insurance from C.I.F. price  
product liability insurance payments

### **INTEREST CHARGES**

treatment of interest charges  
clarification regarding treatment of interest

assists  
computed value  
financing arrangement  
separately identified from price

### **INVOICING REQUIREMENTS**

inconsistent documents presented at time of entry,  
separately identified from the price actually paid or payable

### **LEASE TRANSACTIONS**

elimination of transaction value  
reasonably adjusted transaction value

### **NOTICE**

### **PACKING COSTS**

addition to price actually paid or payable  
hang tags  
packed ready for shipment to Egypt , seaworthy condition  
Egyptian packing

### **POST-IMPORTATION CHARGES**

construction, erection, assembly, or maintenance charges subsequent to importation  
post-importation services  
post-importation transportation  
price actually paid or payable

### **PRICE ACTUALLY PAID OR PAYABLE**

additional payments made by the buyer to the seller; total payment  
advertising/marketing costs  
allowance in price actually paid or payable  
assembly of merchandise  
benefit of seller  
cancellation payments  
charges identified separately from the price actually paid or payable  
charges incident to the international shipment of the imported merchandise  
direct or indirect payments  
discounts  
inspection charges  
insufficient information to determine the price actually paid or payable  
interest charges  
invoice price  
payments to a third party  
payments unrelated to the imported merchandise  
post-importation services  
price renegotiation  
proceeds of a subsequent resale  
selling commissions  
testing costs  
time of payment  
user fee  
Egypt retail price

Egypt.-sourced merchandise  
warehousing charges

#### **PROCEEDS OF A SUBSEQUENT RESALE**

addition to the price actually paid or payable  
transaction value, sufficient information

#### **PROHIBITED APPRAISED**

two or more values

#### **QUOTA CHARGES**

free-quota price manipulations  
payments for quota made directly to the seller  
payments to unrelated third parties  
quota holder acting as "straw" seller

#### **REBATES SUBSEQUENT TO**

discounts  
formula used in determining transaction value  
free-quota price manipulations  
post-importation refund  
price actually paid or payable  
price renegotiations

#### **RELATED PARTY TRANSACTIONS**

control  
definition of related parties  
examination of the circumstances of the sale  
rejection of transaction value  
sales to unrelated buyers  
test values  
transfer prices  
REPAIRS  
price renegotiations  
repairs in Egypt  
warranty provisions  
value of repairs for merchandise damaged in-transit

#### **RESTRICTIONS ON THE USE OF RIGHT OF APPEAL**

#### **ROYALTY PAYMENTS AND LICENSE FEES**

direct costs of processing  
price actually paid or payable  
proceeds of a subsequent resale  
related to the imported merchandise and as a condition of the sale

#### **SALE FOR EXPORTATION**

assembly of merchandise

bona fide sale  
irrevocably destined for exportation to Egypt  
sale for export to Egypt distinguished from domestic sale  
sale which most directly causes the merchandise to be exported to

### **EGYPT**

terms of sale  
timing of sale  
transaction value eliminated due to lack of sale  
transaction value determination

### **SELLING COMMISSIONS**

addition to price actually paid or payable

### **SEQUENTIAL ORDER**

hierarchy of valuation methods

### **SOFTWARE**

### **TRANSACTION**

assists  
condition or consideration for which a value cannot be determined  
consignments  
countertrade  
hang tags/labels  
limitations on use of transaction value  
packing costs  
price actually paid or payable  
proceeds of a subsequent resale, i.e., appropriate adjustment  
related party transactions  
restrictions on disposition or use of imported merchandise  
royalty and license fees  
sale for exportation to Egypt  
selling commissions  
unrelated parties

### **TRANSACTION**

consignment transactions  
exported to Egypt at or about the same time  
identical or similar merchandise  
related parties  
sufficient information  
transaction value readily available  
two or more values

### **TRANSPARENCY**

### **TRANSPORTATION COSTS**

deductive value  
estimated freight costs versus actual foreign-inland freight charges  
freight and related charges incurred in transporting assists  
international freight deduction  
post-importation transportation  
vessel loading charges

### **USED MERCHANDISE**

depreciation allowed for used merchandise  
elimination of transaction value  
waste material

### **VALUE**

computed value  
defective merchandise  
foreign trade zone  
previously established transaction value, reasonably adjusted  
sequential order  
used merchandise  
waste material

I don't know about you, but after thirty years of Customs service, I would have a hard time defining each of those terms, explaining their use, and how they apply to Customs. Perhaps Madame Irina could, as she has been trained and experienced in the field, but most of us would require training to become conversant with these terms. This example shows I feel, the depth of training that is needed. Also don't forget that the "trade" will also have to become familiar with those terms and usage. They will look to Customs to define terms and usage officially.

If compliance units are accepted as a safeguard to new processes, then training again would have to be expanded to provide basic, advanced, and specialized courses in functional areas.

We must also recognize the training impact of the computerization of Customs, as processes are automated. Primary user training, program usage, data input and recall, system development, etc. All will have an impact on training.

An experienced International Customs Training Advisor could assist in the transition, and help in each of the criteria areas. Backed by a program budget for equipment, training aides, printing/publishing, and off-site in-country training costs; the results could begin to be felt in as little as three months, and continue to a point of Institute self sufficiency within a three year period. The CTA could begin the Instructor Development of Institute personnel, to prepare them to become self sufficient Course Developer/Instructors and begin to make the changes needed for modernization.

This would include:

- Improvement in standardization between the Institutes, by enhanced communications, standardization of materials used in courses, instructing from approved lesson plans, instructor development, and increased oversight by the Directorate.
- Improved performance of employees on the job by instructing in task related topics, career spacing levels of training to employee development, reducing employees time away from the job site for training in shorter courses, developing on-the-job training programs, and by providing user reference manuals to be kept by trainees.

- Improved performance by Instructors by train-the-trainer programs, instructor development career paths, better training aids, better course materials, and more hands on monitoring of classes.
- Improved maintenance of state of the art training standards by open communications with WCO, other Customs Trainers Internationally, performance of an annual training needs survey, input to management of training impacts at the planning stage, and access to Training Tapes and Materials world wide.
- Provide a platform for cross communication training/discussion with the trade community and with specific industry interests.(Trade seminars/expositions/how to courses).
- Develop a training library of materials and resources for use nation wide.
- Performing an annual training needs assessment of the entire Customs Authority.

Based on our assessment, Egyptian Customs has the potential to become totally self sufficient in the training field in approximately three years with international assistance. That growth could place the Egyptian Customs in the vanguard of training in Mid-East Nations and well respected by WCO. At that point Egypt might well be called upon to provide training assistance to other, less developed nations.

At the request of the Minister of Finance, we will also offer recommendations for several things that can be done immediately in Customs Training that will assist in the reduction of constraints to implementation of GATT valuation. The recommendations are based on the fact that GATT valuation is a serious change in the way business is done for Customs and requires in depth training.

- Our company is in the process of obtaining a copy of the WCO/CCC Customs Valuation Control Handbook in Arabic. It is recommended that this handbook be re-printed in quantity, and distributed to all employees concerned in the valuation of merchandise.
- A class be convened at the Customs Institute in Alexandria for 30 selected supervisors of valuation units nationwide. Mahmoud M. Abou Alla (X-ray unit) should instruct this class, or another person well qualified in GATT valuation, using the handbook mentioned above as a training manual/lesson plan. This course should run for 2 weeks, five days a week, 4 training hours a day. After the first class graduates, additional classes should be taught by attendees of the first class, in their respective area institute. Again the classes should not exceed 30 people, and the handbook should be the manual. Classes should continue until training of all employees involved in the valuation of importations is complete.
- Trainees of the classes above, upon their return to the work site, should become mentors for untrained, or inexperienced personnel.

#### **A Recommended Short Course in GATT Valuation (30 Training Blocks)**

## **Principles of Customs Valuation**

### **Introduction: Customs Valuation**

- Training Objective: By the end of this Introduction, trainees will have an understanding of the differences in valuation methods, the reason for new systems, and an overview of the change in process.
  
- Time: 2 training blocks (50 minutes each)
- Method: Presentation

### **Lesson 1: *Order of Application of the Valuation Method***

- Training Objective: At the end of this lesson a trainee will be able to:
  - Define the term “price paid or payable”
  - Know how to determine the price paid or payable
  - Identify the situations in which there is no price paid or payable
  
- Authority: The GATT Agreement and the Valuation Control Handbook
- Time: 2 Training Blocks (50 min. each)
- Handouts: Copies of the Authorities
- Method: Discussion from Outline
- Training Aids: Chalk Board, overhead projector

### **Lesson 2: *Requirements for the Application of Article 1***

- Training Objective: By the end of this lesson, trainees will know and be able to:
  - Determine when to use and when not to use transactional value.
  - Understand restrictions on disposition or use that do not preclude the use of transactional value.
  - Enumerate the conditions or considerations associated with the sale or price of imported goods that preclude the use of transactional value.
  - Discuss those situations where the proceeds of resale, disposal, or use of goods accrue back to the seller.
  
- Authority: The GATT Agreement and the Valuation Control Handbook
- Time: 1 Training Block (50 minutes)
- Handouts: Previously given out
- Method: Discussion
- Training Aids: Chalk Board

### **Practical Exercise for Lessons One and Two:**

- Training Objective: This P.E. will allow trainees to:
  - Demonstrate an understanding of the material presented
  - Allow understanding to be extended to actual or simulated cases
  - Participate in group discussion of problems presented
  - Apply procedures learned to practical situations.
  
- Authority: As previously stated
- Time: 1 Training Block (50 minutes)

- Handouts: 3 scenarios which have questionable criteria
- Method: Instructor led consideration of each scenario, this trainees responding to each. Correction, reinforcement, and Application.
- Training Aids: Chalk Board and Overhead Projector

### **Lesson 3: *Commercial Documentation***

- Training Objective: After this lesson trainees will understand:
  - When documentation is required
  - What documentation is required
  - When to ask for documentation
  - When documentation is not required
- Authority: The GATT agreement, Customs Valuation Handbook, Customs Law
- Time: 1 Training Block (50 minutes)
- Handouts: Copies of the Law
- Method: Discussion
- Training Aids: Chalk Board, Overhead Projector

### **Lesson 4: *Adjustments to Value, Article 8***

- Training Objective: Trainees will learn to:
  - Recognize the allowable additions to transactional value
  - Understand the term “objective and quantifiable data”
  - Know the difference between adjustments and parts of the price actually paid or payable
  - Identify buying commissions
  - Answer questions regarding adjustments for commissions and packing
- Authority: The GATT Agreement, Customs Valuation Handbook
- Time: 1 training Block (50) minutes

- Handouts: Previously given
- Method: Discussion
- Training Aids: Chalk Board, Overhead Projector

#### **Practical Exercise for Lesson Four**

- Training Objective: Trainees will gain experience in:
  - Applying the rules of Article 8 to selected cases
  - Demonstrating their understanding of the material presented
  - Extending their knowledge through discussion
- Authority: Same as Lesson 4
- Time: 1 Training Block (50 minutes)
- Method: Application to practical case scenarios, discussion, reinforcement of T.O. of lesson 4
- Training Aids: Copies of scenarios, overhead projector

#### **Lesson 5: *Adjustments Under Article 8.1 (b)***

- Training Objective: The trainees will understand:
  - Those items which are assists
  - Those items that are not assists
  - Establish the value of an assist
  - Prorate an Assist
  - The difference between “research” and “development”
- Authority: The GATT agreement and the Customs Valuation handbook.
- Time: 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board

#### **Practical Exercise For Lesson Five 1 Training Block**

#### **Lesson 6: *Adjustments under Article 8.1 (c) and 8.1 (d)***

- Training Objective: Trainees will be able to:
  - Identify royalties and license fees
  - Determine the applicability to price paid or payable
  - Calculate adjustment in cases of proceeds accruing to the seller
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

#### **Practical Exercise for Lesson Six 1 Training Block**

## **Lesson 7: *Article 8.2***

- Training Objective: At the end of this period, trainees will be able to:
  - Differentiate between international and internal transport
  - Define the term “importation” under national legislation
  - Know the meaning of the most common INCOTERMS (c.i.f., f.o.b.,etc.)
  - Explain the scope of the term “insurance”
  - Understand the treatment of storage and related expense under Article 1
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

### **Practical Exercise for Lesson Seven 1 Training Block**

## **Lesson 8: *Related Persons***

- Training Objective: The trainee will be able to:
  - Know the criteria for determining a related party transaction
  - Understand the treatment of sole distributors or concessionaires
  - Know the difference of branches
  - Establish the acceptability of a price between related parties through the circumstances of the sale and the manner in which the price was arrived at
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

### **Practical Exercise for Lesson Eight 1 Training Block**

## **Lesson 9: *Test Values***

- Training Objective: The trainees will be able to:
  - List three test values provided for in Article 1.2 (b)
  - Apply test values to determine the acceptability of transactional value
  - Apply adjustments for commercial level and quantity
  - Define “closely approximates”
  - Understand the concept of time standard for test values
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

### **Practical Exercise for Lesson Nine 1 Training Block**

## **Lesson 10: *Identical and Similar Goods***

- Training Objective: The trainee will be able to:
  - Apply these alternative bases of appraisement
  - Understand the term “Identical”
  - Understand the term “Similar”
  - Know the order of priority when using these terms
  - Know the factors that prohibit merchandise being considered identical or similar
  
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

### **Practical Exercise for Lesson Ten 1 Training Block**

#### **Lesson 11: *Deductive Value (Part 1)***

- Training Objective: By the end of this lesson the trainee will be able to:
  - Know when deductive value applies
  - Establish the starting point for deductive value
  - Apply the principal of “greatest aggregate quantity” to facts
  
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

#### **Lesson 12: *Deductive Value (Part 2)***

- Training Objective: The trainee will be able to:
  - Define “same class or kind” and apply it to problem solving
  - Identify the proper deductions to be made under the basis of value
  - Apply deductive value to items further fabricated after importation
  
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

### **Practical Exercise for Lessons Eleven and Twelve 1 Training Block**

#### **Lesson 13: *Computed Value***

- Training Objective: The trainee will be able to:
  - Define and list the components of computed value
  - Itemize the costs included under materials and fabrication
  - Define profit and general expenses as they apply
  - Define the role of assists as they relate to computed value
  
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)

- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

### **Practical Exercise for Lesson Thirteen 1 Training Block**

#### **Lesson 14: *Fall-Back Method***

- Training Objective: By the end of this class the trainee will be able to:
  - Appraise merchandise when the five bases of value cannot be found
  - Make a reasonable adjustment in the method set forth
  - Identify and avoid prices and methods forbidden by the agreement as a basis of appraisal
- Authority: The GATT Agreement and the Customs Valuation handbook
- Time 1 Training Block (50 minutes)
- Method: Discussion
- Training Aids: Chalk Board and Overhead Projector

### **Practical Exercise for Lesson Fourteen 1 Training Block**

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# Chapter 4

## Compliance, A Key to Success

HARRY M. ALLISON

### Introduction

How do we assure that the revenue is protected if we start bypassing cargo? A question frequently asked in natic new to the GATT valuation system is; how can we assure that importers are not under valuating declarations value? The answer to both of these questions is Compliance. Compliance is a requirement to protect the reveni voluntary compliance is a goal towards which Customs must strive.

We will explore both. First lets talk about Voluntary Compliance.

### Compliance

Much of the underlying principal of this entire assessment final product has been Voluntary Compliance, a to much used in international customs. The reason for this is that most customs services are coming from confrontational system of forcing compliance through enforcement of laws, regulations, and processes designed control; the carrier, importation, and importer in the favor of revenue protection. While this concept is not inefficient system, it lends itself to being bypassed, negated, and used contrarily to customs interest. Mode systems use voluntary compliance as a more positive and more effective revenue protection.

To see the benefits of the system, consider the drawbacks of the "Brussels System", in the terms of today's mode capabilities. Brussels allowed for a market reference price, wholesale value, or Customs value based on mar reference.

This meant in practice that Customs could increase or decrease a value in accordance with their price reference I If the declared value was low, it was increased by Customs and frequently a penalty was applied for undervaluatii Therefore no attention was allowed to the ability of the importer to purchase at the lowest price possible, or tc, advantage of the numerous business practices that allow discount, favorable business relations, and purchase quantity. To avoid penalties, importers would frequently request sellers to give them a receipt at a higher value th the transaction, to avoid penalties.

Customs to attempt to verify through documentation would seek certified documents and invoice verification throu consular office. As the original document was frequently a designed agreement, the verifications were simply compounding of a falsification. Importers were only interested in getting their merchandise through Customs quickly and with as least problems as possible. The attitude that developed was "give them whatever they ask fo By nature the system was confrontational, with the trade feeling that Customs was arbitrary and capricious. Custo felt the trade was dishonest and prone to undervaluation. Both thought the other corrupt. A communications bars was an unavoidable result.

This was not only the case in Egypt, but common to many nations. The result was that the documentation present to Customs, in most cases had no relationship to real value or price. Customs reference lists, even those based market research, were obsolete in the best of cases.

The modern system of the use of harmonized classification and transactional value allows the importer to declare 1 value as the price paid or payable for the merchandise and lists normal business factors as additions or deductio This recognizes the trader's ability to conduct business in the international market place. It also asks Customs accept this value with recognition of factors that may affect that value. Customs uses the importer's own busine records as a verification, when needed. This is a much more accurate method of verification, with the result

establishing a true base for duty/tax application. This requires that Customs and the trade communicate, and as each other in the learning process. Customs must let the trade know what is required of them, and the trade must help Customs learn the trade practices involved in International Commerce.

The result is that importers tend to want to comply with the system, as the result of compliance is speed of release, and ease of declaration. This voluntary compliance is a Customs goal.

The success of voluntary compliance has been seen world wide in Customs. As voluntary compliance becomes a fact, the customs organization has the manpower to concentrate on the non-compliant population.

The principle of voluntary compliance is simple. It requires the development of systems and process that rewards compliance with the fast release of goods, with less need to use complex verification means. That is the incentive. You get your goods through Customs faster and with fewer problems. For most business users of customs import processes, that is a major incentive. But there must also be negative incentive. If you don't comply voluntarily, then the process is slower, requiring more documentation to verify declarations. To the importer this means loss of profit by increasing costs. As long as the process they are asked to comply with are reasonable, predictable, and flexible then common sense tells the importer that compliance is good business. WTO and WCO have both found that countries making voluntary compliance a goal, actual compliance can reach levels over 90% in a fairly short period.

From the point of view of the customs responsibility of revenue protection, the use of reasonable, predictable, a flexible process, and the lower examination percentage of imports, combined with the speed of the process, present the problem of the increased potential for fraud, false declarations, and undervaluations. This is also internationally recognized area of concern. The Kyoto Convention dedicated an entire chapter of the general annex (chapter 6,) to this problem.

In resolving this problem, which has been titled risk, it was seen that some sources existed that had traditional experience in the area of concern. Insurance companies, banks, and mortgage companies have been applying risk management factors to minimize potential losses for years. Compliance units are doing the same thing in a Customs environment, reducing the potential for lost revenue through risk management techniques.

It is recommended that all compliance units be under one Directorate, or Manager, to promote focus, information sharing, and coordination between units.

A well-run Compliance Unit can very effectively close the door to revenue loss, and provide a significant deterrent to violations. It falls well within the negative incentives category of compliance incentives.

To be effective, all negative incentives must be backed by significant penalties/fines for violations. It must be placed as a cost deterrent for persons even considering an attempt to violate Customs law. Violations should be clearly defined in the law and implementing decrees to include Filing False Documentation, False Declarations, Fraudulent Declarations, Fraud, Smuggling, and Conspiracy to Defraud.

Thus far we have been talking about Voluntary Compliance in the field of Commercial Importations, particularly a control to risks associated with transactional value. But, the concept has much wider application, particularly in the area of passenger baggage, and smuggling control of airports and seaports.

Automation lends itself well to compliance. A compliance database of historical and statistical information allows profiling and sampling for selectivity in a shorter time and more accurately. However, compliance and risk management can begin in a manual system and carried forward, expanding to full range when automation becomes a reality. It is a help to the development of the system to begin it as a manual process. Lessons learned in the formation of the system will make the finalized form more effective.

### **A Practical Example**

A new concept in Customs usually evolves to resolve a problem. In the U. S. it was the advent of the 747 airplane in 1970. When suddenly two or three 747's were arriving at close to the same time, each carrying over 400 passengers, baggage examination enclosures became overcrowded and people were literally fainting from overcrowded facilities. Fire Marshals ordered aircraft to keep passengers on board for up to an hour to avoid

overcrowding. The public outcry was immediate and loud. Customs had to do something. In Europe it started ec, as a way to increase tourism and decrease complaints.

Studies that were done by several nations found similar truths in their results. First, the duty/tax collected fn tourists and business travelers was minimal. Most duty/tax collections came from returning residents. Secondly, tl prohibited items in the baggage of these two classes of passengers was in most cases done through ignoran Third, generally about only 20% of the people passing through customs had any sort of business with Customs, i, duty/tax/prohibited goods/smuggling. That meant that 80% of the persons arriving could be let through custo without delay. The problem, of course became the all-important questions of which ones are the 80% and which the 20%. It was found that most smugglers were posing as tourists or residents. Inspectors were focusing on 1 baggage to be examined instead of the passenger.

A number of nations worked independently on these problems, and under the CCC, and later WCO, talked to ec, other about possible solutions and to compare systems. This led to the growth and modification of selection syster Experience led to further modifications that are still on going.

National interest in each country was based on where they perceived the greatest danger, or risk. In some it was 1 collection of revenue, in others it was the danger of smuggling of narcotics, or prohibited goods. In some it was bol The results of a risk assessment came out in this simple format:

Passenger Class	Risk	Duty/Tax	Smuggling	Awareness
Tourist to the US		Low	Low	Needed
False Tourists		High	High	No
Business Traveler		Low	Low	Needed
False Business Traveler.		High	High	No
Non-resident Immigrant		Low	Med.	Needed
Returning Resident (temp. Sojourn)		High	Med.	Needed
Returning Resident (long Sojourn)		Med.	Med.	Needed
Crew		Low	Med.	Needed

A second study showed seizures by country of origin. More attention was paid to these flights than others. This M shown to have only limited value as connecting flights can allow a smuggler to arrive from any country they choo In risk analysis, persons using multiple transfers became persons of interest for interview.

A matrix of the resolution would have shown:

Problem to be resolved:	Impacts:	Locations:	Challenges:	Authorities:
Passenger flow	Duty collection Enforcement	All international airports nationwide	Reduction in examination. Faster decision making	No changes needed

## Solutions:

- Screen passengers after baggage pick up for by-pass.
- Decrease Inspector collection time of dutiable declarations.
- Increase Inspector skills in interview technique.
- Apply observational techniques by plainclothes inspectors.
- Profile flights from originating countries.
- Increase information to public of compliance.

Results of the risk assessment were based on general data of all airport fines, collections and seizures. As a primary concern was speeding up the flow of traffic, decisions were made to revise the treatment of arriving persons by air to include:

- One stop. A method of determining the correct status of passengers, and a preliminary review of declarations. Passengers are either allowed to leave with no further treatment or are referred to a second location for examination.
- Publication (wide distribution) of exemptions, duty rates, and prohibited/restricted goods.
- Use of a written declaration form to be distributed by the airlines prior to arrival. This indicated that the passengers understood what the declaration requirement was. It also gave Customs a name and address of arriving passengers, allowing us to gauge the frequency of travel and assure that all persons arriving cleared Customs.
- Use of behavioral observation techniques for selection of passengers by "rovers".
- Use of aircraft inspection to look for smuggling indicators.
- Awareness of airport internal conspiracy and counter actions through security and observation.
- Training primary inspectors on interview techniques.
- Change exemptions to increase the dutiable threshold, and use a flat rate of duty for the next one thousand dollars based on average duty collections and amounts. The exemption amount was \$200. The average dutiable declaration was between \$300 and \$800. The average duty rate of collections was 9%. Increase the exemption to \$400 and using a flat duty rate of 10% on the next \$1000 increased the speed at which transactions could be handled increased dramatically. No longer did an Inspector have to classify each item of merchandise but instead simply charged the flat rate of 10%.

What we did in the US has only limited bearing in Egypt, except the process of change. What is significant to Egypt is the problem-solving technique based on risk analysis. It is the same system used in many countries. Voluntary compliance works, it is a proven concept. Risk analysis also works. It allows customs to pay attention to the most important items of business, saves manpower and it improves the image of customs to the public. It is sometimes hard to accept change to a familiar system. Learning a new system and leaving old habits behind is a traumatic event. The passage of time and gaining experience in the new system soon dispels fears as employees see that the new system works.

It is therefore suggested that Egyptian Customs develop the ability to perform risk analysis as a management tool. Assistance could be provided in the form of an advisor to help identify areas of concern and to work through several risk management projects to familiarize personnel with the practical application of the process. This advisor could also provide management with suggestions for the development of the infrastructures needed to support risk management.

## **The Risk Management Process as Part of Compliance\_**

The risk management process is best performed by a mixed group of employees and supervisors, working in a committee, to allow for different levels of perception and ideas. Each should have current experience in the area of interest, as a subject matter expert.

The risk assessment process is a management tool that can be applied to any area of Customs. It is "work smart". It is paying attention to business and moving resources to where they can produce best results. It relieves the burden of the innocent going through the whole process. Placing that burden where it belongs, on the violator.

### **1. Determine the Area of Interest**

This step establishes the organizational unit or process in which risk management will take place. Risk areas have been identified and criteria against which risk will be assessed, established, and the structure of the analysis defined.

### **2. Identify the Risks (Problem)**

Identify what, why and how risks can arise as the basis for further analysis. This step requires an in depth description of the current control process, to include: participants; strengths and weaknesses; where, when, how is the risk likely to be incurred and by whom; what are the threats and their impact in case of circumvention; why do opportunities arise for circumvention. What could someone do to obviate the process or procedure currently in place. It is important that in this step, as many of the risks as possible be documented.

### **3. Analysis**

Study the historical patterns and information available from all official sources to determine the level of risk inherent in current practices. Look for weaknesses in controls and process. Include procedure, process, facility, and environment in your consideration. Analyse risks in terms of likelihood and consequence. The analysis should consider how likely is an event to happen; and what are the potential consequences and their severity. Combine these elements to produce an estimated level of risk. If the estimated levels are low, then risks may fall into acceptable category and action may not be needed.

### **4. Prioritize risks**

Compare estimated levels of risk. Rank the risks to identify management priorities. The assessment into HIGH, MEDIUM, and LOW is widespread. In complex environments a more detailed system may be needed, such as a range from 1 to 100. The latter also requires the determination of high and low risks but allows for more precision.

Risks must be continually monitored for any change in their nature, level or significance.

### **5. Resolve the risks**

Accept and monitor low-priority risks. For other risks, develop and implement a specific

Plan to overcome the risk, which includes consideration of resources (human, financial and technical). This is the "what we're going to do about it" step. Think carefully how to best control the risk, what can be done to reduce the risk. Is it reasonable, do we have the time, personnel, and budget to affect the control? Is this risk unique? If someone else, or some other Customs department found a way to control this risk? If so, consider their solution in your context.

### **6. Monitor and Review the Controls**

Are the controls working? Are they meeting the purpose for which they were designed? Are the controls being conducted and implemented as designed? Is there any modification needed? Can it be done better or more economically?

Controls that are working properly may be left in place. Those needing modification can be changed. Those not working or not producing the desired result can be removed or referred back to the committee for reconsideration.

### **7. Documentation**

It is important that documentation be maintained that gives the rationale behind selecting the risks, and records 1 assumptions on which assessments have been made, to establish an audit trail that ensures important information not lost. It also helps over a period of time to avoid duplication. As this is a new system, experience will improve 1 likelihood of success.

Practical Application of Compliance in the GATT valuation system:

Compliance, including risk assessment, can be a key element to success in Egyptian Customs. As GATT and other WTO agreements are designed to increase by-pass, or entry without examination, then a system must be implemented to assure protection of the revenue. These systems work in concert to provide the positive incentive to voluntary compliance, and provide the basis to identify and penalize violators.

These systems are:

1. Selectivity
2. Verification of transactional value
3. Post Audit
4. Final Review (Liquidation)

1. Selectivity - Under the principle of Customs Control, Customs may select declarations to be examined for cause randomly, or based on high risk. Random selection is used to indicate the success of the release system. When automation is a reality, then random stratified selection, will provide a non-biased methodology for periodic checking imports for correctness.

Random selection can also be used in a manual system, by simply using a numerical variant to decide which imports are selected for examination, i.e. every 100th declaration received, or, the 25th declaration received on a particular day, etc. This can be varied on a daily basis to assure security of the system. It can be stratified manually also selecting the 5th declaration having a value above X\$, or the 37th having a value below X \$. It can also be stratified by import category or by commodity. Random selection, to be successful should not exceed more than 1 % of total importations in a selection category. The word random is of primary importance.

Selection for cause is always allowed. However the cause should be real and the person selecting should be able to articulate that cause. Once the cause is satisfied then the examination is ended. Cause may be based on previous negative experience with a particular person or company. This cause may be removed by rehabilitation through compliance over a period of time or importations. Cause may also be based on intelligence or information from a reliable source that would lead a reasonable person to believe that a violation may be present.

When a determination is made by competent authority that an import may be of high risk, that is, that the import has the potential of a serious risk to loss of revenue, or, is potentially dangerous to the public health, or, the possibility a violation of law may be present, then selectivity is used to reduce that risk.

2. Verification of transactional value. - Although not part of an independent compliance unit, the officer performing the original review of the declaration is the key person to primary compliance. That is because this is the person who has the responsibility to allow a transaction value to be accepted, or, may require further explanation documentation.

In the GATT valuation system the declared transactional value is accepted as declared unless there is a reason to verify it. Market price lists, catalogue prices, or other price reference lists should not be used as a reason to verify historical record of previous imports may be used, provided they are identical to the current importation.

The level of verification is determined by the information needed to satisfy the question. In some cases it may simply be a verbal question to the importer, such as, "your value seems a bit low compared to previous importations, is there a reason for this?" The answer may satisfy the question, such as, "yes, it is the end of this model year". In that case a notation to the file is called for, for future importations, but no further documentation may be asked for. However, if the answer does not satisfy the question, for example if the importer were to say, "Yes, it was a discount for quantity". Then the officer might want to question further or ask for verification in the form of a commercial invoice, order voucher, or a copy of the payment register when payment is made. The point is that the verification is dependant on the question raised, and is progressive only to the point of satisfying the question. It may range from a simple verbal question, to a visit to the importer's premises to review the files of the importer in regard to that importation. The officer makes notes of all contact with the importer and if an importer's premise visit is needed makes a report of that visit to management.

Should the officer be unable to verify the transactional value declared, then the officer is allowed to continue up the hierarchy of establishing value as found in the agreement. The importer is notified of each action taken and the reason for it, allowing the importer an opportunity for response at each stage.

This process is the central core of the GATT agreement, and when followed carefully becomes an important asset for compliance.

3. Post Audit – Audit follows the same pattern as selectivity for examination in targeting audits; for cause, random or high risk.

Audit uses the business records of the importer to verify the transaction(s) that have taken place.

Post audit focuses on persons involved in the international movement of goods. It is an effective tool for Customs control because it provides a clear and comprehensive picture of the transactions relevant to Customs as reflected in the books and records of international traders. At the same time it enables Customs administrations to offer trader facilitation measures in the form of simplified procedures (e.g. periodic entry system).

By combining random examination selectivity with random post audit, a comprehensive program of compliance control can be developed that assures revenue protection while facilitating trade.

Audit plans can be developed as experience is gained to include cyclic audits, commodity class audits, and industry based audits.

4. Final Review (liquidation). Liquidation is the final review of the importation to assure that the proper duty/tax has been collected. It is a full review of the entry from declaration to release that corrects potential errors, assures correctness in classification and valuation, and takes into account changes in information as the process completes itself. It takes into account all of the previous steps in compliance.

At the time of liquidation, the importer is notified of the final duties/taxes to be collected, and once collected becomes the ultimate releasing agent for customs. For practical purposes the customs import action is closed. This does not affect the importer's record keeping responsibility. Under normal conditions, an import by-passed at the time of declaration is considered to be liquidated 5 working days from release.

A senior officer should perform the liquidation with experience in the field of the classification and valuation of merchandise, and who is very familiar with the entry process.

### **Infrastructure (Organization):**

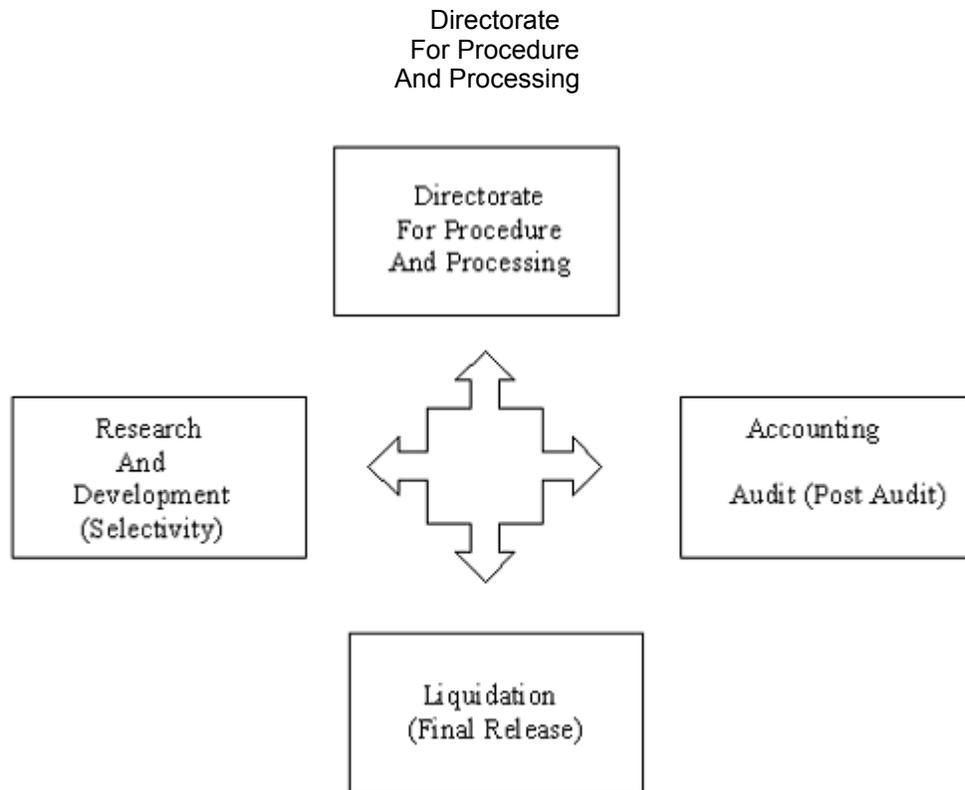
The structure of a compliance unit is composed of three units subordinate to one Directorate, or manager. Because of their close working relationship with classification and valuation, it is a natural inclination to locate them within the Directorate for Procedure and Processing of Cargo.

In the case of geographically separated units, it is recommended that a central oversight manager at Headquarters have the overall responsibility for the program, with local compliance units at each location, sized to the amount of declarations or imports to be handled.

The internal structure of the units may follow local guidelines according to approved personnel formulas.

Personnel selected to work in the units should be persons with experience in dealing with merchandise and the entry process. Auditors must be professionally qualified, and can be supplemented by accounting personnel.

A diagram of the organization would be:



### **Directorate**

The Directorate is responsible for the oversight and direction of all operational and administrative functions of its subordinate units. Assures that the subordinate units function within the Customs Laws and established procedures. Verifies that all actions of subordinate units are based on the Policy of the Customs Authority, free from bias and favoritism.

### **Research and Development Section**

The largest of the sections, or units, is the R&D Section. The function of the unit is to perform continual research and provide customs with the best potential targets for risk management and selective examination/audit.

The following areas of interest are suggested as functional responsibility:

- Selectivity, Profiling and Targeting
- Monitor and Review – Compliance measurement

- Documentation and Record Keeping
- Commercial Intelligence and Information gathering

### **Accounting and Audit Section**

This section is responsible for designing an audit plan to meet the targeting criteria of the person, company, corporation involved. For conducting the audit in a professional manner, using recognized audit techniques, and reporting the results of the audit to the Directorate. The unit should be responsive as opposed to proactive in seek targets for audit.

### **Liquidation**

The liquidation section is the final review of Customs prior to release. This section will review the declaration and subsequent information developed by valuers, selectivity, and audit to assure that policies and procedures have been followed correctly, and that the correct amount of duty/tax has been assessed. They may increase the amount collected (re-bill), decrease the amount collected (refund), or accept the amount collected as correct (release). They will document their reason for change when appropriate. The consignee, owner, or importer will receive a notice of liquidation stating the results. The section will only liquidate those importations that have been verified or selected for examination or audit. Those importations by-passed will be considered liquidated automatically five days after release.

### **Legal Considerations**

#### **The adequacy of powers available to Customs administrations under national law**

must be kept under review and powers should be strengthened where necessary to deal with new threats or facilitation requirements.

As a general guide, national legislation should confer the following powers on Customs for the purposes of control: although many such powers will only actually be invoked selectively in accordance with risk management.

Laws, implementing decrees and guidelines, must contain the following authorities in the proper format for the Nation: \_

### **Surety**

- in order to release cargo or merchandise prior to final liquidation, a surety must be demanded to assure collection of the revenue.

### **Examination**

- to examine goods, means of transport and persons in a manner to be decided by the Customs authority with a view to using the most appropriate control methods.

### **Right of Access**

- to access premises, vehicles, vessels or aircraft of companies/persons involved in international trade transactions, and to access all business records, including computer systems, relating to international trade transactions. The right of access includes the right to stop a person or vehicle to conduct a search.

### **Sampling**

- to take representative samples of goods at importation, post-importation and at export.

**Detention**

- to detain goods imported or intended for export to establish their compliance with Customs laws and regulations.

**Post-clearance Audit**

- to conduct a retrospective audit of the business records, including bank records and computer systems, of any person or company involved in an international trade transaction.

**Exchange of information**

- to exchange and share information on international movements with other Customs Authority for Customs control purposes.

**Information Retention and Submission**

- to require the person/company involved in an international trade transaction to submit the information necessary, as previously defined and publicized by Customs, for the completion of Customs formalities according to the stipulated procedure and control method.
- to require that this information be kept by the person/company involved in the international trade transaction according to the generally accepted accounting principles within the country concerned,
- to allow for the periodic lodgment of declarations and to set up systems-based controls.

**Authorization to Assist**

- to authorize persons or third parties to assist Customs in performing certain Customs control functions. If there are reasonable grounds for establishing a Customs offence, the Customs investigation unit should be brought in, since it has the powers necessary to carry out a formal investigation.

## Chapter 5

### Customs Automation

Edward Tulis

#### Introduction

There are many facets of reality in the Egyptian Customs Administration that have become 'institutionalized' normal business practice, over the years. If Customs were being invented, today, many of these practices would not occur, because there would be no necessity for them. Some of these practices relate to how import representatives are viewed by Customs and how Customs is viewed by importers.

The former practice of setting value for duty and tax purposes, regardless of what the importer actually paid for goods, resulted in Customs being viewed as arbitrary. With GATT value now based on what was actually paid (payable, if not already paid) by the importer, that perception will change, once it becomes normal practice. With the advent of selective processing, and other methods of expediting cargo release, the relationship between Customs and the business community will change. With Voluntary compliance, and the presence of recorded compliance history, Customs respect for importer integrity will change, as will Customs understanding of the sources of relative risk. The environment created by both GATT and automation will alter how the Customs Administration and the Trade Community deal with and view each other and how Customs Officers view themselves. The old reality disappears.

These findings represent the facets of current reality in and around the Customs Administration that favor modernization, increased uniformity, transparency, trade facilitation, cooperation, professionalism, and integrity. Automation will enhance these aspects of reality and provide the tools that Customs Officers need to improve their performance and the performance of the trade community. These will bring salutary results that can only help the economy and business climate of Egypt. As business and investment expand, the Customs Administration will be equipped to manage the increased workload and will have the knowledge to manage the complexity of international commercial business dealings and new products and processes.

#### Commitment

The Egyptian Customs Administration is already automating its business practices, systems and procedures import and export control and trade facilitation. The Minister of Finance and the Commissioner of Customs have openly committed to expedited cargo processing, the use of risk management techniques to promote voluntary compliance, to use automation to facilitate trade and compliance with GATT,

and to create greater transparency and uniformity in the treatment of the importing trade community. "Reform through Automation" as the Commissioner says, is being implemented within the Customs Administration and in the institutions and agencies with which Customs relates in the processing of cargo into and out of the Egypt economy. It is clearly understood within Customs that agency reform is a major initiative, along with tax and other reforms of the Ministry of Finance, and is necessary to remove barriers to improved trade and to create a better climate to attract business and investment. With increased cargo throughput, given stable duty rates, duty collections will rise. The General Organization for Export and Import Control (GOEIC), the other umbrella agency involved in cargo clearance, is also engaged in reform through automation. It is automating a compliance database, of all transactions, using selected bypass procedures for the proven compliant importers and exporters, using pre-clearance procedures for early inspection and sampling, and random examination to monitor continued compliance. It has also published performance commitments on sampling limits and turnaround time for various types of tests and a brochure on information sources and requirements for business. Finally, the Ministry of Telecommunications and Information Technology (MCIT) is providing the 'intranet' to encourage data exchange among trade and agency participants, in an effort to foster the growth of 'e-commerce'. The Post Office is entering this field by providing digital and document exchange among government and private entities, and is EDI capable, an advantage for carriers and express consignment couriers. Reform through automation is clearly present and growing vigorously throughout the environment in which the Customs Administration is operating.

## **Software Support**

The National Cash Register Company (NCR) and its sub-contractor, Tabarak Computer Systems, have been engaged by Customs to facilitate this effort in hardware acquisition, telecommunications, and software development since 1998. Using "POWER DESIGNER", the contractor has designed and pilot-tested an Enterprise (Wide) Sysb Model with 36 interrelated modules to support Customs processing, data recording, and analytical requirements throughout the full range of functions. Local and wide area networks link nodes on the current system, which is running a UNIX operating system with communication elements from CISCO. Flat files have been converted to relational databases using CYBASE. The existing applications have been replaced with relational databases, applications spanning the spectrum of current Customs business procedures. In-Transit, Temporary Admissii and Drawback modules are included. The business area has been expanded to include back office applications for finance, legal, and organization structure. Graphic user interface technology and road mapping are used through to simplify process presentation in a PC environment. Functional access is controlled by a commercial security package that works off personnel, organizational structure, and application factors to define and manage job, user and workstation profiles. The Customs enterprise data model includes over 900 logical entities mapped into 5C physical tables, hosting 5,500 data elements and over 1400 logical relationships. In summary, most of a modern Customs processing system has been designed and pilot-tested, including a data warehouse Management Information System (MIS). Much of this system could be installed by 2003, funding permitting. There are some components missing from this system, only because they were not envisioned in 1998, involving GATT value voluntary compliance, and other World Customs Organization initiatives. The Recommendations section of the report specifies those components. Funding will have to be made available to program and test new features and implement them for Customs Officers, Valuators, Compliance Officer, and others to use. Contract Programmers need clear direction from Customs on the final design features of these new GATT compliance initiatives.

## **Hardware Base**

NCR has completed site preparation and equipment installations that now support import processing, software development, and communications for Customs operations in five clusters. There is an infrastructure including an installed base of 450 Personal Computers (PC's), supported by 35 servers, and modems and peripherals that represent a capacity to develop, conduct Customs business, expand services to Customs and Trade clients, and share data with other government agencies. The equipment needed to support classroom training, on-the-job training, input of inspection and test findings by Customs and GOEIC, inter-agency and trade data interchange, and to support managers, compliance monitoring, audit support staff, classification and valuation operations is not yet available. These latter functions are of significant interest to WCO. In addition, data processing and exchange capabilities need to be expanded to reach some 30 sites where Customs and GOEIC process and test cargo anywhere employees and managers are trained. Funding for more hardware is needed to meet GATT objectives.

## **Communication**

The network, MCIT, controlled by the Ministry of Telecommunication and Information Technology, provides Intranet communication sufficient to serve the Trade Community, Customs, and GOEIC, as automation expands. The intranet currently supports data sharing among Customs locations. The Post Office is seeking to serve the Trade Community, as well, by supporting document and data interchange and is EDI capable, a fact of interest to carriers who use UN-EDIFACT protocols. The General Organization for Export and Import Control (GOEIC), also in the process of automation, will be capable of exchanging data with Customs (and perhaps to the Trade through the intranet) in the near future. Their 169 computers are on order and they have trained 140 technicians in computer use. It is possible for this agency to either use Customs computer facilities for Findings Input, or to share their data with Customs directly or through the Post Office. Communications with GOEIC will depend on the configuration of their computer operations. Linkages will permit communication, but providing data to GOEIC from Customs On-Line Trade participants has yet to be worked out by either agency. It is an important design consideration. The Customs Administration has undertaken to provide a wide range of information and data interchange with various groups and clients. Importers and carrier agents can file data electronically for Customs processing. Importers and clear agents can call up manifest, classification, and tariff data, and GOEIC information requirements for use in prepared declarations. A Kiosk web site has been created for dissemination

of Customs information to the commercial trade and general public. Teleconferencing capability for use in training, management communications, and a policy/procedures dissemination has entered the planning stage. Customs is making use of automation and communication in a variety of modes to serve the full range of their constituent groups. These are not luxury features, but are necessary for clear communication and direction of a large workforce (27,000) and to train such a workforce in new technical and procedural methods.

### **Good Beginning**

This is a good beginning. The agency commitment is there and the agenda to develop and use the tools automation is present among all key parties. Modern databases and expert system information and decisive strategies are in use. The goals of trade barrier reduction, uniform treatment, openness of policy and practice, e collaborative treatment of the commercial sector (voluntary compliance) have been articulated as organizational goals and are in some instances in practice. E-commerce is national policy and being supported in government operations. It is already common in the import industry. Intergovernmental cooperation and facilitation exist. Training the workforce for professional and expert attainment, required in GATT compliance has just begun. Compliance with the terms of GATT is a commitment. The vision to see how to use these tools to improve the effectiveness of the Customs mission, facilitate the economics of business, and change the perspective of the role Customs in the economy of Egypt are all present at some level in the current environment. Further progress in the areas is a potent stimulus for attracting funds for modernization and trade facilitation. A more focused management approach is needed to move Customs as they accommodate to new policy and adopt new methods of process cargo and serving the business community of Egypt.

### **The Challenge**

The challenges facing the Customs Administration are significant:

- To put in place Executive Management of Automation and the support processes needed to plan and implement the development of automation and the structural changes needed to support it (Law, Decree Regulations, Organization).
- To disseminate the voluntary compliance process and trade facilitation initiatives as official policy through all levels of the Customs Administration and the Trade Community
- To identify and pursue Customs and GATT modernization achievement goals which are triggers for funding automation
- To pursue vigorously the technical, training, and implementation strategy required to carry out the program customs modernization
- To achieve full use of the on-line data input and communications facility by Import/Export Trade participants and other agencies
- To raise the competence levels and aspirations of Customs employees and the confidence of the commercial trade partners
- To fight the inertia and resistance to change in the institution with imagination, courage, and persistence.

### **Next Steps**

Customs modernization takes focused management and cooperation from the import/export trade community agencies other than Customs, such as GOEIC, intra- and inter-net providers, the training community, contractors such as NCR. It also requires funding from a variety of sources, some of which may be triggered attaining specific milestones in the development of automation, trade facilitation, and GATT compliance. This means that implementation of specific policy, procedural, and automation initiatives may have to be achieved, before certain funding sources will respond. Since the implementation of GATT value on July 1, 2001, cargo throughput has slowed down, cycle time (from Declaration to Release) has increased, invoice verification has become the norm rather than the exception, and duty assessments have been raised (some as much as 300 percent). Additional payments have been made to expedite cargo clearance, especially on cargo that is just-in-time. Some steps need to be taken to move Customs from old routines into a new mode of doing Customs work. Minimal next steps should include:

- A focused executive management strategy

- An initial implementation schedule
- A matching training schedule for implementation
- Funding to support initial training & implementation
- Acquisition of telecommunication & computing equipment to support the initial implementation program

And most immediately:

- Set an initial 20 percent of imports to by-pass inspections and verifications for the historically most compli, importers (white list)
- Record and report on cycle time from Declaration to Release on all imports
- Track and report on cargo throughput, monthly
- Track and report on Average Duty Rate monthly

These latter steps are required to move Customs employees away from old practices into the new cargo process performance standards (which can be done manually) and to increase cargo throughput in the face of pressures tl result in reduced revenue caused by cargo delays. It will stimulate managers to approach the assessment of relat risk from both importer threat and employee abuse of authority in the absence of knowledge required by GA compliance.

The longer-range steps toward full implementation or automation and risk management are contained in 1 following recommendations. The suggested components are needed to augment the present automated system meet GATT compliance and to support voluntary compliance, faster cargo clearance, and automated receipt processing data from the Commercial sector. They also contain a management strategy needed to move t **program to rapid completion.**

### **Caveat**

Article Twenty Three of the legal decree 166/2000 specifies the documents and certification requirements for the documents required by Customs to be presented as part of the Declaration process by importers or their clear agents. If the interpretation of this decree required importers to have and maintain these documents for the statute period, and gave the Customs Administration discretion in requiring presentation of these documents (for verificatii post audit, etc.), automation (and paperless processing) could be accomplished for compliant importers. If 1 decree denies the Customs Administration this discretionary authority, and mandates review of the documents M every Declaration, then Customs will have to operate both electronic and paper processes concurrently, until 1 implementing decree can be changed to reflect Customs discretionary authority over when it reviews documen Documentation would be reviewed in any case, as part of the decision to bypass or review any transaction.

### **Recommendations**

Introduction. The following recommendations deal with operational strategies for improving the efficiency of cal processing, the capture of data from the importers and exporters or their agents (hereafter called "filers) needed process cargo, and mechanisms to operate and monitor voluntary compliance and to measure and report Customs performance. These recommendations are made within the spirit of "reform through automation" contain in the GATT language and emphasized by the Commissioner. All of these recommendations are in operation other Customs Services and have been proven effective. They also relate to some strategic areas and approach to be considered for which automation support will be required. These areas include:

- Information acquisition & dissemination

- Training for professionalism
- Risk management
- Decision systems
- Trade access to information
- Priority processing
- Data interchange with other agencies

### **1. All Cargo Data Received Electronically. Plan to Receive All Cargo Processing Data Electronically.**

Currently, some import data is received by Customs, electronically (about 1 % from 7 filers). This electronic data converted into paper by Customs for use in the steps of cargo processing. The rest is received on paper and key by Customs for statistical reporting and collections. All of it comes from the importer, carrier agent, or clearar agent. All this data, and more, such as GOEIC data elements, could be sent to Customs through the declaratic process and entered into Customs and other data bases for processing electronically, without Customs keying without redundant data entry. It is then available for inspectors, other agencies, valuator, and cashiers in 1 processing database they require to perform their functions. Information on paper causes redundant keying Customs when all of it in any database Customs uses could come directly, without Customs or other agency effort

Paper is available for Customs, or other agency inspection, when it is required. The paper, itself, tells you noth that the data omits. Anyone can counterfeit the paper. That's why banks like funds transfers. You can always the paper if it is needed for verification, audit, seals, etc. on demand or at the importer's office. The advantage electronic data is that it is early, often transferred directly to the system and therefore more accurate, and it is in 1 system, database, and arranged so that you can use it to do your work.

As part of these recommendations, incentives in features availability and processing priority are suggested encourage as many as can to join the electronic data transfer age with the Egypt Customs Administration. Incenti\ for On-Line Users include:

- Rulings in Advance
- Priority Processing
- Pre-Clearance
- (GDEIC Data Filing)
- Access to User's Compliance Record
- Access to User's Financial Accounts Record
- Implementation Schedule for Trade Features
- Higher bypass rates from higher compliance

Providing faster cargo processing and the advantages of access to User's accounts is a potent incentive adopting on-line filing. Adding GOEIC's data requirements to the Customs on-line data capture system for

GOE would be another incentive and also useful to GOEIC, who could use the data to build their compliance record. Making keying effort for those clients. Including information on the schedule of up-coming features for the trade from 1 automation implementation schedule will encourage paper filers to adopt automation, quicker. This informat could be posted on the Kiosk web page.

As bypass rates go up for high compliance users, cargo throughput will increase, benefiting both the importer and the revenue stream into the Central Bank.

## **2. Rulings. Develop a Customs Rulings Database Accessible to the On-line Importer a Customs Valuator.**

Customs has in operation the process of issuing duty rates and associated costs for future transactions, if given necessary information, beforehand. This is helpful to the importer in calculating the costs of goods sold before a transaction commitment is made. In some countries, such rulings are good for 90 days, can be extended, and are binding on Customs, regardless of changes in tariff rate during the period. If a filer has received a binding ruling, it is lodged in the rulings database by number, importer number, applicable dates, and commodity and the rate. If the importation occurs as specified, it is accepted by Customs on the terms of the ruling. This service is designed to encourage new importers by removing some of the risks of costs and pricing, and for experienced importers with a new commodity. This service will become less useful to the experienced importer as he gains confidence in Customs commitment to the ruling at time of importation. Of course, the rulings database must be available to the Customs personnel on the cargo-processing floor by computer, or fed automatically into the on-line declaration of the linked importer, accessible by Customs during processing. This will speed up cargo release, raise throughput rates, and increase duty collections. This feature of the automated processing system should be an early implementation, since the practice is in place, already.

## **3. Priority Processing. Develop Priority Processing for On-line Filers of Declarations.**

Remote electronic declaration filing should become the dominant method of data exchange between the commercial trade filers and Customs. It saves the industry time and money, which in turn, reduces the cost of goods sold to Egyptian consumers, and enhances the competitive ability of Egyptian traders in international markets. Advance information allows Customs time for review prior to arrival at the gate for processing. It facilitates collection of compliance information, automatically populating the compliance database. It allows the computer to select a transaction for inspection or bypass, without taking Customs personnel time. It frees Customs personnel to focus their effort in compliance enforcement where risk is the highest. Methods should be developed to encourage this modality of conducting Customs business. If there are inspections scheduled by random selection or on the basis of criteria created by analysts, they should be conducted for the on-line customer before the paper-filed declarations are dealt with. In addition, more information-benefits should be made available to the on-line filer, accessible at computer, for example, tariff explanatory notes, applicable decrees and regulations, an importer/exporter bulletin board, and selected items from the 'Customs Gazette'. 'Customer service' is a novel concept to some Customs Administrations. People and corporations doing import or export business in the Egyptian economy are customers of the Customs Administration, and all citizens either benefit from or are harmed by how Customs does its business. Customer service is the fastest way to win compliance with Customs laws and regulations. Experience has shown conclusively, in all countries using voluntary compliance techniques, that compliance rates increase, and that increase first and reach their highest levels with the on-line customers. He wants to capitalize on his investment and includes edits to catch mistakes, and creates sub-systems to insure compliance.

This feature does not require much programming and could be implemented, immediately for the on-line clients. As the Customs system grows, sharing some of the data edits in the declaration system used by Customs computers with the on-line filer would advance error-free processing. In the U.S. in 1985, Customs rejected one out of every 6 declarations for errors. In 1995, the rejection rate was one out of every 876 declarations. By then, 97.6 percent of all filing was done on-line in the U.S. Customer service to the on-line filer yields great dividends for the filer and for the revenue stream into the Central Bank.

## **4. Pre-Clearance. Develop a Pre-Clearance Procedure for On-Line Filers.**

Many imports and exports could be cleared faster if Customs and other agencies had the data required, beforehand and where possible, a sample of the item for inspection and testing. If the sample meets requirements, and 1 declaration is electronically filed beforehand, as well, conditional clearance is possible, if the items at the time import or export match the goods previously inspected (appropriate item within range of serial numbers, marks, etc. Bait and switch is always an issue. But, in the case of imports, a sample can be taken for testing, and the cargo released. If tests fail, cargo can be recalled or destroyed. In most circumstances, if what was tested previously matches what appears for export, the goods can be released. Rules will have to be created to manage the process. It is well worth implementing or augmenting this service to expedite trade and focus efforts on compliance where risks are the greatest. Pre-clearance allows the transaction to be reviewed at more leisure, and eventually will become a major segment of all by-pass actions. Focus on the health and safety issues, rather than on quality issues, will further expedite this process. Quality issues can be tested early, and the importer dealt with according to regulations. For exports, quality can be largely left to the marketplace. Health and safety violations can be detected and stopped, early.

#### **5. Manifest Database. Deploy Manifest Relational Database as soon as Possible.**

This database is useful to the automated filer in the preparation of the Customs declaration, and is so used, today. Integrating it with the declaration database will allow on-line filers to transfer appropriate data from the manifest to the declaration, automatically, without paper processes intervening and redundant keying. This database can also be subject to automated selectivity techniques for enforcement research. It is a resource for GOEIC and Customs for selectivity decisions. It can be used to identify transactions for sampling and inspection, and identify the shipments scheduled for release. If the shipment is of no interest to compliance, and the bypass option is chosen, indicators will have to be programmed as will a record of the particular line selected for inspection or by-pass, that the GOEIC and Customs compliance files will be populated with the data line and the disposition decision. This should be an early implementation, if not the first one, because it is ready, needed by on-line filers, and of great value to GOEIC and Customs inspection officers.

#### **6. Declaration. Make Declaration File Relational, Connected to Appropriate Files, and Useful Other Agencies.**

The current declaration process requires the on-line filer to copy data from the manifest and other files, such as the tariff file, onto paper for re-keying on the declaration. This is but one example of the system features that allow full automation of the process, and eliminate redundant keying and the problem of numerous instances of the same information spread throughout the databases. The design rule should be "key data only once", i.e., retrieve data already in automated form via computer function into the table, process step, or file in which it is needed. In this spirit, data may be added to this database that covers requirements for a paperless transaction and fulfills the needs of GOEIC. A GOEIC declaration screen or screens could be added to the declaration system so that the on-line filer is not re-keying data for GOEIC and so that GOEIC can benefit from electronic filing. Data retrieval, as well as information returned to the filer, without building the whole client interface, thereby duplicating much of what Customs is developing, anyway. The actual paper documents should only be presented for purposes of value verification, or other agency needs for inspection or testing is required. To the extent possible, data needed by GOEIC could be provided, with paper involved only if some form of verification is needed. The results of inspections and clearance or release decisions should be returned to the on-line filer through this interface. This gives the on-line filer an earlier opportunity to finalize shipment arrangements. Customs should plan to make the interface capability available to improve interaction between any other agency that needs it to expedite cargo processing or any other administrative interaction with Customs filer clientele.

#### **7. Classification/Valuation/Intelligence. Develop a Verification Database for Value and Origin for Commercial Intelligence with Links to World Customs Organization.**

For transactions in which invoice value is accepted by Customs, the data on the declaration should be sufficient and no paperwork required. However, when verification is required, input to the declaration database of reasons for classification or value verification will be needed. Indicators of suspension until invoice data are verified, would need to be added. This process may require a sub-database or annex for recording decisions for verification of value and the results of all verification actions. The data should, in addition to reasons for verification, include specific information needed from the importer for verification. Responses to this request could be included on a verification screen, linked to the declaration, since much of the information is

already keyed there. If paper required, such as a copy of the contract, it could be submitted. When the determination of value is made, the information should go back to the on-line filer for his records, using the same database, to avoid redundancy, and assure that the determination is related to the proper filing. In addition, as part of the research base for "lines business" for classification and valuation officers to use, an intelligence database should be developed commercial information provided by Customs research analysts and by WTO on commercial interests.

#### **8. Findings Database. Design a Findings Database for Inspection Results by Customs and Other Government Agencies (e.g. GOEIC).**

Findings from inspections become key data in determining the compliance of an importer or exporter. Methods should be devised to enter findings into a compliance database, discussed below, not only for Customs inspectors but those of other agencies. If the other agencies have developed such databases, links to the Customs compliance database should be developed for them to use in extracting relevant data. If no such other agency database exists, then methods for the other agency inspector's findings to be entered in the Customs compliance database should be created for use by the other agency inspector on site at Customs facilities, or keyed into Customs from paper reports, until such time as the other agency develops the capability for data exchange with Customs. Findings in most instances are of a generic type and can be coded or checked off on a list on the finder computer screen. However, some discrepancies may need explanation or descriptive information, so the capability to enter plain text should be included in the design.

#### **9. Compliance Database. Develop a Compliance Database for Compliance Monitoring Commodity, Line-of-Business, Importer, and Port of Entry.**

Currently Customs inspects every import transaction for compliance to Customs law and regulations. However selective attention should be paid to those commodities or customers that historically present the highest risk of non-compliance, or demonstrate high discrepancy rates, while systematically monitoring those who comply as a matter of course with fewer inspections. To do this, an historical database should be developed to accumulate a history of compliance that can be analyzed by importer, commodity, line-of-business, port, or any other factors that present elevated risk. This analysis is crucial for determining relative risk potential by segment of the database. Relative risk can be measured in this way and used to target for inspection or monitoring. Criteria, or stratified sampling (i.e. value, line-of-business, volume or transactions, etc.) or wholly random sampling, or criteria targeting can be used to select for inspection, or to analyze for uniformity of treatment across locations, teams, or lines of business, as well as for risk management. The type of sampling or selection depends on the nature of the analytical findings and inferential statistics desired. The data on importer, commodity, and other generally relevant data should be entered in the database and extracted routinely to populate the Compliance Database, rather than keying these data redundantly. The findings of compliance or exceptions, violations, fines, or penalties can be added to the database, as importations occur. Activity should be aged, with new transactions being added while old ones are removed, keep the database current (a year or two), depending on the frequency of import activity by the importer. A priority should be given in this design to provide on-line importers selected access to some of his data in this database, that he is well aware of his compliance status before he is subject to audit. In addition to this 'transparency' feature, procedures for handling appeals for the correction of data should be well known, especially during the experience phase for both Customs and the import trade, as part of Customs 'transparency' commitment.

#### **10. Account Processing. Develop a Financial Database Keyed by Importer Account.**

The declaration process generally ends with payment, and may include later additional payment or refunds. The process in Egypt is for the importer/exporter to carry in his customs account sufficient funds to cover the financial obligations his transactions incur. Funds to offset the obligations are drawn down by Customs actions and refunds are credited in the same way. Customs is already established to process by importer account. This database should be relational and linked to the 'charges' elements in the declaration database, such as declaration number. One key to these data must be a transaction identifier, such as declaration number, and if more than one transaction is included in a declaration, a line-item number. This will allow both the filer and the Office (the Office of Taxation) to identify the transaction that the payment or refund is associated with. (The Office of Taxation is developing an audit pilot project involving extracted data from the Customs financial database for use in targeted accounts for audit. Data used in populating their database should be carefully designed, so as to preserve the confidentiality of importer 'transaction level' data integrity, as required in the GATT articles.) Access by the on-line filer to his account status is an important feature for the on-line interface, so that payments (withdrawals) are

refunds (credits) can be monitored. This is another 'transparency' feature of Customs relationship with the trade community.

#### **11. Electronic Kiosk. Continue Development of and Expand the Electronic Kiosk.**

Egyptian Customs Administration has a web site for the dissemination of information important to the import trade and the traveling public. It is a good location, accessible to Egyptians and foreign travelers and tourists, that they may "Know Before They Go" of the regulations on goods brought into Egypt. This very good idea should be developed further with data from other government agencies involved in importation, new regulations, procedural changes affecting importers or exporters, changes in tariff rates, and items on Customs processing baggage (such as a list of prohibited items), and the standards of service the importing public can expect. "Service Level Commitment" (see No. 14, below) is a good public service and serves to improve performance of Customs employees in carrying out their tasks. It lets them know, as well as the public, what performance standards are expected of them. This innovation is part of both 'transparency' and the commitment to 'put service' first. Openness and clarity in this area improves compliance and wins friends for Customs with every traveler entering Egypt for the first time, or as tourists, and those who are returning home (some of Customs's severest critics).

#### **12. Electronic Training. Develop a Unit, with Contractor Support, to Provide Continuous Training Dedicated Computers, PC's installed at Work Stations, Augmented by Computer Projection and Live and Video Recording Capability.**

The Customs Administration should plan on making full use of the computers in the currently installed base of computers dedicated to training at the Institutes and elsewhere, computers acquired in future phases of automation, by using them as "on-the-job" training instruments in addition to operations equipment. I recommend that Customs pursue their internal telecommunications initiative to include distance learning/teaching capabilities as well as teleconferencing. Information dissemination on paper is expensive, quickly outdated, and cumbersome to use. Creating Compact Discs for teaching is less expensive, easily updated, far more cognitively engaging, and easily dispensed to learners through computers at the work site and at Customs Institutes. It can also be used with Customs trade partners for indoctrination about new Customs procedures and continuing education on subjects such as GATT value determination, the benefits of electronic processing, new features, and regulations. Selected discs can be created for use in the Kiosk for public education, public interest, or public relations. Dual use computers can be used to equip the employee, as he first signs on, or for later showing, regulations, procedures, or policy innovations as the Customs environment changes. It provides an opportunity for Customs leadership to reach nearly all employees, without the expense of assembling them in one or many places. Instead of the "fire-side chat" made famous in the U.S. by President Franklin Roosevelt, it is a computer-side chat way of assuring and stimulating employees about their future with automation.

#### **13. Management Information System. Create a Management Information System (Data Warehouse) Accessible through the Desk Top Computer of all Managers.**

Once the operations of the Customs Administration have been automated sufficiently (a gradual process), Rule Number 2 can come into effect, namely, "Management data should result from the operation of the automated business environment and should only be augmented by personnel counts and funds allocated to performance areas, matched to operations." That is, employees and managers should not engage in or be burdened by having to collect data on their operations, off-line. Another view of this is "if the activity does not appear in the automated processing of Customs business, should we count it?" The answer is "No". The "Reform Through Automatic Endeavor" should result in data on all operations within the automated system. This makes it accessible to managers and to the managed, making a clear environment for performance measurement open to all employees. This is a key factor in internal 'transparency' and crucial to employee morale. The areas of interest are operation numbers of personnel in the operations area, and funds budgeted to operations, segregated by administrative level or location. The data warehouse is a performance measurement tool, and should reflect development progress targets that can serve to show management the levels of achievement of interest to GATT compliance that have been attained or still have a way to go. These levels should include those items that are triggers for release of funds from the various sources of support identified by Customs, Office of Finance, and USAID. NCR has already designed a 'Data Warehouse' to be used for just this purpose by managers. It will need to be redesigned to include some of these additional performance areas (percent compliance by type of filer, number of on-line use internally clocked cargo release time, etc.).

#### **14. Service Level Agreement with Users. Develop a Service Level Agreement with Customs, Other Agencies and Trade Users of Customs Automated System.**

The Customs automated system will be used by Customs employees, the Office of Finance, other government agencies involved in import control, and importantly, member of the trade, and the general public (e.g. Kiosk). For concerned, we recommend the development of a "Service Level Agreement" with users that is made public a available on the web, indicating up-time, response-time, decision-time, clearance-time, and other measurable performance indicators that show diligence and care in the quality of agency performance. Data can be in percent time target level is achieved. This is good for morale and a sense of professionalism. It is good for government show such interest in "customer service". And it holds management accountable for quality service. Where possit such a public commitment to quality service should be instituted up front in the developmental process a expanded as new services become available. GOEIC's brochure already has elements of such an agreement I sampling limits and testing turn-around time). Clock software will be needed in some automated processes to tit duration between initial action and final action. These actions can be aggregated by type (filing time to relec, notice issuance) and averaged to obtain percentage elapsed time). Managers can see measurable progress where the system is falling down or in need of redesign.

#### **15. Appoint an "Executive Manager and Advisor ". Place or Create a Champion of Automat Development with Authority and Accountability to Lead Automation.**

Customs Automation will transform the way the agency does business and will affect all parts of the agency, otl agencies, and the import/export trade. Special leadership is required to continuously push this effort forward on fronts, and to oversee the funding and cooperation with other agencies required to assure mission success. 1 person should report and be accountable to the highest level of administration possible, including the Minister Finance who is ultimately responsible for the success of this initiative as part of his Financial Reform endeavor He or she should have authoritative access to other agencies and the trading community, as well as to all Custo levels of administration. His responsibility cuts across traditional organization lines of administration and he shop be given the authority to work across the board. Contracts needed to support this effort should be under oversight as should planning and policy for automation. He should chair a committee dedicated to draft changes in the law and regulations needed to facilitate automation and paperless processes in Customs commerce, and to pursue their implementation. He should chair the Automation Steering Committee where des and implementation decisions are made and monitored (see No. 15, below). He should be responsible for 1 identification and active acquisition of funding for training and automation. This person should not be involved managing any phase of operations, but must be involved in supporting operations managers as automation affe them and their employees, such as use of the relative compliance measurement systems. The occupant of t office must be a good negotiator, acceptable to the trade, and respected in government circles. He must bE focused individual, and of high energy. It may be that this person works on a consultative basis, such as advisor to the Minister of Finance, rather than as a government employee, but endowed with sufficient authority do this job, effectively.

#### **16. Steering Committee. Create a Steering Committee to Support the "Executive Manager/Advisor" Prioritization and Scheduling of Projects.**

There are many interests and organizations within the sphere of Customs Automation that should be involved determining the relative priority and scheduling of components and features of the Customs Automated System. steering committee should be created to help establish project priorities and advise on project scheduling a should include current managers active in the automation effort, so far. This committee should be stable composition over time, because it should become familiar with the development process and be cognizant of 1 implications of one scheduling choice over another, and what projects can be accomplished concurrently with 1 same resources. Priorities should be reconsidered periodically as projects are completed, tested, a implemented. This group might survey users periodically to get responses from experienced users, and cre; ways for those users to suggest improvements. Annual surreys of a representative sample of users, or all them, if that is what they wish, should be done to provide suggestions for improvement of the Customs-Tra interface(s). One method to capture these data from users is to provide a database for improvement suggestioi open to Customs employees, and interface users alike. If these suggestions are weighed, consolidated a ranked as projects, so that users can see the value of their input, this mechanism will continue to be uses Finally, one of the organizations that will become of great value to Customs will be a group from the trade uses They are demanding, assertive, and quarrelsome, to be sure, but they have a great steak in the success operation of this

program and will support Customs within and from without, as they realize the benefits of automation. They are Customs' greatest supporters for operational support from the Legislature in the U.S.

#### **17. Prioritization Control. Use Prioritization To Control Development & Implementation.**

The Steering Committee should control and modify the development and implementation of automation. There are many competing projects involving numerous interests and constituencies. Many projects must logically be developed sequentially, while others can be done simultaneously by the same programmer work group. The Steering Committee will know how to manage complex development and solve development and timing issues because of their continuous involvement in the process. If internal power politics is allowed to control the automation program, stakeholder interests are not protected and development resources are not used to the best advantage. Control by the Steering Committee should be based on project prioritization, which takes account of resources, and the order in which programs must be written, according to interdependent relationships. The Committee should know what program can be opened to accomplish simultaneous objectives. It is this group that must balance needs and resources, and developmental order. Prioritization takes the political out of this decision process, makes development demand driven and user responsive, while it weighs competing needs within resource constraints. It is not only a matter of manpower or money, but also rather which programming resources are available to do what project component. Prioritization and schedule control is the only sane way to manage such a large and complex set of projects.

#### **18. Tested Priorities. Suggested Priorities for Project Software Development Decisions.**

##### **Suggested Priorities for Software Development**

<b>Priority</b>	<b>Meaning</b>
1.	Mandatory: required by law, decree, or regulation.
2.	Must Have: high priority task, accomplishable in less than 1 year
3.	Can Do: ready to do now, accomplishable in 6 months or less
4.	Should Have: high priority, start now, needs more than 1 year
5.	Mid-Priority: schedule for next phase
6.	Nice-To-Have: desirable, schedule for later phase

This series of recommendations does not suggest the order in which particular modules or features are added to the live program. There are some instructional modules, for example, which could be worked on concurrently with process modules by the same contractor personnel. Knowledge of available programming resources, together with knowledge of the training required to use the system, will affect the order in which tasks are undertaken. The Steering Committee process, using the priority system, above, served the United States well in working with a large and complex project agenda in development and implementation of its Automated Commercial System.

#### **19. Software Needed. The Following Software is Needed to Support Incentives, GATT Compliance, R Management (Voluntary Compliance), and Cargo Processing.**

When NCR developed the Enterprise-Wide Processing Module for Customs (plus back office support) GATT compliance requirements were not considered. Developing incentives for on-line declaration filers was only a distant consideration. And the use of voluntary compliance techniques was not on the planning horizon. The following software development and database design need to be undertaken in light of a changed Customs process environment and commitments to transparency, uniformity, risk management, and improved cooperation with the members of the trade community.

Incentive Features for On-Line Filers

- Data for reference and use in on-line filing.
  - Additional declaration data for GOEIC-related cargo
  - Access to user's compliance, and financial records
  - Priority processing for on-line filers
  - Rulings Database & Linkages (to Declaration, Value DB, Compliance DB)
  - Rulings information retrievable by filers and cargo personnel
- Pre-Clearance Processing (On-Line Users)
  - Manifest links to Declaration DB, Customs/GOEIC Review tools
  - Declaration DB Links to New Modules
  - Classification/Valuation Verification DB & Links to Compliance, Filers
  - Findings Processing & Links to GOEIC & Compliance DB
  - Compliance DB
    - Selection software for risk management
    - Analytical Software for relative risk assessment
- Account Processing & Filer Access (payments/refunds)
- On-Line User Link to Development Schedule
  - Future feature suggestions for filers
- Performance Measurement Data Warehouse Additions
  - Internal clocks for performance measurement
- Service Level Program with percent calculations.

## **20. Hardware Program. Development of a Hardware Acquisition Program.**

The acquisition and installation of Hardware (loaded with Off-the-Shelf software like e-mail, spreadsheet database, word-processing) will be scheduled as funds are available. Priorities for receipt of equipment related to GATT compliance in Valuation, Risk Management, and Trade Facilitation. Customs teams will need this equipment to do their work, and computerized curriculum development teams will need equipment generate training materials for these modules and processes. Furthermore, programmer resources will have be used to create verification, and compliance databases and modernization of Customs Cargo processing. In the Customs processing stream to be complete, GOEIC and Customs selective inspection schedules will needed within the system, as well as a Findings Database for both agencies. Audit teams will need computer equipment, as will analytical teams to monitor voluntary compliance, uniformity of cargo processing, a development of inspection selection criteria. Post-audit teams will need equipment to analyze both Customs a Trade performance and investigate fraud. Hardware will be needed by Performance Management & Monitoring

Users (managers, Finance Officers, Schedulers, Manpower Decision-makers, and the Steering Committee control and plan the process we have envisioned here.

As an initial acquisition, I estimate about 1,500 computers, with servers and appropriately shared peripheral will be needed. This is a rough estimate and should be revised by the Steering Committee, once they have had an opportunity to coordinate the development schedule with training and implementation. This should be done in relationship to the numbers of teams designated to use the resources, alluded to, above. Communication will have to reach other agencies (via MCIT) and reach at least the 30 sites from which both Customs and GOEIC process cargo, employees are trained, analysts and managers work, and development takes place. Training needs for computers, projection devices, connectivity, and electronic curriculum need be included in this initial hardware/software/programmer environment, with special attention to training requirements. It is crucial to the achievement of system utilization and the professionalism of Customs employee performance. Finally, in future, these resources will expand, have to be maintained, and be replaced on a regular schedule, at some measurable cost. They should be replaced in approximately the same order which they entered the inventory.

## **21. Clarify Legal Reading of 166/2000. Ascertain Customs Discretionary Review Authority of List Documents, or Seek to Assure Such Authority.**

Currently, Article 23 of 166/2000 may limit the authority of the Customs Administration to determine when review the import documents listed in this decree section. If this decree can be read to permit Customs determine when and under what circumstances to review the listed documents, at Declaration, for Verification at

Post-Audit compliance review, then paperless processing is a possible procedure to use with the mi compliant trade constituents. If document review is required for every transaction, Customs administration authority is limited, and a concurrent document and documentation review must be operated.

We recommend a thorough review of this issue. E-Commerce recognizes the need to base procedures documentation rather than paper documents. It is essential that information can be structured and shared among internal processing files to make e-commerce work. This decree, if strictly interpreted, would essentially preclude e-commerce in the cargo-processing environment, unless it was operated in conjunction with a parallel paper process. Every effort needs to be made to clarify this requirement or to change it to assure that the Customs Administration has the authority to determine when and under what circumstances paper documents are required for review.

## **22. Next Steps. Some Next Steps to be Undertaken, As Soon As Possible.**

Customs modernization takes focused management that reaches throughout the organization, out to the import/export trade community, and across to other cooperating government agencies. It involves both government employees and the contractors that acquire, install hardware and communication and create the software utilities and applications with which the system runs, and computerized training materials. It involves especially the training process for both the employees and the trade users of the automated system. And such an enterprise will engender changes in policy and new policies, procedures, regulations, decrees and laws facilitate the environment envisioned, here. Focused and concentrated management is required to achieve a variety of initiatives automation requires. Next Steps should include:

- Select a Senior Executive Manager reporting at the Ministerial Level to Manage Customs Automation
- Create The Steering Committee to assist the Executive Manager in Prioritization & Scheduling
- Develop The Initial Implementation Schedule of System Components
- Develop a Matching Training Schedule & Curriculum, and Start Training
- Identify & Acquire Funds to Support Initial Acquisition, Development, and Training
- Acquire funding to support additional programming and testing
- Acquire and install the initial equipment allocation
- Begin the programming recommended here to complete the design
- Review Legislation to Permit Customs Document Review Discretion

And most immediately:

- Set a bypass rate of 20% for the most compliance importers (white list)
- Record cycle time from declaration to release for all cargo, monthly
- Report on average duty rate collected, monthly
- Report on cargo throughput statistics, monthly

**Summary.** These recommendations, as they appear in final form, might profitably be shared with Customs employees, other cooperating agencies, and the importing trade community. Sharing intentions is part "transparency", gets your commitments out among the groups involved, and brings them into cooperation in the long run. It also serves to keep your "feet to the fire", because others are looking over your shoulder for the appearance of benefits and features of use to them.

## Chapter 6

### Egyptian Economic Processing (Free) Zones, Bonded Warehouses, and Temporary Importations

Robert B. Drost

#### 1. Free Zones

##### Background

Certain countries have long considered it to be in their interest to encourage development of their external trade granting free zones in which goods are free from import duties and taxes introduced into the designated area. Free zones are considered to be outside the Customs territory; however, certain provisions of the law of the country concerned may remain applicable, for example dangerous materials, prohibited goods, etc. Although outside Customs area, Customs is required to carry out certain controls within the free zone to ensure that the operations carried out are in accordance with the requirements laid down, inventory controls for example. Generally speaking the Customs control exercised over goods placed in free zones is more flexible than that applicable to goods stored in Customs bonded warehouses or admitted under the temporary importation for processing.

The free zone provides the importer with the ability to take advantage of being able to have access to and process imported goods without prior duty payment. The benefits of being able to do so are significant when compared to the alternative of duty payment and later recovery of the duty paid through duty drawback procedures.

Egyptian Customs Law includes provisions for several means of importation of goods without Customs Formal Entry and duty payment. These include the Egyptian Economic Processing Zones (Free Zones), Bonded Warehouses and temporary importations. The conditions and time limits under which the goods are released for each vary, do the activity that may be carried out through the respective provision, and therefore each must be considered separately.

The foregoing provisions are intended to assist the business community in their efforts to be involved in international trade, trade that is essential to the nation's economy. In the interest of appearing to be a good global trader in the eyes of world trade organizations, it is essential that Customs processing related to these special provisions of the law be carried out efficiently so as not to deter the normal course of business. To this extent Customs must take advantage of modern business practices to accomplish required controls over goods that either transit or enter the home market of Egypt.

In accordance with WTO, WCO and GATT, modern day Customs enforcement includes Informed Compliance, Risk Management, Guaranteeing/Bonding Instruments, Post Audit, and most importantly the development of integrity and professionalism that gains the respect of the business public. Each is a part of a modernization process that progressive nations have found to be advantageous in carrying out the mission of Customs. The compelling reason to move forward toward complete modernization in Customs processing is to deal with the steadily increasing volume of international business by developed and developing countries, business needed to sustain the economic level desired by nations.

Communication between the importing business community and the Customs Service is an important element in the move toward developing more efficient systems for control and accountability. The importing business community must be provided with full and accurate information on the importer's choices (consumption entry, zones, in-transit bonding, etc.) available once imported merchandise reaches Egypt, and the procedures required to comply with requirements for release of merchandise. The communication level between Customs and the importing business must advance to the level at which each is able to openly discuss the needs of both parties - the importer-businessman and the Customs representative who is charged with carrying out the law of the country.

##### General Comment on Zones

The terms Foreign-Trade Zones, Export Processing Zones, Free Trade Zones, Free Zones and Economic Processing Zones are essentially the same and therefore throughout this document all will be referred to as zone. The term Economic Processing Zone exemplifies that emphasis has shifted from a traditional import/export concept to that of manufacturing and general business development primarily targeted toward economic development. The benefits of the zone often include an increase in production efficiency, lower cost of

doing business, and an increc, in employment within the country of location. Zones in most countries are privately owned facilities with the prim; purpose being to enable growth in commerce and employment opportunity in the host country. Progress governments view the economic development attributes, which result in taxation gains from increased employmi and a stronger national economy, to more than offset the possible reduction in Customs duty collections. Effective Customs collections may diminish somewhat but this is more than offset by increased revenue being collected by 1 treasury of the government through tax sources.

## **Zones Around the World**

Some zones are no more than duty free holding areas, usually located at or near a seaport. Others offer the abi to process goods or manufacture goods in a duty free environment, and sometimes-subsidized environment, for bi domestic and export purposes at various locations within the country. In operation, zones should be viewed being an enclave, similar to an independent island, with Customs controls being primarily focused on the wl leaves the enclave to enter the commerce of the importing country. Obviously this is somewhat of an ov simplification because in practice it is necessary that additional controls be in place for supervision of invent controls, identification of illegal practices, and compliance. However, these may be accomplished through r management, audit/inspection systems, and the requirement that all zone users have a continuous surety be (guarantee) posted with Customs to ensure compliance and to protect the revenue.

Zones may be established primarily for the holding of goods in duty free status pending a decision on whether goc they will either be exported from the zone, entered for domestic consumption, or they may be established manufacturing purposes. Many manufacturing zones are located at a previously existing company owned faci that was given zone designation; others are located in general use zone areas established for national econor benefit reasons.

Zone users in some countries receive no subsidized benefits; however, they do benefit from deferral of duty paymi and in some instances a lower tariff classification of material consumed in manufacturing. In other countries, why zones are established primarily for export, the zones may be heavily subsidized through the government provid land at no cost and/or tax exemptions (possibly contrary to WTO and Kyoto Convention provisions). Generc speaking, the motivation of the government in approval of a manufacturing zone is to stimulate the economy of 1 nation through increased capital investment and increased labor demand. Zones in some countries allow imporl equipment intended to be used for production purposes in the zone to be exempt from duty, others may require d to be paid on equipment used for production in the zone.

The tariff classification, or application of duty rate on goods produced in a zone and entered for dome: consumption, also varies. In some countries the tariff classification on imported parts is fixed at the time the pa arrive in the zone. Other countries may permit the zone user to choose as to whether the parts used assembly/manufacture will be classified in the condition as imported, or at the duty rate of the finished product. 1 latter offers some duty avoidance as an incentive to the zone user to produce goods that will be entered consumption in the country in which the zone is located, as opposed to choosing to assemble the finished good another country.

## **Economic Processing Zones/Free Zones in Egypt**

Free zones are becoming an important part of the Egyptian economy. A report completed at the end of June, 200<sup>1</sup> stated that the number of companies established in free zones was 851. Of these, 587 companies have actually started production and that the activity has created 83,000 jobs. It is estimated that the other 264 investment companies under construction will create another 39,000 jobs.

Applications to locate in a free zone are presented to the General Authority for Investment and Free Zone (GAFI) Board of Directors for consideration, and approval or denial. The application must clearly state the type of activity, estimated number of employees, and other general information. In granting the land use and authority to locate in the free zone the GAR includes a limitation on the volume of production that may enter the domestic market of Eg., and the percentage that must be exported.

Zones in Egypt are authorized by Law 8 of 1997 which regulates operations in the free trade zones of Egypt . allows for storage, warehousing, mixing, repackaging, assembly, and manufacturing for export; and provision services to firms located in the free zones. There are a number of free trade zones in Egypt , including those Cairo ( Nasr City ), Alexandria , Port Said , Suez , Ismailia and Damietta .

Goods imported into the free zones or exported from the zone are not subject to normal import/export customs procedures, duties or other taxes and fees. Likewise all instruments such as production machinery, product equipment, and transportation equipment used in establishments authorized to be free zones, are exempt from Customs and taxes. Provisions of the labor law do not apply to companies operating in the free zone and they are not subject to currency transaction controls. Commodities manufactured and/or stored in the free zones are considered "imports" subject to full Customs duties if they enter the commerce of Egypt.

There is a 1 % administrative cost to zone users for operating in the zone environment. The fee is assessed on the added value to material and goods used in the zone for production purposes. Merchandise inspected in a zone and found to not meet specifications is subject to duty, even if destroyed in the zone, unless exported from the zone.

To better understand the zone concept in Egypt, visits were made to three Egyptian cities where meetings were held with Customs management and also with zone management. The cities visited were Alexandria, Port Said and Suez; at each location we found all personnel to be most cooperative in supporting our research.

- Alexandria. The Alexandria free zone is located approximately 25 miles from the seaport; imported goods are transported from the seaport to the zone by trucks under Customs control through a bond (guarantee) and release/delivery controls, in addition to the vehicle being accompanied by a Customs representative. Although there is a guarantee, it is a practice to have the transportation accompanied by a Customs representative to ensure delivery to the destination. To support the large volume of activity a number of customs brokers, freight forwarders, and insurance companies are located at the entrance of the zone. Our visit to the zone included a tour of a large textile plant which included an area for spinning raw cotton into yarn, weaving yarn into fabric, and with the fabric producing very high quality table clothes, bed linens and various other cotton goods. All materials used in production are of Egyptian origin and 100% of goods produced are exported. The company employs several thousand workers. The factory visited was only one of a number of factories in the zone.
- Port Said. The Port Said free zone is unique in being located on the Suez Canal within the seaport area of Port Said. The zone is a secure area in which a large number of factories are located, the activity in the zone ranges from metal manufacturing to textiles manufacturing. While in the zone we were given a tour of a garment factory, which produced denim goods (blue jeans, jackets, etc.) for export, primarily to the United States. According to information received in Port Said, the total investment in the zone has been approximately 467 million dollars; approximately 16,000 persons are employed in the zone.

The city of Port Said is a free port city and because of this, part of the garment factory production is sold to vendors there because sales to a free port require no formal Customs clearance. The entire city of Port Said is secured by a fence, all vehicles leaving the city depart through one of eight Customs control points that are similar to a typical Customs border crossing.

El Gamil Exit	6 lanes for passengers - 3 lanes for cargo
El Rasswa Exit	4 lanes for car- 2 lanes for military personnel
El Nasr Exit	4 lanes for passengers - 2 lanes for cargo
El Kobouty Exit	3 lanes for commercial vehicles only
El Manzala Exit	For small boats and their passengers
East Ramification Exit Railway Station Bus Station	1 lane

At each location there is a secondary inspection area to which vehicles may be directed for thorough inspection.

Suez. The public zone in Suez has very limited activity, however, there are plans for the revitalization of the facility. The facility as it exists at this time is a secure fenced area that includes many structures, some occupied and many vacant and in need of repair.

Although not visited, the Free Zone in Ismailia is growing in activity. According to an article in the July 31, 2000 issue of the Egyptian Gazette, the General Authority for Investments and Free Zones (GAFI) announced two projects, "...Chairman Ghamrawi said that the first project involves the assembling and manufacturing of electrical generators, with over 50% of products being exported. The enterprise has a capital of US\$2 million and will create 50 new jobs. He added that the second project, concerned with maritime transport, is expected to generate 75 new jobs."

For Egypt, free zones have resulted in very significant investment in factories and with the investment there have been thousands of jobs made available in the zones. There are two types of zones, one is the General Zone, which is for use by the general business community, and the other is the Private Zone, which is for the benefit of a single company. Within the General Zones land is made available at a very low lease cost to investors willing to build and operate a factory that will manufacture goods primarily for export.

Some of the incentives for companies to locate in an Egyptian Free Zone include:

- Long term lease of real estate within the zone at virtually no cost to the company that will build a factory in the zone. The land on which the manufacturer constructs the factory may be leased for 20 years with the option for renewal at the end of the term.
- Unrestricted occupancy not limited to use only by Egyptian investors.
- Freedom to import foreign components used in goods to be exported free of duty.
- Capital assets benefits. All articles, supplies, and machinery used in production are exempted from Customs duties, sales taxes, and other taxes.

The foregoing incentives, and others not specified are such that the monetary benefits do in fact make zones attractive to new factories, in particular textile oriented operations. However, it should be noted that with the benefits come restrictions that control the percentage of what part of production in the free zone is allowed to enter domestic commerce and what percentage is required to be exported.

The structure of the Egyptian Free Zone is such that consideration should be given to review of whether the incentives and restrictions offered by the Egyptian government fall within the GATT Definition of a Subsidy.

To fully comply with Kyoto Convention and GATT initiatives, to the greatest extent possible zones should be owned and operated by private owners with minimal governmental administrative intervention to avoid there be subsidization of goods exported from the zone. Government involvement should be limited to the authorization of zone locations, gathering of statistical information related to zone activity, and normal labor, safety, environmental and similar regulations, and Customs administration. Customs role in operations would ideally be limited to ensuring that proper inventory controls are in place for control purposes and the collection of duties following GATT valuation and classification procedures on goods imported from the zone and entering the commerce of Egypt. The task of inventory controls, physical and inventory records, should to the greatest extent possible be the responsibility of the zone user, with Customs involvement being limited to spot-checks in post audits to ensure accuracy of the records of the importer/zone user.

### **Overview of Existing Economic Processing Zone Concept**

Historically imports and exports in Egyptian zones have not grown significantly and the value of exports overall has grown more slowly than have imports. Often this limitation was due to an overabundance of administrative controls that were such that it was a disincentive to zone use even though there may have been a small monetary benefit to the potential zone user. Egyptian zones in the past tended to be government owned and managed with the activities taking place within being conducted by private interests.

Newer zone construction has tended to be privately owned because of potential profit incentives and also because privatization has resulted in improvements in management and operations, thereby making the zone more attractive to zone users. Under current law, all foreign and domestic investors have equal access to use of zones and the ability to invest in them for the benefit of the economy of the nation.

## **Considerations for Future Zone Growth and Development\_**

For zone growth to take place in the future it will be necessary to identify and place into practice those attributes that have made zones economically beneficial in other countries. This includes extension of the privatized approach operations, including private ownership and management of the zone locations. In structuring a zone program consideration should be given to what best serves the businesses that are potential zone users within the parameters of the various trade agreements. To accommodate the users, several types of zones should ideally be available, including zone sites that are approved for the benefit of a single user (an existing factory) as well as zone areas that may consist of an industrial area that could accommodate many businesses, both small and large.

## **Customs Involvement in Zone Operations\_**

Government intervention in zone operations should be very limited in order to allow private firms to have the freedom to adopt internationally acceptable commercial behavior enjoyed by zone users in other countries. Following the precept, the adopting of an audit/inspection system is the ideal for zone operations. The audit/inspection system places the burden of accurate inventory control and record keeping on the zone user. Customs activity in an audit/inspection environment would normally consist of periodic spot-checks to verify the physical inventory quantity against inventory records of the zone user and to verify the records for goods removed from the zone are supported by a Customs release authorization. To protect Customs interests and to ensure compliance there must be means of guarantee, such as a continuous surety bond on which charges (liquidated damages) could be assessed in the event of non-compliance on the part of the zone user.

## **GATT - WTO - WCO - KYOTO Convention Considerations**

The Kyoto Convention describes a free zone as part of the national territory of a country where any goods introduced are generally regarded, insofar as import duties and taxes are concerned, as being outside the Customs territory. Imported goods in a free zone do not become subject to national customs laws and the payment of duties until they enter the Customs territory. WTO member countries may not limit free zone activities only to exports, under the GATT Agreement on Subsidies and Countervailing Measures.

The GATT Customs Valuation Agreement provides that the transaction value of imported goods will be the price paid or payable for the goods when sold for *export to the country of importation* (note: this would include goods that enter from the free zone into the domestic market of the country). Here the question arises as to whether the value would be based on the transaction value at the time goods arrive in the free zone or whether it is the transaction value that brought a product that contains imported goods from the zone to domestic territory. The latter would in probability require deductions from the value, for example deducting all costs and/or value added in the free zone; this may then bring the Customs value back to the transaction that brought the goods into the zone.

Most countries exempt goods of domestic (national) origin from the payment of duty when they are returned from a free zone to the Customs territory, whether or not they have been combined or manufactured with goods of foreign origin. "Goods of national origin" includes both goods, which were produced in the Customs territory, and goods which were previously imported into the Customs territory but on which all duties and taxes were paid upon their introduction into the Customs territory, but were later sent to a free zone. The exemption is available so as not to place free zone firms at a disadvantage when competing with goods produced in the Customs territory. Thus, the cost value of goods of national origin will be deducted from the Customs value of the goods to arrive at their dutiable value.

The dutiable value of foreign components, whether from one or several foreign countries, included in the goods manufactured in the zone and later transferred to the Customs territory is considered by most countries to be the sum of the prices paid or payable for the foreign goods in the transaction, which caused them to be admitted to the free zone. The duty rate applied to the value(s) may vary, depending on the provisions of the law of the country which the free zone is located. Some may require that the duty rate (tariff classification) applicable to the goods transferred from the zone to the country in which the zone is located to be that of the article removed to the country. Others may permit the components used in the article removed from the zone to be classified at the rate applicable for the parts when received in the zone, or to be classified at the rate of the finished article, the choice would be that of the owner of the merchandise.

When goods have been damaged or become deteriorated in a free zone, most countries allow a reduction in the dutiable value of the goods to approximate the market value of the goods in their damaged or deteriorated condition. When recoverable scrap or waste is produced in the zone, most countries consider the dutiable value to be the price paid or payable in the transaction, which caused the scrap or waste to be transferred from the free zone to the Customs territory. Recoverable scrap is scrap that has value for recycling or other use. Normally the value and the resulting duty rate are such that the applicable duty is minimal. Most countries consider any good that has been completely destroyed in a zone, either intentionally or not, to not be treated as an importation and therefore is not subject to duty, this would be by reason that the good has not entered the commerce of the country.

## **2. Customs Bonded Warehouses**

The Customs Authority supervises both public and private bonded warehouses. The Ministry of Finance authorizes the establishment of the warehouses, specifying the site of the bonded area, conditions of storage, storage charges, administrative charges, expenditures, guarantees to be presented, and other conditions relating to warehouses under bond. Imported and domestically produced commodities, which may be bonded in either public or private sector bonded warehouses, may not be withdrawn from bond unless the necessary taxes and fees are paid, unless withdrawn for export. The period of stay for goods deposited in the bonded warehouse is limited to six months; however, this may be extended for another three months when required upon approval of an application tendered to the Minister of Finance. Certain goods may not be stored in a bonded warehouse, including explosives, flammable materials, and other goods that may be of a dangerous nature. The activity that may be carried out in a bonded warehouse includes mixing of certain imported and domestic goods for the purpose of export, repackaging, and various limited other activities.

In review it was found that bonded warehouses are not utilized extensively in Egypt. Therefore, the needs for bonded warehouse Customs control would be limited; however, review should be made of the applicable procedures, Customs supervision, procedures for receipt and delivery of goods, and the bonding methods available.

## **3. Temporary Importations**

Temporary Importations or Temporary Exemption is the means used for goods to be released into the commerce of Egypt for processing, items imported for repair, or for completing their manufacture. In taking advantage of this provision, the importer is required to deposit with Customs a bond or guarantee covering the amount of taxes and duties, which would be due if the goods had been entered for consumption.

A condition of the provision is that the goods imported under the bond must be transferred to a free zone or exported within a one-year period; however, the one-year term may be extended by virtue of a decree of the Ministry of Treasury. Exportation of the goods within the one-year period or extension thereof cancels the obligation of the bond or guarantee.

## **Conclusions**

The following is a statement of the needs of Egyptian Customs to ensure the economic growth of Egypt and also comply with the various trade agreements. In regard to free zones, there is the need to present the opportunity to investors, both domestic and foreign, to establish business in a duty-free environment where imported and domestic goods may be used for further manufacturing or assembly of products that may then be either exported or enter for domestic consumption.

In following the spirit of the Kyoto Convention, there should be a free market from the zone to the domestic market as well as the export market. Ideally the environment should be similar to that of normal business practices in Egypt, that being private ownership and operation of duty-free facilities, with the government's involvement limited to the extent required to fulfill government agency requirements. It is essential that there be equal treatment given to foreign investors and local investors in order to encourage foreign manufacturers to invest in product plants which would then use domestic labor. Local industry gains from foreign investment through the need for a foreign investor to source much of their material requirements from local sources and vendors.

The specific needs are based on conclusions reached through communication with customs officers and management, free trade zone managers, free trade zone factory operators, and visits to operating zone facilities.

- Develop a plan that minimizes Customs staffing at free zones. The plan should be based on audit-inspection systems designed specifically for zone and bonded warehouse activity. With the use of audit-inspection, the staffing requirement would be very minimal if rules are developed for the record keeping systems of the zone user supported by a bond/guarantee to ensure compliance. With audit-inspection implementation there comes the need to recommend staffing requirements for zone and bonded warehouse supervision, and recommendation as to whether on site Customs personnel are needed.
- Develop system to expedite the processing and release of goods consigned to the zone or bonded warehouse. Unlike imported goods released for consumption, goods transferred from the first port of arrival the zone may be moved under in-bond control through use of locked and sealed containers that offer shipment integrity. Shipments to the zone are normally available for examination at later date, if needed. Review and recommendation of bonding requirements is needed along with development of procedures to be followed.
- Develop a system of surety bonding. There is a need for a universal type bond that could be used for a number of purposes, including free zone, bonded warehouse, temporary importation, transportation and similar transactions. The Protocol of Amendment to the International Convention on the Simplification of Customs Systems provides for the use of security means to protect the interests of the Customs Service.

The bond must have conditions that provide Customs satisfaction on claims for failure to comply with the terms of the bond. For example, release of merchandise from zone without Customs Permit, shortages in zone or warehouse inventory, failure to comply with record-keeping requirements, failure to deliver imported goods transported under bond, failure to re-deliver goods upon Customs demand, etc. There is the need to develop guidelines for bond amounts that will protect the interests of the government, normally this would be an amount greater than the tax and duty, perhaps the bond amount should be estimated tax and duty in addition to the domestic value. In this way, example, should goods transferred in bond not be delivered to the destination within the allowed time period, a claim by Customs against the carrier could be for the value of the shipment plus the tax and duty. With the system of bonding there needs to be a system developed that allows the violator to petition for mitigation or cancellation of the claim for liquidated damages made by Customs, along with guidelines for mitigation by a Customs manager.

- Develop a bonded system for transportation of imported goods from the first port of arrival to the zone bonded warehouse or vehicles in transit that will result in prompt release for transportation, and for delivery merchandise to the destination. A system is needed that would control goods solely by a bond/guarantee document system rather than relying on personnel to accompany the shipment. This could be accomplished through a bonded transportation system or in the case of zone goods, through an extension of the zone surety bond. For the latter, the transportation would constructively be an extension of the zone inventory system resulting in the inventory control record being extended to the point of first arrival in Egypt on imports and the port of lading for exports. In operation, for goods destined to the zone the user would be responsible for the quantity released from the importing carrier and for goods exported from the zone the user would be responsible for quantities until delivered to the exporting carrier. In the event of failure of delivery to the destination, liquidated damages, based on a developed proposed schedule, could be claimed against the bond.

In the development of the transportation in bond system it is essential to identify the responsibilities of the bonded carrier and the action that would relieve the transportation company from claims by Customs against the bond. It should identify what action obligates the bond (release of goods from the importing carrier to the bonded carrier) and what action relieves further obligation (the transfer of possession from the bonded carrier to the party liable for destination).

- Develop a Zone Procedures Manual and Bonded Warehouse Procedures Manual. Recognizing the complexities that may be involved in zone operations and bonded warehouses, and the need for clarity for the benefit of both Customs and the zone occupant, it is necessary that there be a clear and concise procedure manual available. The manual should be made available to all Customs personnel involved in

zc operations, along with those utilizing the zone and those considering its use. Particular attention should be given to describing a standard format (manual or automated) for the zone or warehouse operator to use inventory control records and storage of goods in the zone. Along with procedures to be followed, the man should clearly set forth the activities that may be carried out within the zone or bonded warehouse.

- Develop a Free Zone Application Manual or Pamphlet. The document should fully describe where a zc may be located, the requirements of the applicant, i.e. surety bond requirement, relationship between 1 zone operator and the zone user, zone operator responsibilities, etc. The manual should also describe 1 application process, including form or type of letter to be used for application, who is required to sign as 1 applicant, of procedures to be followed by the applicant who may wish to establish a zone site, and whc responsible for review and approval or denial of the application.

### **Summary**

The cited needs are intended to assist in efforts to bring the Customs Service of the GOE to the level that will re: in conformity with various trade agreements and changes to result in efficiencies that will minimize the cost fulfilling Customs enforcement and collection obligations. The foregoing will in turn assist the efforts of the GOE efforts to reach their goals of economic growth.

## Chapter 7

### A Recommended Program of Assistance For the Reform of the Egyptian Customs Authority

#### Customs Needs Assessment Team

##### Introduction

The following program is recommended to provide the Egyptian Customs Authority (Customs) with the assistance they will need to meet the challenges of new and modern processes and procedures. Specifically, the automation of the processes and procedures of Customs, and, the overwhelming impact of the change over to the transaction value of merchandise as found in the Agreement on Implementation of Article VII of the General Agreement Tariffs and Trade 1994 (GATT)

The assistance is in four general areas that will affect the overall operational and administrative efficiency of the organization. The four areas are:

- Training,
- Classification and Valuation of merchandise,
- Automation, and
- Organizational structures (infrastructures).

Five advisors are recommended in this assistance program. The positions are; a training advisor, an import specialist, a customs risk management/revenue protection specialist, a specialist in automated information systems and information technology and a lawyer.

##### Timeline

A three calendar year project is recommended, with the potential for a one-year extension.

##### Training

In order to modernize the workforce of Customs, to enable them to effectively meet the challenge of the new processes and procedures found in GATT and Harmonized Tariff Systems (HTS), it is important that career fields established in specialized areas of expertise. These career fields are necessary to provide the level of expertise to examine, classify, and value merchandise correctly; and, to provide the compliance elements of audit, selection and investigation to the process that will assure risk management for revenue protection. Some of these career fields are new to Egyptian Customs and others are in need of intense training in the new systems. It is felt that the existing training institutes will need to change methodologies and training concepts in order to meet the demands of the immediate future.

The training portion of the recommended assistance program is a key element to Customs becoming fully **compliant, with the GATT.**

##### Advisory Assistance: Customs Training Specialist

This position calls for an experienced training advisor. Minimum qualifications should include at least four years of experience in US Customs Training at the Academy level in one of the field operational

programs (Inspector, Spec Agent, or Import Specialist) as an instructor/course developer, supervisory instructor, Program Director, or higher. college degree is required; postgraduate degree in Education or Adult Education is preferred.

### **Performance**

Program Gains:

- To Provide Continuity and Standardization of Training Programs.
- To Meet the Training Needs Demanded by GATT Compliance
- To Produce Higher Quality Training
- Provide Shorter, More Focused Courses in Specific Fields
- To Produce Better Trained, More Efficient Employees

The person selected will (outputs):

- Lead Egyptian Customs Training Personnel through a full Training Needs Assessment.
- Design, establish and teach a full Instructor Development Program, from basic Instructor training throe, design of modules, courses, and curriculum.
- Assist in the design and production of training materials.
- Lead Customs Training Personnel through a transition from present training systems to a full task relal training curriculum in each career field.
- Assist in the task analysis of each training program.
- Recommend, and instruct training personnel in the design, production and use of training aides.
- Assist in determining career level training programs in each career field.
- Provide reports to USAID and Egyptian Customs Management of program gain accomplishment.

**Level of Effort:** This position will be for the full three-year program tenure (36 man months).

### **Material inputs:**

- Training Equipment:
  - 15 Personal Computers, with appropriate software,

- 5 Video Tape Cameras with lights and tripods,  
100 tape cartridges
- 5 Video Monitors
- 5 Slide Projectors
- 5 Overhead Projectors, w/5 replacement lamps each
- 1 PowerPoint Projector
- Audio/Visual Supplies, misc.
- Training Material Production
  - Funding for the production or reproduction of manuals
  - Funding for translation of material
  - Funding of translator services.
- Domestic Training Off-Site
  - Funding to produce off-site training

#### Classification and Valuation of Merchandise (HTS and GATT Compliance)

The implementation of the Valuation Agreement can be viewed as an opportunity to initiate reform, to reorient the commercial cargo process, and to further develop and modernize the Customs Department. The Valuation Agreement alters the methodology of valuation of imports entering Egypt. The primary basis for valuation of goods for Customs purposes is the transaction value of imported goods i.e. the price actually paid or payable for the imported goods sold for export to the country of importation adjusted in accordance with the provisions of Article 8 of the Valuation Agreement. The Agreement specifies six methods of valuation but before a Customs official can reject the transaction value and apply another method of valuation in strict sequential order he must first determine if the transaction value may not exist for the imported good, provide the importer with an opportunity to supply additional information, and only when that information is not provided or does not substantiate the invoice price as reflecting the price paid or payable move to apply the next method of valuation.

This will require some guidance and assistance from a knowledgeable person experienced in the transition to the new system.

#### **Advisory Assistance: Import Specialist**

This position calls for a person with at least ten years experience in US Customs as an Import Specialist, since 1976. A college degree is required, with a post-graduate degree preferred. International experience in a developing nation facing GATT transition would be a plus.

### **Performance**

Program Gains:

- To Provide Expertise in the Use of the System,
- To Provide Guidance to Management in Process and Procedures.
- To Assist in the Development of Basic and Advanced Training in the Classification and Valuation Field
- To Assist Customs Management in Bringing Laws, Decrees, and Officer Guidance Into Compliance with WTO Guidelines.
- To Offer Assistance in Technical Issues of Value Determination.
- To Assist in Developing Trade Seminars and Industrial Information Workshops.

The person selected will (outputs):

- Lead Customs in the Development of Resources and Tools.
- Assist Customs in the Development of Conditional Release Capabilities
- Advise Customs in the Development of Analysis and Research Capability Within the Processing Units.
- Assist in the Development of a Binding Rulings Process.
- Assist in Developing Expertise in the Field of Classification and Valuation.
- Design and Present at Least Two Trade Seminars During the Assigned Period.
- Assist Customs in the Formation of a Team Approach to Classification and Valuation, Working within the Commodity Lines.
- Assist Customs Supervisors in Learning Accurate Review Standards for Valuation.
- Provide Reports to USAID and Customs Management of Program Gains and Challenges.

### **Level of Effort**

This position will be for a one-year period during the first year of the project, and 60 days each during the following two years (18 man months).

## **Material Inputs**

- International Reference Materials:
  - o WTO/WCO pamphlets, manuals, guidance materials on videotape, film and all media.
  - o Web site development for Trade use.

## **Funding Inputs**

- Two Trade Seminar Productions
- Hands on Training Visits to selected Arab Gulf nations for 4 Customs personnel for observation of process.

### **Compliance (Revenue Protection and Risk Management)**

As Customs moves toward full compliance with the requirements of the GATT system, then steps must be taken protect the revenue of the nation through the re-structuring of the processing unit to include risk management through intelligence, selectivity, and audit. This is particularly important to a nation such as Egypt, where Duty e taxes collected by Customs have a significant impact on GNP.

Compliance is a new skill subject to Customs, therefore requiring infrastructure changes and the development function skills as rapidly as possible. This subject also has a training impact as new skills are called for.

### **Advisory Assistance: Risk Management/Revenue Protection Specialist**

This position calls for a person with extensive risk management and revenue protection experience. The candid; should have at least ten years experience as a Customs Special Agent, Auditor, or Intelligence Officer. A colle degree is required.

## **Performance**

### **Program Gains:**

- To develop systems of selectivity for review, verification, and audit that will allow the GATT system to funct as smoothly as possible while using spot checks and random systems as a cross check of the veracity declared information.
- To develop the expertise in commercial international customs intelligence that will allow for the interchange information with other customs services.
- To develop the use of audit principals in the area of Post Declaration verification of information supplied importers.
- Adding transparency to the Customs processing procedures.
- Adding the ability to follow through on serious commercial fraud cases.

The person selected will (outputs):

- Recommend the organizational structure and placement of the compliance units.
- Assist in the training of personnel assigned to the units.
- Assist in the development of training courses and training manuals related to the subject matter.
- Advise the automation committee in the development of databases and selectivity criteria.
- Advise unit managers in the development of guidelines for sharing information with trade users.
- Help unit managers develop guidelines for treatment of errors and unintentional violations to differences between mistake and purposeful misinformation for gain (fraud).
- Assist the legal advisor in the development of guidelines for the application of fines and penalties to violator
- Work with the C&V advisor to clarify the guidelines for Customs Officers in the acceptance of declaratio verification when called for, and the inter-relationship between the two units.

#### **Level of Effort**

This position will be for three man months, followed by an additional three months, six months after the f assignment. An additional three man months will be used in the second year of the project tenure, and a final of month at the end of the third year (total 10 man months).

- **Material inputs**
- Production of manuals, informational materials.
- Purchase of commercial training data.
- Translator services.
- Specific office equipment used in audit function.
- Investigative equipment.
- Intelligence international database cost.

#### **Automation**

The Egyptian Customs Administration is automating its business requirements and procedures for import and exp control and trade facilitation. The Minister of Finance and the Commissioner of Customs have committed expedited cargo processing, to use risk management techniques in compliance enforcement, to use automation facilitate trade and compliance with GATT agreement conditions, and to create greater transparency and uniform in the treatment of the importing trade community. This institutional commitment is evident and being implemented

### **Software Support**

The National Cash Register Company (NCR) and its sub-contractor Tabarak Computer Systems have been engaged by Customs to facilitate this effort in both hardware acquisition, telecommunications, and softw, development, since 1998. Using the automated case tool POWER DESIGNER, the contractor has designed pilot-tested an Enterprise System Model with 36 interrelated modules to support Customs processing, throughout 1 full range of functions. Local and wide area networks link notes on the current system, which is running on a UP operating system with communication elements from CISCO. Flat files have been converted to relational databa: using CYBASE. The existing applications have been replaced with relational database applications spanning 1 spectrum of current Customs business procedures. The business area was also expanded to include back-off applications. In-Transit, Temporary Admission, and Drawback modules are included. Graphic user interfc, technology is used throughout to simplify process presentation in a PC environment. Functional access is control by a commercial security package that works off personnel, organizational structure, and application componi databases to define and manage job, user, and workstation profiles. The Customs enterprise data model includ over 900 logical entities mapped into over 500 physical tables, hosting 5,500 data elements and over 14 relationship. In summary, most of a modern Customs processing system has been designed and pilot-test including a data warehouse Management Information System (MIS) for managers. Much of this system could installed by 2003, funding permitting. There are some components missing from this system, only because ft were not envisioned in 1998. The Recommendations section of this report specifies those components.

### **Hardware Base**

NCR has completed site preparation and equipment installations that now support import processing, softw, development, and communications for Customs operations in five clusters. There is an infrastructure including installed base of 450 PC's, supported by 35 servers, modems and peripherals that represent a capacity to develi conduct Customs business, expand services to Customs and Trade clients, and to share data with other governmi agencies. The equipment needed to support classroom training, on-the-job training, input of inspections findings Customs and GOEIC, inter-agency and trade data interchange, and to support managers, compliance monitor staff, audit support staff, classification and valuation operations is not yet available. These latter functions are significant interest to WTO.

### **Communication**

The network, MTIC, controlled by the Ministry of Telecommunication and Information Technology, provides intrai communication sufficient to serve the trade community, Customs, other agencies involved in processing imports a exports, as automation expands. The Post Office is seeking to serve this community by supporting document a data interchange and is EDI capable, a fact of interest to carriers. Another major agency involved in import a export control, The General Organization for Export and Import Control (GOEIC) is also committed to automat and shares the goal of selective processing for risk management. This agency is creating and uses a tra compliance performance database for assuring uniformity of treatment and the selection of transactions inspection or by-pass, according to a current frequency schedule. It is possible for this agency to either L databases and processes created by Customs or share their data with Customs directly or through the Post Offic Computers and linkages to the intranet, with communication among some 20 sites are needed.

## **Scope**

The Customs Administration has undertaken to provide a large range of information and data interchange in various groups of clients for these services. Importers and carrier agents can file data electronically for Customs processing. Importers and clearing agents can call up manifest and tariff data for use in preparing declarations. Kiosk web site has been created for dissemination of Customs related information to the commercial trade and general public. Teleconferencing capability for use in training, management communications, and policy/procedure dissemination has entered the planning stage.

## **Advisory Assistance: Automated Information Systems and Information Technology Systems Specialist**

This position calls for a minimum of ten years experience in the design, management and implementation of Automated Information Systems and Information Technology Systems in a Customs environment. It requires a depth of knowledge of hardware, software, interconnectivity, user design, and database function.

## **Performance.**

### Program Gains:

- All cargo data will be received electronically.
- Implement a rulings database accessible on-line to the trade.
- Implement priority for on-line filing of declarations.
- Implement pre-clearance procedures for on-line filers.
- Implementation of a fully electronic manifest database.
- Make the declaration files fully relational to all appropriate files and Agencies.
- Develop value historical database.
- Develop a commercial intelligence database with connectivity to WCO.
- Implement a compliance database with restricted partial access by the trade.
- Develop a financial database keyed to importer accounts.
- Implement a fully functioning electronic kiosk for public information of Customs requirements and dissemination of information.

### The person selected will (outputs):

- Serve as the principal advisor to the Customs executive automation committee.
- Assure the proper location, installation, and use of project-funded equipment related to automation.

- Act as a liaison between Customs and contractors to clarify technical questions and I. T. interests.
- Assist Customs in prioritizing implementation issues.
- Assist Customs in designing testing procedures for new software and automated processes.
- Help Customs to assure that automation development proceeds on schedule and in the best use direction.
- Assist Customs in developing a user service agreement with other agencies and the trade using the Custo Automated system.
- Assist Customs in the development of a hardware implementation prioritization program, to place hardware at the most advantageous location to meet operational priorities.
- Assist Customs in developing specific user requirements for contractor use.
- Assist Customs in developing in-house computer training programs and contracted basic computer user training programs.

**Level of Effort:** This position will be for the entire first year of the program (12 man months), and three months thereafter (18 man months total).

**Material Inputs:**

- Computers: 150 PCs the first year and 150 PCs the second year, and 150 PCs the third year.
- Contract with local computer training company having multiple locations within Egypt for basic computer training.

**Legal Authority and Guidance**

The interest and importance of this section of the project is to assure that the Laws, Implementing Decrees, and Customs Operational Guidance is in accord with the processes and procedures to be changed. Customs must have the legal authority and the Institutional approval to function within the guidelines of the GATT valuation system and WTO implementation notes.

It is important that those legislative and institutional authorities are not in conflict with the aims of the system, and provide the officers with clear guidance in the performance of their duties.

It is also fundamental to the success of the program that the penalties for violation of law be substantial, but allow the application of officers' judgment in determining intent and forgiving common error.

These indications of national policy and Customs management direction must encourage Officer independent judgment while increasing the transparency of transactions.

**Advisory Assistance: Lawyer**

This position calls for a licensed, practicing attorney, with Customs, Office of Regulations and Rulings, International Trade experience.

**Performance.**

Program gains:

- The clarification of laws rules and guidance to officers.
- The removal of conflicting legislation.
- Assurance that Officers have the authority needed to perform their duties.
- Remove disincentives to compliance through the use of Officers' judgment.

The person selected will (outputs):

- Review all existing laws, decrees, and guidance concerned with the process of entry of merchandise.
- Review all guidance to officers regarding procedure in the entry process.
- Review all legal guidance regarding fines, penalties and forfeitures.
- Advise the Customs Legislation Committee regarding the drafting of implementing decrees and institutio guidance.

### **Level of Effort**

This position will have a 90 day (three man months) assignment.

### **Material Inputs**

- Translation and Document production only.

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