21

International Trade Compliance

While it may be valid to say that the world is shrinking as a result of globalization and technological advancements, conducting international business has definitely become more complex over the past decade. There are a myriad of local and international regulatory requirements to consider in any given transaction. Security and safety have become top priorities in an era marked by terrorism and recalls of toxic toys. Further, the industrialized global community has grown intolerant of bribery or any other forms of corruption in the international supply chain.

This chapter provides a high-level summary of the current compliance requirements facing international supply chain, discusses future trends in this arena, and offers opportunities to increase competitiveness while playing by the rules. Given the nature of this chapter as a supplemental appendix to the primary book, we will focus only on the main premises and offer links to numerous websites where readers may conduct more in-depth research into each focus area as desired.

No More Grease

If we had to provide the single greatest compliance risk facing those conducting international business, our first response would relate to corruption. Until recently, bribes were considered tax deductible in many industrialized nations, in Germany for example. However, in 2008, Siemens was targeted with some of the largest corruption-based fines, penalties, settlements, and disgorgements of all time, costing the company billions of Euros.[1] The U.S. Foreign Corrupt Practices Act of 1977 (FCPA) was one of the first anti-bribery statutes in the

world and has been for many years the gold standard of corruption requirements. The FCPA focuses primarily on prohibiting bribery of government officials for the purposes of obtaining or retaining business. Enforcement of the FCPA represents some of the highest penalties assessed on those conducting international business. The FCPA also offers some exceptions to its requirements, such as so-called *grease* or facilitation payments. An example of a grease payment might be the paying of a customs official $25 dollars on the side (where this is a normal, accepted local cultural practice) to expedite the clearance of your goods, something the official must do anyway.

The trend in this area is to eliminate all forms of bribery and corruption from the international supply chain: not just industry to government, but industry to industry, and no exceptions for things like facilitating payments. One example of this trend is the United Kingdom's 2010 Bribery Act, which establishes an offense for receiving, as well as giving, a bribe. In contrast to the FCPA, the new United Kingdom law criminalizes bribery of private individuals and companies (not just government officials), and there is no need to prove corrupt intent. Further, there is a strict liability for corporations who fail to prevent bribery and the extraterritorial provisions are far-reaching for companies and individuals.

Another trend in the area of anti-corruption is the global harmonization of requirements and expectations. This trend can be evidenced by the fact that at the time of writing, thirty-eight countries are parties to the Organisation for Economic Cooperation and Development's (OECD) Anti-Bribery Convention and have adopted OECD's 2009 Anti-Bribery Recommendations.[2] Further, there are currently 140 signatories to the United Nations Convention against Corruption.[3]

Despite these trends, corruption remains fairly prevalent.[4] Other than the Western World, the rest of the globe still maintains fairly high levels of corruption as an acceptable practice. This means that those engaged in international business must take great care to screen business partners, such as agents and intermediaries, to assure violations of the FCPA (or other local anti-corruption laws) are not occurring. If you don't, you may be faced with fines, penalties, disgorgements, and associated legal fees so great that the existence of your business is jeopardized.

Export Controls

Following the risk of corruption, it is fair to say that violation of export controls poses the biggest potential threat to those engaged in international business. The risk may be stated as simply as preventing the bad guys from getting hold of our most sensitive products and technologies. When we say bad guys, we are referring to terrorists, narcotic traffickers, and those nations and political actors who are suspected of supporting those activities.

Multilateral Export Control Regimes

Export controls are harmonized to a degree through multilateral export control regimes in which the United States and its allies participate. These regimes include the Wassenaar Arrangement,[5] the Nuclear Suppliers Group,[6] the Missile Technology Control Regime,[7] the Chemical Weapons Convention,[8] and the Australia Group.[9]

Export Control Classification

Within these regimes, a system of classification of goods and technologies has been developed for determining whether an export license is required to export the goods or transfer the technology to a given destination or end user. Within the United States, this classification system is currently comprised of two lists: the Commerce Control List (CCL) and the U.S. Munitions List (USML).

The USML controls the export of military items. It controls actual military equipment like tanks and mortars (see examples in Figure 21.1), as well as items that have been specifically designed, modified, or adapted for military end use. Licensing of items subject to the USML falls under the jurisdiction

CATEGORY IV—LAUNCH VEHICLES, GUIDED MISSILES, BALLISTIC MISSILES, ROCKETS, TORPEDOES, BOMBS AND MINES

*(a) Rockets (including but not limited to meteorological and other sounding rockets), bombs, grenades, torpedoes, depth charges, land and naval mines, as well as launchers for such defense articles, and demolition blocks and blasting caps. (See §121.11.)

*(b) Launch vehicles and missile and anti-missile systems including but not limited to guided, tactical and strategic missiles, launchers, and systems.

(c) Apparatus, devices, and materials for the handling, control, activation, monitoring, detection, protection, discharge, or detonation of the articles in paragraphs (a) and (b) of this category. (See §121.5.)

*(d) Missile and space launch vehicle powerplants.

*(e) Military explosive excavating devices.

Figure 21.1 Example description from the United States Munitions List

of the state department's Directorate of Defense Trade Controls (DDTC).[10] Licenses are generally required to export to all non-U.S. destinations.

The CCL controls the export of so-called dual use goods. Dual use goods generically refer to items that have a civil application, but they could also be used for a military (or other sensitive) end use (see examples in Figure 21.2). In practice, the CCL covers basically anything not covered by the USML. Under the CCL, products and technologies are assigned a classification referred to as an Export Control Classification Number (ECCN). Licensing requirements are determined by evaluating both the ECCN and the destination based on the reasons for control of a given product. For example, an ECCN of 1C350 covers certain chemicals that are either considered chemical weapons or their precursors. Chemicals classified as 1C350 may be exported to Canada or Sweden without a license, but they require a license to be exported to India or China. The general licensing policy of the U.S. government can be seen by reviewing the Commerce Country Chart (see Figure 21.3). The more Xs present for a given country, the more items that require a license to export to that country. The licensing of items subject to the CCL falls under the jurisdiction of the commerce department's Bureau of Industry and Security (BIS).[11]

2A290 Generators and other equipment specially designed, prepared, or intended for use with nuclear plants.

License Requirements

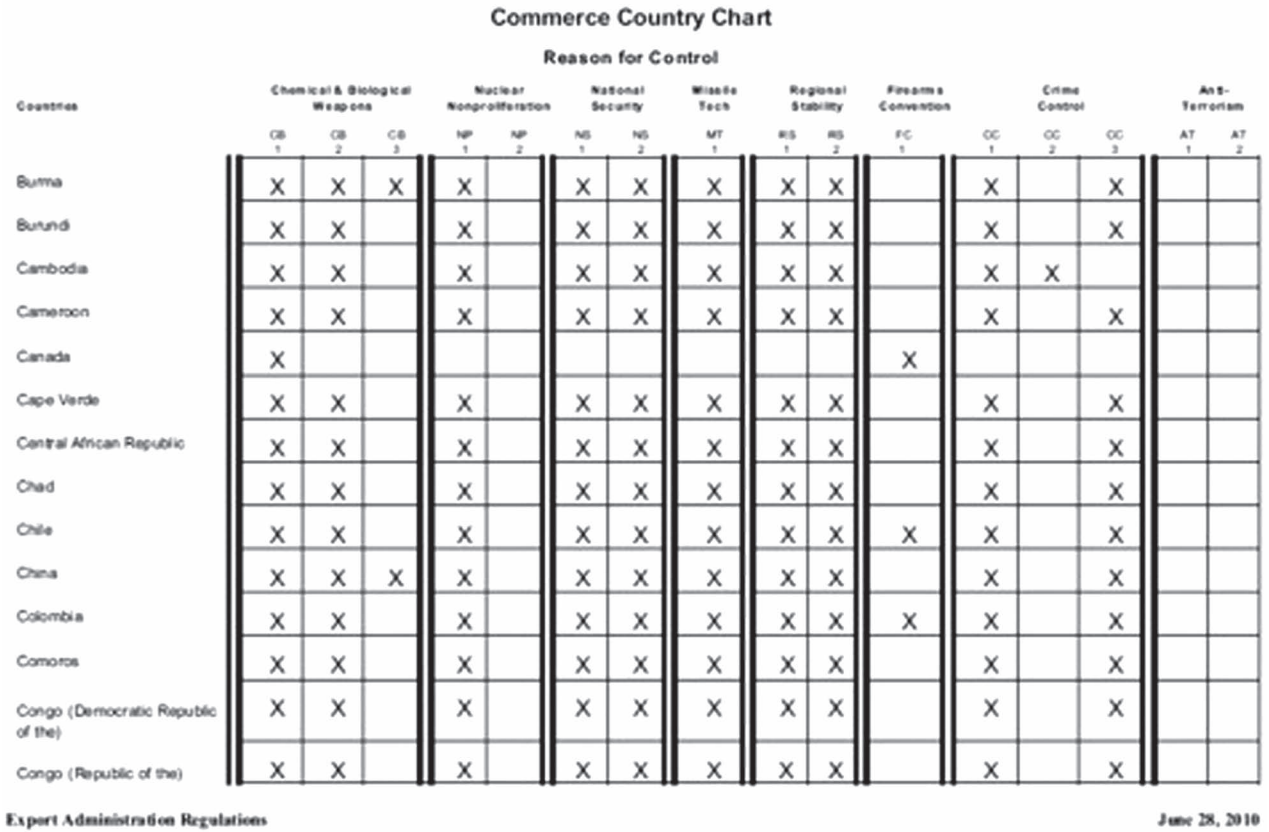
Reason for Control: NP, AT

Control(s)	*Country Chart*
NP applies to entire entry	NP Column 2
AT applies to entire entry	AT Column 1

License Exceptions

LVS: N/A
GBS: N/A
CIV: N/A

Figure 21.2 Example export control classification number from the Commerce Control List



Commerce Country Chart

Reason for Control

Countries	Chemical & Biological Weapons			Nuclear Nonproliferation		National Security		Missile Tech	Regional Stability		Firearms Convention	Crime Control			Anti-Terrorism	
	CB 1	CB 2	CB 3	NP 1	NP 2	NS 1	NS 2	MT 1	RS 1	RS 2	FC 1	CC 1	CC 2	CC 3	AT 1	AT 2
Burma	X	X	X	X		X	X	X	X	X		X		X		
Burundi	X	X		X		X	X	X	X	X		X		X		
Cambodia	X	X		X		X	X	X	X	X		X	X			
Cameroon	X	X		X		X	X	X	X	X		X		X		
Canada	X										X					
Cape Verde	X	X		X		X	X	X	X	X		X		X		
Central African Republic	X	X		X		X	X	X	X	X		X		X		
Chad	X	X		X		X	X	X	X	X		X		X		
Chile	X	X		X		X	X	X	X	X	X	X		X		
China	X	X	X	X		X	X	X	X	X		X		X		
Colombia	X	X		X		X	X	X	X	X	X	X		X		
Comoros	X	X		X		X	X	X	X	X		X		X		
Congo (Democratic Republic of the)	X	X		X		X	X	X	X	X		X		X		
Congo (Republic of the)	X	X		X		X	X	X	X	X		X		X		

Export Administration Regulations June 28, 2010

Figure 21.3 Example of the commerce country chart

Sanctioned Parties

Another complicating element of export controls is the fact that many U.S. government agencies maintain lists of sanctioned parties that may include individuals or companies. Rather than one single list of bad guys to check, there are many, making the screening of transactions against all the right lists a daunting task. The best-known list of sanctioned parties is the Specially Designated Nationals (SDN) list maintained by the Treasury Department's Office of Foreign Assets Control (OFAC).[12] The OFAC SDN list covers primarily terrorists and their supporters, drug traffickers, and global political bad actors. There are thousands of individuals and entities on the SDN list alone, and there are numerous other similar lists in both the United States and globally that should be consulted to make sure you are not doing business with someone you shouldn't.

Embargoed Nations

In addition to these list-based sanctions, the United States also maintains comprehensive (albeit unilateral) embargoes against Iran, Syria, Sudan, Cuba, and North Korea. Any dealings with these nations will generally require a license from the U.S. government and, unless for a humanitarian need such as food or medicine, the United States maintains a general policy of presumption of denial of any license applications. Licensing for dealings with these embargoed nations by U.S. persons and entities may fall under either OFAC or BIS jurisdiction—or possibly both depending on the country involved and the nature of the given transaction.

Extraterritorial U.S. Re-export Requirements[13]

The United States also asserts its export control requirements extraterritorially, such that the re-export of goods of U.S. origin from a second country to a third may require a re-export license. For example, you may supply a French firm with sophisticated electronic equipment. The export from the United States to France does not require a license, but if the French firm re-exports the equipment to Iran, the United States would assert jurisdiction over that transaction, requiring a license for the transaction. However, the U.S. government would likely refuse to grant the license because the United States does not want Iran to receive the electronic equipment.

Technology Transfers or *Deemed Exports*

The United States does not limit its control of exports to just tangible goods. The transfer of technology is also controlled on a similar basis. For example,

to transfer military technology to another country (or to a foreign national of another country while physically in the United States) will most likely require a license. Transfers of technology of a dual use, nonmilitary nature will depend upon the sensitivity of the technology and the country (or nationality) in question. For example, it is normally okay to transfer chemical production technology to our allies in Europe (i.e., NATO), but it likely requires a license to transfer satellite-related technology to a Pakistani national across the table in a conference room. The commerce department refers to the transfer of technology to a foreign national (while in the United States) as a *deemed export*,[14] and enforcement in this area is on the steady rise—although, this is an extremely difficult area to control and enforce given the proliferation and velocity of data transferred in today's instant, Internet-based society.

The Future of U.S. Export Controls

In his 2010 State of the Union address, President Obama declared, "We will double our exports over the next five years, an increase that will support two million jobs in America."[15] This initiative is referred to as the National Export Initiative (NEI). In conjunction with the NEI program, the Obama administration has also announced an initiative targeted at drastically revising the U.S. system of export controls, the Export Control Reform Initiative (ECRI). There are four main components of the ECRI strategy:

1. *Single Control List*, in essence combines the separate CCL and USML. The proposal seeks to harmonize definitions to end jurisdiction confusion between the two lists, and establishes new independent control criteria to be used to screen items for control into a new, tiered control list structure.
2. *Single Primary Enforcement Coordination Agency* seeks to consolidate certain enforcement activities into a Primary Enforcement Coordination Agency and thereby synchronize and de-conflict enforcement of U.S. export laws.
3. *Single Information Technology (IT) System* seeks to create a single electronic licensing system.
4. *Single Licensing Agency* combines separate licensing regimes, jurisdictions, and systems currently under the commerce (BIS), state (DDTC), and treasury (OFAC) departments.

In an August 31, 2010 video message to the trade community, President Obama outlined his plans for the ECRI, "For too long, we've had two very different control lists, with agencies fighting over who has jurisdiction. Decisions were delayed, sometimes for years, and industries lost their edge or moved abroad. Going forward, we will have a single, tiered, positive list—one which will allow us to build higher walls around the export of our most sensitive items

while allowing the export of less critical ones under less restrictive conditions. In the past, there was a lot of confusion about when a license was required. It depended on which agency you asked. Now, we will have a single set of licensing policies that will apply to each tier of control, bringing clarity and consistency across our system. In addition, I plan to sign an executive order that creates an Export Enforcement Coordination Center to coordinate and strengthen our enforcement efforts—and eliminate gaps and duplication—across all relevant departments and agencies. Finally, right now, export control licenses are managed by multiple, different IT systems or, in some cases, even on paper. Going forward, all agencies will transition to a single IT system, making it easier for exporters to seek licenses and ensuring that the government has the full information needed to make informed decisions. While there is still more work to be done, taken together, these reforms will focus our resources on the threats that matter most and help us work more effectively with our allies in the field. They'll bring transparency and coherence to a field of regulation, which has long been lacking both. And by enhancing the competitiveness of our manufacturing and technology sectors, they'll help us not just increase exports and create jobs but strengthen our national security as well. All of this represents significant progress. And as we implement these reforms and take further steps—including working to create a single licensing agency—I look forward to working with both congress and the export control community to ensure their success."

The future of these export reform initiatives remains uncertain, but there is a general consensus forming between both the government and private sectors that seems to point to some significant changes to the current U.S. export control regime being inevitable and likely happening sooner rather than later.

Customs Compliance

The next set of rules and regulations for those engaged in international business are the customs requirements. There are a virtual myriad of laws, regulations, and other requirements related to the importation of merchandise into any country. The rules are generally harmonized among the majority of countries of the world under agreements made at the World Trade Organization[16] and World Customs Organization (WCO).[17] For this appendix chapter, we'll focus on the U.S.-specific requirements with the understanding that similar rules likely apply in each nation you may have business with. While there are many requirements, we will focus on the primary requirements: classification, valuation, and origin/marking.

Classification

The foundational principle of customs compliance is the classification of goods. There is a numeric system of classification that forms the basis of the

identification of goods crossing borders along with trade statistics and tariff rates. This *Harmonized System* (HS) of classification is maintained by the WCO and agreed upon for use by WCO members. The system is intended to be harmonized globally at the six-digit level, and then individual countries can maintain systems that range from 8 to 11 digits for local customization, (e.g., tracking different statistics or providing for tariffs on specific items).

In the United States, the HS has been adopted by the Harmonized Tariff Schedule of the United States (HTSUS). The HTSUS is legislatively provided for by the U.S. Congress and the executive branch and carries the weight of law. The HTSUS is maintained by the U.S. International Trade Commission.[18] The HTSUS is divided into 97 chapters and several thousand unique tariff provisions. Classification is governed by a series of rules including the general rules of interpretation (GRIs), chapter notes, and section notes. While not binding, the WCO also publishes a comprehensive set of explanatory notes to provide additional classification guidance. The United States and most other WCO nations also maintain a process for obtaining classification rulings issued by the customs authority. In the United States, binding rulings are issued by U.S. Customs and Border Protection (CBP)[19] and are maintained in an online library called Customs Rulings Online Search System or CROSS.[20]

The HTSUS is broken down into chapters (e.g., Chapter 14), headings (e.g., 1404), subheadings (e.g., 1404.90) and then the tariff, or 8-digit level (1404.90.90) and the statistical or 10-digit level (1404.90.9020). Classification according to the HTSUS must be performed from the heading down, so you may only select the 8- and 10-digit provisions if the product is first accurately and correctly (according to the GRIs, section and chapter notes) classified in the heading and subheading levels. For example, our 1404.90.9020 (Figure 21.4) classification breaks down as follows:

- Chapter 14: Vegetable Plaiting Materials; Vegetable Products Not Elsewhere Specified or Included
- Heading 1404: Vegetable products not elsewhere specified or included:
- Subheading 1404.90: Other:
- 1404.90.90: Other
- 1404.90.9020: Raw vegetable materials of a kind used primarily in dyeing or tanning: Canaigre, chestnut, curupay, divi-divi, eucalyptus, gall nuts, hemlock, larch, mangrove, myrobalan, oak, quebracho, sumac, tara, urunday, valonia, wattle, and other materials of a kind used primarily in tanning.

Tariffs

Each tariff classification has a corresponding import tariff. There are several options for duty rates: duty-free, ad valorem, specific, or compound. Duty-free products have 0% tariffs. Ad valorem is a Latin term that indicates that

1404		Vegetable products not elsewhere specified or included:				
1404.20.00	00	Cotton linters	kg	Free		Free
1404.90		Other:				
1404.90.10	00	Vegetable hair	kg	0.5¢/kg	Free (A+,AU,BH,CA,CL,D,E,IL,J,JO,MA,MX,OMP,PE,SG)	2.2¢/kg
		Vegetable materials of a kind used primarily in brooms or in brushes (for example, broomcorn piassava, couch grass and istle), whether or not in hanks or bundles:				
1404.90.20	00	Broomcorn (Sorghum vulgare var. technicum)	t	$4.95/t	Free (A+,AU,BH,CA,CL,D,E,IL,J,JO,MA,MX,OMP,PE,SG)	$22/t
1404.90.30	00	Istle	kg	Free		Free
1404.90.40	00	Other	kg	2.3%	Free (A,AU,BH,CA,CL,E,IL,J,JO,MA,MX,OM,P,PE,SG)	20%
1404.90.90		Other		Free		Free
		Raw vegetable materials of a kind used primarily in dyeing or tanning:				
	20	Canaigre, chestnut, curupay, divi-divi, eucalyptus, gall nuts, hemlock, larch, mangrove, myrobalan, oak, quebracho, sumac, tara, urunday, valonia, wattle and other materials of a kind used primarily in tanning	kg			
	40	Other	kg			
	90	Other	kg			

Figure 21.4 Example tariff classification from the harmonized tariff schedule of the United States

the duty will be based on the customs value (discussed later) of the imported merchandise—for example, 5% tariff on the customs value. A specific duty refers to a duty per specific quantity—for example, $0.03/kilogram or $0.12/liter. Quantities declared to customs was not included as one of our focus areas of customs compliance, but we should note that it is an important element, especially when it may be the basis of duty and thereby directly related to customs revenue being correct. Compound duty rates occur when a given tariff classification has both an ad valorem and specific duty assessed—for example, 7.2% + $0.015/kilogram.

Customs Valuation Categories

The majority of tariffs are ad valorem, and value is also a critical statistical component. There are complex rules related to how imported goods must be valued for customs purposes. Getting the customs value wrong on a customs entry is analogous to declaring an incorrect amount for earnings on your tax return—both have a direct impact on government revenue and statistics. The rules for customs valuation are generally harmonized under WTO agreements.[21] These valuation rules are adopted and customized by local nations but normally can be categorized into one of six categories:

1. *Transaction value* is the preferred method and is basically the invoice or selling price (with adjustments described later). Transaction value is the price paid or payable for the imported goods. In related party transactions, transaction value is not permitted if the relationship influences the price.
2. *Transaction value of identical goods* is basically what is sounds like. It can be used to value *free of charge* goods where there is no sale and therefore no transaction value. It can also be used to value goods between related parties where the relationship did influence the price paid and there are identical goods sold to a nonrelated party during a similar time frame at a true arm's length.
3. *Transaction value of similar goods* is again fairly self-explanatory. In order to use this method, the similar goods must closely resemble the goods being valued in terms of component materials and characteristics. The similar goods must be capable of performing the same functions and must be commercially interchangeable with the goods being valued.
4. *Deductive method* starts by determining the selling price of imported goods or identical or similar goods between a seller and an unrelated buyer in the greatest aggregate quantity in the country of importation—for example, the United States resale by the importer to its unrelated customer. Things like transportation, insurance, duties, commissions,

and profits are deducted from this selling price to determine the correct customs value.

5. C*omputed method* is based on the cost to produce the goods by the seller and then adjusted to include a reasonable amount for profit, general expenses, and overhead to determine the valid customs value.
6. *Fall-back method* is when the customs value cannot be determined under any of the previous methods, and it may be determined using reasonable means consistent with the principles and general provisions of the WTO valuation agreements, and on the basis of data available in the country of importation. This method should be based on previously determined values and methods with a reasonable degree of flexibility in their application.

Invalid Valuation Criteria

Customs value must not be based on the selling price of goods in the country of importation (i.e., the sale price of goods manufactured in the importing country); a system that provides for the acceptance for customs purposes of the higher of two alternative values (the lowest should be used); the price of goods on the domestic market of the country of exportation; the cost of production other than computed values that have been determined for identical or similar goods; the price of goods for export to a third country (two export markets are always to be treated as separate, and the price to one should not control the customs value in the other); minimum customs value; or arbitrary or fictitious values. Even something like price takes on added complexity when engaging in international trade.

Value Adjustments

The six customs valuation methodologies provide the basis for valuation; however, there are also adjustments that may be appropriate to make. Additions can include (casually referred to as CRAPP) selling commissions, royalties, assists, proceeds of a subsequent resale, and packing costs. Deductions can also be made for transportation, insurance, and forwarding fees when they are adequately documented and included in the selling price. We will not discuss these adjustments in this chapter but be aware they exist and research them thoroughly in any international transaction.

The Future of Valuation

As you may have realized from just this summary, customs valuation is a complex art and one often inundated by customs attorneys or consulting firms. One possible development in the area of customs value would be the harmonization of customs and tax valuation rules. Presently, these two valuation

regimes are at odds as customs authorities seek to maximize duties by having a higher customs value and tax authorities seek to maximize income taxes by having a lower customs value (and higher local profits). Customs also considers the valuation of each individual transaction while tax authorities generally only consider overall profitability of an entire business. Because the two objectives are so diametrically opposed, harmonization may be a long way off. Nevertheless, it is often a point of discussion by consultants at customs conferences, so it seems to remain a desired possibility.

Country of Origin

C*ountry of origin* for customs purposes refers to the country of manufacture, production, or growth of the merchandise. Further work or material added to an article in another country must effect a *substantial transformation* in order to render such other country the country of origin. In nonpreferential trading transactions, the country of origin can be generally determined by following the substantial transformation principle. This is not always a straightforward determination, so it may be advisable to consult an expert or to request an origin ruling from customs.

In preferential trading arrangements such as a FTA (e.g., NAFTA), there are explicit rules of origin for each tariff classification that determine whether a given commodity qualifies for the preferential treatment sought under the given FTA. Unfortunately, there are seemingly countless numbers of bilateral and multilateral trade agreements throughout the world. Each has been negotiated independently; therefore, each has a unique set of rules of origin, and they are not always consistent.

Marking

There are some specific marking requirements in the United States related to non-U.S. goods: every article of foreign origin (or its container) imported into the United States must be marked in a conspicuous place as legibly, indelibly, and permanently as the nature of the article (or container) will permit, in such a manner as to indicate to an ultimate purchaser in the United States the English name of the country of origin of the article, at the time of importation into the customs territory of the United States. Penalties can be extremely high for failure to mark or for improperly marking goods, so it is clearly advisable to assure marking requirements are addressed for any imports into the United States.

Customs Trends: Automation and Account Management

Two future trends for customs/importation processes are automation and account management—both driven by the availability of data. Customs

processing has historically been a paper-based and transaction-by-transaction system. With technology and time, customs authorities globally are gradually moving to fully electronic customs processing systems driven by the receipt of more data elements earlier in the entry process. It is not unthinkable that in the near future, customs clearances may be electronically processed, and the product released from customs custody before it has even been shipped. Further, as systems and requirements harmonize, one country's export declaration may serve automatically as another country's import declaration.

Customs authorities are also gradually shifting away from looking at only case-by-case shipments and beginning to truly evaluate importers on an aggregate basis. In the United States, major importers are already assigned customs account managers who focus on enhancing compliance of their accounts and serving as a single point of contact for traders into U.S. CBP. CBP is presently evaluating significantly growing the account management concept and has already provided processes for companies to pay duties and fees on a monthly basis, rather than exclusively on a shipment-by-shipment basis.

Supply Chain Security Requirements

Following the tragic events of September 11, 2001, there was a grave concern that terrorists would use international supply chains to launch a future attack, and recent incidents of bombs on U.S. cargo planes support this fear. The potential threat most frequently described has been the so-called bomb-in-the-box—that is, a nuclear dirty bomb loaded into a sea container and detonated in a sea port. Such a device could not only harm humans, but the resulting fallout and response would likely cost the global economy billions of dollars.

The United States has led efforts in this area by introducing a series of new initiatives targeted at minimizing the risk of terrorism infiltrating the supply chain:

- The Customs-Trade Partnership Against Terrorism (C-TPAT) is a voluntary private-public partnership program where companies voluntarily enhance the security of their supply chains in return for a lower level of scrutiny and fewer customs examinations. By having assurance that the trusted partner companies have good security practices, U.S. Customs is able to focus its resources and efforts on the unknown and higher risk companies. C-TPAT was launched in 2002, and by 2010, there were more than 10,000 member companies. C-TPAT is mirrored globally under the WCO's Framework of Standards to secure and facilitate global trade (SAFE Framework)[22] and local country programs most commonly referred to as authorized economic operator.
- The Container Security Initiative (CSI)[23] is another post-9/11 supply chain security initiative launched by the United States. Under CSI,

multidisciplinary teams of U.S. officers from both CBP and immigration and customs enforcement are stationed in foreign ports to work together with host foreign government counterparts. Their mission is to target and prescreen containers and to develop additional investigative leads related to the terrorist threat to cargo destined to the United States before the cargo leaves the foreign country. Since its original launch in 2002, CSI had expanded to 58 ports by 2007 (see Figure 21.5).

- Increasing requirements for advanced data related to inbound shipments originated with the 24-Hour Manifest Rule[24] and ultimately resulted in a more robust requirement called importer security filing (ISF).[25] Under ISF, U.S. importers are required to submit to CBP significant amounts of data related to the import transaction, which in turn, CBP uses to screen transactions to identify those with the highest risk for further review, physical examination, or even prohibit high risk goods from entering the U.S. commerce.

All of these supply chain security initiatives are designed to push out the border and provide customs with greater transparency into transactions at a much earlier time. Trends here include global harmonization (or proliferation of unharmonized local variations) and ever increasing requirements for more data sooner in the process. It may be that ultimately, customs clearances are finalized by the importing country completely before the export clearance/shipment in the originating country.

Product Safety Concerns

Starting around 2007, several incidents led to a heightened level of scrutiny related to the safety of consumer goods imported into the United States—primarily from China. One of the initial big issues in this area dealt with pet food from China that had been contaminated with the chemical melamine, resulting in renal failure in dogs and cats. The pet food incident was followed by several others including toothpaste contaminated with diethylene glycol, faulty tires, and toys with recalls due to lead paint and tiny magnets that could be swallowed.

As a result of these incidents, President Bush established an interagency working group on import safety in July 2007. Bush was quoted at that time as saying, "The world is changing, and in order to make sure that we can continue to have the confidence of our consumers, we will continually review practices and procedures to assure the American consumer." One of the tangible results of this study was the enactment of the Consumer Product Safety Improvement Act of 2008 (CPSIA).[26] The CPSIA established new safety standards, requirements, and testing/recall protocols for a broad array of consumer goods ranging from toys to all-terrain vehicles.

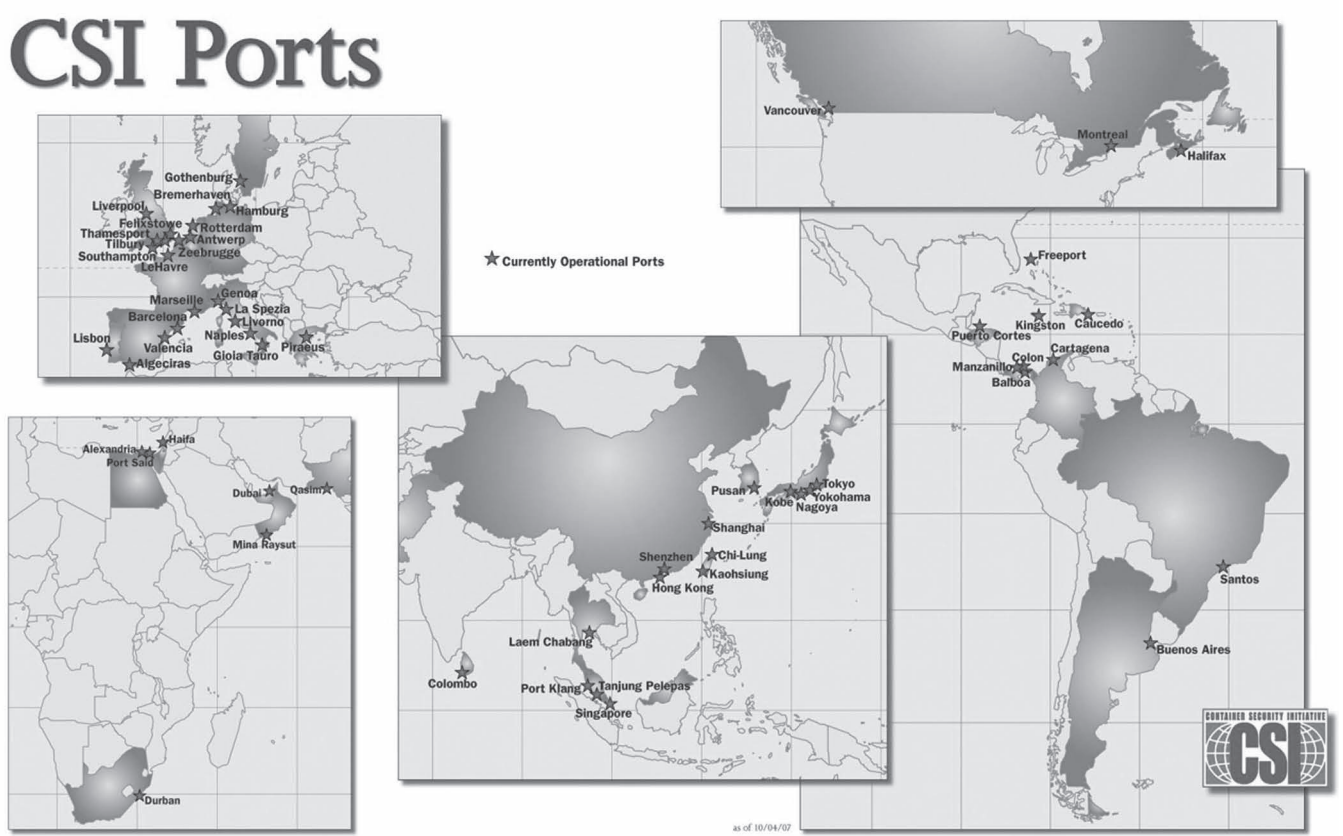


Figure 21.5 Map of container security initiative ports

The trend in this area seems to be gradual but ever increasing regulation designed to assure safe consumer goods and food are delivered to U.S. customers. Product safety requirements are also being developed in nations across the globe with little guarantee of harmonization.

Preferential Programs

If you are able to absorb and comply with all of the foregoing rules and regulations, there are also extensive ways to gain a competitive edge by taking advantage of preferential trading programs. Preferential programs are generally aimed at minimizing duties and fees, so they are highly monitored and scrutinized by customs administrations seeking to protect and maximize government revenues.

Free Trade Agreements

Free trade agreements (FTAs) are the result of bilateral or multilateral negotiations between two or more countries. Probably the most famous trade agreement is the North American Free Trade Agreement (NAFTA),[27] which was agreed upon by the United States, Canada, and Mexico.

FTAs provide reduction or elimination of duties on trade in qualifying goods between the participating nations. As referenced in the discussion about origin, each FTA has its own set of rules or origin. In order to qualify for the preferential duty rates, the goods must satisfy the respective rules of origin.

Countries throughout the world have independently negotiated FTAs, so it is highly advisable to research whether trade between any two given nations may or may not be eligible for preferential tariffs under a FTA before entering into a contract or proceeding with any international transaction. If there is a FTA in place, it is also wise to make sure the goods in question actually qualify under the respective rules of origin, or you may pay the price at a later date under customs audit or investigation.

Duty Drawback

If you import merchandise and later export it, either directly or after it has been manufactured into another product, you may be eligible to recover a portion of the duties under a program called duty drawback.[28] There are a wide variety of types of drawback and specific rules for each type; however, if you are exporting goods containing any imported content, it is worth investigating. Many of the types of drawback allow for broad substitution, so the exported goods don't need to necessarily contain the actual imported merchandise (normally just commercially interchangeable equivalents).

Tariff Suspensions

If your company is importing goods into the United States that are not manufactured domestically, you may be able to pursue tariff suspension legislation. Members of Congress sponsor individual bills that temporarily (normally for three years) suspend or reduce duties on specific individual products. The individual bills are normally bundled into a package that Congress ultimately votes on (historically, about once every two years). The bundled legislation is often referred to as the Miscellaneous Tariff Bill.[29] This is a legislative process that amends the U.S. Harmonized Tariff Schedule. As legislation, it is highly variable and dependent on Congress to actually pass the bill. It can be extremely beneficial to pursue this alternative if you are importing unique products with no domestic equivalents.

Foreign Trade Zones and Bonded Warehouses

Foreign trade zones (FTZs)[30] and bonded warehouses provide a process to physically bring merchandise into the United States without formally entering the goods into the U.S. commerce and having to pay duty. FTZs allow for manufacturing of goods prior to the assessment of goods while bonded warehouses only allow for limited processing.

Under a manufacturing FTZ arrangement, dutiable raw materials may be used in the production of a duty-free finished good that is then entered into U.S. commerce, and zero duty is owed. Goods exported out of FTZs or bonded warehouses normally do not require any payment of duties. FTZs and bonded warehouses may also be used to increase cash flow by delaying payment of duties until the goods are withdrawn (normally for sale to a paying customer).

Trade Compliance Program Recommendations

International trade involves a myriad of regulations and demands a high level of compliance. If you will engage in international transactions to any significant degree, we recommend that you implement a corresponding compliance program. The hallmark for compliance and ethics programming can be researched in the U.S. Federal Sentencing Guidelines (FSG)[31] (see Chapter 8, "Effective Compliance and Ethics Program"). To summarize the FSG compliance recommendations at a high-level, the following core elements should be considered:

- Senior management commitment—that is, *tone at the top*
- Adequate resources
- Policies and procedures
- Discipline and incentives
- Monitoring

- Training
- Enforcement
- Risk assessment/management
- Reporting mechanisms (including ones that provide for anonymity)

Concluding Thoughts

Trade is complicated and ever changing. The requirements are high—but the rewards can be even higher. If nothing else after reading this chapter, you should conclude that international trade compliance is a complex and detailed subject area. However, like procurement involvement in new product development, capital expenditure projects, and energy management, it is another area where next level supply managers must expand their base of knowledge.

Chapter Notes

1. http://www.secactions.com/?p=655 and http://www.justice.gov/opa/pr/2008/December/08-crm-1105.html.
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