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CUSTOMS AND BORDER PROTECTION'S EXAMINATION OF IMPORTERS' OPERATIONS: THE FOCUSED ASSESSMENT

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OVERVIEW

"We are from the government, and we are here to help you." This is the sentiment behind what is benignly called a "Focused Assessment"—by any other name, however, it is an audit conducted by U.S. Customs and Border Protection (CBP). Its objectives are to determine the adequacy of an importer's internal controls, ascertain potential risk of noncompliance with CBP laws and regulations, and encourage the development, as needed, of improved internal compliance policies and procedures. One other "small" purpose of a Focused Assessment must be recognized for what it is—the collection of additional duties and fees if there has been material noncompliance and the assessment of monetary penalties where appropriate. For instance, from fiscal years 2008 to 2010, CBP's Office of Regulatory Audit (hereinafter, "Audit") completed 1,053 audits and identified and recommended² the collection of approximately \$154.2 million in additional revenue.³

The Focused Assessment program was introduced in 2001, but its roots go back to the Compliance Assessment (CA) program⁴ and the Customs Modernization Act of 1993 (see Chapter 1, "Introduction and Overview"), and the recognition of the need for more efficient use of CBP personnel in fulfilling traditional revenue and trade functions. CBP is authorized to conduct audits under 19 U.S.C. § 1509. The statute authorizes CBP to examine and audit records of parties to:

- ascertain the correctness of any entry;
- determine the liability of any person for duty, fees, and taxes due, or which may be due, the United States;
- determine liability for fines and penalties; or
- ensure compliance with the laws of the United States administered by CBP

Section 1509(b) describes specific procedures for conducting a formal audit authorized under the statute. These procedures are found in sections 163.1 and 163.11 of the Customs regulations.⁵ CBP is also planning numerous important

updates to the program for the government's fiscal year 2015, which will be discussed herein.⁶

A Focused Assessment allows CBP to take advantage of the formal statutory obligation⁷ placed on importers to exercise "reasonable care," with its implicit recognition of the need for internal control and monitoring of customs transactions. The premise is straightforward: CBP wants importers to effectively police themselves so that CBP can focus on and identify the bad guys. If, in CBP's judgment, the company is doing a good job of compliance through the adoption—and implementation—of effective internal controls, CBP is willing to lessen its scrutiny over the company's import transactions. As a high-level CBP official once said: "We know from experience that companies with good internal customs controls are much more likely to be compliant and that companies without sufficient system controls pose a high risk to Customs."⁸ Of course, an importer and CBP will generally have very different views as to what is "sufficient" or "adequate."⁹ Nevertheless, an effective internal compliance program is a fundamental necessity for all importers, and the contours of an effective program are discussed later in this chapter, in the section on Acceptable/Unacceptable Risk and Development of Internal Controls. When necessary, CBP also uses targeted, "single-issue" or Quick Response Audits (QRAs) to review specific questions or assess individual risk areas. What to expect and how to prepare for these are also discussed in this chapter, in the section on related audit programs.

PRACTITIONER'S TIP: While an importer may have become accustomed to a certain level of routine review by local CBP personnel (for example, periodic reviews of tariff classification), the Focused Assessment is, by definition, far more invasive. For an importer that has never been audited, a Focused Assessment represents a serious endeavor that often warrants consultation, preparation, and review with subject matter experts, such as a licensed customs broker, financial expert, and specialized legal counsel. In a Focused Assessment, time is a critical factor. The importer may wish to clarify gray areas of customs law to establish that it acted with "reasonable care" or file one or more voluntary prior disclosures (see "Prior Disclosure" in Chapter 11, "U.S. Customs and Border Protection's Authority to Assess Monetary Penalties"). If material errors or omissions are discovered and the importer has not yet filed a prior disclosure, Audit will notify the importer of its findings and refer the matter for possible imposition of civil penalties under 19 U.S.C. § 1592, thus forestalling the importer's ability to file a prior disclosure (see Chapter 11, "U.S. Customs and Border Protection's Authority to Assess Monetary Penalties").

WHAT IS A FOCUSED ASSESSMENT?

A Focused Assessment is a targeted audit of sample import transactions for a period of time (usually the most recently completed company fiscal year) selected on the basis of perceived risk. "Risk," according to CBP, is the "degree of exposure that would result in loss to the trade, industry, or the public," both in "ordinary day-to-day transactions as well as those extraordinary transactions that happen infrequently or unintentionally."¹⁰ Key considerations of risk exposure in Customs compliance audits are significance and/or sensitivity of the area (e.g., textiles or enforcement of IP rights), susceptibility (complex area prone to errors), the existence of "red flags," lack of management support, and lack of trained personnel.

By *focusing* on the importer's internal control practices, an auditor identifies and *assesses* areas of potential risk to CBP. The auditor then selects sample import and financial transactions to validate acceptability of compliance with customs requirements and company procedures, determines what improvements are needed, and, if material noncompliance is found, recommends additional action be taken to determine the extent of any duties owed. Additionally, the auditor recommends whether monetary penalties should be imposed. CBP's Focused Assessment program consists of three distinct phases:

- Pre-Assessment Survey (PAS);
- Assessment Compliance Testing; and
- Post-Assessment Follow-Up

SELECTION AS A SUBJECT OF A FOCUSED ASSESSMENT

When Focused Assessments were first introduced, selection as a subject of a Focused Assessment was more likely if a company was among the largest importers in terms of quantity or value of imports. After 13 years of the program, however, CBP is now looking at medium- and smaller-size importers. Certain factors make a company more likely to be audited, including whether the importer imports high-risk articles, has a history of noncompliance, engages in substantial importing under special trade programs, or has experienced rapid import expansion. Regardless of any specific factor, the CBP audit pool is growing. Certainly, major importers in terms of value of goods imported are always on CBP's radar, as well as importers in Priority Trade Issues (PTIs).¹¹ But, for the past several years, CBP has been frequently selecting medium-size importers with imports of \$10 million or more.

PRACTITIONER'S TIP: Regardless of whether an importer has been notified that it has been selected for a Focused Assessment or any other type of CBP audit, an importer should take the time to thoroughly review its importing practices and identify compliance vulnerabilities. An importer can obtain a complete history of its importing activity from CBP. This data provides detailed information, including date of entry, duties and fees paid, suppliers, classifications, values, preferences claimed, origin, and so on, for a period of up to five years. This information is instrumental in identifying potential risk areas. There are two ways to obtain this information: submit a Freedom of Information Act request to CBP for your Importer Trade Activity (ITRAC) data;¹² or sign on as a participant in CBP's Automated Commercial Environment (ACE) and download your own personalized reports using the ACE secure data portal.¹³

KEY ELEMENTS OF THE FOCUSED ASSESSMENT PROCESS

Once a Focused Assessment candidate is selected, CBP will assemble its audit team. The team generally consists of CBP import specialists and auditors from the Office of Regulatory Audit,¹⁴ with a team leader, and perhaps even an information technology expert. They generally will be from the region in which the importer is located; however, creation of CBP Centers of Excellence may bring in "subject matter experts" from CBP offices in other geographic regions.¹⁵

Before the PAS begins, the audit team prepares a preliminary assessment on the importer (a Preliminary Assessment of Risk, or PAR). The PAR provides the audit team with an initial scope of work and possible risk areas. It is based on information the audit team gathers on the company from internal CBP sources (Customs rulings, ITRAC, import specialists, responses to Requests for Information (CF-28), account managers, and Fines, Penalties, and Forfeiture Offices), as well as publicly available information (including the company website, SEC postings, and other sources). Utilizing this information, the audit team develops a preliminary audit plan.

PRACTITIONER'S TIP: CBP has made significant resource materials available to an importer to prepare for and to better understand the entire Focused Assessment process. These resources can be accessed at <http://www.cbp.gov/trade/audits/focused-assessment>. This page contains a link to CBP documents related to Focused Assessments, including a step-by-step explanation of the PAS, Common Importer Errors, a Compliance Improvement Framework, the Focused Assessment Follow-up Audit Program, and an Internal Control Manual template. All of these materials and the many other informed compliance documents on the CBP website provide excellent guidance for the importer when preparing for a Focused Assessment.

Notification: The PAS Questionnaire and Walk-Through Samples

CBP typically alerts an importer by telephone and then by mail or e-mail that it is the subject of a Focused Assessment and confirms procedural information with the importer. At this time, the auditor may indicate a tentative date for the entrance conference. The auditor may also request certain readily available company information (e.g., written policies and procedures, trial balance, chart of accounts, and general ledger detail) be provided prior to the entrance conference so the audit team may better tailor the initial risk assessment plan and company questionnaire to fit the importer's specific circumstances and profile.

PRACTITIONER'S TIP: In an ideal world—before any contact by CBP, and as a means of getting one's house in order even if never audited—an importer should ensure it has adequate internal controls and prepare a comprehensive strategy for responding to a Focused Assessment or QRA. Once the audit process begins, the importer will have very little time to prepare. First impressions are important in this process and it is certainly more likely the auditor will be looking for and expecting to find errors if the importer has no or inadequate controls over its import transactions.

PAS Questionnaire

Shortly after initial contact, CBP will send the importer a PAS Questionnaire (PASQ). For fiscal year 2015, CBP has prepared a completely revised questionnaire. The importer is instructed to complete the PASQ within 30 days of receipt. Often times though, an importer will need additional time to respond. The PASQ

is intended to assist CBP in focusing on the specific risks relative to the company's imported merchandise and the processes/procedures used to mitigate the risk of being noncompliant with CBP laws and regulations.

The PASQ is divided into six sections: (1) organization, policy, and procedures pertaining to CBP activities; (2) information about the valuation of imported merchandise; (3) information about the classification of imported merchandise; (4) information about use of special classification provisions, such as Harmonized Tariff Schedule of the United States (HTSUS) 9801 and 9802, Generalized System of Preferences/Free Trade Agreements and North American Free Trade Agreement (NAFTA) provisions; (5) information about merchandise subject to antidumping and countervailing duties (AD/CVD), and (6) information about compliance with intellectual property rights restrictions. The new questionnaire also requests certain business records, such as a copy of the general ledger, working trial balance, and company-written accounting procedures for recording purchases and payments. In addition, the importer's responses will help CBP identify the individuals responsible for performing the procedures and the type of documentation that will be available for CBP to review.

The importance of how the PASQ is answered cannot be overstated. The PASQ is the primary tool used to determine a company's level of risk of non-compliance. Many subsequent aspects of the Focused Assessment hinge on the response to a specific set of questions. An incomplete response will serve to raise more questions than it answers and perhaps result in an increase to the size of the sample transactions that are selected. An ideal response will provide a thorough and complete description of a company's internal policies and procedures on the subject, along with references to the company compliance manual or any other written procedures and how the procedures are applied as part of the importer's daily operations.

PRACTITIONER'S TIP: Responding to the PASQ provides a further opportunity for the importer to review and, where necessary, improve its procedures. If internal controls are less well-developed than one would like, this is a good time to address shortcomings and implement corrective fixes; however, be clear as to what is an improvement or a new process.

Walk-Through Samples

In addition to the PASQ, CBP will request a number of "walk-through" sample entries that will permit an importer to demonstrate the actual implementation of company internal control procedures in real-life situations. CBP will work with the importer to select import transactions that represent a cross-section of the company's import activity. In response, the importer should provide to CBP not only entry summaries and commercial invoices, but also purchase orders and payment records, including those related to supplemental payments or additions to value (e.g., assists and/or royalty or license fee payments), origin certifications, and product specifications and classification materials or checklists.

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PRACTITIONER'S TIP: Walk-through sample entries should be reviewed thoroughly by the importer and its trade counsel or consultant to determine if there are any errors or omissions before the documents are provided to CBP. If errors or omissions are identified, the company should be prepared to expand its review to determine if similar or other errors are present. If so, the company should consider filing a prior disclosure with CBP on or before presentation to CBP. A prior disclosure is an effective way to limit exposure to monetary penalties under 19 U.S.C. § 1592, but only if done correctly and timely. See Chapter 11, "U.S. Customs and Border Protection's Authority to Assess Monetary Penalties."

Entrance Conference

The entrance conference will be the first opportunity for the importer and CBP Audit representatives to meet face to face.¹⁶ For its part, CBP will explain each step of the Focused Assessment, the way the audit team plans to proceed, and an anticipated timeline for each step from start to finish. This is also CBP's opportunity to ask questions about the importer's responses to the PASQ, internal procedures, and financial information.

PRACTITIONER'S TIP: While the company should be fully prepared to provide CBP with satisfactory answers, it should not hesitate to explain, if necessary, that more research may be required to respond to a question and that the company will respond once it has had time to investigate the question and provide a complete and accurate answer.

The entrance conference is also the importer's opportunity to walk CBP through the selected sample transactions and explain how the company's formal and/or informal internal controls facilitate compliance with Customs law and regulations. The importer should carefully walk the CBP audit team through each document, focusing on each phase of the transaction—from selection of suppliers and products, to orders and the order processing system, through shipment and receipt of goods, and finally payment, including recording purchases in the company accounting system that ultimately tie to the declared value of the goods. Again, this is an opportunity to show in detail the implementation of the company's internal control procedures, not just as a theoretical matter, but with respect to real, actual imports. The importer should thoroughly prepare for the entrance conference and, when appropriate, "take control" (politely, to be sure) of its portion of the meeting, with the goal of demonstrating the company's preparation and commitment to compliance.

PRACTITIONER'S TIP: One recommended approach is for the internal company team at the meeting to be made up of subject matter experts from across the company and high-level management personnel responsible for CBP compliance. This is the importer's opportunity to explain the seriousness with which the company takes its import responsibilities and to make a presentation (PowerPoint is always nice). This presentation should include a brief overview of the company's products and importing operations, the organizational structure and individuals responsible for CBP compliance, the procedures that are followed for each

importation to assure compliance, and the company's commitment to compliance by reference to its compliance procedures (if they exist) and any internal or external employee training that is provided.

PRACTITIONER'S TIP: At the entrance conference, the importer should discuss with and obtain agreement from the auditor that all requests for information or documents shall be in writing, numbered, and delivered by e-mail or other timely means to a single designated employee of the company. This individual may be responsible for responding to the question or gathering the information, or for identifying the proper individual at the company to do so, and for coordinating a timely response to the auditor. All responses should reference the original request number for tracking purposes and to avoid issues with regard to whether a response to any particular request was provided.

Field Work and Auditing of Selected Representative Samples

Following the entrance conference and review of the company's internal controls, PASQ responses, walk-through samples, and accounting books and records, the auditors will examine the information provided and identify risk areas to examine more closely. This is the "field work" portion of the Focused Assessment. It generally consists of employee interviews, review of selected transactional documentation, and review and demonstration of electronic or automated systems (e.g., ordering, accounting, and receiving). This may be done on-site or through a combination of on-site and off-site work by the CBP audit team.

PRACTITIONER'S TIP: Caution should be exercised here to carefully brief employees regarding this process and instruct them not to answer questions outside the employee's area of expertise or speculate about matters not immediately known. Companies should keep notes of the questions and answers, and it is advisable that the interview include the company's trade consultant or advisor.

PRACTITIONER'S TIP: The timeline for completion of the PAS phase of the Focused Assessment does not appear to be particularly aggressive (generally about eight months) but time passes quickly. The most common issue in a Focused Assessment is that the importer falls behind schedule in responding to or providing the myriad of documents and numerous requests for information made by the auditor. As a result, auditors cannot meet their internal deadlines, causing them to put pressure on the importer to produce the information or conclude the information does not exist, which can be adverse to the importer. Audit document or information requests typically give an importer 10 to 14 calendar days to respond. This requires a quick, organized turnaround from the team of players who need to be involved in the Focused Assessment, including outside divisions or departments, such as finance, tax, legal, accounting, and purchasing, who often have different priorities, agendas, and schedules.

A core component of the field work is the selection of sample transactions for risk analysis. These are not the walk-through entries. In this phase, CBP is

looking to see if the importer does what it says it will do in its internal controls over customs transactions, and if there are errors, mistakes, or oversights in the documentation or customs transaction (e.g., misclassified or undervalued goods).

Besides the revised PASQ, the next most noticeable change to the Focused Assessment process due to the 2014 enhancements for importers is the size of PAS sampling. CBP is making major changes here. Instead of requesting a fixed number of samples for each importer, CBP has implemented more general guidelines that allow for flexibility and customization. For example, if there is a population of 250 items or more in the universe of data, the auditor may select between 25 and 40 samples. Alternatively, if the population is 250 or less, the tested quantity will be about 10 percent. (These ranges are meant only as general guidelines and exceptions can and will occur.)¹⁷ CBP notes the increase in sample size will enable it to better assess the risk of material noncompliance and determine the most appropriate corrective action plan. CBP believes the increased assurance that comes from testing larger sample sizes will enable it to better assess if errors are immaterial or nonsystemic in nature or whether there is a lack of documented internal controls.

The audit team selects the samples ultimately chosen for PAS review with great deliberation. Samples are selected on a judgmental basis (meaning they were selected by the auditor based on his or her judgment rather than purely random or statistical methods). Transactions that appear incorrect or questionable on their face (e.g., an unusual classification or valuation) are targeted. Accordingly, judgmental sampling often leads to findings of a greater percentage of errors on the part of the importer than might otherwise result from application of purely objective or "statistical" sampling techniques.

PRACTITIONER'S TIP: Audit selects a line item from a customs entry summary (CF-7501) at the Harmonized Tariff Schedule level and not the entire entry. Whenever possible, CBP will also try to narrow down the selection to an individual item on the commercial invoice. CBP will do the same when selecting specific general ledger or accounts payable transactions for review; however, this is a winnowing process and it will often take several requests for information before the final set of transactions are identified from targeted accounts. Once the final general ledger or accounts payable transactions are selected, CBP will then request documents and information associated with the account transaction and information as to whether it relates to the production and/or importation of merchandise.

PRACTITIONER'S TIP: Importers should not overlook the fact that CBP will separately test general ledger and accounts payable transactions. CBP is looking for unreported assists and additions to value, such as parts and components or test equipment provided free of charge to a supplier, or the payment of a royalty or license fee to a third party for the right to use a patented process in the manufacture or production of merchandise imported.¹⁸

Importers need to remember the number of transactions selected is based on each targeted subject area. Thus, there likely will be separate sample pools for entry summary line items (although, one entry summary line can be used to

examine more than one element of compliance, e.g., classification and value), general ledger transactions, and accounts payable transactions. In addition, separate sample pools may be taken if the importer has significant activity in other risk areas, such as special trade or preference programs, and AD/CVD transactions.

Identifying and Disclosing Errors during Field Work

Even the most careful importers can have errors in their judgmentally selected transactions. The questions that frequently present themselves to importers as they gather and review the necessary documents and records associated with a CBP audit request are (1) should the transaction details be reviewed before presenting the requested information to CBP; (2) if an error or omission is found, should the error or omission be brought to the attention of the CBP auditor and an explanation provided; and (3) should the importer conduct a broader examination of its transactions to identify similar errors or omissions in its universe of transactions?

Without a doubt, best practices suggest an employee knowledgeable on customs matters, or a third party, such as a licensed customs broker or attorney, should thoroughly review the details of the transaction before presenting the requested information to CBP. This is consistent with the idea that participating in a Focused Assessment really is a team sport, facilitating a complete and accurate response, as well as a means of alerting the importer to possible violations before the auditor sees them. Most importantly, however, it gives the importer the opportunity to consider whether to disclose the circumstances of the violation in the context of a prior disclosure. (See "Prior Disclosure" in Chapter 11 "U.S. Customs and Border Protection's Authority to Assess Monetary Penalties.") While Customs is responsible for enforcing 19 U.S.C. § 1592 and ensuring compliance with the laws and regulations that govern imports, the agency seeks to improve compliance and encourages parties to submit prior disclosures. Section 1592(c)(4) describes the conditions under which an importer may avail itself of protections from civil fines or penalties afforded by prior disclosure.

A critical element of prior disclosure is that it be filed before, or without knowledge of, the commencement of a formal investigation of that violation by CBP. Thus, the question often asked is whether a prior disclosure may be filed once an importer is notified it is the subject of a Focused Assessment, or more importantly, if an importer may do so during the course of the Focused Assessment. A Focused Assessment is not a formal investigation of the importer based on a reasonable suspicion there is a specific violation of section 1592. While such matters are very fact specific, as a general rule, an importer may disclose a perceived violation during the course of a Focused Assessment right up until the moment it receives notification from a CBP auditor or other representative of Customs that the specific matter is being investigated as a violation of section 1592, or other customs law. An importer may make his or her disclosure orally during a meeting or phone call with the auditors or other CBP officials, but it should be subsequently supported in writing as soon as possible.

Pre-Assessment Survey Report and Exit Conference

At the conclusion of the PAS portion of the Focused Assessment, CBP prepares a draft PAS Report that is given to the importer to review. The draft PAS Report describes the scope and methodology of the assessment undertaken and the auditors' findings of errors, if any, alleged to have been found during the PAS field work, whether the internal controls of the company in each area reviewed pose an "acceptable" or "unacceptable" risk, and recommendations for actions the company should take to improve its compliance posture. In some cases, the PAS Report may include a quantification of a loss of revenue, if possible, but more often, this will be necessary in a subsequent stage of the Focused Assessment.

The importer is given the opportunity to comment in writing on the draft PAS Report, and these written comments will be included in the final PAS Report. Such comments generally state the importer's agreement or disagreement with the auditors' findings and provide an explanation of the importer's position. Although the company may disagree with the findings or conclusions of the auditors, it is rare that anything the company says at this point in the process will cause the auditors to change their opinion. Should there be a disagreement, the auditors will try to agree on the resolution of issues with the importer. The auditors will also review any recommendations for the adoption of a Compliance Improvement Plan (CIP) (discussed next, in "Post-Assessment Follow-Up"). At the exit conference, the PAS results are again discussed and any CIPs are likely to be memorialized. Then, the PAS Report will be finalized and sent to CBP Headquarters.

PRACTITIONER'S TIP: Differences of opinion with regard to the findings of the audit team and the importer or its representatives frequently occur. While in some cases it is possible to reach an agreement or compromise with the auditors, the importer will more likely need to avail itself of the Internal Advice procedure¹⁹ as a means to resolve the dispute. The Internal Advice procedure refers the matter to CBP Headquarters and the Office of International Trade, Rulings, and Regulations for administrative resolution. This procedure can be used, for example, to resolve differences of opinion with regard to the proper tariff classification of merchandise, or a complex valuation question, such as the acceptability of the entity's transfer price as a viable transaction value for related party transactions. Because of procedural changes, CBP will not hold the audit report pending a decision by CBP Headquarters on the internal advice question, but rather it will state its findings and indicate the matter is under review. Thus, the earlier in the audit process the importer can raise and address these issues the better. The importer does not have to wait for the draft PAS Report, but may request internal advice or request a ruling²⁰ at any time in the process, and preferably as soon as it is identified.

POST-ASSESSMENT FOLLOW-UP

While it is possible that CBP will find its audit of the selected entries reveals no material errors and the company has adequate internal controls that require no further action, this is not typical. In a much more probable scenario, the PAS Report will document errors CBP found in the PAS walk-through samples

reviewed. At a minimum, the importer will be expected to agree to develop and implement a CIP to correct noted areas of deficiency. Customs also expects there will be follow-up activity to identify and quantify the extent of noncompliance and to compute the loss of revenue for the identified areas of risk. This activity is completed not only for the year under review for each area of risk identified in the PAS, but for prior years as well (as many as five years in total).

Typically, the importer agrees to engage in a self-assessment and revenue loss calculation. In this situation, the importer and CBP try to devise a methodology (including statistical sampling)²¹ by which the importer may calculate the impact of any additional errors or omissions in the universe and pay duties and interest based on a more extensive review of transactions in the audit period, or expand the audit to cover additional years.²² The importer then applies the agreed-upon methodology, subject to CBP oversight, and tenders the amount of duties calculated to be owed. The amount of CBP involvement in this process varies.

If the importer and CBP cannot work out a satisfactory resolution, CBP will proceed to an Assessment Compliance Test (ACT), a more comprehensive review by CBP of all unacceptable risk areas identified in the PAS Report. Its purpose is to determine the full extent of noncompliance and the resulting total loss of revenue using, in many cases, statistical sampling and projection methods.²³ CBP's Fines, Penalties, and Forfeitures Officer at the primary port of entry will also decide if the initiation of a section 1592 penalty case is appropriate, taking into account any recommendations from the auditor. CBP needs to allege and find negligence, gross negligence, or fraud in order to capture the calculated lost revenue for liquidated entries for the period of review and permit the assessment of a civil penalty.

Although some Focused Assessments proceed to an ACT, most do not. In truth, neither CBP nor the importer wants to face this step. Depending on the findings of the PAS and the nature of any outstanding issues (e.g., what the issues involve, their egregiousness, the claimed amount of lost duties involved, the cooperation of the importer, and whether an alternative solution is possible), an ACT may be avoided. If there are findings of area(s) of unacceptable risk (and there most likely will be) at the completion of the PAS, CBP and the importer will try to arrive at an acceptable resolution of the overall audit without proceeding to an ACT.

PRACTITIONER'S TIP: The vast majority of Focused Assessment revenue loss tenders are made on a voluntary basis, that is, without CBP actually initiating a section 1592 penalty case. Under 19 U.S.C. § 1514, all decisions and findings on liquidated entries are final and conclusive on all parties (including CBP) unless the United States was deprived of lawful duties or fees as a result of a violation of section 1592(a). Thus, an importer may wish to analyze whether it acted with "reasonable care" even if it reached a different conclusion than CBP before it agrees to tender duties or fees.

Should errors that result in loss of revenue be identified, import specialists will also act on any unliquidated entries, including issuance of notifications of (duty) rate advances. If CBP rate advances unliquidated entries, thereby requiring

payment of additional duties upon liquidation, the importer can file protests challenging the additional duties assessed. (See "Protests" in Chapter 8.) If this is the case, the importer may wish to consider withholding the tender of any duties for this issue pending an ultimate decision on the protest. Likewise, CBP can be challenged in its pursuit of penalties or its issuance of a section 1592(d) demand to collect duties on liquidated entries. An importer has the right to contest any penalty or duty demand pursuant to well-established procedures within CBP and ultimately in court, if necessary. This is described in detail in Chapter 11, "U.S. Customs and Border Protection's Authority to Assess Monetary Penalties."

The final phase of the Focused Assessment is the Post-Assessment Follow-Up. This takes place after any CIPs are put into place to ensure proper implementation. This follow-up is targeted to occur within six months, but in reality it rarely occurs within this time frame. The follow-up is limited to areas of noncompliance found in the original PAS Report, although there is nothing to preclude CBP from identifying a new issue if it was discovered during the course of the follow-up activity. At this time, the audit team may also conduct a verification of the process used by the importer to quantify and tender any loss of revenue.²⁴ Follow-up audits will continue until Audit is satisfied that the importer is fully compliant and there is no further loss of revenue.

● ACCEPTABLE/UNACCEPTABLE RISK AND DEVELOPMENT OF INTERNAL CONTROLS

Focused Assessment is primarily a risk-based assessment, identifying the areas that represent the greatest risk of noncompliance and focusing attention there. If CBP identifies an area of probable risk, it then inquires whether the company has adequate internal controls in place to reasonably assure compliance, acknowledging no system is foolproof. The greater the degree of CBP's comfort in terms of internal controls, the better off the company is. Conversely, the existence of "red flags" (e.g., prior history of noncompliance, lack of effective monitoring of CBP operations, lack of accountability, and high rate of personnel turnover), lack of "management support" for CBP compliance, and "unskilled personnel"²⁵ may indicate there is a higher likelihood of errors or mistakes.

What is internal control? For CBP, internal control is broadly defined as "a process—effected by an entity's board of directors, management, and other personnel—designed to provide *reasonable assurance* regarding the achievement of objectives in the following categories: [1] reliability of financial reporting, [2] effectiveness and efficiency of operations, and [3] compliance with applicable laws and regulations."²⁶ Internal control can also be described as systematic measures (such as reviews, checks and balances, methods, and procedures) instituted by an organization to (1) conduct its business in an orderly and efficient manner; (2) safeguard its assets and resources; (3) deter and detect errors, fraud, and theft; (4) ensure accuracy and completeness of its accounting data; (5) produce reliable and timely financial and management information; and (6) ensure adherence to its policies and plans.²⁷ Following the Committee of Sponsoring Organizations of the Treadway Commission (COSO) framework,²⁸ CBP has broken down the

concept of "internal control" into five interrelated components. Each of these components must be adequately addressed for any single process or procedure to be recognized as an "internal control" by CBP. The five components²⁹ are:

- Control environment;³⁰
- Risk assessment;³¹
- Control activities;³²
- Information and communication;³³ and
- Monitoring³⁴

An internal control program should be documented and must be regularly updated and constantly monitored to see where improvements can be made as processes change. Equally importantly, it must actually be implemented, with proof of implementation for CBP to review. This often means checklists and signoffs, or other means of acknowledging a task was performed. In sum, the Focused Assessment comes down to three Ps: policies, procedures, and personnel. Oh, yes . . . and one A for Audit, as CBP expects the importer will constantly be reviewing itself and its transactions and procedures, and reporting to management to ensure it remains compliant.

OPTING OUT OF A FOCUSED ASSESSMENT

A question often asked by company officials after being selected for a Focused Assessment is whether there is any way to get out of it! Although the answer is "yes," the cure, to some, is worse than the pain of a Focused Assessment. An importer can be removed from the Focused Assessment audit pool by joining CBP's Importer Self-Assessment (ISA) program. This is, however, no easy feat. The ISA program allows interested importers to assess their own compliance with Customs laws and regulations and report annually to CBP. The ISA program is primarily based on the development and use of good internal controls designed specifically for an importer's Customs operations. See Chapter 14, "Trusted Trader Programs," for additional discussion of CBP's ISA program. To be eligible for ISA, an importer must first be admitted into the Customs-Trade Partnership against Terrorism (C-TPAT). Not every company that attempts to be validated under the ISA program will succeed. Nonetheless, highly compliant C-TPAT importers with well-documented procedures already in place may wish to consider this option, as benefits afforded under the program are said to be growing.

Recently, CBP has announced that an importer who successfully completes a Focused Assessment may elect to enter ISA without participating in the otherwise required conference and review (as presumably these were accomplished in the just-completed audit).³⁵ There are, however, ongoing expectations of ISA participants. An ISA importer is expected to adopt "best practices," which some critics contend is a stricter standard than the statutory requirement of the exercise of reasonable care. Best practices include the performance of periodic self-testing, preparation and submission of annual reports to CBP, and a commitment to voluntarily self-disclosing to CBP any violations that are found. Not surprisingly,

many importers do not believe the trade-off is worth it, even taking into account removal from the Focused Assessment pool and the purported preferential treatment that goes along with validation.

RELATED AUDIT PROGRAMS

There are other methods used by CBP to examine an importer's operations. The most common example is the QRA or single-issue audit. Unlike the Focused Assessment, this type of audit is limited in scope and duration and is not intended to cover all importing activities. Even ISA participants are not exempt from QRAs. QRAs tend to be more enforcement-oriented from the start, with the attendant risk of a penalty case at the conclusion of the audit being that much greater as well. A single-issue audit is generally initiated based on a referral from another CBP entity with the view that some aspect of a company's importing activities poses a potential risk that requires immediate scrutiny. It may also be initiated by a tip provided by a competitor or disgruntled employee.

A QRA operates similar to a Focused Assessment, but is smaller in scale. These audits are typically initiated at the local port level and the extent of scrutiny undertaken can vary depending on the port and personnel involved. Typically, a QRA will be wrapped up in a shorter period of time and will not involve significant or wide-reaching sampling. As discussed, if an importer finds an error while collecting information in response to an auditor request during a QRA, the benefits of filing a voluntary prior disclosure (discussed in Chapter 11) may possibly remain available. Single-issue audits can, and often are, the proverbial "slippery slope"—they can get out of control and spiral into a full Focused Assessment if the auditors find cause.

CONCLUSION

While it is true that CBP's stated goal of the Focused Assessment program is to work with importers in assisting with compliance, an audit is fundamentally concerned with compliance, enforcement, and identification and collection of loss of revenue—and it must be recognized for what it is. The old adage "an ounce of prevention is truly worth a pound of cure" applies to Focused Assessments. Importers that take the time to understand and thoroughly review their importing practices and identify and fix weak spots in their import operations will be in a better position to control the process and outcome of their Focused Assessment.

NOTES

1. Many thanks and credit goes to the original author of this chapter, Michael D. Sherman.
2. The Office of Regulatory Audit does not have the authority to collect underpayments, but it has the responsibility to advise the appropriate CBP collection officials of the amounts it believes are owed.

3. Office of the Inspector Gen., Dep't of Homeland Sec., OIG-12-117, Report on Customs and Border Protection's Office of Regulatory Audit (2012), 13, 17.

4. Prior to the advent of the Focused Assessment, CBP engaged in much broader-sweeping, data-intensive audits, known as Compliance Assessments, regardless of the company's internal control policies and procedures. See JOHN GOODRICH, *The Customs Focused Assessment—Part I: An Audit by Any Other Name* (Feb. 6, 2006), http://www.i-b-t.net/anm/templates/trade_article.asp?articleid=211&zzoneid=3 (last visited July 3, 2015).

5. In 2011, CBP published important amendments to section 163.11 that address CBP's ability to use statistical sampling as a method for calculating duties and fees owed in audits and allow the offsetting of overpayments against underpayments in certain circumstances. CBP Audit Procedures; Use of Sampling Methods and Offsetting of Overpayments and Over-Declarations, 76 Fed. Reg. 65953 (Oct. 25, 2011) (hereinafter, CBP Audit Procedures).

6. In January 2014, Audit announced its intention to make certain needed enhancements to the Focused Assessment program. CBP implemented the updated program in early fiscal year 2015 (see October 2014 updates to CBP Focused Assessment webpage at <http://www.cbp.gov/trade/audits/focused-assessment> (last visited August 20, 2015)). The more relevant changes affecting importers are addressed herein.

7. 19 U.S.C. § 1484.

8. CYNTHIA A. COVELL, FOCUSED ASSESSMENT PROGRAM (FAP) COVER LETTER, rev. Dec. 2002.

9. The cost of internal controls should not exceed the expected benefits; however, precise measurement of costs and benefits is not possible. Accordingly, CBP recommends that management makes both quantitative and qualitative estimates and judgments in evaluating cost-benefit relationships. See *Consideration of Internal Control in a Customs Compliance Audit, Exhibit 3B*, U.S. CUSTOMS AND BORDER PROTECTION, available at http://www.cbp.gov/sites/default/files/documents/exh3b_4.pdf (hereinafter "Consideration of Internal Control"; last visited July 3, 2015).

10. *Importer Self-Assessment Handbook*, U.S. CUSTOMS AND BORDER PROTECTION, available at http://www.cbp.gov/sites/default/files/documents/isa_hb_3.pdf (last visited July 3, 2015).

11. PTIs represent high-risk areas that can cause significant revenue loss, harm the U.S. economy, or threaten the health and safety of the American people. Focused Assessments are not limited to companies with PTIs, but the presence of a PTI makes it more likely that a company will be selected for a Focused Assessment. Current PTIs include AD/CVD, Import Safety, Intellectual Property Rights, Textiles/Wearing Apparel, and Trade Agreements. See <http://www.cbp.gov/trade/priority-issues> (last visited Nov. 4, 2014).

12. For information on how to obtain your ITRAC report, go to https://help.cbp.gov/app/answers/detail/a_id/1182/~/foia-importer-trade-activity-%28itrac%29-requests (last visited Nov. 4, 2014).

13. For additional information on how to participate in ACE, go to <http://www.cbp.gov/trade/automated> (last visited Nov. 4, 2014).

14. Audit Headquarters is in Washington D.C., with ten field offices currently located in Atlanta, Boston, Charlotte, Chicago, Houston, Long Beach, Miami, New York, Philadelphia, and San Francisco. In addition, field offices may have multiple branch offices in other cities. See <http://www.cbp.gov/trade/audits/field-offices> (last visited Nov. 4, 2014).

15. Auditors with special expertise with respect to either a particular customs area, such as valuation, or a particular product, such as petroleum, may be involved in the Focused Assessment regardless of their location.

16. Previously, an auditor would contact the importer to schedule an Advance Conference. This year, however, CBP announced that it was changing its process, as it no longer believes a formal Advance Conference is necessary. CBP is quick to note that auditors will still be available to the importer on an informational basis to explain the Focused Assessment process and provide reference materials.