

AMERICAN ASSOCIATION OF EXPORTERS AND IMPORTERS

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Testimony on "Customs Trade Facilitation and Enforcement in a Secure Environment"
before the House Ways and Means Subcommittee on Trade

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A. Introduction and Overview

Chairman Tanner, Ranking Member Brady and Members of the Committee, good afternoon. My name is Marianne Rowden and I am the President and CEO of the American Association of Exporters and Importers (AAEI). AAEI appreciates the opportunity to offer its comments on "Customs Trade Facilitation and Enforcement in a Secure Environment."

It is a privilege to appear before you today at this hearing, and we are honored that the Committee has again invited AAEI to provide our expertise about trade security related, facilitation and operational issues. We hope that AAEI's testimony provides tools to assist Congress overcome the hurdles that the international trade community has struggled with over the past several years since enactment of the Homeland Security Act, P.L. 107-296, 116 Stat. 2135 (November 25, 2002).

AAEI has been a national voice for the international trade community in the United States since 1921. AAEI represents the entire spectrum of the international trade community across all industry sectors. Our members include manufacturers, importers, exporters, wholesalers, retailers and service providers to the industry, which is comprised of brokers, freight forwarders, trade advisors, insurers, security providers, transportation interests and ports. Many of these enterprises are small businesses seeking to export to foreign markets. AAEI promotes fair and open trade policy. We advocate for companies engaged in international trade, supply chain security, export controls, non-tariff barriers, import safety and customs and border protection issues. AAEI is the premier trade organization representing those immediately engaged in and directly impacted by developments pertaining to international trade. We are recognized as the technical experts regarding the day-to-day facilitation of trade.

B. Enhancing Facilitation and Enforcement in a Secure Environment

AAEI's testimony on Enhancing Facilitation and Enforcement in a Secure Environment addresses the five issues explored in this hearing: 1) Successful Implementation of the Automated Commercial Environment (ACE) and the International Trade Data System (ITDS); 2) Advance Data for Security and Facilitation; 3) Account-Based Management; 4) CBP's Structure for Facilitation and Enforcement; and 5) Overcoming Challenges in Revenue Collection and Compliance Enforcement.

AAEI believes that Congress is at its best when it enacts legislation that provides a framework and tools to achieve certain outcomes rather than mandating processes to achieve a particular result. The Customs Modernization Act, passed as Title VI of the North American Free Trade Agreement Implementation Act (Pub. L. 103-182, 107 Stat. 2057), is a good model for this approach as it set the foundation for CBP's predecessor, the U.S. Customs Service, to manage the impact of trade liberalization and globalization – a feat unmatched by other federal agencies, despite a rash of "modernization" legislation enacted by Congress in the 1990's.

With today's hearing and subsequent legislation, this Committee has an excellent opportunity to refine the framework set forth in the Customs Modernization Act through the use of robust administrative tools in reauthorization legislation for CBP. AAEL believes that risk management is the "Rosetta Stone" by which Congress should guide CBP to allocate its resources and employ different administrative techniques. For each risk area identified by this Committee (e.g., security, facilitating legitimate trade, revenue collection, and enforcement), CBP needs to distinguish high-risk and low-risk companies. The only way for CBP to implement such a risk management strategy is by developing a profile of characteristics as criteria to determine in which risk category a company should be placed. Account-based management enhances CBP's ability to assess risks posed by U.S. companies and deploy their limited resources to the transactions that create the greatest threat to the safety of the American people. Both account-based management and transaction-based regulation require sophisticated use of data. This data is supplied by U.S. importers through the multiple data entry programs, before, during and after entry or through voluntary partnership programs.

1. Successful Implementation of ACE and ITDS

ACE and ITDS are the principal information technology infrastructure systems envisioned to handle both entry transactions and account-based data through reports aggregating, isolating and analyzing entry data. ACE is not only behind schedule and over budget, it has become the proverbial "chicken and egg" conundrum. Importers are not able to use ACE because of the limited functionality of ACE, and CBP is frustrated by the low number of importers with ACE accounts. This current stalemate makes it difficult for both CBP and the trade community to procure additional funding for ACE.

The same holds true for ITDS – Participating Government Agencies (PGAs) are no longer waiting for full development of ITDS to manage their data needs relating to imported or exported goods, and proceeding with agency specific systems. A major milestone was achieved with the enactment of Section 405 of the Security and Accountability for Every (SAFE) Port Act of 2006, P.L. 109-347, 120 Stat. 1929 (October 13, 2006), which requires:

[a]ll Federal agencies that require documentation for clearing or licensing the importation or exportation of cargo shall participate in the ITDS.

This section is now codified at 19 U.S.C. § 1411. This provision was implemented through a Memorandum for the Heads of Departments and Agencies issued by the Office of Management and Budget (OMB) which mandated the designation of senior executive to participate in the interagency team (ITDS PGAs) and to develop a plan for the agency "to complete each stage of its interface, including any necessary rulemaking and acquisitions." See, OMB Memorandum on "Requiring Agency Use of the International Trade System" (M-07-23) dated September 10, 2007, which may be found at <http://www.whitehouse.gov/omb/memoranda/fy2007/m07-23.pdf>. Therefore, completion of ITDS is not a "wish list" item for an agency's information technology system, but a statutory mandate and a Presidential directive to executive agencies.

Unfortunately some agencies, such as the U.S. Food and Drug Administration (FDA), have utilized scarce government resources to develop their own electronic systems designed to meet admissibility and compliance requirements. Other agencies, such as the U.S. Department of Agriculture are leading the effort with ITDS to assess the viability of developing a Product Information Code (PIC) system using existing public or commercial product characterization dictionaries which describe goods differently than the Harmonized Tariff Schedule. Examples such as these highlight the extreme urgency we face in completing ACE.

AAEI wishes to convey to the Committee that the trade community's support for ACE is still high as reflected in AAEI's recently completed 2010 Benchmarking Survey. This survey - completed by over 100 companies - showed that 74% of the respondents have an ACE account; however, only 56% of the companies use the reports function in ACE. Moreover, 25% of the respondents utilize the post-entry review functionality. Twenty-five percent use a combination of functionality available through ACE, including reports, entry status, post-entry review, and the preparation of prior disclosures. Most importantly, the clear majority of respondents (57%) to the Benchmarking Survey believe that ACE is worth the time and money spent if the system ultimately works. Please be aware that most of these responding companies are large importers with internal support structure for trade compliance, but we believe that ACE accounts fall precipitously once we look below the top 1,000 importers.

The choice for Congress is stark - either fund completion of ACE and ITDS or prepare to spend multiple times that sum on information technology for each federal agency which has responsibility for regulating imported or exported goods. Multiple information technology systems which are not interoperable and require independent data submissions create gaps in intelligence, targeting, and risk profiles for agencies who are now working together at operations centers. Clearly, Congress, CBP and the international trade community must work together over the next year to get ACE and ITDS back on track.

AAEI and a number of leading international trade associations recently issued a letter to U.S. Customs and Border Protection (CBP) outlining a "Transition Plan to ACE." In the letter, we focused CBP's attention on three critical deliverables: 1) cargo release; 2) account-based management; and 3) automating manual processes to eliminate duplicate data entry. AAEI also supports the ACE priorities set forth in the Trade Support Network (TSN) ACE Prioritization Recommendations dated November 5, 2009. The international trade community has shown continued support for the full implementation of ACE by providing ongoing time, effort and energy to the TSN. The members of the TSN have worked tirelessly over the last 10 years to partner with CBP in developing and rolling out a system that will work. The TSN has spent the better part of the past year developing an implementation plan that will work for CBP, the trade community, and the limited budget that both parties have. We urge you to consider allocating CBP's time and the government's resources to fulfill the deliverables set forth in TSN's recommendations.

We believe that by focusing on these basic deliverables, CBP can best utilize the limited funds appropriated by the Congress while fulfilling the "planned components" set forth in section 631 of P.L. 103-182:

- (A) The electronic filing and status of protests.
- (B) The electronic filing (including remote filing under section 414) of entry information with the Customs Service at any location.
- (C) The electronic filing of import activity summary statements and reconciliation.
- (D) The electronic filing of bonds.
- (E) The electronic penalty process.
- (F) The electronic filing of drawback claims, records, or entries.
- (G) Any other component initiated by the Customs Service to carry out the goals of this subpart.

See, 19 U.S.C. § 1411.

Finally, we bring to the Committee's attention that the President's Export Reform Agenda entails changes that will impact information technology infrastructure for ACE and ITDS. Administration officials tasked with developing the new export control regime are aware of the

SAFE Port Act requirements for ITDS, but CBP has not developed a conceptual overview of how ACE, the Automated Export System (AES) administered by the Census Bureau and maintained by CBP, and ITDS would interact. Therefore, we recommend that the artificial bifurcation of import and export be eliminated – at least for data collection purposes.

To ease the ACE programming burden and to facilitate the efficient filing of drawback claims, the drawback simplification legislation developed in partnership between CBP and the trade community should be enacted. AAEI believes that drawback simplification would support the President's export promotion agenda while the ACE programming and implementation costs would be quickly recouped through electronic filing and tracking of claims.

AAEI believes that this Committee must continue its critical oversight function to ensure that scarce funding is used effectively by CBP over the next fiscal year for continued development of ACE.

2. Advance Data for Security and Facilitation

AAEI supports CBP's mission of securing our homeland while facilitating legitimate trade. We believe that advance data initiatives provide CBP with powerful information tools – if used properly. Since 9/11, AAEI members have willingly provided additionally data to CBP for trade security purposes – both on a transaction basis and as members of the voluntary Customs-Trade Partnership Against Terrorism (C-TPAT), an account-based program. Now with the implementation of the Importer Security Filing (ISF or 10+2) interim final rule, AAEI's members have become increasingly weary of additional demands for data – many of which are merely duplicate submissions of the same basic data but required at different points throughout supply chain.

Since 2007, AAEI has been tracking the various federal government, private and multi-lateral security programs affecting the international trade community in "The American Trader's Guide to Post 9/11 and Homeland Security Programs." We have recently updated this chart to reflect the implementation of ISF as well as the addition of several new programs: Canada's Importer Admissibility Data (know as "10+2+3"), the European Union's Advance Transport Data program, the Transportation Security Agency's 100% Screening of air cargo requirement, FDA's Predictive Risk-based Evaluation for Dynamic Import Compliance Targeting (PREDICT) program and Secure Supply Chain pilot, the Department of Homeland Security's Chemical Facility Anti-Terrorism Standards (CFATS) requirements as well as development of PIC for ITDS. As the chart demonstrates, the distinct security programs proliferate unabated nearly a decade after 9/11 – all of which drain finite resources from both the government and the private sector without multiplying the effectiveness of homeland security.

Almost all of the ISF data elements required to be filed by U.S. importers prior to 24 hours of lading the cargo at the port of export were already required via the entry documents, which are furnished at a later point in the supply chain. The biggest shift is making the U.S. importer of record responsible for data collection earlier in the supply chain than its ability to verify the data as they neither have control or legal title to the goods to meet U.S. requirements.

In response to AAEI's 2010 Benchmarking Survey, 55% of the importers indicated that the ISF data requirement was "somewhat difficult" to implement, in large part because of dealing with overseas suppliers (58%). As one AAEI member noted, his company's internal processes and data systems were designed around U.S. import requirements using data over which his company (the U.S. importer) has total control. Now, as a result of ISF, the company as the U.S. importer of record is responsible for the filing and accuracy of data developed by the foreign supplier over which the U.S. importer has little actual control. Unfortunately, 50% of

the companies responding to AAEL's 2010 Benchmarking Survey believe that ISF will not enhance supply chain security.

3. Account-Based Management

The heart of risk management must be account-based management, which is essentially a pre-entry assessment of a company's risk profile and a post-entry assessment of its actual compliance with U.S. customs laws. In order for account-based management to be successful, CBP needs to make Account Managers the backbone of its trade compliance structure.

After enactment of the Customs Modernization Act, Customs was able to clearly identify the risk posed to the revenue of the United States – the top 1,000 importers accounted for 70% of the value of U.S. imports. As a result, Customs embarked on a series of audits designed to ensure that the compliance rate of these top 1,000 importers was above 96%. First, Customs used the Customs Assessment Team (CAT) audits which took a sampling of 200 line items and audited the entries relating to those line items. The CAT audits often took up to two years to complete and were an enormous drain on both Customs' and the company's resources. After reviewing ways to refine the CAT audit, Customs realized that there was a high correlation between a company's internal controls and its compliance rate. As a result, it developed a new risk-based approach to customs audits, the Focused Assessment (FA) audit, which looked at the strength of the company's internal controls before conducting an audit based on a smaller sample size than the CAT. This approach was complemented by changes in corporate governance brought about by the Sarbanes-Oxley legislation, and remains the audit model that CBP currently uses.

During this time, in 2002, CBP developed the Importer Self-Assessment (ISA) program, another voluntary CBP-business partnership that allows the company to monitor its own compliance to U.S. trade laws and regulations. In order to join ISA, a company must be a member of C-TPAT (also a voluntary program) and demonstrate that its internal controls mitigate against various customs risk areas (e.g., tariff classification, valuation, origin and marking, NAFTA claims, etc.). After a company is accepted into the ISA program, it conducts post-entry self-assessments of the company's entries on which it reports the results to CBP on an annual basis. There is an understanding that the company will submit a prior disclosure to correct any errors and a compliance improvement plan to strengthen its compliance program to mitigate the risk of such a violation recurring. Companies that join ISA are removed from CBP's pool of importers subject to a Focused Assessment audit.

AAEL has designed a chart entitled "A Multi-Layered Approach to Holistic Risk Assessment" which categorizes importers by risk based on certain characteristics. For example, companies which are "ultra-low risk" are those who join public-private partnership programs (such as C-TPAT or ISA) because they work with CBP on a continual basis to ensure that their compliance level is high. Importers which import cargo from low-risk countries should be designated as low-risk, whereas importers that have high-risk characteristics or import from high-risk countries are medium-risk, and unknown importers with infrequent shipments from the highest risk countries pose the highest risk for both trade compliance and supply chain security. However, such assessments can only be made using an account-based system whereby CBP develops a risk-based methodology to create a company profile for CBP to determine the appropriate tools for the level of risk posed by the company.

National Account Managers are assigned to companies who enroll in the ISA program to serve as the "single point of contact" for the importers to coordinate compliance issues. Unfortunately, the knowledge and skill of account managers vary widely as CBP has not fully embraced or promoted the critical role of account managers in its overall trade compliance

strategy. Currently, there are less than 50 full-time national account managers handling approximately 200 ISA companies. In part, we believe this is because CBP remains culturally a law enforcement agency. AAEL believes that expansion of the ISA program to the top 1,000 importers is critical for CBP to make significant progress in managing trade compliance risk accounting for 70% of the value of imported trade (i.e., revenue collection and customs enforcement). For reasons that are not entirely clear, CBP has not promoted ISA as aggressively as C-TPAT (which has over 9,000 members), and as a result, the program only has about 200 member companies, a number that has been static over the last few years. After nearly a decade, the number of national account managers and ISA members do not reflect a sincere commitment by CBP to make this program a reality or a success.

AAEL continues to work with CBP and other trade associations on developing industry coalitions to negotiate enhanced benefits for the ISA program. In 2007, AAEL completed an "industry ISA" for the chemicals industry after two and half years of negotiations with CBP. (The aerospace and petroleum industries have also negotiated "industry ISA's" with CBP.) Currently, AAEL is working with CBP to negotiate another "industry ISA" for the pharmaceutical/biotechnology industry, which is a high value industry. AAEL commends CBP's willingness to work with the trade to use the ISA program to enhance trade compliance and provide benefits to importers reducing regulatory burdens imposed by current requirements, but such negotiations are painfully slow.

Many AAEL members remain concerned about CBP's use of Quick Response Audits (QRAs), which are single-issue audits with a narrow focus. We understand that CBP intends to use QRAs on specific risk areas, such as transshipments or intellectual property rights. However, CBP has stated that companies who have applied for or are current members of the ISA program are not exempt from QRAs. Anytime importers and exporters commit their companies' limited resources to multi-year sustaining voluntary programs, they must receive defined benefits to make their choice the right choice from a compliance, security, safety and business point of view.

As noted previously, CBP has found a correlation between companies with good internal controls and highly compliance rate with U.S. customs laws. It is this correlation which forms the foundation of ISA, and can support the development of account-based management programs. Companies join ISA in order to be removed from the annual Focused Assessment audit pool so that they can devote the resources necessary (e.g., compliance personnel) to conduct the periodic self-audits required by ISA. ISA requires companies to document these periodic audits. As a result, many AAEL members are now asking "Why did our company spend the time and resources to join ISA if we are still subject to QRA audits?" AAEL supports ISA's risk-based analysis of companies' business processes, and is concerned that CBP's use of QRAs will undermine the risk management principles that are the foundation of the ISA partnership forged between the agency and trade in continuing to expand the program. Not exempting ISA importers from QRAs is a contradiction in CBP policy.

4. CBP's Structure for Facilitation and Enforcement

Since the reorganization of customs revenue functions in the Office of International Trade (OT) in the SAFE Port Act, we have become concerned that it does not appear that the creation of OT has resulted in any discernible trade community benefits or enhanced efficiencies attributable to the creation of that office. First and foremost among our concerns is the additional administrative layers of review that further diminish the efficiencies and effective operation of its current sub-offices, particularly the Office of Regulations & Rulings (OR&R).

It is our perception that the current OT structure serves as an impediment to trade facilitation, compliance and enforcement. First, it stymies importers from obtaining rulings expeditiously from OR&R prior to the importation of the merchandise. Secondly, importers are unable to complete settlement offers for violations with the Office of Chief Counsel. Both are subject to OT management review. We understand that OT management needs to be apprised of matters that involve policy issues which may change CBP's position or treatment of merchandise, but it is inappropriate in routine matters.

In November 2009, AAEI brought its concerns to then CBP Acting Commissioner Ahern who expressed interest in discussing these issues, but did not have the opportunity to do so before his retirement. Since this structure is set in statute, we believe it is within the purview of Congress to assess the effectiveness of the current arrangement. This current state of affairs dissuades importers from seeking prospective advice from CBP and undermines the heart of the Customs Modernization Act's concept of "shared responsibility" for compliance between CBP and importers.

CBP has also perplexed the international trade community by issuing proposed rulemaking notices (or announcing a change in position via the Customs bulletin) on long-settled customs issues such as the elimination of the First Sale Rule (i.e., using the value paid by the foreign seller as the declared value for entry of goods clearly destined to the United States) and the elimination of the "substantial transformation" test in favor of tariff shift rules to determine origin of merchandise. Both of these basic rules of customs laws have been the subject of litigation and case law through the U.S. Court of International Trade and other federal courts whose decisions are binding on CBP as well as importers. While these proposed changes are "on hold," U.S. importers are upset at the prospect of changing their trade compliance programs on fundamental issues by overturning settled case law, and revising matters that do not pose a high-risk for non-compliance, particularly in light of other high priority changes such as ISF and product safety requirements.

5. Overcoming Challenges in Revenue Collection and Compliance Enforcement

AAEI believes that adoption of account-based management tools would enhance CBP's revenue collection and increase the trade community's compliance rate. For trade sensitive areas, such as intellectual property rights (IPR) and anti-dumping/countervailing duties (ADD/CVD), additional tools can be developed to mitigate these risks within the framework of account-based management. CBP would then be free to use its resources to take enforcement action against importers who are not in C-TPAT, ISA or another account-based management program. We also note that enforcement of trade laws is an important part of the President's National Export Initiative (NEI), and as a result, we believe there will be a convergence between import and export practices which will have the effect of supporting increased enforcement.

C. Conclusion

In conclusion, we wish to thank the House Ways and Means Subcommittee on Trade for its invitation to provide our observations, comments, and suggestions on the "Customs Trade Facilitation and Enforcement in a Secure Environment." We greatly appreciate the Committee's oversight obligation to ask tough questions about whether CBP's efforts to ensure that trade facilitation equals trade security. We hope that our testimony will provide practical ideas for the Committee in developing legislation to reauthorize CBP, and we are happy to answer any additional questions you may have or provide further clarification and information on any of the ideas described in our testimony today. AAEI looks forward to both supporting this Committee's active involvement and to continuing our partnership with CBP in pursuit of these goals.