

**TRADE AND PASSENGER PROCESSING:  
Customs NAFTA Enforcement Program  
Information Is Limited**

OIG-02-096

June 19, 2002



**Office of Inspector General**

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The Department of the Treasury

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## Abbreviations

ACS	Automated Commercial System
OIG	Office of Inspector General
CF	Customs Form
CM	Compliance Management
EET	Enforcement Evaluation Team
FP&F	Fines, Penalties and Forfeiture
FY	Fiscal Year
ISDA	Import Specialist Discrepancy Add
JVT	Joint Verification Team
NAFTA	North American Free Trade Agreement
OST	Office of Strategic Trade
RAD	Regulatory Audit Division
SEACATS	Seized Asset and Case Tracking System
STC	Strategic Trade Center
TASP	Trade Agreement Sub Plan

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*The Department of the Treasury  
Office of Inspector General*

June 19, 2002

Mr. Robert C. Bonner  
Commissioner  
U.S. Customs Service

The North American Free Trade Agreement (NAFTA) provides preferential tariff treatment for merchandise imported from Canada and Mexico that qualify under specific rules of origin. Customs created the North American Free Trade Agreement Subplan (TASP) to ensure that only goods entitled to NAFTA duty-free benefits were given such treatment. The TASP consists of enforcement tools such as mandatory Compliance Measurement (CM) Verifications, port-initiated verifications, Joint Verification Teams (Regulatory Audit Division reviews), and enforced compliance. Penalties would be assessed for NAFTA violations.

This audit was included in our *Office of Inspector General Annual Plan for FY 2001*. We performed the audit to determine the adequacy of Customs efforts to identify and penalize violators who falsify country of origin in order to qualify for NAFTA duty-free treatment. We conducted our audit work from August 2000 through February 2002 at Customs headquarters, and at seven Customs ports of entry that process the majority of NAFTA-related entries. A more detailed description of our objective, scope and methodology is provided in Appendix 1.

## Results in Brief

We could not fully assess the adequacy of Customs enforcement efforts to identify NAFTA noncompliance or identify and penalize violators, because Customs does not have accurate and sufficient NAFTA enforcement data. Customs does not have a reliable tracking system that identifies and allocates monies generated from

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NAFTA enforcement activities such as mandatory and port-initiated verifications and penalty actions. In addition, because it is difficult to identify NAFTA penalties from Customs Seized Asset and Case Tracking System data, accurate NAFTA penalty data is not available to determine if penalties were appropriately assessed for NAFTA violations.

The systems for recording noncompliant NAFTA claimants and the collections of duties from these parties were not reconciled. Also revenue recoveries from penalty cases were not consistently recorded and reconciled with the collections for violations of NAFTA regulations. As a result, Customs has no means of measuring the effectiveness of its NAFTA enforcement efforts.

In addition, we found that the Regulatory Audit Division (RAD) has not been able to identify significant noncompliance from its NAFTA-related audits. While we do not have evidence that significant noncompliance exists, we believe RAD could enhance its opportunity to identify noncompliance by modifying how it selects potential noncompliant claimants for audit. Customs targeting efforts have centered almost solely on large importers and manufacturers who appear to have generally followed NAFTA rules of origin, instead of reviewing industries and companies that have shown trends of noncompliance, and who have been scrutinized by port personnel who process import entries for NAFTA filers.

We recommended that Customs implement a (1) tracking system that accurately accounts for Customs NAFTA-related enforcement efforts and (2) RAD audit targeting strategy that includes more of a risk-based focus.

## Background

### Significance of NAFTA

The Customs Service's Strategic Plan for Fiscal Years (FY) 2000 through 2005 has, as one of its objectives, improving the enforcement of international trade agreements. NAFTA is by far the largest of these trade agreements. Approximately 40 percent

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of all entry lines in FY 2001 were subject to a claim for reduced duty treatment under NAFTA.

In passing NAFTA, Congress appropriated a significant amount of funds and resources for the verification of NAFTA claims. Therefore, it is important for Customs to demonstrate that it is effectively enforcing NAFTA trade provisions.

Customs created the TASP to ensure that only goods entitled to NAFTA preferential treatment actually receive such treatment. The TASP consists of the following components: mandatory CM verifications, port-initiated verifications, joint verification teams (JVT), and enforced compliance that we reviewed in our audit.

### **Verifications of NAFTA Claims**

NAFTA authorizes each member country to conduct verifications to confirm imported merchandise is eligible for NAFTA benefits. Verifications are conducted by import specialists via either a *Request For Information* (CF-28), a *NAFTA Questionnaire* (CF-446) or by on-site visits to exporter or producer sites in Canada and Mexico.

Customs completed 2,110 mandatory verifications in FY 2001. Each port of entry is provided with lists of specific line items that they are required to verify. Eight ports of entry accounted for approximately 80 percent of the NAFTA line items verified by the Customs Service.

The results of the verification are entered into the Import Specialist Discrepancy Add (ISDA) module of the Automated Commercial System (ACS). In addition, automated ports also input their results directly into the NAFTA database while non-automated ports will mail or fax their results to Customs personnel in Buffalo, NY, and to the Trade Agreements branch in Headquarters. Whenever NAFTA benefits are denied, Customs generates a bill and collects applicable duties and fees plus interest.

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The results of the mandatory verifications are compiled and a compliance rate is calculated and reported by Customs. For NAFTA transactions, Customs has established a compliance goal of 95 percent and the collection of 99 percent of all NAFTA-related duties, fees, and interest by the year 2005. However, Customs has recently reported a 96 percent NAFTA compliance rate and a 99 percent revenue collection rate for FY 2001 NAFTA-related transactions.

Similar to mandated verifications, Customs ports are assigned to review import entry line items to ensure they qualify for NAFTA duty free benefits in a port-initiated verification. Each year Customs is required to perform 800 port-initiated verifications that are assigned to each port. The verification techniques are identical to those used in the mandatory verifications and the results are also entered into the ISDA module in ACS and into the NAFTA database. During FY 2001 a total of 1,425 port-initiated verifications were completed.

As with mandatory verifications, when non-compliant importers are identified, bills are generated for collection of duties, fees and interest owed to Customs. Customs has reported a 70 percent compliance rate for port-initiated verifications. This lower compliance rate compared to the mandatory rate is understandable since these reviews typically focus on problem importers and high-risk merchandise.

A JVT is composed of a regulatory auditor, import specialist and international trade specialist, with other team members as necessary. JVTs are conducted annually and involve audit-based verifications of NAFTA claims from approximately 40 importers. The Office of Strategic Trade (OST), RAD, selects the companies to be audited.

### **Enforced Compliance**

Each Customs service port is required to maintain an Enforcement Evaluation Team (EET) led by a port trade compliance program officer and an Office of Investigations representative. Additional

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members may include an account manager, a RAD audit manager, the local Fines Penalties & Forfeiture (FP&F) officer, a supervisory import specialist and a compliance assessment team leader. EETs are required to meet at least once a month.

Customs officers make NAFTA enforcement referrals to their local EET, who assess and prioritize violations and allegations, and select the appropriate enforcement action. If the impact level warrants, the EET refers the violation or allegation to the local trade enforcement coordinator for action. Low impact violations are returned to the referring officer for administrative resolution.

### **Penalty Cases And Prior Disclosures**

The two main types of penalty cases that affect NAFTA transactions involve violations of 19 USC 1592 and of 19 USC 1509. The provisions of 19 USC 1592 authorize penalties against any person who enters any merchandise into the commerce by fraudulent means. The penalty provisions of 19 USC 1509 can be invoked whenever certain persons fail to produce, upon demand, an entry record enumerated in Customs Regulations. This includes individuals who complete and sign a NAFTA Certificate of Origin.

A valid prior disclosure is an admission of a violation of 19 USC 1592. This section of law permits Customs to assess monetary penalties against parties who make material false statements, acts or omissions in connection with their importations. Parties who elect to make a complete disclosure of such a violation before or without knowledge of a formal Customs investigation of the violation are eligible for reduced penalties.

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## Findings and Recommendations

### Finding 1      Customs Does Not Track Its Efforts To Improve NAFTA Compliance

Customs does not have a reliable tracking system that accurately summarizes the revenue recoveries resulting from its NAFTA verifications and penalty actions. Customs maintains its NAFTA enforcement program activity in several databases—the NAFTA database, ISDA Module, ACS module, and the Seized Asset and Case Tracking System (SEACATS)—but these databases do not reconcile with each other and only raise further questions about the actual benefits achieved from enforcement activity. As a result, Customs cannot ensure that resources committed to various program efforts are being effectively or efficiently utilized. Specifically, we found that:

- there was no system link between the databases and collection records to ensure that revenue recoveries reflected the dollar amounts collected from importers,
- the listing of NAFTA penalties identified by Customs Headquarters FP&F was not appropriately updated in the NAFTA database with amounts collected from penalties,
- it is difficult to identify NAFTA penalties from existing SEACATS data, and
- the SEACATS listing was incomplete, as amounts collected from prior disclosures for non-compliant filers were not consistently recorded as penalties by each port.

We believe that Customs should focus more attention on accurately recording and accessing the results of its enforcement efforts in ensuring NAFTA compliance. This information would allow Customs to better evaluate its current performance and plan its future enforcement efforts.



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### **NAFTA Database Is Inaccurate**

Most NAFTA enforcement activity is devoted to conducting the annual mandatory and port-initiated verifications. Import specialists are required to verify NAFTA eligibility for thousands of line items and to calculate any projected revenue recoveries that result from denial of NAFTA benefits. These recoveries usually consist of duty amounts, fees, and taxes that were not assessed at the time entry was made.

Once these revenue amounts are determined, the import specialists enter the amounts into the ISDA module in ACS and into the NAFTA database. Entry personnel use the ACS collection modules for billings and collections of duties from NAFTA denials.

The results of enforcement efforts, including both the mandatory verifications and port-initiated verifications, showed discrepancies between the amounts reported in the NAFTA database and the amounts collected by Customs personnel. During a 21-month period covering October 1999 through June 2001, the seven major ports in our review completed a total of 2,545 mandatory verifications, 65 of which resulted in NAFTA denial, and 1,675 port-initiated verifications, 635 of which were denied.

We reviewed 56 of the 65 mandatory verifications that were denied, and 260 of the 635 port verifications that were denied. We found that discrepancies occurred in the databases for each type of verification, although the mandatory verifications yielded smaller discrepancies. In the 260 line items from port verifications, we found a total of \$639,929 in revenue recoveries had been input into the NAFTA database but only \$204,730 were identified as actually collected in the ACS module. Discrepancies were found in 187, or 72 percent, of these line items, totaling \$435,199 as follows:

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**Table 1. Discrepancies Between The NAFTA Database  
And The ACS Collections System**

Discrepancy Category	Line Items with Exceptions	Dollar Amount Of Discrepancies
Collections Exceeded Database Amounts	80	(\$ 8,141)
Database Amounts Not Collected	28	43,714
Collection Not Entered Into Database	24	(13,447)
Database Amount Exceeded Collection	55	413,073

The largest number of discrepancies, though not in dollar amount, resulted from the posting and payment of interest in ACS. The potential revenue recoveries entered into the NAFTA database do not include interest.

In certain instances, the amounts billed were successfully protested by importers and the bills were cancelled but never updated in the database. In other cases, there was no evidence of any collection being initiated or outstanding bills for amounts reported in database. In addition, we found a case in which the amount in the database may have significantly overstated the revenue recovery. The entry had \$256,641 recorded in the NAFTA database, but when ACS was queried for that entry only \$2,755 was entered as collected.

Further, there were several instances in which collections were deposited but the corresponding revenue amounts had not been input into the database. In these cases, it appeared that the import specialist failed to record the amount of revenue recovered.

#### **Inaccurate Penalty And Prior Disclosure Records**

Several ports showed discrepancies between the revenues reported from penalties as recorded in penalty case files with the amounts shown on the listing provided by Customs Headquarters FP&F. For example, at Champlain, NY, there were three penalty case files in which the revenue recovered did not agree with the amounts

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recorded on the listing. At Laredo, TX, a penalty case with a collection recorded in the amount of \$500 actually generated a \$24,027 collection. The listing had only three penalty cases for Buffalo with revenue recoveries collected for each case. However, we determined that 2 of the 3 cases had been cancelled with no revenue recoveries.

The listing also contained cases that did not involve NAFTA violations. At the port of Detroit, 1 of the 9 cases listed on the FP&F listing was not a NAFTA case while at the port of St Albans 1 of the 7 cases listed was a drug seizure case.

One reason for discrepancies was the different handling of prior disclosure cases. Prior disclosures are admissions of violations that are sent to the local FP&F officer, often accompanied by a check for monies owed Customs.<sup>1</sup> We found that whether or not these cases were treated as penalty cases depended on the port. For example:

- At the port of Buffalo, only three cases were on a Headquarters listing provided by FP&F showing revenue recoveries because of the frequent receipt of valid prior disclosures that the port did not record as NAFTA penalty cases.
- At St. Albans, prior disclosures were reviewed and closed without being designated as penalty cases.
- In the penalty case files at the ports of Otay Mesa, CA, and Detroit, MI, prior disclosures were assigned penalty case numbers unlike Buffalo, NY. For the port of Detroit, a case was listed with a \$10,000 revenue recovery for which there was no documentation. This case, however, was a prior

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<sup>1</sup> When a prior disclosure is made, there could be a number of reasons for its submission. It may be the result of a company's discovery of an honest mistake, or it may be the result of some type of action taken by Customs personnel. In these cases import specialists will make contacts and queries with companies, often in mandatory and port-initiated verifications about NAFTA filings that reveal duties that should not have qualified for NAFTA duty-free status. There are cases in which companies are made aware of an upcoming JVT audit, so they concede to errors in their claim for NAFTA duty free benefits. Other companies become aware that competitors have been targeted and found ineligible for NAFTA benefits and disclose this information to Customs.

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disclosure case and a \$135,000 recovery was collected by Customs.

The revenue recoveries from these prior disclosures are not properly allocated to the enforcement effort that may have prompted such action on the part of the companies. To review this issue we requested from the Dallas Strategic Trade Center (STC) a report of all prior disclosures for the period during April 24, 2000, through November 3, 2000. This listing showed thirty prior disclosures totaling almost \$5.9 million that had been submitted to Customs. This listing, however, did not identify the source that generated the prior disclosure in order that the revenue generated was properly recorded for the port. This additional information would allow Customs the means of measuring the performance of the NAFTA enforcement program.

#### **Improving Validity And Reliability Of Revenue Data**

The numerous discrepancies in revenue recoveries being entered into ACS and the NAFTA database limit their usefulness as sources for valid data on actual revenue recoveries that result from NAFTA verification. However, we believe, with a minor adaptation, the NAFTA database can be used as the source of determining actual revenue recoveries.

NAFTA coordinators already monitor their port's compliance with mandated and port-initiated verifications. They have access to the NAFTA database and can easily identify those line items denied NAFTA benefits and the amounts of revenue recoveries entered by the import specialists. NAFTA coordinators, on an annual basis, could query ACS and determine actual revenue billed and collected for those line items as well as for those that were cancelled as a result of successful protests.

The line items of NAFTA denials is not voluminous. To illustrate, for the seven major NAFTA ports of entry there were approximately 700 potential line items that were denied NAFTA benefits in the 21-month period from which we selected the

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mandatory and port-initiated verifications to review. This averages out to approximately five line entries per month per port of entry that would need to be queried and results tracked by the NAFTA coordinators.

We believe this additional step would provide a valid and reliable means of determining actual revenue recoveries. It would require a minimal effort by a small number of personnel who are already charged with monitoring NAFTA transactions. It would recognize the successful efforts of port personnel in ensuring that parties not eligible for NAFTA benefits are being identified and revenue due the government is being billed and collected. It would also demonstrate additional evidence that Customs, through its effective use of TASP resources, is able to ensure a high degree of NAFTA compliance.

### **Recommendations**

1. The Commissioner of Customs should ensure that Customs personnel implement a TASP related tracking system that accomplishes the following:
  - identifies revenue recoveries from NAFTA enforcement activities for Customs Management Centers with the necessary details for management;
  - requires a periodic reconciliation of ACS collection and revenue recoveries records;
  - provides an annual report of the accomplishments of TASP enforcement efforts; and
  - utilizes TASP performance results to evaluate the deployment of NAFTA related resources.

Management Comments. Customs concurred. Customs will compile protected revenue data from denied 520 (d) claims, and will conduct a feasibility study to determine how to reconcile ACS collection and revenue recovery records. Customs will implement a reconciliation process that will be done annually if this study finds it feasible to do so. An annual report on TASP

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accomplishments will be produced, and the performance results will be used to evaluate deployment of NAFTA resources. The planned completion date for these actions is June 30, 2003.

OIG Comment. We consider this recommendation to have a management decision with final action to be completed at June 30, 2003.

2. The Commissioner of Customs should ensure that Customs personnel are handling prior disclosures in a uniform manner.

Management Comments. Customs concurred and stated that a working group has been established to focus on establishing policies and procedures to uniformly handle prior disclosures with the goal of developing a Prior Disclosure Directive. The planned completion date for this action is June 30, 2003.

OIG Comment. We consider this recommendation to have a management decision with final action to be completed at June 30, 2003.

## Finding 2

### **Customs NAFTA Audits Have Not Identified Significant Noncompliance**

Based on the results of RAD audits, significant noncompliance with NAFTA has not been identified. Customs targeting has centered on large importers and manufacturers that have been highly compliant with NAFTA rules of origin. As a result, the majority of audits conducted have not reported evidence of NAFTA discrepancies nor have they resulted in significant revenue recoveries. In order to enhance enforcement efforts to identify noncompliance, Customs should develop a targeting strategy that considers significant areas of risk, the companies' NAFTA filing histories, and referrals from port personnel.

#### **Office Of Strategic Trade Recommends Risk-Based Audits**

Results from prior regulatory audits of NAFTA have not yielded significant revenue recoveries. RAD personnel reported that only

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20 out of 225 NAFTA audit teams conducting audits during May 1995 through May 2001 had identified any negative NAFTA determinations. The 20 audits had yielded about \$8.7 million in additional revenue, with over \$5 million of that total resulting from a single audit. Each year, as part of the TASP, RAD selects and assigns 40 audits to be conducted by teams in various field locations.

OST conducted a review of RAD audits because RAD's reviews had not identified or resulted in significant NAFTA revenue recoveries. They wanted to ensure that future selections for audits were risk based and more likely to identify material report discrepancies. OST concluded that there were no established patterns of NAFTA non-compliance that were identified in the audits, and that OST and RAD needed to evaluate the use of resources to perform reviews that were not resulting in any significant NAFTA issues.

The OST review also recommended that an effort be undertaken to identify risk areas that future audit selections would be based on. OST organized the NAFTA Task Force that would recommend to RAD the areas that should be audited. The majority of this Task Force work was assigned to the Dallas STC.

Personnel at the Dallas STC identified 313 major importers that account for 60 percent of the total value of NAFTA imports. At the time of our reviews, the STC personnel were in the process of developing individual profiles for each of the 313 candidates. Each profile addressed the major risk elements that Customs has identified as being inherent in NAFTA transactions. The Dallas STC also devised a targeting strategy that assigned a numerical risk factor to each specific NAFTA rule of origin based upon the difficulty in meeting the requirement for each rule. As a result, candidates that must meet tougher requirements to qualify for NAFTA benefits are more likely to be targeted for audit.

Upon completion of its targeting initiatives that was planned for completion at March 2002, the Dallas STC would forward the results to OST personnel in Customs Headquarters. The results

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would be used as the basis for targeting candidates for audits and will also be used to aid port personnel in selecting candidates for port-initiated NAFTA verifications.

### **RAD Should Enhance Targeting Of Noncompliance**

Customs has historically focused its resources on covering those industries or companies that account for the majority of NAFTA transactions. During the period FY 1997 through FY 1999, many of the audit candidates were selected from the automotive and telecommunication industries. The importations pertaining to these industries comprised 85 percent of the total value of NAFTA merchandise that entered the country. As a result, Customs can accurately report that it is dedicating its limited audit resources to cover a substantial segment of NAFTA-related importations.

We realize that Customs has to maximize the efficient use of limited resources. Customs, however, could enhance its identification of non-compliance if it also considered smaller companies that could pose a risk, and review requests from port personnel to investigate suspected noncompliance. These personnel have the experience with the companies' NAFTA filings and could identify problems.

Revenue recoveries resulting from RAD work involving the petroleum industry illustrate how a particular industry may yield results when RAD targets a potentially non-compliant industry. Of 248 audits that were finalized during May 1995 and November 2001, a total of 38 audits resulted in revenue recoveries totaling around \$11.9 million of which \$9.5 million or approximately 80 percent pertained to five audits that involved petroleum importations. RAD has the potential of identifying additional NAFTA noncompliance and revenue recoveries in the future if they focus audit selections on those industries with such filing histories.

To support the issue of noncompliance in this industry, we found that in a report prepared by Chicago STC that there was a high risk associated with oil and petroleum derivatives for which specific



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Canadian-based companies were claiming NAFTA benefits. The report identified seven specific companies that should be considered as potential candidates for audits. Three of the seven were audited and \$3.8 million in revenue recoveries was reported.<sup>2</sup>

In order to target non-compliant filers, Customs may want to consider the companies filing histories as well as port personnel audit referrals of potentially high-risk small importers that have not historically been selected by RAD. Because of their experience and knowledge of local manufacturers and importers, field personnel are in a good position to establish noncompliance issues, and their requests should be more of a priority for RAD to address. If Customs wants to be effective in identifying noncompliance, it may need to modify its strategies.

We believe that any targeting strategy that is ultimately developed and implemented needs to ensure there is efficient coverage for noncompliance issues, and that enforcement efforts are properly targeted. As part of this, Customs existing policy for establishing audit schedules should be enhanced with a review of all sources NAFTA noncompliance, such as industry results of prior audits, and referrals from port personnel who have knowledge of companies' NAFTA import entries.

### **Recommendation**

1. The Commissioner of Customs should ensure that Customs finalizes and implements a NAFTA Targeting Strategy this fiscal year and that the Office of Inspector General be provided with a copy. The Targeting Strategy should address areas of risk and include the following:
  - justification for targeting parties for RAD compliance audits that include high risk companies; and

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<sup>2</sup> Changes to the current rules of origin for oil have been agreed upon by U.S., Canada, and Mexico. The changes will allow NAFTA duty-free benefits to those who under the current rules of origin would have been denied. The U.S. and Canada have completed their formal notification and comment periods for the new rules and are waiting for Mexico to initiate a formal review. These new rules will not be effective until Mexico completes this review process.

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- consideration of port referrals of potentially noncompliant filers.

Management Comments. Customs concurred and is in the process of developing a risk-based strategy for targeting NAFTA verification candidates. This strategy will include procedures for field personnel to communicate referrals and recommend candidates for verification by means of an audit. Customs also noted the limitations in determining the relationship between actions taken and compliance results in enforcement of trade agreements as complex as NAFTA, and the impossibility of measuring the effect of discontinuing audits for candidates not deemed as high-risk on the NAFTA compliance rate. Planned completion for this action is September 30, 2002.

OIG Comment. We consider this recommendation to have a management decision with final action to be completed September 30, 2002. We recognize the considerations noted by Customs that need to be made when Customs develops this risk-based strategy for targeting NAFTA audit candidates.

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We would like to extend our appreciation to Customs for the cooperation and courtesies extended to our staff during the review. If you have any questions, please contact me at (617) 223-8640 or a member of your staff may contact Sharon Torosian, Audit Manager, at (617) 223-8642. Major contributors to this report are listed in Appendix 3.

/S/

Donald P. Benson  
Regional Inspector General for Audit

The objective of this audit was to determine the adequacy of Customs efforts to identify and penalize violators who falsify country of origin in order to qualify for NAFTA duty-free treatment.

To achieve this objective we reviewed policies and procedures pertaining to the processing of NAFTA-related transactions. We also reviewed the policies regarding the implementation of the NAFTA Trade Agreement Sub Plan. We verified operational statistics reported by Customs regarding NAFTA determinations, and verifications. We conducted on-site fieldwork at the following major NAFTA ports of entry:

St. Albans, Vermont	El Paso, Texas
Champlain, New York	Laredo, Texas
Buffalo, New York	Otay Mesa, California
Detroit, Michigan	

We selected a judgmental sample of NAFTA verifications to determine the validity and reliability of information in the Customs NAFTA database to source documents maintained by port personnel. We determined that Customs personnel billed and/or collected revenue due when NAFTA benefits were denied. For each port we visited we verified that self-inspections were conducted and that Enforcement Evaluation Teams were in operation and were reviewing NAFTA-related issues. We also verified the status and results of NAFTA-related penalties cases established at each port.

We selected a judgmental sample of NAFTA-related audits and validated revenue recoveries reported by Customs' Office of Regulatory Audit. We also conducted fieldwork at Customs' Strategic Trade Center in Dallas, TX, and reviewed the results of NAFTA-related Interventions authorized by Customs' Office of Strategic Trade.

Our audit fieldwork also included a visit to the Port of Buffalo to review policies and procedures pertaining to the operations and maintenance of Customs' NAFTA database. We held meetings at

Customs Headquarters with personnel assigned to the Office of Strategic Trade, Office of Field Operations, Office of Investigations, Laboratories and Scientific Services, and the Office of Rulings and Regulations.

Audit work was performed from August 2001 through February 2002. We conducted our audit in accordance with generally accepted government auditing standards.



**U.S. Customs Service**

*Memorandum*

DATE: **June 14, 2002**

FILE: AUD-1-OP CN

MEMORANDUM FOR DONALD P. BENSON  
REGIONAL INSPECTOR GENERAL FOR AUDIT

FROM: Director, Office of Planning

SUBJECT: Draft Audit Report Entitled Customs NAFTA  
Enforcement Information Is Limited

Thank you for providing us with a copy of your draft report entitled "Customs NAFTA Enforcement Information Is Limited" and the opportunity to discuss the issues in this report.

Customs had taken a number of steps to address the issues identified during your review. These steps, and additional on-going actions, are outlined in the attached document, as are Customs comments on this draft report.

We have determined that the information in the audit does not warrant protection under the Freedom of Information Act.

If you have any questions regarding the comments, please have a member of your staff contact Ms. Cecelia Neglia at (202) 927-9369.

Handwritten signature of William F. Riley.  
William F. Riley

Attachment

TRADITION



SERVICE



HONOR

Attachment

Responses to Audit Recommendations  
OIG Draft Report on Customs NAFTA Enforcement Information Is Limited

**Finding 1: Customs Does Not Track Its Efforts To Improve NAFTA Compliance**

**Recommendation 1** - The Commissioner of Customs should ensure that Customs personnel implement a North American Free Trade Agreement Subplan (TASP) related tracking system that accomplishes the following:

- Identifies revenue recoveries from NAFTA enforcement activities for Customs Management Centers with the necessary details for management;
- Requires a periodic reconciliation of ACS collection and revenue recoveries records;
- Provides an annual report of the accomplishments of TASP enforcement efforts; and
- Utilizes TASP performance results to evaluate the deployment of NAFTA related resources.

**Response:** Concur. Customs will compile protected revenue data from denied 520 (d) claims. We will conduct a feasibility study to determine how to reconcile ACS collection and revenue recovery records. If the study finds reconciliation is feasible, we will implement a reconciliation process and reconcile the data annually. We will also provide an annual report on TASP accomplishments and utilize TASP performance results to evaluate deployment of NAFTA resources. Planned completion date June 30, 2003.

Furthermore, we have begun to identify NAFTA requirements for the Automated Commercial Environment (ACE). The system will be designed to incorporate the OIG's recommendations. At this time, it is anticipated that ACE's entry and liquidation modules will become operational by December 2005.

**Recommendation 2** - The Commissioner of Customs should ensure that Customs personnel are handling prior disclosures in a uniform manner.

**Response:** Concur. A working group has been established with the goal of developing a Prior Disclosure Directive. This group will focus on establishing policies and procedures for handling prior disclosures in a uniform manner. Planned completion date June 30, 2003.

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**Finding 2: Customs NAFTA Audits Have Not Identified Significant Noncompliance**

**Recommendation 1** – The Commissioner of Customs should ensure that Customs finalizes and implements a NAFTA Targeting Strategy this fiscal year and that the Office of Inspector General be provided with a copy. The Targeting Strategy should address areas of risk and include the following:

- Justification for targeting parties for Regulatory Audit Division compliance audits that include high risk companies; and
- Consideration of port referrals of potentially non-compliant filers.

**Response:** Concur. Customs is in the process of developing a risk-based strategy for targeting NAFTA verification candidates. The new risk-based strategy will include a procedure for field personnel to communicate referrals or recommendations for candidates for verification by means of an audit. A method to evaluate field referrals will also be presented as part of the strategy plan. Planned completion date September 30, 2002.

We would like to note that despite the seeming lack of apparent results in terms of uncovering egregious non-compliance, violations or major revenue recoveries, there may be additional positive results that are not obvious or easily measured. The cause and effect relationship between actions taken and compliance results in the enforcement of a trade agreement as complex as the NAFTA cannot always be specifically identified. For example, it is not possible to measure the impact that the verification audits may have had in causing the major corporations to directing resources to increase compliance with the requirements of the NAFTA. Likewise, it is impossible to measure the increased risk of non-compliance if audits in the major sectors, such as the automotive and telecommunications industries are discontinued and the deterrent effect of being subject to audit is, consequentially, removed.

**Northeastern Region**

Donald P. Benson, Regional Inspector General for Audit  
Sharon Torosian, Audit Manager  
Thomas Mason, Auditor-in-Charge  
Preston O'Toole, Auditor



**The Department of the Treasury**

Under Secretary of the Treasury for Enforcement  
Office of Strategic Planning and Evaluations  
Office of Accounting and Internal Controls

**U.S. Customs Service**

Commissioner  
Assistant Commissioner, Field Operations  
Director, Evaluation Oversight, Office of Planning

**Office of Management and Budget**

OIG Budget Examiner