Aspects of Risk Management in Customs Area

University Lecturer Emilia Iordache, Ph.D.
„Constantin Brâncoveanu" University of Piteşti
The Faculty of Management Marketing in Economic Affairs Râmnicu-Vâlcea

Abstract:

Any organization benefits from the application of a risk management strategy since this benefits organizational performance as a whole. Risk management in any organization consists of well-defined steps which, when taken in sequence, support better decision making by contributing to greater insight into risks and their impacts.

For Customs administrations adoption of risk management as an organizational philosophy is essential since it provides quantifiable improvements in the effectiveness and efficiency of the administration as a whole. Risk Management can operate in any organization with manual or automated application ranging from tactical to strategic approaches. It can be applied to nearly every decision-making situation.

The WCO defines Risk Management as the systematic application of management procedures and practices providing Customs with the necessary information to address movements or consignments which present a risk. This focus is necessary since the fundamental task of the Customs is to control the movements or consignments across national frontiers and ensure compliance with national laws. When adopted as a management philosophy it enables the Customs to not only carry out its key responsibilities effectively but also organize its resources and deploy them in a manner so as to improve its overall performance.

Keywords: risk management, SAFE, Authorised Economic Operator, global supply chain, customs

Development of customs control practices based on risk management has become synonymous with customs modernization. Because of the rapid rise in the volume of trade and limited resources of customs administrations, the traditional method of inspecting every item upon arrival at customs borders has become a barrier to trade and is no longer practical. Risk management offers a solution, enabling customs administrations to balance their control functions with trade facilitation. Risk management is a system that involves systematic risk assessment, profiling and selectivity, intelligence gathering, and analyses that enables customs to target high risk cargos and traders while maintaining effective controls at all stages of clearance. Its growing application reflects a fundamental change in the role of government in economic development and its relationship with the private sector. Customs administrations are today adopting a role of "informers" and "facilitators" of customs rules and procedures.

Based on the subsequent work of the High Level Strategic Group, in June 2005 the WCO Council adopted the WCO Framework of Standards to Secure and Facilitate Global Trade, which was later referred to as the SAFE (security and facilitation in a global environment) Framework of Standards. The SAFE Framework of Standards aims to enhance security and facilitation of global trade and improve customs operations. Modern customs principles include risk management, use of technology and a partnership with the trade. They are well developed by the WCO and are incorporated in the Revised Kyoto Convention, adopted by the WCO Council in 1999. Based on past efforts, the SAFE Framework of Standards further improves customs operations and addresses the security concern by expanding the customs focus to the entire trade supply chain and setting the necessary security requirements. Enhanced cooperation between customs administrations and strengthened Customs-to-Business partnerships are recognised as the key to achieve this goal. These Standards enable Customs to receive cargo information for security risk assessment as early as possible in the trade supply chain. This enables Customs to concentrate on a small percentage of cargo that poses a genuine security risk, while promoting the free and smooth flow of legitimate trade. Security and facilitation are thus combined as two sides of the same coin, because only efficient and effective Customs can meet these requirements. Moreover, the establishment of global standards will avoid an unnecessary burden on the trade as it obviates the risk of different sets of requirements by different customs administrations and improves coordination with other governmental agencies. In this way, the new WCO Standards will enhance the role, functions and capabilities of Customs to meet the challenges and opportunities of the 21st Century. This feature will help governments to improve revenue collection and the proper application of laws and regulations to protect society while continuing trade facilitation efforts, thereby contributing to economic and social development.[1]

In substance, the WCO SAFE Framework consists of the following four core elements:

• harmonisation of the electronic cargo information requirements by Customs

• a consistent risk management approach

• an outbound inspection of high-risk cargo, preferably using non-intrusive detection equipment, at the reasonable request of the receiving nation

• partnership with trade.

These core elements are achieved through the two-pillar approach: Customs-to-Customs network arrangements and Customs-to-Business partnerships. The first pillar encourages cooperation among customs administrations on the basis of common and accepted standards to facilitate the use of advance electronic information to identify high-risk cargo. The second pillar encourages the establishment of Customs-to-Business partnerships by enabling customs to identify businesses with a high degree of security guarantees as Authorised Economic Operators (AEOs).

Pillar one: Customs-to-Customs

The first pillar on Customs-to-Customs network arrangements consists of the following eleven standards,many of which are accompanied by technical specifications with reference to the available WCO tools (attached as Annex 1 to the Framework):

• Standard 1 provides for the use of ISCM guidelines, which is supported by technical specifications that outline the requirements for the submission of data and the Authorised Supply Chain. The former requirements include the list of standardised data elements for assessing security risk as well as the time limit for their submission.

• Standard 2 provides for the customs authority to inspect outbound, inbound, transit and transshipment cargo.

• Standard 3 provides for the use of modern technology in inspection equipment, such as large-scale X-ray machines and radiation detectors.

• Standard 4 provides for the establishment of risk management systems, including automated selective systems.

• Standard 5 provides for the identification of high-risk cargo or containers.

• Standard 6 provides for advance electronic information in time for risk assessment, supported by information and communication technologies, as outlined in the Revised Kyoto Convention Guidelines and other WCO tools.

• Standard 7 provides for joint targeting and screening based on standardised criteria and information exchange, which will lead to mutual recognition of control between customs administrations.

• Standard 8 provides for the maintenance of reports of customs performance, to be compiled by the WCO.

• Standard 9 provides for cooperation with other competent authorities to identify security gaps.

[1] Kunio Mikuriya, SUPPLY CHAIN SECURITY: THE CUSTOMS COMMUNITY'S RESPONSE, Volume 1, Number 2, www.wcoomd.org, p.52.

• Standard 10 provides for employee integrity of customs and other competent authorities, based on the WCO Revised Arusha Declaration, which contains the guiding principles to establish anti-corruption systems.

• Standard 11 provides for the conduct of outbound security inspection of high-risk cargo at the reasonable request of the importing country.

As described above, the eleven Standards, together with their technical specifications, outline the basic and common requirements for enhanced risk management, using advance electronic information. They are the basis for future customs cooperation to ensure security and facilitation of global trade. It is therefore important to improve the competencies of customs administrations through capacity building to assure the compatibility of customs systems in the global supply chain. This should lead to mutual recognition of customs control, upon which customs cooperation should be further developed.

Pillar two: Customs-to-Business

The second pillar on Customs-to-Business partnerships consists of the following six standards, each accompanied by technical standards (attached as Annex 2 to the Framework):

• Standard 1 provides for the partnership program with AEOs who will carry out a self-assessment to ensure security in their business model.

• Standard 2 provides for the incorporation of pre-determined security best practice into the business practice of AEOs.

• Standard 3 provides for the validation and accreditation process of AEOs.

• Standard 4 provides for the encouraged use by AEOs of more advanced technologies to maintain cargo and container integrity.

• Standard 5 provides for Customs-to-Business communication to promote security.

• Standard 6 provides for the joint efforts of Customs and AEOs to maximise security and facilitation.

As described above, the six Standards focus on the identification of private businesses that offer a high degree of security guarantees with respect to their role in the supply chain as AEOs. To the extent that Customs can rely on its partners in the trade community to evaluate and address threats to their own supply chain, the risk confronting Customs is reduced. Therefore it is essential to define the tangible benefits that the AEOs reap from their status. These benefits should include quicker cargo through customs with reduced examination rate and priority clearance in case of trade disruption or high security threats.

The WCO SAFE Framework of Standards provides a structured framework for Customs and business to secure the international supply chain and facilitate the movement of legitimate trade. It will enable Customs and business to gain better insight into the supply chain from point of origin to the arrival of cargo for customs clearance purposes. A more secure supply chain will increase transparency and predictability of the movement of goods and reduce the opportunity for theft and pilferage too. This will act as a deterrent to potential terrorist threats, trans-national organised crime and smuggling whilst protecting revenue collection. In order to realise this global trade scheme of the 21st Century, customs administrations around the world will have to work in partnership with the business community and other stakeholders. It is only through commitment, dialogue and close cooperation between all roleplayers that we will be able to jointly address the issues associated with supply chain security.

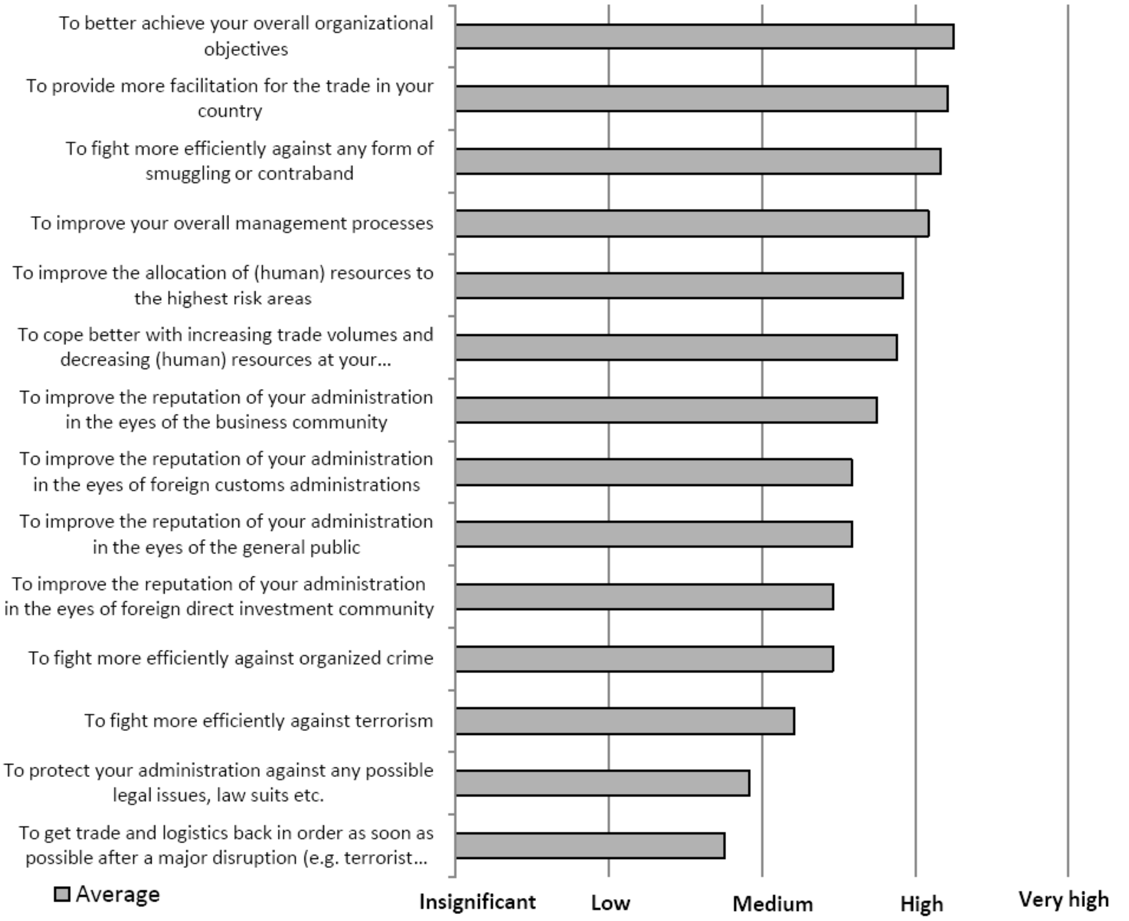
The benefits of a comprehensive risk management programme include: better human resource allocation; increased revenue; improved compliance with laws and regulations; reduced release times and hence lower transaction costs; and improved cooperation between traders and Customs.[1]

---

[1] Martyn Dunne, *Getting to grips with risk management*, WCO News, No 62/2010, www.wcoomd, org, p. 16.

Graph 1

Expected benefits of Customs Risk Management



Source: Hintsa, J., Männistö, T., Hameri A.P., Thibedeau C., Sahlstedt, J., Tsikolenko, V., Finger M., Granqvist M., Customs risk management (CRiM): A Survey of 24 WCO Member Administrations, WCO, 2011, www.wcoomd.org, p.17

The benefits of risk management to customs administrations can be categorized in the following way:

- Achieving organizational objectives
- Improved management processes
- Improved public and business profile.

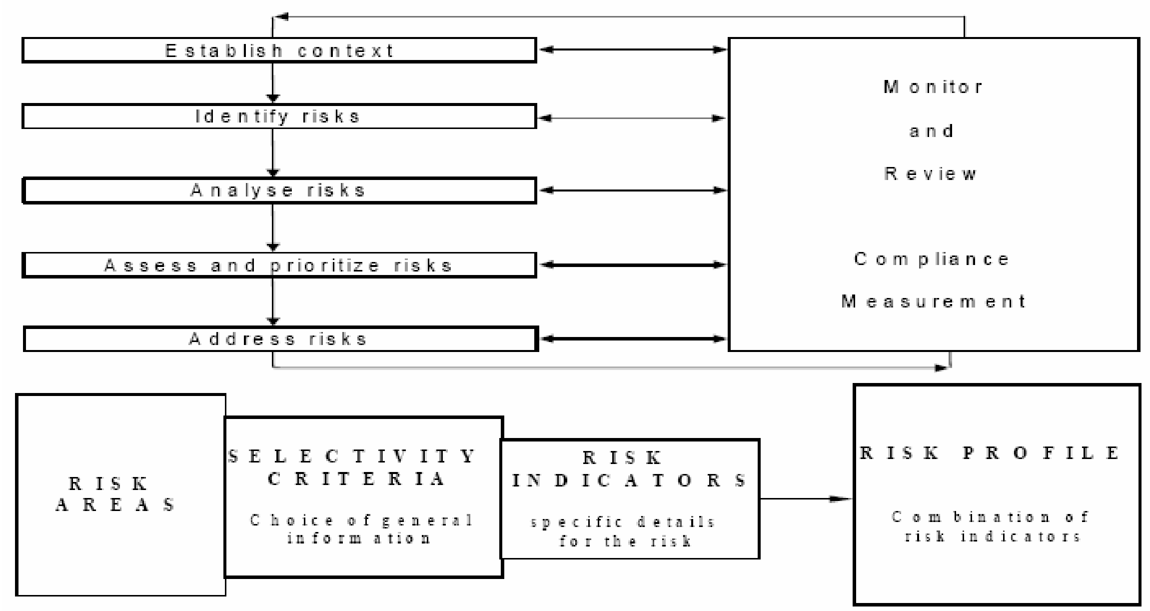
Customs administrations operating in the modern global economy are faced with a complex range of challenges. The prime responsibilities remain the collection of revenues and the protection of society, but these demanding tasks must be performed effectively and efficiently, whilst at the same time facilitating the flow of legitimate goods.

Risk management is a logical and systematic method of identifying, analyzing and managing risks. Risk management can be associated with any activity, function or process within the organization and will enable the organization to take advantage of opportunities and minimize potential losses. Risk management is successfully applied in the private sector, where insurance, banking, trade and industry find that it creates opportunities to improve business results. The use of risk management can also help the public sector to determine where the greatest areas of exposure to risk exist, and can support management in deciding how to allocate limited resources effectively. In managing risk a balance must be struck between costs and benefits, as clearly it will not be cost effective to address all risks equally. Criteria are needed to decide what constitutes an acceptable or unacceptable level of risk. The broad legal basis for application of risk management by Customs is provided for in the Standards of Chapter 6 of the General Annex of the revised Kyoto Convention. The application of risk management enhances the effectiveness and efficiency of customs business in collecting revenue and protecting society. Risk management will have a beneficial impact on all Customs activities and responsibilities, including, the collection of revenue, implementing trade policy, ensuring public safety and provide trade facilitation to legitimate traders, travellers and carriers. Customs administrations should also apply risk management for general and IT Security concerns and in the preparation of corporate business continuity planning strategy and support services, such as IT.

The risk management process comprises the establishment of the risk management context, risk identification, risk analysis, risk assessment, addressing the risks and monitoring and reviewing the process through compliance measurement.

Graph 2

Risk management process



Source: James Giermanski, Risk management: what can you really manage?, WCO News, No 62/2010, www.wcoomd.org, p.20

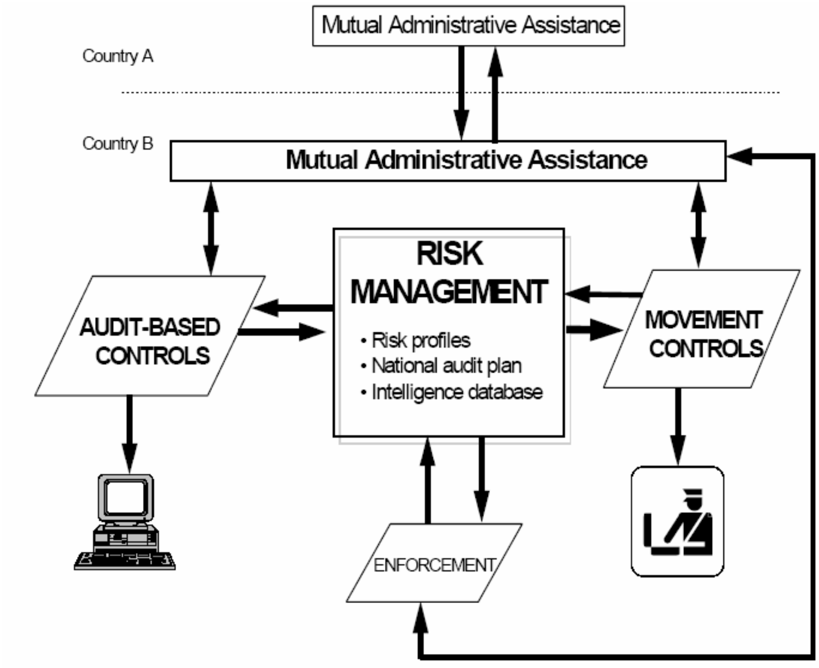
Risk management, involves every aspect of an organization's status and operations. In the supply chain there are risk elements like third parties, foreign shippers, carrier, weather, foreign government involvement, disruption in the process, timing, language, cargo quality and quantity and other forces[1]. Organizations (and firms) need to focus their risk management efforts on what they can control. Therefore, those tasked with risk management duties must understand three definitive categories: no control; direct control; and indirect control with indirect control being the most difficult since the fundamental component of risk is the human element, the most difficult element to manage.

[1] James Giermanski, Risk management: what can you really manage?, WCO News, No 62/2010, www.wcoomd.org, p.20.

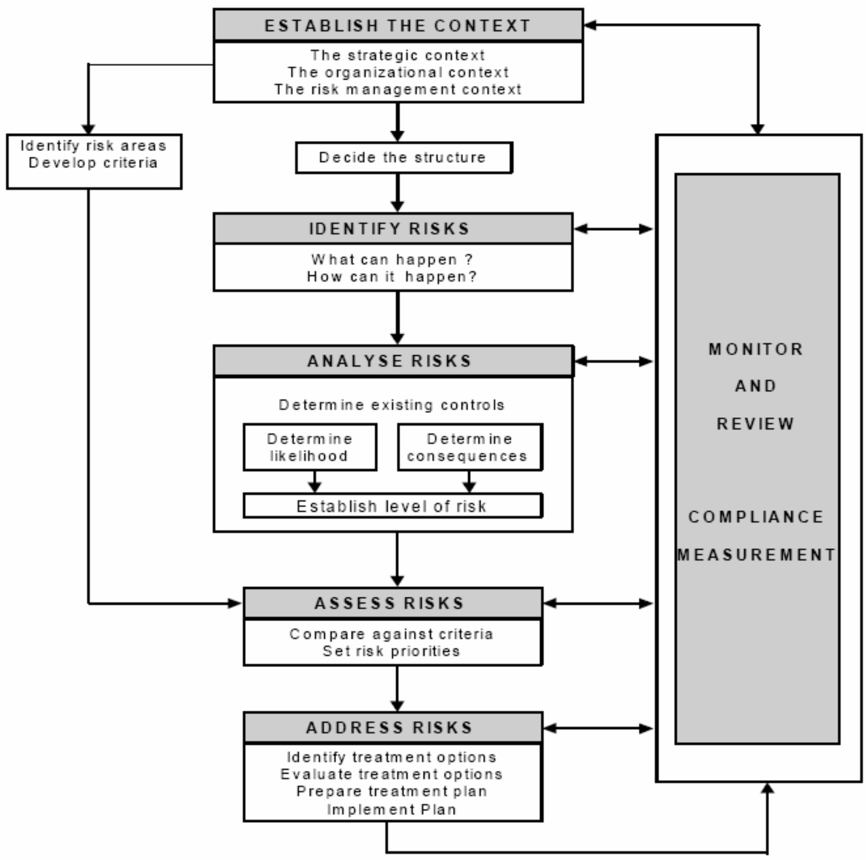
Graph 3

Example of a Customs control process

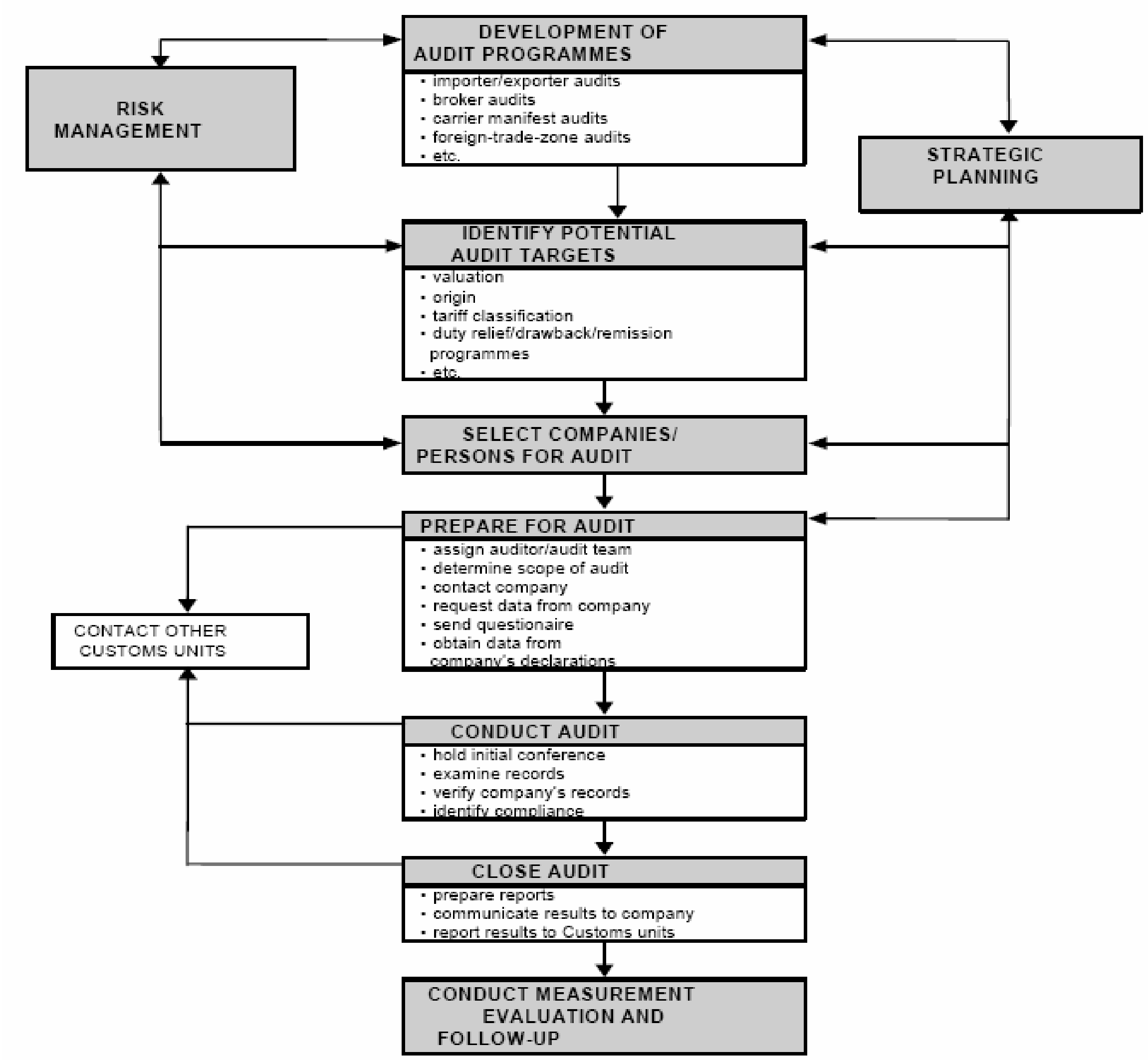
1. High-Level Scenario of a Customs control process



2. Low-Level Scenario of a risk management process



3. Low-Level Scenario of a post-clearance audit



Source: Risk Management Guide, Governance, Finance and Trade Division East and Central Asia Department Asian Development Bank, www.adb.org, 2005, p.23-25.

Customs should develop an organizational risk management philosophy with the support of senior management. This could be done by training, education, and briefing of senior Customs management. The designation of a senior manager to sponsor the risk management initiative would be helpful. Building on the organizational philosophy, Customs should develop and document a corporate policy and framework for managing risks, which should receive endorsement by the senior management and be implemented throughout the organization.

The corporate policy may include the objectives and rationale for managing risk, the links between the policy and the management/strategic plan, the extent or range of issues to which the policy applies, guidance on what may be regarded as acceptable risk, who is responsible for managing risks, the support/expertise available to assist those responsible for managing risks, the level of documentation required and the plan for reviewing organizational performance.

References:

1. Altemöller, Frank, *Towards an international regime of supply chain security: an international relations perspective*, "World Customs Journal", Volume 5, Number 2, 2011, www.wcoomd.org

2. Giermanski, James, *Risk management: what can you really manage?*, WCO News, No 62/2010, www.wcoomd.org
3. Hintsa, J., Männistö, T., Hameri A.P., Thibedeau C., Sahlstedt, J., Tsikolenko, V., Finger M., Granqvist M., *Customs risk management (CRiM): A Survey of 24 WCO Member Administrations*, WCO, 2011, www.wcoomd.org
4. Mikuriya, Kunio, *Supply chain security: the customs community's response*, "World Customs Journal", Volume 1, Number 2, www.wcoomd.org
5. ***, *Risk Management Guide*, Governance, Finance and Trade Division East and Central Asia Department Asian Development Bank, www.adb.org, 2005