U. S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Focused Assessment Program

October 2003

Documents Required for a Focused Assessment

NOTE: These documents supersede the Focused Assessment Program documents dated October 2002.

INTRODUCTION

In March 2003, the U.S. Customs Service became part of U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The passage of the Customs Modernization Act (Mod Act) in 1993 provided the framework for a partnership between the importing public and Customs. Under the Mod Act, Customs and the importer share the responsibility for compliance with trade laws and regulations. The importer is responsible for declaring the value, classification, and rate of duty applicable to entered merchandise, and Customs is responsible for informing the importer of its rights and responsibilities under the law.

Customs is committed to providing the importer with all the information needed to be in compliance with Customs laws and regulations. To fulfill this commitment, Customs is making available on its Web site (www.customs.gov) the documents commonly referred to as the FA Kit. These documents are the same handbooks, audit program, sampling plans, and guidelines that regulatory auditors and other Customs specialists on a Focused Assessment (FA) team use to conduct a Pre-Assessment Survey (PAS), Assessment Compliance Testing (ACT), and FA follow-up. Providing the FA Kit to the trade is intended to help importers prepare for a Focused Assessment and conduct an assessment of their own Customs systems.

Focused Assessment Program Table of Contents

Exhibit	*Subject*
1	**Introduction**
	General Audit Guidance
2A	Internal Control Questionnaire for Focused Assessments
2B	Electronic Data Processing (EDP) Questionnaire for Focused Assessments
2C	Pre-Assessment Survey (PAS) Audit Program
2D	Assessment Compliance Testing (ACT) Audit Program
2E	Focused Assessment Follow-up Audit Program
	Specific Audit Guidance
3A	Guidance for Using Risk Exposure to Determine Review Areas
3B	Consideration of Internal Control in a Customs Compliance Audit
3C	Internal Control Summary by Component
3D	Internal Control Management and Evaluation Tool
3E	Guidance for the Internal Control Interviewing Process
3F	Risk Opinion under Focused Assessments
3G	Timely Completion and Resolution of Issues of Focused Assessments
3H	Resolving “Gray Areas” of Harmonized Tariff Schedule (HTS) Classification
3I	Errors Disclosed to Customs
3J	Treatment of Ultimate Consignee Transactions in a Focused Assessment
	Trade Guidance
4A	Example of Internal Control Manual
4B	Common Importer Errors Identified during Assessments and Audits
4C	Prior Disclosures during a Focused Assessment
4D	Timely Completion and Resolution of Issues of Focused Assessments (see Exhibit 3G above)
4E	Compliance Improvement Plan Framework
4F	A Guide for Supporting Generalized System of Preferences (GSP) Claims
4G	(Not assigned)
4H	Internal Control Management and Evaluation Tool (see Exhibit 3D above)
4I	Importer Quantification
	Technical Information for Pre-Assessment Survey
5A	PAS Internal Control Overview
5B	Transaction Value – Technical Information for Pre-Assessment Survey
5C	Computed Value – Technical Information for Pre-Assessment Survey
5D	Classification – Technical Information for Pre-Assessment Survey
5E	HTSUS 9801.00.10 – U.S. Goods Returned – Technical Information for Pre-Assessment Survey
5F	HTSUS 9802.00.40 and HTSUS 9802.00.50 – Articles Exported for Repairs and Alterations – Technical Information for Pre-Assessment Survey
5G	HTSUS 9802.00.60 – Metal Articles Previously Exported for Processing – Technical Information for Pre-Assessment Survey
5H	HTSUS 9802.00.80 – U.S. Articles Assembled Abroad – Technical Information for Pre-Assessment Survey

Focused Assessment Program Table of Contents

Exhibit	*Subject*
5I	HTSUS 9802.00.90 – U.S. Formed and Cut Fabric Assembled in Mexico – Technical Information for Pre-Assessment Survey
5J	Antidumping Duties and Countervailing Duties – Technical Information for Pre-Assessment Survey
5K-1	Foreign Trade Zones – Manufacturing – Technical Information for Pre-Assessment Survey
5K-2	Foreign Trade Zones – Petroleum – Technical Information for Pre-Assessment Survey
5L	Transshipment – Technical Information for Pre-Assessment Survey
5M	Generalized System of Preferences – Technical Information for Pre-Assessment Survey
5N	Caribbean Basin Economic Recovery Act and Caribbean Basin Trade Partnership Act – Technical Information for Pre-Assessment Survey
5O	Andean Trade Preference Act – Technical Information for Pre-Assessment Survey
5P	Products of Insular Possessions – Technical Information for Pre-Assessment Survey
5Q	Israel Free Trade Area – Technical Information for Pre-Assessment Survey
5R	African Growth and Opportunity Act – Technical Information for Pre-Assessment Survey
5S	Quantity – Technical Information for Pre-Assessment Survey
5T	Reconciliation – Technical Information for Pre-Assessment Survey
5U	Intellectual Property Rights – Technical Information for Pre-Assessment Survey
5V	NAFTA - Technical Information for Pre-Assessment Survey
	Sampling
6A	Sampling Policy
6A Appendix I	Sampling Steps
6A Appendix II	Sampling Methodology Diagrams
6A Appendix III	FA Sampling Methodology Table
6A Appendix IV	Sampling Plans
6A Appendix V	Examples Report Tables
6A Appendix VI	Glossary of Sampling Terms
6A Appendix VII	Reading List for audit Sampling

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Internal Control Questionnaire for Focused Assessments

Introduction

In March 2003, the U.S. Customs Service became part of U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The purpose of the Internal Control Questionnaire for Focused Assessments (FAs) is to obtain information about the company's organizational structure and internal controls related to Customs transactions. The questionnaire is designed to give the audit team a general understanding of the company's import operations and internal control structure as well as to inform the audit candidates of the areas on which the assessment may focus. As each company's operations are unique, this questionnaire may have been modified to fit the circumstances of each audit candidate.

Review Scope

When the importer responds to the questionnaire completely and comprehensively, the Pre-Assessment Survey (PAS) team can plan its approach to the Focused Assessment. The results of the questionnaire, interviews with company officials and Customs personnel, survey of company procedures, and limited testing will be used to determine the effectiveness of the company’s internal control system. A PAS of the company's importing operations and internal controls will be used to determine whether more extensive testing is necessary. Any additional testing will be done in the Assessment Compliance Testing (ACT) phase of the Focused Assessment.

Answering the questionnaire affords the company the opportunity to evaluate its own internal controls and operations pertaining to Customs activities. The company will also be more prepared for the Focused Assessment.

I. General

A. Provide the name, title, and telephone number of the official(s) preparing information for this questionnaire.

B. Provide the name, title, and telephone number of the person who will be the contact for Customs during the Focused Assessment.

II. Control Environment

A. <u>Organizational Structure, Policy and Procedures, Assignment of Responsibilities</u>

1. Provide a copy of the company's organizational chart and related department descriptions. Include the detail to show the location of the Import Department identified and any structure descriptions that are relevant.

2. Identify the key individuals in each office responsible for Customs compliance (may be included on the organization chart).
3. Provide the names and addresses of any related foreign and/or domestic companies, such as the company's parent, sister, subsidiaries, or joint ventures.
4. If the company has operating policies and procedures manuals for Customs operations, provide a copy of the manuals (preferably in electronic format).
5. If the policies and procedures have the support and approval of management, identify the individuals who approve the procedures.

B. Employee Awareness Training
1. What specialized Customs training is required for key personnel working in the Import Department? If available, provide copies of training logs or other records supporting training.
2. What Customs experience have key personnel involved in Customs-related activities had?
3. Who in other departments is responsible for reporting Customs-related activities to the Import Department?
4. What training is provided to personnel in other departments responsible for reporting Customs-related activities to the Import Department?
5. How does the company obtain current information on Customs requirements?
6. Does the company use the U.S. Customs and Border Protection Web site?
7. Does the company request and disseminate binding rulings?

III. Risk Assessment

A. How does the company identify, analyze, and manage risks related to Customs activities?

B. What risks related to Customs activities has the company identified, and what control mechanisms has it implemented?

IV. Control Procedures

A. Using source records for support, provide a description and/or flowchart of the company's activities, including general ledger account numbers for recording the acquisition of foreign merchandise in the following areas:
- Purchase of foreign merchandise
- Receipt of foreign merchandise
- Recording in inventory
- Payments made to foreign vendor
- Distribution to customers (e.g., drop shipments)
- Export of merchandise (e.g., assists, Chapter 98)

B. For each aspect of value listed below, respond to the following. Where procedures are documented, reference the applicable sections.
1. What internal control procedures are used to assure accurate reporting to Customs?
2. Who is the person assigned responsibility for accurate reporting?
3. What records are maintained?
   - ❏ Basis of Appraisement (19 CFR 152.101)

- ❏ Price Actually Paid or Payable
- ❏ Packing
- ❏ Selling Commissions
- ❏ Assists (e.g., Materials/Component Parts, Tools, Dies, Molds, Merchandise Consumed, Engineering, Development, Art Work, Design Work, Plans)
- ❏ Royalties and License Fees
- ❏ Proceeds of Subsequent Resale
- ❏ Transportation Costs (e.g., International Freight, Foreign inland Freight, Transportation Rebates, Insurance)
- ❏ Retroactive Price Adjustments
- ❏ Price Increases
- ❏ Rebates
- ❏ Allowances
- ❏ Indirect Payments
- ❏ Payment of Seller's Debt by Buyer (e.g., quota)
- ❏ Price Reductions to Buyer to Settle debts (e.g., Reductions for Defective Merchandise)
- ❏ Purchases on Consignment
- ❏ Quota/Visa
- ❏ Currency Exchange Adjustments

C. For each of the following Customs-related activities, respond to the following. Where procedures are documented, reference the applicable sections.
   1. What internal control procedures are used to assure accurate reporting to Customs?
   2. Who is the person assigned responsibility for accurate reporting?
   3. What records are maintained?
      - ❏ Classification
      - ❏ Quantity
      - ❏ Reconciliation
      - ❏ Trade Agreements
        - (1) Generalized System of Preferences (GSP)
        - (2) Caribbean Basin Economic Recovery Act (also known as Caribbean Basin Initiative(and Special Access Provision (SAP)
        - (3) Israel Free Trade
        - (4) Insular Possessions
        - (5) Andean Trade Preference
        - (6) Trade Development Act of 2000
          - i. African Growth and Opportunity Act (AGOA)
          - ii. Caribbean Basin Trade Partnership Act (CBTPA)
      - ❏ Special Duty Provisions
        - (1) 9801.00.10
        - (2) 9802.00.40
        - (3) 9802.00.50
        - (4) 9802.00.60
        - (5) 9802.00.80
        - (6) 9802.00.90
      - ❏ Antidumping/Countervailing Duties

V. Information and Communication

A. Describe the procedures for the Import Department to disseminate relevant Customs information to other departments.

B. Describe the procedures for other departments to communicate with the Import Department on matters affecting imported merchandise.

C. Describe the procedures for the Import Department to participate in major planning processes involving importation activities.

VI. Monitoring

A. What methods of oversight and monitoring does the Import Department management use to ensure compliance with Customs requirements?

B. Provide information and/or reports on the review and evaluation of compliance with Customs requirements by other internal and external entities (e.g., internal audit department, financial statement auditors).

C. What level of management are these self-reviews reported to for action?

VII. Miscellaneous

A. Identify the account numbers in which costs for imported merchandise are recorded.

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Electronic Data Processing (EDP) Questionnaire for Focused Assessments

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

An important factor in conducting Focused Assessments (FAs) in a timely manner may include obtaining electronic data files needed to facilitate comparisons between the company's data and Customs data, sampling, and transactional testing. Generally, two or more data universes are identified. The first universe consists of a fiscal year's imports. The sampling unit may be entry line items unless a more efficient sampling unit, such as invoice line items or the equivalent, is available from the company. Other universes of financial transactions are used to test for possible unreported dutiable expenses. These universes and sampling items will be determined after the team has an understanding of your system and Customs procedures.

Typically, files useful for the FA program may include, but not be limited to: Customs entry log, purchase orders, vendor master, general ledger (GL), invoice line detail, chart of accounts, foreign purchases journal, AP (Payment History File) or GL expense file for imported merchandise, accounts payable with GL reference, cash disbursements, wire transfers, letters of credit, and inventory records.

Please return a hard copy and a *disk copy* of the completed questionnaire to

U.S. Customs and Border Protection

Regulatory Audit Division

Attention:

[address]

Email:

Phone:

Fax:

1. List the files, or an equivalent of the same information, that are maintained on each of your computer systems, and describe how each system communicates or links with other systems. For each system, identify the contact person responsible for maintaining that system or information. Identify which information is maintained manually. The following format may be used:

Record	System	Link to Other System	Contact Person	Title	Division
Customs entry (CF 7501)					
Special duty provision					
Payment history					
Accounts Payable					
Purchase order					
Invoice line detail					
Inventory and receiving					
Shipping, freight, insurance, and bill of lading					
Vendor codes and addresses					
Finished product specifications					
Country of origin certification					
Imported product					
Cost data					
Letters of credit					
Wire transfers					
Cash disbursement					

2. Provide flowcharts and/or narrative description of the data flow between systems

3. Are your computer systems IBM Compatible? Yes/No

4. What types of electronic media do you use to transport data? [C-Tape, E-Tape, CD-ROM, Zip Cartridge

5. Specify the capacity for your electronic media

6. List data center location(s).

7. Specify the EDP Department contact person and phone number.

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Focused Assessment Program
Pre-Assessment Survey
Audit Program

October 2003

Focused Assessment Program
Pre-Assessment Survey Audit Program

Table of Contents

PART 1 BACKGROUND 3

1.1 OVERVIEW 3
1.2 AUTHORITY TO CONDUCT AUDITS 3
1.3 RISK MANAGEMENT 3

PART 2 PRE-ASSESSMENT SURVEY 5

2.1 OBJECTIVE 5
2.2 PLANNING AND PREPARATION 5
2.3 PRELIMINARY ASSESSMENT OF RISK 5
2.4 INITIATE THE AUDIT 6
2.5 INTERNAL CONTROL ASSESSMENT 6
A. Transaction Value 6
B. Classification 8
C. Special Trade Programs and Special Duty Provisions 9
D. Antidumping/Countervailing Duties (ADD/CVD) 10
E. Transshipment 12
F. Intellectual Property Rights 13
G. Quantity 15
H. Foreign Trade Zones 16
I. Computed Value 17
J. Other Area 19
2.6 FINALIZING THE AUDIT 20

ATTACHMENT 1 PRELIMINARY ASSESSMENT OF RISK - EXAMPLE OF BLANK FORM 21

PRE-ASSESSMENT SURVEY AUDIT PROGRAM

PART 1 BACKGROUND

1.1 OVERVIEW

On December 8, 1993, the U.S. Congress enacted modernization provisions for the U.S. Customs Service under Title VI of the North American Free Trade Agreement Implementation Act (Public Law 103-182). These provisions are commonly called the Customs Modernization Act (Mod Act). The Mod Act is based on two basic tenets: shared responsibility and informed compliance. Shared responsibility means that importers and the U.S. Customs Service have a mutual responsibility to ensure compliance with trade and U.S. Customs Service laws. The purpose of informed compliance is to maximize voluntary compliance. The informed compliance concept imposed many publication, consultation, and notice obligations on the U.S. Customs Service.

The Mod Act fundamentally altered the relationship between importers and the U.S. Customs Service. The Mod Act shifted the legal responsibility for declaring the value, classification, and rate of duty applicable to entered merchandise to the importer and requires importers to use reasonable care to assure that the U.S. Customs Service is provided accurate and timely data. The U. S. Customs Service retained the ultimate responsibility to "fix" the value, classification, and rate of duty. Informed compliance is based on the premise that, in order to meet their responsibilities, importers need to be clearly and completely informed of their legal obligations. To meet its obligations under the Mod Act, the U.S. Customs Service will spend more time and use more effective methods to inform the public, with the goal of maximizing voluntary compliance and reducing the need for enforced compliance.

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

1.2 AUTHORITY TO CONDUCT AUDITS

Under 19 U.S.C. 1509, Customs may examine records to ascertain the correctness and determine the liability for duty, fees, and taxes due the U.S. The Focused Assessment Program was developed to guide the audit team through the examination process.

1.3 RISK MANAGEMENT

Customs performs its duty in an environment in which decisions regarding the allocation of finite resources have become increasingly important. We define risk as the degree of exposure that would result in loss to the trade, industry, or the public. Risk management is the integrated process for identifying and managing risk in trade compliance.

Risk management is a method of managing by identifying and controlling those events that have the potential to cause significant problems. The key to risk management is to gather and analyze all relevant data efficiently and effectively and use these data to make decisions about allocating resources. In Customs trade terms, that means identifying those imports that represent the greatest risk of noncompliance so that we can focus our resources in those areas. Customs acknowledges that not all importers present the same level of risk for noncompliance, and many importers do not present a risk that justifies a significant allocation of resources.

The Focused Assessment Program fulfills critical components of Customs risk management process. First, the Focused Assessment (FA) provides a systematic approach to data collection. Next, an analysis of data can be used to determine the likelihood of noncompliance. Once a potential risk has been identified and analyzed, importers can design an action plan and assign resources to address that risk. Finally, the results of the assessment are reported, tracked, and input back into the risk management process.

The Focused Assessment Program is composed of two processes: Pre-Assessment Survey (PAS) and Assessment Compliance Testing (ACT). During the PAS process, Customs identifies areas of risk by evaluating the adequacy of the importer's internal control system. In ACT, Customs identifies the extent of compliance and/or computes the loss of revenue for areas of risk.

PART 2 PRE-ASSESSMENT SURVEY

2.1 OBJECTIVE

Identify risks to U.S. Customs and Border Protection and evaluate the adequacy of internal control over Customs activities to determine if risk is acceptable.

2.2 PLANNING AND PREPARATION

Sub-objective: Plan the Pre-Assessment Survey (PAS) process of the Focused Assessment (FA) program.

NOTE: If the importer submits a prior disclosure to Customs at any time, the team should decide whether to review it as a part of the PAS and develop appropriate audit steps.

Audit Step	Initials & Date	Work Paper Ref.
A. Obtain clearance from the U.S. Immigration and Customs Enforcement.		
B. Contact company to determine fiscal year, verify location of records, and notify them they are being considered for audit.		
C. Obtain the profile and/or ACS data.		

2.3 PRELIMINARY ASSESSMENT OF RISK

Sub-objective: Evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information and make a preliminary assessment of risk.

Audit Step	Initials & Date	Work Paper Ref.
A. Identify potential areas of risk using Customs data		
B. Justify the elimination of areas with insignificant risk.		
C. Complete the Preliminary Assessment of Risk form in Attachment 1.		

2.4 INITIATE THE AUDIT

Sub-objective: Prepare necessary documents and contact the company to initiate the audit.

	Audit Step	Initials & Date	Work Paper Ref.
A.	Prepare confirmation letter and customize the Internal Control questionnaire.		
B.	Identify walk through transactions for each review area and forward to company with confirmation letter and internal control and EDP questionnaires.		
C.	Hold and document the advance conference, including the walk through. Additional information about risk obtained during this stage of the audit may be used to adjust the audit scope.		
D.	Hold and document the entrance conference.		

2.5 INTERNAL CONTROL ASSESSMENT

Sub-objective: To determine if the company has implemented internal control, test the effectiveness of internal control and determine if internal control is adequate to control risk.

A. Transaction Value

	Audit Step	Initials & Date	Work Paper Ref.
(1)	Evaluate the company's financial records to determine which cost elements affecting transaction value pose a risk to Customs.		
(2)	Use the Technical Information for Pre-Assessment Survey (TIPS) for Transaction Value to conduct a preliminary internal control assessment of transaction value. Use the Worksheet for Evaluating Internal Control (WEIC) in TIPS for Transaction Value to conduct interviews, review documentary evidence of control implementation, and document the internal control review.		

Audit Step	Initials & Date	Work Paper Ref.
Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire • Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(3) Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC for Transaction Value) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		
(4) Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (3) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of the WEIC for Transaction Value		
(5) Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC for Transaction Value.		
(6) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(7) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up.		

Audit Step	Initials & Date	Work Paper Ref.

B. Classification

Audit Step	Initials & Date	Work Paper Ref.
(1) Use the Technical Information for Pre-Assessment Survey (TIPS) for Classification to conduct a preliminary internal control assessment of classification. Use the Worksheet for Evaluating Internal Control (WEIC) in TIPS for Classification to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire • Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(2) Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC for Classification) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		
(3) Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (2) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors		

Audit Step	Initials & Date	Work Paper Ref.
➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of the WEIC for Classification.		
(4) Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC for Classification.		
(5) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(6) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up		

C. Special Trade Programs and Special Duty Provisions

Audit Step	Initials & Date	Work Paper Ref.
(1) Use the Technical Information for Pre-Assessment Survey (TIPS) for the review area to conduct a preliminary internal control assessment of the review area. Use the Worksheet for Evaluating Internal Control (WEIC) in the TIPS for the review area to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire • Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(2) Using the results of the preliminary assessment of risk and		

Audit Step	Initials & Date	Work Paper Ref.
internal control review, determine which and how many sample items will be tested to determine if internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC for the review area) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		
(3) Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (2) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of the WEIC for the review area.		
(4) Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC for the review area.		
(5) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(6) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up		

D. Antidumping/Countervailing Duties (ADD/CVD)

Audit Step	Initials & Date	Work Paper Ref.
(1) Evaluate the company's imports to determine which imports may be subject to ADD/CVD and thereby pose a risk to Customs.		

Audit Step	Initials & Date	Work Paper Ref.
(2) Use the Technical Information for Pre-Assessment Survey (TIPS) for ADD/CVD to conduct a preliminary internal control assessment of ADD/CVD. Use the Worksheet for Evaluating Internal Control (WEIC) in the TIPS for ADD/CVD to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire • Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(3) Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if the internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC for ADD/CVD) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		
(4) Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (2) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of the WEIC for ADD/CVD.		
(5) Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC for ADD/CVD.		

	Audit Step	Initials & Date	Work Paper Ref.
(6)	If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(7)	If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up.		

E. Transshipment

	Audit Step	Initials & Date	Work Paper Ref.
(1)	Evaluate the company's imports to determine which imports may be subject to transshipment and thereby pose a risk to Customs.		
(2)	Use the Technical Information for Pre-Assessment Survey (TIPS) for Transshipment to conduct a preliminary internal control assessment of transshipment. Use the Worksheet for Evaluating Internal Control (WEIC) in the TIPS for Transshipment to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire • Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(3)	Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if the internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC for Transshipment) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		

Audit Step	Initials & Date	Work Paper Ref.
(4) Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (2) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of the WEIC for Transshipment.		
(5) Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC for Transshipment.		
(6) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(7) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up.		

F. Intellectual Property Rights

Audit Step	Initials & Date	Work Paper Ref.
(1) Evaluate the company's imports to determine which imports may be subject to IPR violations and thereby pose a risk to Customs.		
(2) Use the Technical Information for Pre-Assessment Survey (TIPS) for Intellectual Property Rights (IPR) to conduct a preliminary internal control assessment of IPR. Use the Worksheet for Evaluating Internal Control (WEIC) in the TIPS for IPR to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire		

Audit Step	Initials & Date	Work Paper Ref.
• Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(3) Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if the internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC for IPR) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		
(4) Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (2) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of the WEIC for IPR.		
(5) Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 4 of the WEIC for IPR.		
(6) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(7) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up.		

G. Quantity

	Audit Step	Initials & Date	Work Paper Ref.
(1)	Use the Technical Information for Pre-Assessment Survey (TIPS) for Quantity to conduct a preliminary internal control assessment of quantity. Use the Worksheet for Evaluating Internal Control (WEIC) in the TIPS for Quantity to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire • Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(2)	Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if the internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC for Quantity) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		
(3)	Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (2) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of the WEIC for Quantity.		
(4)	Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC for Quantity.		

Audit Step	Initials & Date	Work Paper Ref.
(5) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(6) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up.		

H. Foreign Trade Zones

Audit Step	Initials & Date	Work Paper Ref.
(1) Use the Technical Information for Pre-Assessment Survey (TIPS) for Foreign Trade Zones (FTZ) to conduct interviews, review documentary evidence of control implementation, and document the internal control review. A separate TIPS is available for Petroleum FTZ. Use the Worksheet for Evaluating Internal Control (WEIC) in the TIPS for FTZ to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire • Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(2) Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if the internal control is implemented and effective. • Complete the matrix “Sample Sizes,” (in Section 3 of the WEIC for FTZ) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		

Audit Step	Initials & Date	Work Paper Ref.
(3) Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (2) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of WEIC for FTZ.		
(4) Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC for FTZ.		
(5) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(6) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up.		

I. Computed Value

Audit Step	Initials & Date	Work Paper Ref.
(1) Evaluate the company's financial records to determine which cost elements affecting computed value pose a risk to Customs.		
(2) Use the Technical Information for Pre-Assessment Survey (TIPS) for Computed Value to conduct a preliminary internal control assessment of computed value. Use the Worksheet for Evaluating Internal Control (WEIC) in the TIPS for Computed Value to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire		

Audit Step	Initials & Date	Work Paper Ref.
• Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(3) Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC for Computed Value) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		
(4) Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (3) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of the WEIC for Computed Value		
(5) Using the results of the internal control review (including testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC for Computed Value.		
(6) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(7) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up		

J. Other Area

Note: If other areas are identified for review, develop specific tests for the review area using steps similar to the following.

	Audit Step	Initials & Date	Work Paper Ref.
(1)	Conduct a preliminary internal control assessment of the review area. Develop a Worksheet for Evaluating Internal Control (WEIC) using the format for other review areas to conduct interviews, review documentary evidence of control implementation, and document the internal control review. Complete Sections 1 and 2 of the WEIC. Assess internal control to determine the strength (weak, adequate or strong) of internal control by analyzing and comparing: • Responses to the Internal Control Questionnaire • Review of Policies and Procedures Manual • The walk through • Interview information • Documentation supporting control implementation • Other information.		
(2)	Using the results of the preliminary assessment of risk and internal control review, determine which and how many sample items will be tested to determine if the internal control is implemented and effective. • Complete the matrix "Sample Sizes," (in Section 3 of the WEIC) to determine the sample size. Multiple samples may be taken for the review area. • Complete the sampling plan, FA Program Exhibit 6, with particular emphasis on documenting reasons for selecting transactions.		
(3)	Test the effectiveness and implementation of internal control and determine if internal control is adequate to control risk. • Review sample items from (2) above ➢ Request documentation ➢ Identify errors in the sample ➢ Identify the cause of the errors ➢ Relate systemic errors to internal control weaknesses • Identify potential corrective action • Complete Section 4 of WEIC.		
(4)	Using the results of the internal control review (including		

Audit Step	Initials & Date	Work Paper Ref.
testing), develop an opinion whether risk is acceptable or unacceptable. Document the opinion in Section 5 of the WEIC.		
(5) If the risk to Customs is unacceptable, prepare a finding sheet, discuss the results with the company and obtain their response.		
(6) If unacceptable risks are identified determine whether to proceed to ACT or schedule a follow-up.		

2.6 FINALIZING THE AUDIT

Sub-objective: Finalize the audit.

Audit Step	Initials & Date	Work Paper Ref.
A. Draft the PAS report.		
B. Discuss the draft report with all Customs offices and the company and obtain comments.		
C. Hold the exit conference with the company to discuss PAS results.		
D. Finalize and issue the PAS report.		

ATTACHMENT 1 PRELIMINARY ASSESSMENT OF RISK - EXAMPLE OF BLANK FORM

Name of Auditee:
Audit Assignment No:
Subject of Audit Documentation: Preliminary Assessment of Risk Review
Purpose/ Sub-objective Evaluate identified potential risks to Customs based on analytical reviews of Customs data about the company's areas of Customs activities and make a preliminary assessment of risk.
Source

Scope/ Work Performed

Conclusion/ Findings & Conclusion **The risk level for each area selected for review is as follows:**

Area	Risk Level
XXX	
YYY	

(End of PSSC)

Section 1: Risk Level for Areas Selected for Review

Preliminary Assessment of Risk– XXX		
Element	**Explanation**	**Risk Level**
Significance **Quantitative Analysis**		
Sensitivity and Customs red flags **Qualitative Analysis**		

Preliminary Assessment of Risk– XXX		
Element	**Explanation**	**Risk Level**
Overall Preliminary assessment of risk:		

Preliminary Assessment of Risk– YYY		
Element	**Explanation**	**Risk Level**
Significance **Quantitative Analysis**		
Sensitivity and Customs red flags **Qualitative Analysis**		
Overall Preliminary assessment of risk:		

Section 2: Areas Not Included in the Audit Scope Because of Insignificant Risk

Areas with Insignificant Risk	
Area	**Explanation for Insignificance and Lack of Sensitivity**

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Focused Assessment Program
Assessment Compliance Testing
Audit Program

October 2003

Focused Assessment Program
Assessment Compliance Testing (ACT)
Audit Program

TABLE OF CONTENTS

ASSESSMENT COMPLIANCE TESTING AUDIT PROGRAM 3

PART 3 BACKGROUND 3

PART 4 ASSESSMENT COMPLIANCE TESTING AUDIT PROGRAM 4

4.1 OBJECTIVE 4
4.2 SAMPLING PLAN/SAMPLE SELECTION 4
4.3 ASSESSMENT COMPLIANCE TESTING 5
A. Classification 5
B. Transaction Value 6
C. Transaction Value of Identical or Similar Merchandise 7
D. Deductive Value 7
E. Computed Value 7
F. Derived Value 7
G. HTSUS 9801.00.10 8
H. HTSUS 9802.00.40 AND 9802.00.50 9
I. HTSUS 9802.00.60 (Metal Articles Exported for Processing) 10
J. HTSUS 9802.00.80 (U.S. ARTICLES ASSEMBLED ABROAD) 11
K. HTSUS 9802.00.90 (U.S. Formed and Cut Textile Fabric Assembled in Mexico, Formerly Mexican Special Regime) 12
L. Antidumping/Countervailing Duties 14
M. Bonded Warehouse 15
N. Foreign Trade Zone 16
O. Quota/Visa Merchandise Entered in an FTZ 16
P. Transshipment 18
Q. Generalized System of Preferences (GSP) 18
R. Caribbean Basin Economic Recovery Act (CBERA) & Caribbean Basin Trade Partnership Act (CBTPA) 19
S. Andean Trade Preference Act 20
T. Israel Free Trade 20
U. Products of Insular Possessions 20
V. Additional Sampling Issues 21
4.4 ASSESSMENT COMPLIANCE TESTING CLOSURE 21

ASSESSMENT COMPLIANCE TESTING AUDIT PROGRAM

PART 3 BACKGROUND

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The Focused Assessment Program is composed of two processes: Pre-Assessment Survey (PAS) and Assessment Compliance Testing (ACT). During the PAS process, Customs identifies areas of risk by evaluating the adequacy of the importer's internal control system. In ACT, Customs identifies the extent of compliance and/or computes the loss of revenue for areas of risk.

Under the following circumstances, the FA team may have to proceed to the ACT portion of the FA for review areas determined to have unacceptable risks to Customs.

- The company does not maintain adequate internal controls and ACT testing is necessary to determine the level of compliance of the company's imports.
- The FA team is not able to confirm that internal controls are adequate to control risks to Customs and ACT testing is necessary to determine the level of compliance of the company's imports.
- Revenue issues are involved but cannot be resolved without additional testing by the FA team.

PART 4 ASSESSMENT COMPLIANCE TESTING AUDIT PROGRAM

4.1 OBJECTIVE

Determine the extent of compliance with Customs laws and regulations and compute revenue loss during the period of review. The results of ACT are used to render an opinion on the importer's risk.

Note: ACT is completed only for areas of risk identified in the PAS. Therefore, this audit program should be customized to include only the areas requiring testing in the ACT.

4.2 SAMPLING PLAN/SAMPLE SELECTION

Sub-objective: Develop a sampling plan and select samples for testing the company's compliance with Customs laws and regulations and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
A. For each area requiring testing, select and validate the most efficient sampling frame(s) with the assistance of the computer audit specialist, if required. (Note: Statistical sampling may not always be required.) Indicate below the applicable areas that will be reviewed. ❑ Classification ❑ Value ❑ Harmonized Tariff Schedule of the United States (HTSUS) 9801.00.10 ❑ HTSUS 9802.00.40 and 9802.00.50 ❑ HTSUS 9802.00.60 ❑ HTSUS 9802.00.80 ❑ HTSUS 9802.00.90 ❑ Antidumping/Countervailing Duties (ADD/CVD) ❑ Bonded Warehouse ❑ Foreign Trade Zone (FTZ) ❑ Quota/Visa Merchandise Entered in an FTZ ❑ Transshipment ❑ Generalized System of Preferences (GSP) ❑ Quantity ❑ Reconciliation ❑ Caribbean Basin Initiative (CBI) ❑ OTHER: Identify		
B. Prepare a sampling plan.		

Audit Step	Initials & Date	Work Paper Ref.
C. Select sample items and request related documents from company.		

4.3 ASSESSMENT COMPLIANCE TESTING

A. Classification

Sub-objective: Determine whether the importer met an acceptable level of compliance for classification of imported merchandise and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, obtain the specifications, part numbers, or other applicable descriptions, lab reports, and binding rulings from the company for each selected article. Provide this information and the entry containing the article to the import specialist for a review of classification including: ❑ Quota ❑ ADD/CVD ❑ Admissibility requirements ❑ Other classification issues.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a Compliance Improvement Plan (CIP). (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable.		

	Audit Step	Initials & Date	Work Paper Ref.
	Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6)	Refer to the EET if results meet EET's impact level for referral.		
(7)	Discuss with the company and obtain comments.		

B. Transaction Value

Sub-objective: Determine whether the importer met an acceptable level of compliance for the transaction value of imported merchandise and/or compute revenue loss.

	Audit Step	Initials & Date	Work Paper Ref.
(1)	Using the sample(s) selected, determine specific tests for areas requiring review, such as determining if the declared value was the price actually paid or payable and/or whether there were any payments or additions to the price actually paid or payable. (402(b)(1)(A)-(E)		
(2)	Evaluate errors to determine whether errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3)	Determine the total amount of undeclared value both actual and/or projected from different sampling frames and apply materiality criteria, if applicable.		
(4)	Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		

Audit Step	Initials & Date	Work Paper Ref.
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if findings meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

C. Transaction Value of Identical or Similar Merchandise

Section 402 of the Tariff Act of 1930, as amended by Section 201, Trade Agreements Act of 1979, requires transaction value of identical or similar merchandise to be considered as the method of appraisement if transaction value is not appropriate. However, because this method is not commonly used, audit steps for transaction value of identical or similar merchandise are not included here, but will be determined by the auditor.

D. Deductive Value

Section 402 of the Tariff Act of 1930, as amended by Section 201, Trade Agreements Act of 1979, requires deductive value to be considered as the method of appraisement if neither transaction value nor transaction value of identical or similar merchandise is appropriate. However, because this method is not commonly used, audit steps for deductive value are not included here, but will be determined by the auditor.

E. Computed Value

Sub-objective: Determine whether the importer met an acceptable level of compliance for computed value and/or compute revenue loss. However, because this method is not commonly used, audit steps for computed value are not included here, but will be determined by the auditor.

F. Derived Value

Section 402 of the Tariff Act of 1930, as amended by Section 201, Trade Agreements Act of 1979, requires "derived value" to be considered as the method of appraisement if none of the other methods of appraisement is appropriate. However, because this method is not commonly used, audit steps for derived value are not included here, but will be determined by the auditor.

G. HTSUS 9801.00.10

Sub-objective: Determine whether the importer met an acceptable level of compliance for imported merchandise entered under HTSUS 9801.00.10 and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, determine eligibility for each sample item by: a) Verifying U.S. origin; b) Verifying reported value; and c) Determining if drawback was claimed on the exportation.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

H. HTSUS 9802.00.40 AND 9802.00.50

Sub-objective: Determine whether the importer met an acceptable level of compliance for imported merchandise entered under HTSUS 9802.00.40 and 9802.00.50 and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, determine eligibility for each sample item by: a) Verifying that the items were exported for repair or alteration; b) Reviewing foreign operations to determine whether the operations qualify for partial exemption under the provisions of HTSUS 9802.00.40/50; c) Verifying that no drawback was claimed for the articles exported from the U.S.; d) Verifying that a repair or alteration took place; and e) Requesting and reviewing importer support for costs of repair work performed abroad.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 (“the Act”) was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		

Audit Step	Initials & Date	Work Paper Ref.
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

I. HTSUS 9802.00.60 (Metal Articles Exported for Processing)

Sub-objective: Determine whether the importer met an acceptable level of compliance for imported merchandise entered under HTSUS 9802.00.60 and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, determine eligibility for each sample item by: a) Verifying that the article exported meets the definition of "metal"; b) Verifying no drawback was claimed for the articles exported from the U.S.; c) Verifying that imported metal articles were: • Manufactured in the U.S. and then exported for further processing at a foreign plant • Returned to the U.S. for further processing • Processed in the U.S. after return d) Ascertaining that foreign processing operations qualified for HTSUS 9802.00.60 treatment; and e) Obtaining and verifying the importer's support for: • Total value of the imported article • Nondutiable value claimed under HTSUS 9802.00.60.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance.		

Audit Step	Initials & Date	Work Paper Ref.
a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

J. HTSUS 9802.00.80 (U.S. ARTICLES ASSEMBLED ABROAD)

Sub-objective: Determine whether the importer met an acceptable level of compliance for imported merchandise entered under HTSUS 9802.00.80 and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, for each sample item verify: a) Claimed component(s) meet requirements for HTSUS 9802.00.80 treatment • No drawback claimed on component(s) • Component(s) maintain identity from time of U.S. exportation through time of assembly into article imported under HTSUS 9802.00.80 • Component(s) ready for assembly at time of U.S. exportation; no foreign fabrication required before assembly • Foreign operation was assembly and not manufacturing. b) Origin of claimed components. c) Claimed components were actually used to produce imported article (usage). d) Claimed 9802.00.80 value of the component, whether consigned or sold to the assembler, was the cost or value at the time of export for assembly. Ensure that claimed value included all costs (i.e., freight and insurance) to the U.S. port of exportation.		

Audit Step	Initials & Date	Work Paper Ref.
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

K. HTSUS 9802.00.90 (U.S. Formed and Cut Textile Fabric Assembled in Mexico, Formerly Mexican Special Regime)

Sub-objective: Determine whether the importer met an acceptable level of compliance for imported merchandise entered under HTSUS 9802.00.90 and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, for each sample item verify: a) Claimed component(s) meet requirements for HTSUS 9802.00.90 treatment • No drawback claimed on component(s) • Fabric was wholly formed and cut in the U.S. • Component(s) were exported in condition ready for assembly without further fabrication • Component(s) were not advanced in value or improved in condition in Mexico except by operations incidental to assembly • Component(s) have not lost their physical identity in the assembled article by change in form or shape. b) U.S. is the country in which the components were formed and cut. c) Claimed components were actually used to produce imported articles (usage). d) Claimed 9802.00.90 value of the component, whether consigned or sold to the assembler, was the cost or value at the time of export for assembly. Ensure claimed value included all costs (i.e., freight and insurance) to the U.S. port of exportation.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable.		

Audit Step	Initials & Date	Work Paper Ref.
Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

L. Antidumping/Countervailing Duties

Sub-objective: Determine whether the importer met an acceptable level of compliance for ADD/CVD and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, for each sample item determine: a) The accuracy of ADD/CVD included on 03 and 07 entries. b) ADD/CVD omitted from Customs entries.		
(2) If errors were found when testing for undisclosed ADD/CVD: a) Discuss with team members and decide course of action (audit, investigation, etc.) b) Discuss with Strategic Trade Center (STC) or EET special agent.		
(3) Evaluate errors to determine if errors were systemic. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(4) Compute the compliance rate, if applicable.		
(5) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance:		

Audit Step	Initials & Date	Work Paper Ref.
(i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Compute actual or projected revenue loss, if applicable.		
(7) Refer to the EET if results meet EET's impact level for referral.		
(8) Discuss with the company and obtain comments.		

M. Bonded Warehouse

Sub-objective: Determine whether the importer met an acceptable level of compliance for quota merchandise stored in a bonded warehouse and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, for each sample item verify: a) Accuracy of tariff number b) Quantities for quota/visa merchandise entered into the warehouse. c) Re-warehoused quota merchandise was correctly classified as quota merchandise. d) Quota was available at the time merchandise was withdrawn for consumption. If tariff rate quota was involved, verify that the appropriate duty rate was paid.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance.		

Audit Step	Initials & Date	Work Paper Ref.
(ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

N. Foreign Trade Zone

Sub-objective: Determine whether the importer met an acceptable level of compliance for storing or processing non-quota merchandise in an FTZ and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) If FTZ storage or processing of non-quota merchandise is an integral part of the company's importing program (ratio of annual value of FTZ merchandise shipped from the zone is at least 30 percent of the total annual value of imported merchandise), refer to the FTZ audit program for audit steps. If it is not an integral part of the company's importing program and does not process quota merchandise, document in work papers, but do not complete remaining steps.		

O. Quota/Visa Merchandise Entered in an FTZ

Sub-objective: Determine whether the importer met an acceptable level of compliance for storing or processing quota merchandise in an FTZ and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, for each sample item verify: a) Propriety and accuracy of circumstances associated with any quota/visa merchandise admitted into the FTZ. Document any quota merchandise that was transferred to another FTZ or to a bonded warehouse. b) Merchandise was admitted to the other FTZ or entered in the warehouse as quota merchandise for quota merchandise that was transferred to another FTZ or to a bonded warehouse. c) Quota was available at the time merchandise was withdrawn for consumption. If tariff rate quota was involved, verify that the appropriate duty rate was paid.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

P. Transshipment

Sub-objective: Determine whether the importer met an acceptable level of compliance for controlling transshipment of merchandise.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, develop specific audit steps for the import specialist to test for transshipment.		
(2) Evaluate test results and take appropriate action.		
(3) If no transshipment was found, prepare the work paper.		
(4) If any transshipment was found, discuss with team members. a) Determine the best course of action (audit or investigation). b) Discuss with the STC special agent. c) Further action depends on individual circumstances.		

Q. Generalized System of Preferences (GSP)

Sub-objective: Determine whether the importer met an acceptable level of compliance for GSP entries and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, determine eligibility for claimed GSP for each sample item by verifying: a) Country and merchandise are eligible for GSP treatment. b) Components of imported articles (i.e., sets) are produced in the beneficiary developing country (BDC). c) Merchandise was directly imported into the U.S. d) Merchandise was wholly the growth, product, or manufacture of a BDC. e) Merchandise was not wholly the growth, product, or manufacture of a BDC; however, the sum of the cost or value of the materials produced in the BDC plus the direct costs of processing operations performed in the BDC was not less than 35 percent of the appraised value.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below. a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance.		

Audit Step	Initials & Date	Work Paper Ref.
(ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

R. Caribbean Basin Economic Recovery Act (CBERA) & Caribbean Basin Trade Partnership Act (CBTPA)

Sub-objective: Determine whether the importer met an acceptable level of compliance for entry under provisions of CBERA or CBTPA and/or compute revenue loss.

Audit Step	Initials & Date	Work Paper Ref.
(1) Using the sample selected, determine eligibility for claimed CBERA or CBTPA for each sample item.		
(2) Evaluate errors to determine if errors were systemic. Determine whether referrals should be made for enforcement action. Also see step (6) below.		

Audit Step	Initials & Date	Work Paper Ref.
a) If systemic: (i) Include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Project the effect and recommend collection of unpaid duties and fees. Note: If projections are not appropriate, all reasonable means will be used to determine the unpaid duties and fees. b) For nonsystemic errors: (i) Do not include in computation of compliance rate, if applicable, and/or determination of acceptable level of compliance. (ii) Recommend collection of duties and fees on identified errors.		
(3) Compute the compliance rate, if applicable.		
(4) Determine if the company met an acceptable level of compliance. a) If the company met an acceptable level of compliance, prepare the work paper. b) If the company did not meet an acceptable level of compliance: (i) Coordinate with the account manager to help the company develop a CIP. (ii) Prepare the finding sheet.		
(5) Compute actual or projected revenue loss, if applicable. Note: The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002. The Act contains a provision (Section 382) to offset duty overpayments with duty underpayments on liquidated entries during audits. The Act must be considered when computing actual or projected revenue loss.		
(6) Refer to the EET if results meet EET's impact level for referral.		
(7) Discuss with the company and obtain comments.		

S. Andean Trade Preference Act

Audit steps for Andean Trade Preference Act will be determined by the auditor.

T. Israel Free Trade

Audit steps for Israel Free Trade will be determined by the auditor.

U. Products of Insular Possessions

Audit steps for Products of Insular Possessions will be determined by the auditor.

V. Additional Sampling Issues

Sub-objective: Team members or other Customs officials may identify other issues that require testing. Determine the necessary audit steps to test these issues.

	Audit Step	Initials & Date	Work Paper Ref.
(1)	Using the sample(s) selected, develop tests for any additional sampling issues.		

4.4 ASSESSMENT COMPLIANCE TESTING CLOSURE

Sub-objective: Perform steps required to close ACT and issue the ACT report.

	Audit Step	Initials & Date	Work Paper Ref.
A.	Summarize in the working papers ACT results for each area tested, and develop a risk opinion. NOTE: The FA should not be delayed to wait for the company to take corrective action. The ACT report should be written and issued as soon as adequate information is available and work is complete.		
B.	Meet with team members to discuss results of the audit and risk opinion and plan the exit conference.		
C.	Finalize the draft ACT report.		
D.	Hold the exit conference with the company to discuss ACT results.		
E.	Issue the ACT report.		

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Focused Assessment Program
Follow-up Audit Program

October 2003

FOCUSED ASSESSMENT FOLLOW-UP AUDIT PROGRAM

PART 5 FOCUSED ASSESSMENT FOLLOW-UP

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

Determine whether corrective actions specified in the Compliance Improvement Plan (CIP) were implemented and were effective in managing risk to Customs and correcting the deficiencies identified during the previously conducted Focused Assessment (FA). (Objective may be modified for specific requirements such as verification of loss of revenue calculations by company.)

Audit Step	Initials & Date	Work Paper Ref.
A. Review the applicable Pre-Assessment Survey (PAS) or Assessment Compliance Testing (ACT) report, working papers, and CIP related to each non-compliant area identified during the PAS or ACT.		
B. Meet with team members, including the account manager, to determine the scope of the follow-up review. • Determine if the CIP has been fully implemented. • Determine if a reasonable time period has elapsed since completion of the CIP for a representative sample of transactions to be tested. • Determine whether the account manager, port officials, etc., have concerns that affect follow-up. • Plan for the follow-up entrance conference.		
C. Check with the local OI office to determine if any investigative activity would preclude follow-up.		
D. Hold the entrance conference to discuss the purpose of the follow-up and Mod Act requirements.		
E. Review the actions taken by the company to correct the problem(s).		
F. Develop a sampling plan (statistical or judgmental as appropriate) and tests for the areas with inadequate internal control and/or compliance tests for the areas identified as non-compliant.		
G. Select sample(s) and test internal control and/or selected records for compliance.		
H. Evaluate test results in coordination with the account manager and other members of the team.		
I. Refer to enforcement if results meet impact level for referral.		

Audit Step	Initials & Date	Work Paper Ref.
J. Draft follow-up report.		
K. Hold an exit conference with the company.		
L. Issue the report to the original recipients of the FA program report(s) and new team members.		

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Guidance for Using Risk Exposure to Determine Review Areas

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

This document is designed to provide general guidance for determining review areas for a Focused Assessment (FA). The FA reviews internal controls to evaluate the level of risk to Customs that exists from a company's imports.

In order to assess risk, Customs needs to identify the areas of Customs activity that represent risk (risk exposure) to Customs. The FA team must assess risk exposure by assessing the quantitative and qualitative risk associated with each of the company's Customs activities. Customs management determines qualitative risk. Quantitative risk is more easily evaluated because that can be evaluated based on volume of activity: for example, volume of imports under a particular activity or volume of duty impact or potential impact.

Each company has different organization structures, policies, and procedures and interacts differently with its various suppliers and customers. Each company has different staffs with different experience, capabilities, training, and knowledge. In addition, each company has different Customs activities, different volumes of Customs activities, and imports from different suppliers, countries, etc. Because of all the above variables and many more, each company represents a different challenge when Customs attempts to assess Customs risk related to the company's imports.

Procedures

Before starting an evaluation of internal controls, the FA team will have information about the company's Customs activities based on:

- Declarations to Customs,
- Other information in Customs databases,
- Information from various Customs disciplines such as import specialists and account managers, and
- Information from public sources such as Dun and Bradstreet.

In addition, the FA team will have company information through the company's response to the Pre-Assessment Survey (PAS) questionnaires, the advance conference, written internal control and procedures (if available), and possible preliminary interviews or discussions with company representatives.

Determination of a company's Customs risk exposure is a continuing process. The FA team will make a preliminary assessment of Customs risk exposure based on preliminary information

as soon as it becomes available and will reassess the risk exposure as more information becomes available. For example, the profile for a company may indicate that a risk of misclassification of a particular item exists because of previous occurrences within the industry. But when the company is interviewed and additional records are examined, the FA team may determine that the company does not import that item and that the risk of misclassification therefore does not exist for that company. The FA team will need to develop sufficient information about the company's actual import operations before risk exposure can be assessed. After the FA team has worked with the company and become familiar with the company's operations, the estimate of Customs risk exposure may vary significantly from the preliminary risk exposure based on the profile and initial analysis. The scope of the internal control review will be based on the assessment of the company's risk exposure.

The FA team will review all of the company's internal control policies and procedures by reviewing the company's written policy and procedures and/or responses to the FA questionnaire.

However, the FA process is designed to concentrate on the areas of significant risk to Customs. Accordingly, the FA team will focus its limited resources on the areas of greatest risk exposure for Customs, as determined by the team's evaluation of risk exposure and Customs-identified risks as determined by the analysis of risk identified by Compliance Assessments (CA), as explained below.

Risk Exposure

A major objective of the Focused Assessment is to verify that the company's internal control is adequate for the level of Customs risk. Accordingly, the FA team must work with the company to assess risk exposure. The following guidelines are intended to help the FA team assess risk exposure. They are general guidelines only and may not be appropriate in all circumstances.

Quantitative Factors

In an evaluation of internal control, the first measure of risk exposure should be quantitative because it is the easiest, most objective measure of risk.

If the company has relatively low activity in an area, the FA team may consider the area to be low risk unless qualitative factors increase the risk exposure.

Company plans for changes in operations affect risk exposure. A rapidly growing company may have higher risk exposure because of the increase in imports and the dynamic aspects that may affect control, particularly if the company does not have adequate risk assessment to respond to dynamic changes.

In contrast, if a company is discontinuing or significantly reducing some Customs operations, this change should be considered when assessing risk exposure. For example, if a company is discontinuing imports under provisions of Harmonized Tariff Schedule of the United States (HTSUS) 9802.00.80 to begin imports under a special trade program (STP), the FA team should discuss with appropriate company representatives the company's risk assessment of its planned operations under the STP. This discussion should provide some information about the company's plans to manage risk related to the imports under the STP program, even if imports have not begun under the STP.

If duty is a factor in determining risk exposure, risk exposure may be higher for some commodities than for others, even at the same activity level (volume of imports), because of variations in duty rate. This factor should be considered when company risk exposure is evaluated for duty.

Qualitative Factors

The other primary measure of risk exposure relates to qualitative factors. Historically, Customs has been highly concerned with transshipment, antidumping duties/countervailing duties (ADD/CVD), quota, matters of national interest, and matters related to protection of domestic industries. This includes issues related to special duty provisions that are often designed to assist domestic industry.

Special trade programs are becoming increasingly important as more international trade agreements are negotiated and go into effect. The increasing impact of these international agreements will undoubtedly be a major concern to Customs in the future. The FA team should emphasize the importance of internal control to assure compliance with current trade programs and the importance of risk assessments when instituting new trade programs if the company indicates possible activity in new trade programs. In addition to increasing compliance in current special trade programs, this emphasis will help importers prepare adequate internal control systems for the new special trade programs as they are negotiated and implemented.

The FA team should place particular emphasis on known areas of Customs interest, such as those above, when considering qualitative risk.

Analysis of Compliance Assessments

Since the basic concept of an FA is to limit the focus of the audit so that Customs resources can be used most effectively, the FA team will limit the areas that it reviews extensively to form a risk opinion. The CA process has provided extensive information about companies' compliance in a variety of Customs activities. An analysis of results from 5 1/2 years of CAs has helped identify review areas that the FA team should focus on. The CA analysis showed that deficiencies most frequently occurred in value, classification, special duty provisions, and special trade programs. Some areas are of specific concern to Customs and must be considered high risk because of their significance and sensitivity (for example, transshipment and antidumping duties).

Summary Guidance for Using Risk Exposure Experience Related to Review Areas

The FA team will do a cursory review of all the company's internal control procedures by reviewing its documented internal control procedures and its responses to the PAS questionnaires. But the risk exposure of an area will determine whether a risk opinion should be issued for the area. A risk opinion will be issued only on areas with significant potential risk. Some areas will be reviewed extensively only when specific issues have been identified. The following general guidelines are designed to help the FA team determine the scope of the internal control review.

Value. The CA process identified extensive errors in value reporting. In addition, this is an area of major concern to Customs, and the FA is the only Customs program that addresses value, through a structured review of the company's accounting books and records. Because of these factors, a risk opinion on value should be issued with each FA report. The level of risk exposure may be higher for imports with higher duty rates.

Classification. The CA process identified extensive errors in classification reporting. In addition, this is an area of major concern to Customs. A risk opinion should be issued with each FA report. In some industries and some companies, the risk exposure will be low for classification, but a risk opinion should be developed to reflect that risk exposure. The level of risk exposure may be higher for imports with higher duty rates.

Special Trade Programs. The CA process identified extensive errors in STPs, and these areas have international impact. A risk opinion should normally be issued with each FA report if the importer has sufficient activity in STPs to indicate that a potential risk exists. The volume of the STP should be clearly considered when evaluating the adequacy of internal control. In some companies the risk exposure will be low for STPs when the quantitative measure (volume of imports) is considered.

Special Duty Provisions. The CA process identified extensive errors in special duty provisions, and these areas are of special interest to Customs. Many special duty provisions were developed to assist domestic industry or as part of international programs. A risk opinion should normally be issued with each FA report if the importer has sufficient activity in the special duty provision to indicate that a potential risk exists. The volume of the special duty provisions should be considered when evaluating the adequacy of internal control. In some companies the risk exposure will be low for special duty provisions when the quantitative measure (volume of imports) is considered.

Antidumping Duties/Countervailing Duties. The CA process did not pursue ADD/CVD issues extensively, so reliable historic information is not available. These duties are of special interest to Customs, to domestic industry, and to Congress. A risk opinion should normally be issued with each FA report when ADD/CVD have been identified as a risk area.

Transshipment. The CA process did not pursue transshipment issues extensively, so reliable historic information is not available. Transshipment is of special interest to Customs, to domestic industry, and to Congress. A risk opinion should normally be issued with each FA report when transshipment has been identified as a risk area. This is particularly important in textile audits but may be identified as a risk area in other audits as well.

Recordkeeping Compliance. A separate risk opinion for recordkeeping is required only when some specific risk exists related to recordkeeping. A separate review and testing of recordkeeping compliance is not normally required. The adequacy of recordkeeping procedures (compliance with 19 CFR 163) will be verified during reviews of each Customs review area. If the company cannot provide records required by 19 CFR 163.3, the cause of the problem should be identified and addressed. The company may be subject to recordkeeping penalties for 19 USC 1509(a) (1)(A) violations. In most cases recordkeeping issues will cause deficiencies or errors in other Customs activities, so it will not be necessary to prepare a separate recordkeeping risk opinion.

Quantity. A separate risk opinion for quantity is required only when some specific risk exists related to quantity. For example, when specific or compound duty rates are based on quantity, then quantity may represent a risk that should be addressed. Quantity may be a risk area for imports of petroleum, footwear, alcoholic beverages, commodities subject to quota, and others. When quantity is identified as a risk area, a risk opinion should be issued.

Harbor Maintenance Fee and User Fee. Customs maintains automated controls to assure that harbor maintenance fees and user fees are accurately calculated. Previous experience has not indicated significant issues related to harbor maintenance fee and user fee compliance. A separate risk opinion is required only when specific risks are identified.

The following table summarizes the above guidance for determining FA review areas for developing risk opinions:

Summary Guidance for Determining Review Areas to Develop Risk Opinions

Review Area	Risk Opinion
Value	Always
Classification	Always
Special Trade Program	When identified as a risk area
Special Duty Provision	When identified as a risk area
ADD/CVD	When identified as a risk area
Transshipment	When identified as a risk area
Recordkeeping	When identified as a risk area that must be addressed separately
Quantity	When identified as a risk area
Harbor Maintenance Fees and User Fees	When identified as a risk area

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Consideration of Internal Control in a Customs Compliance Audit

Consideration of Internal Control in a Customs Compliance Audit

Table of Contents

Introduction 3

Definition of Internal Control 4

Relationship Between Objectives and Components 4

Benefits of Internal Control Assessments 5

Assessing Risk 6

Evaluating Internal Controls 6

- Assessing Risk Exposure 7
  - Significance and Sensitivity 7
  - Susceptibility 8
  - The Existence of any “Red Flags” 8
  - Management Support 9
  - Competent Personnel 9
- Assessing the Effectiveness of the Internal Control System 9
  - Identifying Controls 10
  - Known Control Effectiveness 11
  - Assessing Control Design 11
  - Assessing Control Implementation 11
  - Proper Transaction Documentation 11

Determining Reliability of Computer-Processed Data 12

Reporting on Internal Control Assessments 12

Appendix I 13

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Consideration of Internal Control in a Customs Compliance Audit

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

This document provides direction for the Customs team in evaluating a company's internal control during an audit of a company's compliance with Customs requirements. It defines internal control, describes the objectives and components of internal control, and explains how the Customs team should consider internal control in planning and performing an audit. In particular, it provides guidance for implementing United States General Accounting Office (GAO) *Government Auditing Standards*[1] (the Yellow Book) relating to internal controls for audits of Customs requirements.

The Yellow Book, paragraph 2.4 b., states that financial audits include financial statements and financial related audits.

> Financial related audits include determining whether (1) financial information is presented in accordance with established or stated criteria, (2) the entity has adhered to specific financial compliance requirements, or (3) the entity's internal control structure over financial reporting and/or safeguarding assets is suitably designed and implemented to achieve the control objectives.

The Yellow Book, paragraph 2.5, states that financial related audits may include audits for compliance with laws and regulations.

The Yellow Book, paragraph 4.21, includes the following field work standard for financial audits:

> Auditors should obtain a sufficient understanding of internal controls to plan the audit and determine the nature, timing, and extent of tests to be performed.

In the Yellow Book, paragraph 6.39, GAO fieldwork standards for performance audits require auditors to obtain an understanding of management controls. The GAO publication *Assessing Internal Controls in Performance Audits* [2] (the Gray Book) provides extensive guidance for assessing internal controls.

Customs compliance audits are different from traditional financial audits because Customs audits are not audits of financial statements. The primary objective of Customs compliance audits is to determine compliance, including correct reporting to Customs. Reporting to Customs includes numerous financial issues. In addition, some elements of Customs compliance audits, such as correct reporting of classification, country of origin, and other specific information of

concern to Customs, are more closely related to performance audits than financial audits.

Since Customs compliance audits include aspects of financial audits and performance audits, this document combines appropriate internal control aspects applicable to financial and performance audits. Internal control aspects that would not be relevant to Customs compliance audits, such as control of assets, are not included. Because GAO and American Institute of Certified Public Accountants (AICPA) standards for financial audits are not oriented to Customs regulatory compliance, this document combines applicable information from GAO standards for financial and performance audits to develop procedures for evaluating compliance with Customs requirements. Information from AICPA Statement on Auditing Standards (SAS) No. 78 *Consideration of Internal Control in a Financial Statement Audit* [3] is included for guidance when appropriate.

In Customs compliance audits, the Customs team should obtain sufficient understanding of internal control to plan the audit by performing procedures to understand the design of controls and whether they have been placed in operation and are effective.

Definition of Internal Control

AICPA SAS 78 (paragraphs 6–7) states the following regarding internal controls:

> Internal control is 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: (a) reliability of financial reporting, (b) effectiveness and efficiency of operations, and (c) compliance with applicable laws and regulations.
>
> Internal control consists of the following five interrelated components.
>
> a. *Control environment* sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure.
> b. *Risk assessment* is the entity's identification and analysis of relevant risks to achievement of its objectives, forming a basis for determining how the risks should be managed.
> c. *Control activities* are the policies and procedures that help ensure that management directives are carried out.
> d. *Information and communication* are the identification, capture, and exchange of information in a form and time frame that enable people to carry out their responsibilities.
> e. *Monitoring* is a process that assesses the quality of internal control performance over time.

Relationship Between Objectives and Components

The relationship between objectives and components of internal controls is explained in AICPA SAS No. 78 as summarized below.

There is a direct relationship between objectives, which are what an entity strives to achieve, and components, which represent what is needed to achieve the objectives. In addition, internal control is relevant to the entire entity or to any of its operating units or business functions. These relationships are depicted in the following figure.

Generally, controls that are relevant to an audit pertain to the entity's objective of preparing financial statements for external purposes. Controls relating to operations and compliance are particularly relevant to Customs compliance audits because they pertain to the Customs team's evaluation of the risk to Customs that the company's importing process may result in significant noncompliance with laws and regulations.

The five components of internal control are applicable to assessments of compliance with Customs requirements. The components should be considered in the context of the following:

- The entity's size.
- The entity's organization and ownership characteristics.
- The nature of the entity's business.
- The diversity and complexity of the entity's operations.
- The entity's methods of transmitting, processing, maintaining, and accessing information.
- Applicable legal and regulatory requirements.

Benefits of Internal Control Assessments

The Gray Book (page 12) states the following:

> Internal control assessments can help auditors perform assignments more quickly and work with greater assurance that objectives are achieved. Such assessments help to:

- Determine when internal controls can be relied on to reduce audit testing,
- Focus on areas of weakness for emphasis during the assignment, and
- Identify potential causes of problems or deficiencies to which recommendations for corrective action can be directed.

Internal controls, no matter how well designed and implemented, can provide only reasonable assurance regarding achievement of an entity's control objectives. The likelihood of achievement is affected by limitations inherent to internal control, such as human judgment in decision making and human errors or mistakes. In addition, the cost of internal controls should not exceed the expected benefits. Usually, precise measurement of costs and benefits is not possible. Accordingly, management makes both quantitative and qualitative estimates and judgments in evaluating cost-benefit relationships.

The steps taken to assess controls may simultaneously help attain other objectives, such as resolving the overall assessment objective or assessing compliance with applicable laws and regulations.

The audit objective determines the extensiveness of internal control assessment as well as

the scope and methodology of the audit. Assignments with broad objectives are generally more difficult and require more resources and time than assignments with limited objectives. Therefore, objectives should be defined as precisely as possible to preclude unnecessary work while meeting the assignment's purpose.

Assessing Risk

The following guidance should be used for assessing risk:

- If the Customs team concludes that transaction testing can be limited because the company has an acceptable level of internal controls, the Customs team must document the controls and tests of those controls made to assure their operation and effectiveness.
- The Customs team can use a combination of different types of tests to get sufficient evidence of a control's effectiveness.
- Inquiries alone generally will not support an assessment that internal controls are adequate and effective.
- Observation provides evidence about a control's effectiveness only at the time observed; it does not provide evidence about its effectiveness during the rest of the period under audit.
- The Customs team can use evidence from tests of controls done in prior audits, but it has to obtain evidence about the nature and extent of significant changes in policies, procedures, and personnel since it last performed those tests.

Evaluating Internal Controls

The first step in evaluating internal controls is to determine the risk exposure, which is the likelihood of significant noncompliance with laws and regulations. The next step in the process is to review the system of internal control. The relationship of risk exposure to the system of internal control determines the nature and extent of audit tests. The audit tests provide an evaluation of the effectiveness of internal controls. The combined results from the risk exposure, review of the design of the internal control system, and tests of internal controls are the basis for an opinion on the adequacy of internal controls. The extensiveness of tests of internal controls is illustrated below:

Determine Extensiveness of Audit Tests

Risk Exposure	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test
High		Weak Adequate Strong		High Moderate to High Low to Moderate
Moderate		Weak Adequate Strong		Moderate to High Moderate Low
Low		Weak Adequate Strong		Low to Moderate Low Very Low

Source: Table adapted from the GAO Gray Book.

AICPA SAS 78 (paragraphs 19–21) provides the following internal control guidance:

> In all audits, the auditor should obtain an understanding of each of the five components of internal control sufficient to plan the audit by performing procedures to understand the design of controls relevant to an audit of financial statements, and whether they have been placed in operation. In planning the audit, such knowledge should be used to—
>
> - Identify types of potential misstatements.
> - Consider factors that affect the risk of material misstatement.
> - Design substantive tests.
>
> The nature, timing, and extent of procedures the auditor chooses to perform to obtain the understanding will vary depending on the size and complexity of the entity, previous experience with the entity, the nature of the specific controls involved, and the nature of the entity's documentation of specific controls. For example, the understanding of risk assessment needed to plan an audit for an entity operating in a relatively stable environment may be limited. Also, the understanding of monitoring needed to plan an audit for a small, noncomplex entity may be limited.
>
> Whether a control has been placed in operation is different from its operating effectiveness. In obtaining knowledge about whether controls have been placed in operation, the auditor determines that the entity is using them. Operating effectiveness, on the other hand, is concerned with how the control was applied, the consistency with which it was applied, and by whom it was applied. For example, a budgetary reporting system may provide adequate reports, but the reports may not be analyzed and acted on. This Statement does not require the auditor to obtain knowledge about operating effectiveness as part of the understanding of internal control.

Although SAS 78 does not require the auditor to obtain knowledge about operating effectiveness as part of understanding of internal control, knowledge about operating effectiveness is necessary to determine the reliability of internal controls, decide the extent of audit testing, and assess risk. Therefore, Customs assessments of internal controls will include evaluations of the effectiveness of internal controls.

Assessing Risk Exposure

The key considerations of risk exposure for audits of Customs compliance are:

- Significance and Sensitivity
- Susceptibility
- The Existence of "Red Flags"
- Management Support
- Competent Personnel

Significance and Sensitivity

The Gray Book (pages 16–17) defines significance and sensitivity as follows:

Significance refers to the importance of items, events, information, matters, or problems. Frequently significance can be assessed in terms of dollars. In other instances, assessing significance requires a more subjective judgment. For example, the unauthorized use of a government vehicle in a single instance is normally considered of limited significance, but unsafe operation of a nuclear power plant is of great significance since a failure could be a catastrophe.

Sensitivity refers to the likely perception and emotional response by others to conditions or circumstances. Determining sensitivity requires judgment based on the circumstances in each case, but some issues likely to be judged as sensitive include:

- issues that have received media coverage;
- issues that have been the subject of congressional interest and inquiry;
- issues of a highly partisan nature;
- issues involving mistreatment of children or the elderly; and
- issues involving environmental contamination or pollution.

A high degree of risk exposure may be indicated by either the significance or the sensitivity of the subject matter under review, or matters may be both significant and sensitive.

Issues likely to be judged significant and sensitive by Customs include the issues listed above as well as issues of antidumping/countervailing duty, transshipments, Intellectual Property Rights, health and safety, and others.

Susceptibility

Susceptibility refers to the propensity for noncompliance with laws and regulations. An issue of large significance does not necessarily involve great susceptibility. For example, the risk of misclassification of large quantities of imports may have a high significance because the total duty involved may be high. But these imports may not have a high susceptibility to misclassification if a limited number of Harmonized Trade Schedule of the United States (HTSUS) numbers are involved and the classification issues are not complex.

The Customs team should formulate questions to assess susceptibility based on the inherent nature of the import. Examples of questions to ask follow:

- Is the imported item, manufacturer, country of origin, or other element designated as high risk by Customs?
- Does Customs have information that indicates internal control weaknesses pertaining to the importer?
- Do incentives to make false representations/declarations outweigh the penalties?
- Are requirements imposed reasonable, or are they so complicated and cumbersome that failure to comply can be expected?
- Does the activity have numerous transactions or diverse activities?
- Does the importer contract out activities without adequate control systems?

The Existence of any “Red Flags”

The Customs team should be alert to and consider any red flags, including:

- A prior history of Customs problems;
- A history of material weaknesses described in prior Customs audits;

- Poorly defined and documented internal control procedures;
- Lack of or ineffective monitoring of Customs operations;
- Complex Customs transactions;
- Lack of specific performance measures for Customs operations, thereby making accountability for results difficult or impossible to measure;
- Management inability to correctly establish priorities;
- A high rate of personnel turnover in key occupations related to Customs activities;
- Inadequate Customs training for personnel responsible for reporting, monitoring or otherwise involved in Customs activities;
- Poor communication systems regarding Customs requirements and reporting; and
- Poor oversight of Customs brokers and other agents involved in Customs activities.

Management Support

The Customs team should consider whether management recognizes the importance of, and has made a commitment to implement, internal controls of Customs operations. Examples of questions to ask follow:

- Has management set the right tone by clearly stating, in writing, its expectations for compliance with Customs requirements?
- Is there a strong and competent organization within the company to assure Customs compliance?
- Does the Import Department have sufficient authority within the organization to assure Customs compliance?
- Does management require periodic reviews of Customs operations?
- Does management promptly respond when Customs problems are identified, or have problems been repeatedly disclosed in prior audits/evaluations?
- Is management knowledgeable about Customs and potential Customs issues?
- Is management willing to discuss various aspects of Customs operations cooperatively?

AICPA SAS 78 (paragraph 25) discusses this concept as the control environment that sets the tone of an organization, influencing the control consciousness of its people. The control environment is the foundation of all other components of internal control, providing discipline and structure.

Competent Personnel

Managers and employees responsible for Customs operations should maintain a level of competence that allows them to accomplish their duties as well as understand the importance of developing and implementing good internal controls. Examples of questions to ask follow:

- Is there a stable management team with continuity?
- Are employees periodically reminded of their responsibilities?
- Are employees provided with needed formal and on-the-job training?

Assessing the Effectiveness of the Internal Control System

After assessing risk exposure, the Customs team should review the internal control system and then test internal controls to assess the effectiveness of the internal control system. In most cases, internal control assessments are necessary to ensure that audit work will meet assignment objectives. Any transaction examined might be atypical. Control assessments give evidence whether transactions are likely to be handled in the same manner. Internal controls for Customs compliance should be designed to include the five components of internal control: (1)

control environment, (2) risk assessment, (3) control activities, (4) information and communications, and (5) monitoring.

The Gray Book lists the following key steps in assessing internal controls:

- Identify and understand relevant internal control(s);
- Determine what is already known about control effectiveness;
- Assess adequacy of control design;
- Determine if controls are properly implemented; and
- Determine if transactions are properly documented.

Internal control testing is particularly important in the last three steps for assessing internal controls.

The objective of determining the effectiveness of internal controls is to determine the extent to which they can be relied on and thereby reduce the extent of audit testing. The greater the reliance that can be placed on internal controls, the less testing may be required.

Identifying Controls

The auditor must identify the controls that are needed to assure Customs compliance. An effective internal control system consists of five components. Internal control of Customs activities should be designed to include controls for the five components. The following information can be used to identify the controls necessary to assess the components of a Customs control system:

- The control environment sets the tone of the organization. Management and employees should have a positive and supportive attitude toward Customs internal control and conscientious management of Customs-related operations. Management should support the development and maintenance of effective internal control. The control environment includes a message of integrity and ethical values, commitment to competence of personnel, an organizational structure that contributes to effective internal control for Customs operations, and a philosophy and operating style that supports the development and maintenance of effective internal control.
- Risk assessment is an evaluation of risk pertaining to Customs activities. Management should establish clear and consistent company-wide objectives and support activity-level objectives related to Customs activities. Management should make a thorough identification of risks from both internal and external sources. Management should analyze those risks and develop an appropriate approach to manage risk. Mechanisms should be in place to identify changes that may affect the company's ability to achieve its missions, goals, and objectives related to Customs activities.
- Control activities are policies, procedures, techniques, and control mechanisms to ensure adherence to established Customs requirements. Proper control activities should be developed for each of the company's Customs activities. A system for Customs compliance includes the methods and records used to identify, assemble, analyze, classify, record, and accurately report Customs information and maintain accountability for Customs compliance.
- Information and communication systems must be in place to identify and record pertinent operational and financial information relevant to Customs activities. A system must be in place to communicate information to management responsible for Customs activities and others within the company who need it, in a form that enables them to carry out their duties and responsibilities efficiently and effectively. Such a system also assures that effective external communications occur with groups that can affect the achievement of the company's missions, goals, and objectives related to Customs.

- Monitoring assesses the quality of performance related to Customs activities over time. Management should have procedures in place to monitor internal control continuously as a part of the process of carrying out its regular activities. In addition, separate evaluations of internal control should be performed periodically and deficiencies investigated. Findings of all audits and other reviews should be evaluated, decisions made about the appropriate response, and actions taken to correct or otherwise resolve the issues.

Internal control component guidance is modified from the GAO Exposure Draft *Internal Control Management and Evaluation Tool*.[4]

Known Control Effectiveness

The Customs team should consider what, if anything, is known about control effectiveness. If Customs or another organization made an internal control assessment, the Customs team should consider how recent and thorough the assessment was, as well as the organization's reputation, qualifications, and independence. A determination can then be made whether to rely on the results or do additional tests. If prior control assessments are considered to be sufficiently recent and thorough, the Customs team need not further assess internal control design and effectiveness.

Assessing Control Design

Considering the information developed during the assessment of risk exposure, the Customs team should decide what is most likely to be wrong (e.g., valuation, classification, special trade programs). Then the internal controls should be examined to determine whether they are logical, reasonably complete, and likely to deter or detect possible failures or errors that will result in noncompliance. Generally, the greater the risk exposure, the stronger the internal controls should be.

Controls should provide reasonable but not absolute assurance of deterring or detecting noncompliance. In assessing the extensiveness of needed controls, the Customs team should consider the reasonableness of the controls in relation to the benefits to be gained.

Assessing Control Implementation

The Gray Book (pages 26–27) provides the following guidance pertaining to the implementation of internal controls:

> Even though internal controls may be logical and well-designed and may seemingly be strong, system effectiveness may be impaired if control procedures are not correctly and consistently used. . . .Thus, the extent that control procedures are adhered to should be determined.
>
> Control procedures may not be complied with because management may override them; employees may secretly be working together (collusion) to avoid using or circumvent them; and employees may not be correctly applying them due to fatigue, boredom, inattention, lack of knowledge, or misunderstanding.
>
> Sufficient testing should be conducted to afford a reasonable basis for determining whether the controls are being consistently applied.

Proper Transaction Documentation

Transactions and events pertaining to Customs compliance should be clearly documented, and

documentation should be readily available for examinations. Examples of questions to ask follow:

- Are internal control objectives and procedures formalized in writing?
- Are all transactions and events adequately documented, and is documentation readily available for examination?
- Does documentation show personnel involved in monitoring, evaluation methods used, key factors considered, tests performed, and conclusions reached?
- Does documentation show corrective actions taken for problems identified during monitoring processes?
- Are follow-ups to verify adequacy of corrective actions documented?

In summary, when evaluating internal control, Customs audits must consider the five components of internal control, five factors for determining risk exposure, and five factors for assessing the design and effectiveness of the internal control system. This internal control approach is summarized in the 5-5-5 Guidance in Appendix I.

Determining Reliability of Computer-Processed Data

Generally accepted government auditing standards in the Yellow Book (paragraph 6.62) require that computer-processed data be valid and reliable when those data are significant to the auditors' findings. This is generally done through tests such as macro tests, comparison of company data to Customs data, and verifications of computer data to audited financial statements when possible.

Reporting on Internal Control Assessments

The Yellow Book sets specific standards for reporting on internal controls. These standards will be applied in Customs audits.

[1] United States General Accounting Office, *Government Auditing Standards*, 1999 revision.

[2] United States General Accounting Office, Office of Policy, *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, September 1990.

[3] American Institute of Certified Public Accountants, Statement on Accounting Standards No. 78, *Consideration of Internal Control in a Financial Statement Audit,* December 1995.

[4] United States General Accounting Office, *Internal Control Management and Evaluation Tool EXPOSURE DRAFT*, GAO-01-131G, February 2001.

Appendix I

Internal Control
5-5-5 Guidance

5 Interrelated Components of Effective Internal Control

- Control Environment
- Risk Assessment
- Control Activities
- Information and Communication
- Monitoring

How to Assess Internal Control

5 Considerations for Risk Exposure, Determine:

- Significance and Sensitivity
- Susceptibility
- Red Flags
- Management Support
- Competent Personnel

5 Considerations to Assess Control Effectiveness:

- Identify and Understand Control
- What is Known about Control Effectiveness?
- Examine Control Design
- Are Controls Implemented?
- Are Transactions Documented?

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Internal Control Summary by Component

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

This document should be used with the Internal Control Management and Evaluation Tool to summarize conclusions of adequacy of internal control by component. Although use of this tool is not required, it is intended to help management and evaluators determine how well a company's internal control is designed and functioning and help determine what, where, and how improvements, when needed, may be implemented.

This tool is not authoritative but is intended as a supplemental guide that managers and evaluators may use to assess the effectiveness of internal control and identify important aspects of control in need of improvement. Users should keep in mind that this tool can and should be modified to fit the circumstances, conditions, and risks relevant to the situation of the company.

Internal Control Component

Control Environment

Management and employees have a positive and supportive attitude toward Customs internal control and conscientious management of Customs-related operations. Management conveys the message that integrity and ethical values must not be compromised. Management has a philosophy and operating style that is appropriate to the development and maintenance of effective internal control for Customs as evidenced by the following:

- The company demonstrates a commitment to the competence of its personnel responsible for Customs-related activities.
- The company's organizational structure and the way in which it assigns authority and responsibility for Customs operations contribute to effective internal control.
- The company's management cooperates with auditors, does not attempt to hide known problems from them, and values their comments and recommendations.

Risk Assessment

The company has established clear and consistent company-wide objectives and supporting activity-level objectives related to Customs activities as evidenced by the following:

- Management has made a thorough identification of risks pertaining to Customs activities, from both internal and external sources, that may affect the ability of the company to meet those objectives.

- An analysis of those risks has been performed, and the company has developed an appropriate approach for risk management.
- Mechanisms are in place to identify changes that may affect the company's ability to achieve its missions, goals, and objectives related to Customs activities.

Control Activities

Appropriate policies, procedures, techniques, and control mechanisms have been developed and are in place to ensure adherence to established Customs requirements. Control activities are evidenced by the following:

- Proper control activities have been developed and documented for each of the company's Customs activities.
- The control activities identified as necessary are actually being applied properly.
- All documentation of transactions and records are properly managed, maintained, and reviewed as necessary.
- Control procedures are reviewed and revised as necessary.

Information and Communications

Information systems are in place to identify and record pertinent operational and financial information relevant to Customs activities. Management ensures that effective internal communications take place. The company employs various forms of communications appropriate to its needs and manages, develops, and revises its information systems in a continual effort to improve communications. Effective information and communication for Customs are evidenced by the following:

- Appropriate information is identified, recorded, and communicated to management responsible for Customs activities and others within the company who need it and in a form that enables them to carry out their duties and responsibilities efficiently and effectively.
- Effective external communications occur with groups that can affect the achievement of the company's missions, goals, and objectives related to Customs activities.
- Individual roles and responsibilities for Customs activities are communicated through policy and procedure manuals.

Monitoring

Company internal control monitoring assesses the quality of performance related to Customs activities over time. Monitoring is evidenced by the following:

- Procedures to monitor internal control occur on an ongoing basis as a part of the process of carrying out regular activities.
- Separate evaluations of internal control are periodically performed, and deficiencies found are investigated.
- Procedures are in place to ensure that the findings of all audits and other reviews are promptly evaluated, decisions are made about the appropriate response, and actions are taken to correct or otherwise resolve the issues promptly.

Source: Adapted from United States General Accounting Office, Internal Controls Management and Evaluation Tool EXPOSURE DRAFT, GAO-01-131G, February 2001.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Internal Control Management and Evaluation Tool
(Guidance not Required)

Introduction

In March 2003, the U.S. Customs Service became part of the Bureau of Customs and Border Protection, which will continue to be referenced as Customs in this document.

This document is an Internal Control Management and Evaluation Tool. Although use of this tool is not required, it is intended to help management and evaluators determine how well a company's internal control is designed and functioning and help determine what, where, and how improvements, when needed, may be implemented. This is a good tool for auditors to use when developing questions and conducting interviews with company personnel, particularly in large, complex companies.

The tool is presented in five sections corresponding to the five components of internal control: (1) control environment, (2) risk assessment, (3) control activities, (4) information and communications, and (5) monitoring.

Space is provided beside each issue for the user to note comments or provide descriptions of the circumstances affecting the issue. Comments and descriptions usually will not be of the "yes/no" type, but will generally include information on how the company does or does not address the issue. This tool is intended to help users reach a conclusion about the company's internal control as it pertains to the particular component.

This tool could be useful in assessing internal control in compliance with laws and regulations. It could also be useful in assessing internal control as it relates to various Customs activities within a company.

This tool is not authoritative but is intended as a supplemental guide that managers and evaluators may use in assessing the effectiveness of internal control and identifying important aspects of control in need of improvement. Users should keep in mind that this tool is a starting point and that it can and should be modified to fit the circumstances, conditions, and risks relevant to the situation of the company. Not all of the issues need to be considered for every company or activity.

Control Environment

According to the first internal control component, which relates to control environment, management and employees should establish and maintain an environment throughout the organization that sets a positive and supportive attitude toward internal control and conscientious management. Several key factors affect the accomplishment of this goal. Management and evaluators should consider each of these control environment factors when determining whether a positive control environment has been achieved.

The factors that should be focused on are listed below. Management and evaluators should concentrate on the substance of controls rather than their form, because controls may be established but not acted upon.

	Internal Control Point	Comments/ Descriptions
	Integrity and Ethical Values	
1.	Management has promoted a climate that emphasizes integrity and ethical behavior by its Import Department employees. The company employs a code of conduct that emphasizes proper behavior and sets penalties for unethical conduct.	
2.	Dealings with Customs are conducted on a high ethical plane. • Reports to Customs are proper and accurate (not intentionally misleading). • Management cooperates with auditors and other evaluators, does not attempt to hide known problems from them, and values their comments and recommendations.	
3.	The company has a well-defined and -understood process for dealing with Customs requests and concerns in a timely and appropriate manner.	
	Commitment to Competence	
1.	Management has performed analyses of the knowledge, skills, and abilities needed to perform Customs-related jobs in an appropriate manner.	
2.	The company provides training and counseling in order to help employees maintain and improve their competence for the job relating to Customs. • There is an appropriate training program to meet the needs of employees. • The company emphasizes the need for continuing training and has a control mechanism to help ensure that all employees actually received appropriate training.	
	Management's Philosophy and Operating Style	
1.	Management employs a philosophy that emphasizes the correct reporting of information to Customs.	
2.	Management places a high degree of importance on retaining competent personnel in key functions over its Customs transactions.	
3.	The company Import Department has adequate authority to interact with other offices as needed, and strong synchronization and coordination exist between the Import Department and other departments with responsibilities or information related to Customs activities.	
4.	Management places a high degree of importance on the work of Customs officers, external audits, and other evaluations and studies with Customs information and is responsive to information from such officers.	
5.	There is appropriate interaction between management of the company Import Department and senior management.	

	Internal Control Point	Comments/ Descriptions
	Organizational Structure	
1.	The Import Department is appropriately located in the organization.	
2.	Key areas of authority and responsibility relative to Customs activities are defined and communicated throughout the organization. Consider the following: • Executives in charge of major activities or functions are fully aware of their duties and responsibilities. • Executives and key managers understand their internal control responsibilities and ensure that their staff also understands their own responsibilities.	
	Assignment of Authority and Responsibility	
1.	The company appropriately assigns authority and delegates responsibility for Customs activities to the proper personnel to deal with organizational goals and objectives. • Authority and responsibility are clearly assigned throughout the organization and clearly communicated to employees. • Responsibility for decision making is clearly linked to the assignment of authority and responsibility.	
2.	Each employee knows how his or her actions related to Customs activities interrelate to others' actions and is aware of his or her related duties concerning Customs internal control.	
3.	Delegation of authority is appropriate in relation to the assignment of responsibility for Customs activities. • Employees at the appropriate level are empowered to correct problems or implement improvements. • There is an appropriate balance between the delegation of authority at lower levels to "get the job done" and the involvement of senior-level personnel.	
	Human Resource Policies and Practices	
1.	Employee's responsibilities for Customs activities are properly supervised.	
	Oversight Groups	
1.	Within the company, there are mechanisms in place to monitor and review operations and programs. • The company has a committee or senior management council that reviews internal audit work of Customs activities. • The internal audit function reviews the company's Customs activities and systems and provides information, analyses, appraisals, recommendations, and counsel to management.	

Risk Assessment

The second internal control component addresses risk assessment. A precondition to risk assessment is the establishment of clear, consistent company goals and objectives at both the entity level and the activity level. Once the objectives have been established, the company needs to identify the risks that could impede the efficient and effective achievement of those objectives. Internal control should provide for an assessment of the risks the company faces from both internal and external sources. Once risks have been identified, they should be analyzed for their possible effect. Management then must formulate an approach for risk management and decide upon the internal control activities required to mitigate those risks and achieve the internal control objectives of efficient and effective operations, reliable Customs reporting, and compliance with laws and regulations. A manager or evaluator will focus on management's processes for setting objectives, risk identification, risk analysis, and management of risk during times of change. Listed below are factors a user might consider.

	Internal Control Point	**Comments/ Descriptions**
	Establishment of Activity-Level Objectives	
1.	Company Customs office objectives are linked with company objectives.	
	Risk Identification	
1.	Management identifies Customs risk. • Qualitative and quantitative methods are used to identify risk and determine relative risk rankings on a scheduled and periodic basis. • How risk is to be identified, ranked, analyzed, and mitigated is communicated to appropriate staff. • Risk identification and discussion occur in senior-level management meetings. • Risk identification takes place as part of short- and long-term forecasting and strategic planning. • Risk identification occurs as a result of consideration of findings from audits, evaluations, and other assessments.	
2.	Adequate mechanisms exist to identify risks to Customs activities arising from external factors. The company should consider the risks: • Arising from changing needs or expectations by Congress, Customs officials, or the public. • Posed by new legislation, regulations, rulings, and court decisions. • Resulting from business, political, or economic changes. • Associated with major suppliers, brokers, contractors, and agents. • Resulting from interactions with other companies and outside parties.	
3.	Adequate mechanisms exist to identify risks to Customs activities arising from internal factors. The company should consider the risks: • Resulting from downsizing operations and personnel. • Associated with major changes of operating processes, foreign sourcing, or importing operations. • Resulting from new lines, products, or other business activities.	

	Internal Control Point	Comments/ Descriptions
	• Associated with restructuring and reorganizations. • Posed by disruption of information systems. • Posed by highly decentralized Customs operations. • Posed by personnel turnover or personnel who are not adequately qualified and trained. • Resulting from heavy reliance on agents or other parties to perform critical company operations. • Resulting from rapid growth or expansion of import operations.	
4.	Management assesses other factors such as a history of compliance problems.	
	Risk Analysis	
1.	After Customs risks have been identified, management should undertake an analysis of their possible effect. Consider the following: • Management has established a formal or informal process to analyze risks. • Criteria have been established for determining low, medium, and high risks. • Appropriate levels of management and employees are involved in the risk analysis. • Risks identified and analyzed are relevant to the corresponding activity objective. • Risk analysis includes estimating the risk's significance and sensitivity. • Risk analysis includes estimating the likelihood and frequency of occurrence of each risk (susceptibility) and determining whether if falls into the low-, medium-, or high-risk category. • A determination is made on how best to manage or mitigate the risk and what specific actions should be taken.	
2.	Management has developed an approach for risk management related to Customs compliance and control based on how much risk can be prudently accepted. Consider the following: • The approach will vary from company to company based on the company's Customs activities. • The approach is designed to keep risks within levels judged to be appropriate, and management takes responsibility for setting the tolerable risk levels. • Specific control activities are decided upon to manage or mitigate specific risks, and their implementation is monitored.	
	Managing Risks During Change	
1.	The company has mechanisms in place to anticipate, identify, and react to risks presented by changes in government, economic, industry, regulatory, operating, or other conditions that can affect Customs compliance.	
2.	The company gives special attention to risks presented by changes that can have a more dramatic and pervasive effect on Customs compliance.	

	Internal Control Point	Comments/ Descriptions
	The company is attentive to risks related to: • Changes in Customs information systems. • Rapid growth and expansion or rapid downsizing. • Imports under Customs programs and activities that are new to the company. • Imports from a new geographical area.	

Control Activities

The third internal control component addresses control activities. Internal control activities are the policies, procedures, techniques, and mechanisms that help ensure that management's directives to mitigate risks identified during the risk assessment process are carried out. Control activities are an integral part of the company's planning, implementing, and reviewing processes.

Control activities occur at all levels and functions of the company. They include a wide range of diverse activities, such as approvals, authorizations, verifications, reconciliations, performance reviews, security activities, and the production of records and documentation. A manager or evaluator should focus on control activities in the context of the company's management directives to address risks associated with established objectives for each significant activity. Therefore, a manager or evaluator will consider whether control activities relate to the risk assessment process and whether they are appropriate to ensure that management's directives are carried out. In assessing the adequacy of internal control activities, a reviewer should consider whether the proper control activities have been established, whether they are sufficient in number, and the degree to which those activities are operating effectively. This analysis and evaluation should also include controls over computerized information systems. A manager or evaluator should consider not only whether established control activities are relevant to the risk assessment process, but also whether they are being applied properly.

Given the wide variety of control activities that companies may employ, it would be impossible for this tool to address them all. However, there are some general, overall points to be considered by managers and evaluators, as well as several major categories or types of control activity factors that are applicable at various levels throughout practically all companies. In addition, some control activity factors are specifically designed for information systems. These factors and related issues are listed below as examples of issues to be considered. They are meant to illustrate the range and variety of control activities that are typically used.

	Internal Control Point	Comments/ Descriptions
	General Application	
1.	Appropriate policies, procedures, techniques, and mechanisms exist with respect to Customs activities. • All relevant objectives and associated risks have been identified in relation to the risk assessment and analysis function of internal control. • Management has identified the actions and control activities needed to address the risks and directed their implementation.	
2.	Control activities identified as necessary are in place and being applied. Consider the following:	

	Internal Control Point	Comments/ Descriptions
	• Control activities described in policy and procedures manuals are actually applied and applied properly. • Supervisors and employees understand the purpose of internal control activities. • Supervisory personnel review the functioning of control activities. • Timely action is taken on exceptions, implementation problems, or information that requires follow-up.	
	Common Categories of Control Activities	
1.	Management tracks Customs compliance in relation to goals. • Managers at all activity levels review performance reports, analyze trends, and measure results against targets. • Appropriate control activities are employed such as reconciliations of summary information to supporting detail	
2.	The company effectively manages its workforce to achieve Customs compliance. • Procedures are in place to ensure that personnel with appropriate competencies are recruited and retained. • Employees are provided with orientation, training, and tools to perform their duties and responsibilities, improve their performance, and meet the demands of changing organizational needs. • Qualified and continuous supervision is provided to ensure that internal control objectives are being met.	
3.	The company employs a variety of controls of Customs activities to ensure accuracy and completeness of information processing.	
4.	The company has established and monitors performance measures and indicators for Customs activities. • Actual performance data are continually compared and analyzed against expected or planned goals. • Unexpected results or unusual trends are investigated to identify circumstances where achievement of goals for Customs compliance is threatened. Corrective action is taken.	
5.	Customs transactions and other significant events are properly classified and promptly recorded so that they maintain their relevance, value, and usefulness to management in controlling operations and making decisions.	
6.	Only authorized individuals can make adjustments to Customs information.	
7.	Internal control and all transactions and other significant events related to Customs activities are clearly documented. • Written documentation exists for the company's internal control structure and all significant transactions and events. • Documentation is readily available for examination. • Documentation for internal control includes identification of the company's activity-level functions and related objectives and control activities and appears in management directives, administrative policies, accounting manuals, and other such manuals.	

	Internal Control Point	Comments/ Descriptions
	• Documentation of transactions and other significant events is complete and accurate and facilitates tracing the transaction or event and related information from before it occurs, through its processing, to after it is completed. • Documentation, whether in paper or electronic form, is useful to managers in controlling their operations and to auditors and others involved in analyzing operations. • All documentation and records are properly managed, maintained, and periodically updated.	
8.	This analysis and evaluation should also include controls over computerized information systems.	

Information and Communication

According to the fourth internal control component, for a company to run and control its operations, it must have relevant, reliable information relating to external as well as internal events. That information should be recorded and communicated to management and others within the company who need it in a form and within a time frame that enables them to carry out their internal control and operational responsibilities. Managers and evaluators should consider the appropriateness of information and communication systems to the entity's needs and the degree to which they accomplish the objectives of internal control. Listed below are factors a user might consider. The list is a starting point. It is not all-inclusive, nor will every item apply to every company or activity within the company. Even though some of the functions and points may be subjective in nature and require the use of judgment, they are important in collecting appropriate data and information and in establishing and maintaining good communication.

	Internal Control Point	Comments/ Descriptions
	Information	
1.	Information related to Customs activities from internal and external sources is obtained and provided to management as a part of the company's reporting on operational performance relative to established objectives.	
2.	Pertinent information related to Customs activities is identified, captured, and distributed to the right people in sufficient detail, in the right form, and at the appropriate time to enable them to carry out their duties and responsibilities efficiently and effectively.	
3.	Management ensures that effective internal communications occur related to Customs activities. • Employees understand the aspects of internal control, how their role fits into it, and how their work relates to the work of others. • Employees are informed that when the unexpected occurs, they must give attention not only to the event but also to the underlying cause, so that potential internal control weaknesses can be identified and corrected before they can do further harm. • Mechanisms exist to allow the easy flow of information down,	

	Internal Control Point	Comments/ Descriptions
	across, and up the organization and to allow easy communications to exist between functional activities. • Informal or separate lines of communications exist to serve as a "fail-safe" control for normal communications avenues. • Mechanisms are in place for employees to recommend improvements in operations.	
4.	Management ensures that effective external communications occur with groups that can have a serious impact on Customs compliance. • Open and effective communications have been established with customers, suppliers, consultants, brokers, and others who can provide significant input relative to Customs compliance. • Communication with external parties such as Customs and other federal agencies is encouraged since it can be a source of information on how well internal control is functioning. • Management makes certain that advice, rulings, and recommendations from Customs officers are fully considered and that actions are implemented to correct any problems or weaknesses they identify.	
	Forms and Means of Communication	
1.	The company employs many and various forms and means of communicating important information with employees and others (policies and procedures manuals, memorandums to staff and regular meeting with staff, etc.).	

Monitoring

Monitoring is the fifth and final internal control component. Internal control monitoring should assess the quality of performance over time and ensure that the findings of audits and other reviews are promptly resolved. In considering the extent to which the continued effectiveness of internal control is monitored, both ongoing monitoring activities and separate evaluations of the internal control system, or portions thereof, should be considered. Ongoing monitoring occurs during normal operations and includes regular management and supervisory activities, comparisons, reconciliations, and other actions that people take in performing their duties. Separate evaluations are a way to take a fresh look at internal control by focusing directly on their effectiveness at a specific time. These evaluations may take the form of self-assessments as well as review of control design and direct testing, and may include the use of this Management and Evaluation Tool or some similar device. In addition, monitoring includes policies and procedures for ensuring that any audit and review findings and recommendations are brought to the attention of management and are resolved in a timely manner. Managers and evaluators should consider the appropriateness of the company's internal control monitoring and the degree to which it helps them accomplish their objectives.

	Internal Control Point	Comments/ Descriptions
	Ongoing Monitoring	
1.	Management has a strategy to ensure that ongoing monitoring of	

	Internal Control Point	Comments/ Descriptions
	Customs activities is effective and will trigger separate evaluations where problems are identified or systems are critical and testing is periodically desirable. • Management's strategy provides for routine feedback and monitoring of performance and control objectives. • The monitoring strategy includes identification of critical operational Customs-related systems that need special review and evaluation. • The strategy includes a plan for periodic evaluation of control activities for critical Customs activities.	
2.	In the process of carrying out their regular activities, company personnel obtain information about whether internal control is functioning properly.	
3.	Communications from external parties corroborate internally generated data or indicate problems with internal control. • Communications from Customs officers about compliance or other matters that reflect on the functioning of internal control is used for follow-ups on any problems indicated.	
4.	Meetings with employees are used to provide management with feedback on whether internal controls are effective.	
	Separate Evaluations	
1.	Scope and frequency of separate evaluations of internal control are appropriate for the company. • Risk assessment results and the effectiveness of ongoing monitoring determine the scope and frequency of separate evaluations. • Separate evaluations may be prompted by events such as major strategies, expansions, or downsizing, etc. • Appropriate portions or sections of internal controls are evaluated regularly. • Personnel with required skills, who may include the company's internal auditor or an external auditor, conduct separate evaluations.	
2.	The methodology for evaluating the company's internal control is logical and appropriate. Consider the following: • The methodology used may include self-assessments using checklists, questionnaires, or other such tools, and it may include the use of this Management and Evaluation Tool or some similar device. • The separate evaluations may include a review of the control design and direct testing of the internal control activities. • The evaluation team develops a plan for the evaluation process to ensure a coordinated effort. • If the evaluation process is conducted by company employees, it is managed by an executive with the requisite authority, capability, and experience. • The evaluation team gains a sufficient understanding of the company's objectives related to Customs compliance. • The evaluation team gains an understanding of how the company's internal control system is supposed to work and how it actually works. • The evaluation team analyzes the results of the evaluation against	

	Internal Control Point	Comments/ Descriptions
	established criteria. • The evaluation process is properly documented.	
3.	Deficiencies found during separate evaluations are promptly resolved. • Deficiencies are promptly communicated to the individual responsible for the function and also to at least one level of management above that individual. • Serious deficiencies and internal control problems are promptly reported to top management.	
	Audit Resolution	
1.	The company has a mechanism to ensure the prompt resolution of findings from audits and other reviews. Consider the following: • Managers promptly review and evaluate findings resulting from audits and assessments, including those showing deficiencies and those identifying opportunities for improvements. • Management determines the proper actions to take in response to findings and recommendations. • Corrective action is taken or improvements made within established time frames to resolve the matters brought to management's attention. • In cases where there is disagreement with the findings or recommendations, management demonstrates that those findings or recommendations either are invalid or do not warrant action. • Management considers consultation with auditors when it is believed to be helpful in the audit resolution process.	
2.	Company management is responsive to the findings and recommendations of audits and other reviews aimed at strengthening internal control.	
3.	The company takes appropriate follow-up actions with regard to findings and recommendations of audits and other reviews. • Problems are corrected promptly. • Underlying causes giving rise to the findings or recommendations are investigated by management. • Actions are decided upon to correct the situation or take advantage of the opportunity for improvements. • Management and auditors follow up on audit and review findings, recommendations, and the actions decided upon to ensure that those actions are taken. • Top management is kept informed through periodic reports on the status of audit and review resolutions so that it can ensure the quality and timeliness of individual resolution decisions.	

Source: Adapted from United States General Accounting Office, *Internal Controls Management and Evaluation Tool EXPOSURE DRAFT*, GAO-01-131G, February 2001.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Guidance for the Internal Control Interviewing Process

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The following questions are designed to illustrate the type of questions that can be used to obtain information needed to evaluate the adequacy of internal controls. They are intended to illustrate the type of questions that may be used to evaluate each internal control component and may be used as deemed necessary. They are not intended to be all-inclusive or exhaustive.

Control Environment

- Do individuals receive training, and is it updated periodically through distribution of latest information relevant to their responsibilities, classroom training, etc.?
- Do individuals have specific knowledge and tools needed to perform their duties—relevant rulings on value to the legal department, etc.?
- Is there evidence that the company's Customs department and its operations are supported by upper management and management throughout the organization?
- Can the individual interviewed make recommendations for improvement to the processes related to Customs?
- Can company Customs representatives make recommendations pertaining to Customs operations in other offices, and are they seriously considered and implemented when appropriate?

Risk Assessment

- Are the responsible individuals aware of the specific risks to Customs that they must address in their work—the risk to Customs if the engineering department does not report information on the use of foreign companies for research and development?
- Are individuals periodically asked to make risk assessments of possible negative impact to Customs from their operations and asked to identify any improvements that are needed to processes or internal controls, e.g., training, better manuals, improved communication?
- Are company Customs representatives included in planning processes and operational changes—specifically, when foreign purchases and imports are involved?

Control Activities

- Are individuals aware of their responsibilities to record and report significant events and transactions to Customs—does the department authorizing foreign payments understand that it must report payments related to imports to the Customs department even if the

payments are not specific invoices for the imports?
- Do individuals with responsibility for Customs-related activities document their activities and transactions and retain the documentation?
- Do the individuals understand the importance and significance of internal control procedures—does the purchasing department know why it must report all foreign payments to the Customs department?
- Do responsible individuals maintain analytical information to support decisions regarding reporting to Customs—does legal retain information to support decisions related to reporting of commissions, royalty agreements, etc.?
- Is the documentation readily available, and does it include adequate information to track transactions to ensure accurate reporting to Customs?

Information and Communication

- Are responsible individuals aware of the communication requirements that are necessary to ensure that Customs receives appropriate information—is the representative in the legal department aware of reporting requirements pertaining to any contracts involving international purchasing, provisions for assists to foreign entities, etc.?
- Do the company Customs representatives have open, effective communication channels to other offices in the company?
- Does the Customs department have open and effective external communication with foreign suppliers, agents, brokers, and Customs?
- Are external parties clearly informed of the company's ethical standards, and do they understand that improper and illegal Customs activities will not be tolerated?
- Does management use effective communication methods, which may include policy and procedures manuals, management directives, memoranda, bulletin board notices, Internet and intranet Web pages, etc.?
- Does upper management support clear communication regarding Customs operations?

Monitoring

- Do supervisors review the functioning of control activities—is someone in purchasing assigned to review the purchasing log, purchasing account, or appropriate purchasing records to ensure that appropriate purchasing information is reported to the Customs department?
- Are review and monitoring processes of Customs-related activities and internal controls in operation?
- Are the results or review and monitoring processes used to improve operations and correct errors and deficiencies in controls?
- Does management have a process for ensuring timely and accurate responses to inquiries from Customs?
- Does management have a process for making system or internal control changes when necessary as a result of inquiries from Customs, etc.?
- Does management have a system for ensuring that advice and recommendations of import specialists, account managers, and other Customs officers are fully considered and that actions are implemented to correct any problems or internal control procedures they identify?
- What methods are used by the company to evaluate its internal Customs control processes?

- Does the company's internal audit function monitor Customs activities?

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Risk Opinion under Focused Assessments

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

Prior to the implementation of the Customs-Trade Partnership Against Terrorism (C-TPAT) on April 16, 2002, the results of Compliance Assessments and Focused Assessments were used by Customs to assist in determining the level of cargo examinations of imports. Results of Compliance Assessments and Focused Assessments will no longer determine the level of cargo examinations. Accordingly, the FA team will not issue an opinion that will be used by Customs to place a company in a Compliance Risk Category. The Focused Assessment (FA) will develop a risk opinion, which will state whether imports by the company are an acceptable or unacceptable risk to Customs. If a company has unacceptable risk to Customs, the company can implement a Compliance Improvement Plan (CIP) to improve their risk.

This document provides guidance to Regulatory Audit field offices concerning the development of an opinion on risk. The acceptability of a company's risk to Customs in an FA is based on a review of the company's internal control procedures and, if necessary, substantive testing to determine a compliance rate. The review provides Customs with valuable information about the way the company manages its Customs risk.

This document does not consider or elaborate on specific FA issues such as whether testing is necessary to quantify the loss of revenue. All errors, discrepancies, or loss of revenue detected during an FA may be subject to review and possible referral for action under Customs laws.

Procedures

Risk Opinion

The FA team will develop a risk opinion on each area reviewed during the FA and will state in FA reports whether risk is acceptable or unacceptable for each review area. By stating a risk opinion by review area, the risk is clearly identified as acceptable or unacceptable in the company's various areas of Customs operations and the materiality of risk is clearer.

During the Pre-Assessment Survey (PAS) part of the FA program, the FA team attempts to evaluate the adequacy of internal controls for each review area with limited testing. If the volume of transactions is extremely high or if for some other reason, it is not possible to determine if risk for a review area is acceptable in the PAS, the FA team may have to proceed to Assessment Compliance Testing (ACT) to determine a compliance rate for the review area. If ACT is necessary, Appendix 1 illustrates the use of a compliance rate for review areas to determine if risk is acceptable. If ACT testing reveals that a company meets an acceptable rate of compliance in all review areas, the FA team should conclude that the company's risk is acceptable to Customs.

Opinion Issued during the PAS Process

Adequate Internal Controls and Acceptable Risk

During the PAS, the FA team will evaluate the risk to Customs that a company's importing process may result in significant noncompliance with Customs laws and regulations. If importing procedures and controls are found to be documented and adequate, and no unacceptable risks or deficiencies are identified, then the FA team will express an opinion that the company's imports are an acceptable risk to Customs because it has adequate internal controls over Customs operations.

Inadequate Internal Controls with Compliance Improvement Plan

If unacceptable risks or deficiencies are identified in PAS because importing procedures and controls are not adequate, the company may elect to prepare a Compliance Improvement Plan (CIP) to improve its internal controls and reduce the risk to Customs. If the company elects to use this plan, it has a conditional period of six months from the date of the audit report to implement the CIP. Although the CIP indicates the intent of the company to improve internal controls, unacceptable risks will not be eliminated until the CIP has been implemented and is effective. Accordingly, even if the company agrees to implement a CIP, the FA team will issue a report expressing an opinion that the company's imports are an unacceptable risk to Customs in the area(s) identified with inadequate internal controls. Facts about the company's decision to implement the CIP will be clearly reported and the report will state that a follow-up review will be made to determine if internal controls are improved to an acceptable level.

Inadequate Internal Controls without Compliance Improvement Plan

If inadequate internal controls are identified in PAS and the company does not agree to prepare a CIP to improve its internal controls, the FA team will probably proceed to ACT to determine the extent of compliance. If the company agrees to quantify or if the team can readily quantify the risk, the team will not have to proceed to ACT. The PAS report will explain that the FA team believes that the company's internal controls of the risk area are not adequate but the company has not agreed to implement corrections; so the team must proceed to ACT to calculate a compliance rate to determine the extent of compliance.

Adequacy of Internal Controls not Known

If PAS does not provide adequate information to determine whether the company has adequate internal controls to provide reasonable assurance that they will meet an acceptable level of compliance for a review area, the FA team cannot express an opinion on the acceptability of risk for the review area. The FA team will have to proceed to ACT or take other action to determine the extent of compliance. The PAS report should explain that the FA team could not determine if internal controls are adequate in the PAS process and explain what action will be taken.

Opinion Issued during the ACT Process

During the ACT process, the company's extent of compliance will be determined by testing of areas found to have identified risk. The company's extent of compliance will be part of the basis for a risk opinion for the review area.

Acceptable Level of Compliance

If the company meets an acceptable level of compliance in a review area, the FA team may express an opinion that the company's imports are an acceptable risk to Customs in the review area because the company met an acceptable level of compliance for the area. If the FA team identified significant weaknesses in internal controls that need to be corrected even though the company met an acceptable compliance rate, the team should include a statement after the risk opinion in the Executive Digest that internal controls should be instituted to address the risks as an element of reasonable care.

Unacceptable Level of Compliance with Compliance Improvement Plan

If the company does not meet an acceptable level of compliance in the ACT process, the company may elect to prepare a CIP to improve its internal controls and reduce its risk to Customs. If the company elects to implement a CIP, it has a conditional period of six months from the date of the audit report to implement the CIP. Although the CIP indicates the intent of the company to improve internal controls, unacceptable risks will not be eliminated until the CIP has been implemented and is effective. Accordingly, even if the company agrees to implement a CIP, the FA team will issue an opinion that the company's imports are an unacceptable risk to Customs in the area(s) identified with inadequate internal controls. Facts about the company's decision to implement the CIP will be clearly reported and the report will state that a follow-up review will be made to determine if internal controls improved to an acceptable level.

Unacceptable Level of Compliance without Compliance Improvement Plan

If the company does not meet an acceptable level of compliance in the ACT process and does not elect to prepare a CIP to improve its internal controls and reduce the risk to Customs, the FA team will issue an opinion that the company's imports are an unacceptable risk to Customs in the area(s) identified with an unacceptable rate of compliance. The ACT report will explain that the company has not agreed to implement corrections and the report will be issued to headquarters requesting guidance for trade enforcement action.

Opinion Issued During the Follow-up Process

At the conclusion of a follow-up, the FA team will express an opinion on whether the company's imports should be considered acceptable or unacceptable risk.

If the company has implemented internal controls and taken adequate corrective action, the FA team can issue an opinion that the company's imports should be considered an acceptable risk.

If the company has implemented some internal controls and is obviously making a good faith effort to improve compliance but has not implemented adequate corrective action, Customs may allow another conditional period to implement more corrective action before taking any trade enforcement action. Field Directors should not allow more than one extension (two opportunities) to a company to implement corrective action without obtaining approval from headquarters.

The FA team should issue an opinion that the company's imports are an unacceptable risk in the review areas covered by the CIP if:

- The company does not agree to a follow-up after the conditional period has expired,
- The CIP was not implemented, or
- The follow-up reveals that the company is not working to improve internal controls.

The report should explain that the company has not complied with the terms of the CIP and provide detailed information supporting the statement. The report will be issued to headquarters requesting guidance for trade enforcement action.

Guidelines for ACT for Determining Acceptable Level of Compliance (See Appendix 1)

During ACT, the FA team uses the guidelines below and in Appendix 1 to determine the level of compliance. For each area tested, systemic errors are included in the computation of the compliance rate/amount, but nonsystemic errors are not included in the computation of the compliance rate and/or materiality criteria. See Appendix 2 for an explanation of systemic errors.

Compliance Rate for Classification and Classification-Related Areas

The value of the materially misclassified items (systemic classification errors at the 8th digit level, plus systemic errors at the 9th or 10th digit that affect duty or admissibility) will be considered errors for purposes of compliance calculations. When samples are used, compliance should be based on manual ratios/projections appropriate for the type of sampling performed. If the compliance rate is greater than or equal to 99 percent, the company is considered to have met an acceptable level of compliance.

Compliance Rate/Amount for Transaction Value

The absolute value of all systemic value errors is calculated to determine the overall value discrepancy amount. When samples are used, manual ratios/projections appropriate for the type of sampling performed should be used. Compliance in value is not acceptable if the overall value discrepancy amount is greater than $10,000,000 or greater than 1 percent of entered value, whichever is less.

Compliance Rate for Other Areas

Compliance for most test areas will be evaluated based on value. These test areas include Harmonized Trade Schedule (HTS) chapter 98; quota merchandise in bonded warehouse; Foreign Trade Zone (06 Entries); trade agreements (Generalized System of Preferences (GSP), Caribbean Basin Initiative (CBI), etc.); declared Anti-Dumping Duties (ADD); declared Countervailing Duties (CVD);and computed value. When sampling is used, compliance should be based on manual ratios/projections appropriate for the type of sampling performed. If the compliance rate is greater than or equal to 99 percent, the company is considered to have met an acceptable level of compliance.

Undeclared ADD/CVD and transshipment are areas of high risk to Customs. Because of their sensitivity and the obvious difficulty of establishing a universe for these areas, no compliance rate will be calculated. All systemic errors (undeclared ADD/CVD or transshipment) are material.

Corrective Action during the FA

In some cases, the company may take action to correct noncompliance and internal controls before completion of the focused assessment. The corrective actions may have been taken to correct internal controls and noncompliance identified by the company and disclosed to Customs

or identified by the FA team. In either case, if the company has corrected the underlying cause of the noncompliance, and the FA team has validated the improvements during the FA, the improvements should be considered the same way an implemented and validated CIP would be considered when determining whether internal controls are adequate. The FA should clearly report that the company improved their internal controls and issue an opinion that the company is acceptable risk in the corrected area. The FA should not be unnecessarily delayed to wait for a fully implemented CIP.

ACCEPTABILITY OF COMPLIANCE RATE

Review Area	Compliance Calculation	Compliance	
		Rate	Result
Classification Additional Sampling Issues (Classification Related)	The value of materially misclassified items (systemic errors at the 8th digit level plus systemic errors in the 9th or 10th digit that affect duty or admissibility) cannot exceed 1 percent of the merchandise value tested. The compliance rate percentage is calculated as follows: 100 percent minus the percentage of material dollars misclassified.	Dollars Compliant ≥ 99%	Compliance Acceptable
		Dollars Compliant < 99%	Compliance Unacceptable
Transaction Value (This is an Overall Value Discrepancy Test. This test will include the absolute amount of all value variances occurring during the fiscal year reviewed.)	The absolute value of all value variances resulting from systemic errors cannot exceed 1 percent of the entered value or $10,000,000, whichever is less, for the period under review. The 1 percent or $10,000,000 is a test for all of transaction value, not for a smaller review area such as research and development or assists.	Value Variances ≤ $10,000,000 or ≤ 1%	Compliance Acceptable
		Value Variances > $10,000,000 or > 1%	Compliance Unacceptable
Chapter 98 Quota Merchandise in Bonded Warehouse Foreign Trade Zone (06 Entries) Trade Agreements (GSP, CBI, etc.) Additional Sampling Issues (non-classification-related)	The absolute value of systemic errors cannot exceed 1 percent of the value for the review area. This is for the review area such as GSP, not for a smaller test area such as GSP from one country or one manufacturer.	Dollars Compliant ≥ 99%	Compliance Acceptable
		Dollars Compliant < 99%	Compliance Unacceptable
Computed Value	Total absolute value variance (resulting from systemic errors) between company declared value and audit value cannot exceed 1 percent of total actual computed value.	Dollars Compliant ≥ 99%	Compliance Acceptable
		Dollars Compliant < 99%	Compliance Unacceptable
ADD/CVD (Declared on 03 and 07 entries)	The absolute value of duty variances resulting from systemic errors cannot exceed 1 percent of the total ADD/CVD tested.	Dollars Compliant ≥ 99%	Compliance Acceptable
		Dollars Compliant < 99%	Compliance Unacceptable
Undeclared ADD/CVD Transshipment	No compliance rate. All systemic errors are material.		

Systemic Errors

Q. What are systemic errors?

A. Systemic errors are caused by a breakdown in a system. If the system is corrected, the errors would not reoccur. To consider an error or errors systemic, you have to be able to identify the system failure that caused the problem or identify a control that would correct or alleviate the problem. Generally, if you cannot identify the system that broke down or a reasonable change in the system that would remedy the problem, you do not have a systemic problem.

For example, assume that in situation x you find 3 clerical errors in your sample of 20:

a. One of the errors was caused by Big Broker, who copied an invoice quantity incorrectly. Even though the importer reviewed a substantial sample of the broker's work and compared the amounts on Customs entries to accounting records, the importer did not catch the error.
b. One of the errors was caused by a receiving clerk writing down the wrong quantity.
c. One was due to an error by the accounting department in recording the quantity into inventory records.

Each of these errors had a different cause, and there is no pattern. It would be difficult to imagine a reasonable system correction that would prevent these errors from occurring in the future.

Compare the situation in X with that in situation Y, where you found 8 clerical errors out of 20, all caused by the same broker. The importer had no system for reviewing the broker's work and did not compare Customs entries to quantities in company records. In this case, creation of a system to review the accuracy of Customs entries would be a reasonable recommendation.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Timely Completion and Resolution of Issues of Focused Assessments

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

Customs is committed to ensuring the efficiency and timely completion of focused assessments (FAs). FAs are audits designed to evaluate the risk to Customs that the company's importing process may result in significant noncompliance with laws and regulations. FAs include a review of the effectiveness of a company's internal controls and testing of data using statistical sampling and other analytical methods. Evaluating the company's internal control procedures, selecting samples, and obtaining and reviewing the records requires a significant investment in time for both the FA team and the company. Experience has shown that lack of a clear understanding of expected completion dates and the need to have records provided timely has contributed to unnecessary delays in completing assessments and audits. It is Regulatory Audit's policy that no Focused Assessment will take more than 1 year to complete. Consequently, Regulatory Audit will be closely monitoring the progress of each assessment to ensure that it is completed within a year. This document helps accomplish this goal by establishing procedures to (1) develop mutually agreed-upon timelines to complete the FA, (2) uniformly respond to lengthy delays by the importers and (3) advise importers of Regulatory Audit lines of authority to help resolve issues before they delay the FA.

Procedures

Mutually Agreed-upon Timelines

At the advance conference—the first formal meeting Customs holds with the importer before beginning an FA—the FA team will outline the requirement for a plan to complete the FA within 1 year. The plan will include a timetable and will be tailored to the circumstances of the company.

As soon as practical, the FA team and company representatives will jointly develop and agree to a timetable for completing the FA. The plan should specify, at a minimum, the following dates and time periods:

- Dates for the importer to return requested documents, such as the company's documented internal control policies and procedures, documentation, and examples.
- Period of time after receipt of requested documents for the FA team to gain an understanding of the company's organizational structure, procedures, and internal controls, including interviews of company personnel and review of applicable documents to determine how and where the company records Customs transactions in its books and records.

- Period of time for the FA team to complete preliminary review of internal controls, including selection of limited samples to perform internal controls testing and identification of documents needed for review.
- Agreed-upon time for the company to provide requested documents for the test samples to the FA team.
- Projected date for completion of the Pre-Assessment Survey (PAS) phase of the FA, including identification of internal control weaknesses, problems, or potential problems and development of mutually acceptable corrective action.
- Projected PAS audit report date.
- Period of time after the completion of the PAS phase for the FA team to select samples and identify documents needed for review during the Assessment Compliance Testing (ACT) phase of the FA.
- Agreed-upon time for the company to provide requested ACT documents to the FA team.
- Projected date for completion of the ACT phase of the FA, including identification of problems, causes, and resolution of issues and development of mutually acceptable corrective action.
- Projected ACT audit report date (no longer than 90 days after the exit conference).

If either the FA team or the company is unable to meet the schedule, they should work together to establish a revised timeline. Customs management will monitor progress of the audit and take appropriate action to ensure that the FA team is meeting its commitments.

If the Customs team is not meeting the FA schedule, the team leader will report the delay, the reason, and proposed actions to bring the FA back on schedule to the Assistant Field Director. The Assistant Field Director will review the reasons for delays and proposed corrective action and take additional action or escalate the issue to higher levels of management as appropriate.

Response to Lengthy Delays by Importers

RAD will closely monitor the company's level of cooperation toward the completion of the FA within the stipulated 1-year time frame. The Regulatory Audit FA team will continually update the company on the progress of the FA. Should there be a delay or interruption of progress that is the responsibility of the importer or the importer's third party representative, Customs will notify the importer in writing immediately.

If delays result because the company does not provide records or information, Customs will notify company management in writing of the delay and request that the records be provided as agreed. If records cannot or will not be provided in a reasonable time, Customs will stop the review of the imports for the area under review related to the missing records. The FA team will assess the impact of the missing records relative to the overall review of the area in accordance with existing procedures. If it is concluded that the company does not have an adequate system in place to support the import activity for the area under review, the area will be considered noncompliant.

Lengthy delays resulting from any other constraints placed on the progress of the Focused Assessment by the importer or third party representative may be grounds for terminating any further review activity and closing the Focused Assessment. Should that situation occur, Regulatory Audit would issue a PAS or ACT report based on the information provided and issue an opinion on a risk level for the company predicated upon the information in hand.

Regulatory Audit Lines of Authority for Resolution of Issues

The FA team must advise the importer of the appropriate lines of authority and resolution levels for issues that may occur during the FA. The importer will be advised that the lines of authority

are being provided to facilitate communications with Regulatory Audit and to assist in meeting timelines for the Focused Assessment. The company should follow the lines of authority and should advise its third party representatives to follow the lines of authority. The following points of contact and resolution levels will be provided to the importer at the first meeting between the FA team and the company.

Focused Assessment Team Leader
Name
Telephone Number

Resolution Level 1

Assistant Field Director
Name
Telephone Number

Resolution Level 2

Field Director
Name
Telephone Number

Resolution Level 3

Appropriate Headquarters Director (Focused Assessments Branch or Trade Agreements Branch)
Name
Telephone Number

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Resolving "Gray Areas" of Harmonized Tariff Schedule (HTS) Classification

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

During the course of testing a company's import transactions in a Focused Assessment (FA), technical issues regarding the correctness of certain "gray areas" of Harmonized Tariff Schedule (HTS) classification sometimes arise. Customs has developed a resolution process where the FA import specialist (FA IS) may make a determination that the tariff classification of a particular product is a "gray area" and is not to be counted as an error in Customs risk opinion for a company. The resolution process also provides for the auditee to request a review of a particular classification determined by the FA IS to the appropriate national import specialist (NIS).

Correct classification of imports has always been difficult. The increase in tariff rate lines, the explosion of imports, and the variety of new products being imported complicates the classification of merchandise. Customs must identify the risk associated with importer errors when evaluating importer noncompliance. Customs, as well as the importer, is negatively affected when costs to achieve compliance are out of proportion to the risks associated with noncompliance.

As part of an FA, the FA team, including the import specialist, reviews the company's internal controls relating to the classification of imported merchandise, which may include a review of a sample of classifications imported by the auditee. In some cases the classification used by the importer is a plausible alternative to the Customs classification determined to be correct by the FA IS.

Procedures for Resolution of "Gray Area" Classifications

The following procedures cover "gray area" classifications and collection of unpaid duties in such cases, and provide for a referral for review to the NIS concerning the correct HTS classification.

When reviewing classifications that fall into a "gray area," the FA IS should consider whether:

- Customs considers the classifications ambiguous and subject to varying interpretations, including the interpretation by the auditee.
- The auditee has a trained and knowledgeable staff that used a documented, reliable, and systematic approach to arrive at the entered HTS classification. Attributes of a reliable system are suggested by the questions in the "Reasonable Care Checklist" contained in Customs Informed Compliance Publication on Reasonable Care.

If the FA IS applies the criteria discussed above and concludes that the interpretation by the company is a "gray area," the importer's internal controls will be considered sufficient to provide

reasonable assurance that the appropriate classification is used, and the classification will not be counted as an error for the risk opinion. The correct classification, however, should be conveyed to the company to ensure that the appropriate classification is used in the future.

Referral Procedures for Resolving Classification Differences

If the auditee disagrees with the FA IS on the correctness of a classification, the auditee or the FA team may refer the issue to the NIS for a final determination on the correct classification. The auditee must request the FA IS to refer the issue to the NIS within 30 days of being advised by the FA IS of the classification difference(s). To request a decision from the NIS for either the auditee or FA team, the FA IS, in cooperation with the FA team leader, will submit documentation of Customs review along with company information. The NIS will review all the information provided and, usually in 30 days, provide a decision on the correct classification.

Revenue Owed as a Result of “Gray Area” Determinations

If the FA IS or NIS determines that an entered classification is a “gray area” and use of the correct classification would have resulted in additional revenue owed to Customs, the revenue should be collected only if the relevant entries are unliquidated.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Errors Disclosed to Customs

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The Regulatory Audit Division has updated its policy for determining the treatment of errors disclosed to Customs before or after commencement of an assessment or audit. These changes resulted from the implementation of the Focused Assessment (FA) and an ongoing effort to address trade concerns. While companies want to be given recognition when they find errors and disclose them, Customs must provide equitable and consistent treatment of those errors during the FA. Also, special procedures are included to address post-entry adjustments resulting from official Customs programs designed for that purpose.

Procedures

Systemic errors are caused by a breakdown in a system. If the system was corrected, the errors would not recur. To consider an error systemic, the FA team has to be able to identify the system failure that caused the problem. Generally, if the system weakness that caused the error cannot be identified, or if a reasonable change in the system would not prevent the problem, then there is no systemic problem. Nonsystemic errors will not be considered in the evaluation of adequacy of internal controls or in the calculation of extent of compliance.

Systemic errors that appear in Customs samples will not be included as errors in determinations of adequacy of internal controls or compliance if the company has submitted a correction for the error to Customs and:

1. The submission was the result of a Customs post-entry program, such as a supplemental information letter (SIL), Post-Entry Adjustment (PEA), Customs reconciliation, or a specific agreement with Customs for recurring, periodic post-entry adjustments;
2. The company has an internal control system in place to review its Customs transactions, inform Customs of any errors through the Customs post-entry process, and correct the cause of the systemic problem, when possible; and
3. The company can demonstrate this practice was being followed prior to the commencement of the FA (i.e., company has not disclosed errors just because it is being audited).

If the submission was not the result of a Customs program designed for post-entry adjustments, such as SIL, PEA, Customs reconciliation, or a specific agreement with Customs for recurring, periodic post-entry adjustments, the systemic errors will be considered in determinations of adequacy of internal controls or in the calculation of extent of compliance.

However, if the importer implements system improvements to prevent recurrence of those errors and these system improvements have been tested by the FA team and found to have

corrected the deficiency, then this will be considered when issuing an opinion on the importer's risk.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Treatment of Ultimate Consignee Transactions in a Focused Assessment

Introduction

A Focused Assessment (FA) provides U.S. Customs and Border Protection (CBP) with the ability to review and verify information disclosed to CBP for accuracy and completeness. During an audit, the auditor may review records where the auditee is the Importer of Record (IOR) and/or the Ultimate Consignee (UC). Many issues can arise during an audit involving the auditee's responsibilities for reporting entry information to CBP and for record keeping. This document addresses IOR and UC responsibilities and audit procedures.

Background

The entry statute (19 U.S.C. 1484 (a)) establishes responsibilities of the IOR as follows:

(a) Requirement and time
- (1) Except as provided in sections 1490, 1498, 1552, and 1553 of this title, one of the parties qualifying as "importer of record" under paragraph (2) (B), either in person or by an agent authorized by the party in writing, shall, using reasonable care -
  - (A) make entry therefor by filing with the Customs Service -
    - (i) such documentation or, pursuant to an electronic data interchange system, such information as is necessary to enable the Customs Service to determine whether the merchandise may be released from customs custody, and
    - (ii) notification whether an import activity summary statement will be filed; and
  - (B) complete the entry by filing with the Customs Service the declared value, classification and rate of duty applicable to the merchandise, and such other documentation or, pursuant to an electronic data interchange system, such other information as is necessary to enable the Customs Service to -
    - (i) properly assess duties on the merchandise,
    - (ii) collect accurate statistics with respect to the merchandise, and
    - (iii) determine whether any other applicable requirement of law (other than a requirement relating to release from customs custody) is met.

The statute (19 U.S.C. 1484(a)(2)(B)) defines the term “importer of record” as the owner or purchaser of the merchandise or a licensed customs broker appropriately designated by the owner, purchaser or consignee of the merchandise. Statutory obligations make the IOR “accountable” for the declarations made at entry. However, while the entry statute clearly identifies the “accountable “party, liability for penalties may attach to any culpable party under civil penalty statute, 19 U.S.C. 1592 (a).

In some instances, in order to meet the burden of using reasonable care when making declarations at entry, the IOR or his agent must necessarily seek information from another source. Sometimes that is the UC. For example, the IOR may not be the owner or purchaser of the merchandise, but rather, a customs broker retained by a UC. In such a case, it is unlikely that the IOR will have sufficient information to meet its reasonable care obligation without obtaining information about the transaction from another party. The IOR is always “accountable.” If the UC provides the IOR with information that is material and false and that information is used to make entry, the UC may be culpable under 19 U.S.C. 1592.

In addition to responsibilities as IOR, auditees may be subject to recordkeeping requirements in 19 U.S.C. 1508, which state:

(a) Requirements
Any -
(1) owner, importer, consignee, importer of record, entry filer, or other party who -
(A) imports merchandise into the customs territory of the United States, files a drawback claim, or transports or stores merchandise carried or held under bond, or
(B) knowingly causes the importation or transportation or storage of merchandise carried or held under bond into or from the customs territory of the United States;
(2) agent of any party described in paragraph (1); or
(3) person whose activities require the filing of a declaration or entry, or both; shall make, keep, and render for examination and inspection records (which for purposes of this section include, but are not limited to, statements, declarations, documents and electronically generated or machine readable data) which -
(A) pertain to any such activity, or to the information contained in the records required by this chapter in connection with any such activity; and
(B) are normally kept in the ordinary course of business.

Procedures

During an audit, the FA team will primarily address issues related to responsibilities of the auditee as IOR. Issues related to auditee’s responsibilities as the UC will be

addressed as needed on a case-by-case basis. The IOR will be held "accountable" for the declarations made at entry. Both the IOR and UC will be held responsible for maintaining records required by 19 U.S.C. 1508. If the UC provides the IOR with information that is material and false, that information is used to make entry, and the resulting errors have significant impact, the auditors will refer the information to appropriate action officials for possible action under provisions of 19 U.S.C. 1592.

The following three scenarios provide guidance to the auditors when the auditee is the UC but NOT the IOR.

Consolidated Entries with Multiple Ultimate Consignees

In the past, shippers and importers used consolidated release and entry summary for shipments that had multiple UCs arriving at the border in a single conveyance. But CBP's automated system has limitations that allow for the submission of only a single UC. Because only one UC can be designated for the consolidated shipment, a company may be listed as the UC on the consolidated entry summary in CBP's automated system but may not be responsible for all portions of the consolidated entry summary.

An audit sample may include a consolidated entry that identifies the auditee as the UC when other UCs are responsible for part of the consolidated shipment. When this occurs and the auditee is not the IOR, the auditee must arrange with the entry filer to provide information to CBP to prove that the auditee is not the UC responsible for all portions of the consolidated entry. The auditee is only responsible for those portions of the consolidated entry for which he is the UC. Under provisions of 19 U.S.C. 1508, the auditee must maintain records related to those portions of the entry for which he was the UC.

Unsolicited Merchandise on Entries Listing a Company as UC

Sometimes companies are listed as the UC on an entry when the company does not initiate or have any information about the specific import transaction. For example, a related company may send unsolicited prototypes or samples. This may also occur if unrelated entities send unsolicited merchandise (such as returned merchandise) to a company listed as UC on the entry. During an audit, the sample may include unsolicited entries where the auditee is listed as the UC but is not the IOR. If the auditee did not initiate the import transaction, has no records related to the importation, and can adequately explain the circumstances and its lack of records to support this transaction, the auditee will not be held responsible for records required by 19 U.S.C. 1508 or for accuracy or completeness of entry information.

Entries Initiated by the UC but Another Entity is IOR

In some cases, a company initiates an import or is in some way responsible for information related to the import, is listed as UC, but is not the IOR. For example, this may occur when the overseas supplier (or other entity) is IOR and handles the details of

the importation. If these entries are included in an audit sample, the UC is responsible for maintaining and making available records required by 19 U.S.C. 1508.

The IOR is always accountable for entry information. However, if the UC provides the IOR with information, which is material and false, and that information is used to make entry, the UC may be culpable under 19 U.S.C. 1592**.**

Aside from the record keeping obligations and the situation where the UC may be liable under 19 U.S.C. 1592 for false statements or omissions, the auditee will be responsible for entry information or internal control of entry information provided to CBP only when designated as the IOR.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Focused Assessment Program
Example of Internal Control Manual

October 2003

PTC

CUSTOMS POLICIES AND PROCEDURES MANUAL

PHANTOM TRADING COMPANY
DALLAS, TEXAS

October 2003

Foreword

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The Regulatory Audit Division of the U.S. Customs and Border Protection has prepared this publication for the trade community to encourage importers to develop their own compliance programs. Although the information contained in this manual is provided to promote voluntary compliance with Customs laws and regulations, it has no legal, binding or precedent. It can not be overemphasized that this manual has been drafted for the sole purpose of encouraging importers to develop their own unique compliance plans designed for their specific circumstances. In addition, this manual has not been designed to be all-inclusive, exhaustive or encyclopedic.

The facts and circumstances surrounding imports by every company differ—from the organizational structure and size of the importer, to the nature of the imported articles, to the circumstances of the sales, etc. Consequently, foolproof, standard guidance and procedures can not be developed to effectively deal with every importing company and circumstance. On the other hand, in keeping with the Modernization Act's theme of "informed compliance," Customs would like to take this opportunity to recommend that the importing community examine this publication for ideas. In Customs view, the example framework may prompt or suggest ideas or methodology which importers may find useful in their own companies. Actual manuals may vary significantly based on the needs of the companies and may be much smaller or larger depending on the size of the company, the number of Customs programs the company is involved with and other factors.

Table of Contents

CHAPTER 1 INTRODUCTION....1

1.0 BACKGROUND 1
1.1 COMPANY INFORMATION 1
1.2 COMPANY ORGANIZATION 1
1.3 COMPANY CUSTOMS POLICY....2
1.4 PURPOSE OF MANUAL....2
1.5 PERIODIC REVIEW AND UPDATE OF PROCEDURES 3

CHAPTER 2 IMPORT PROCESS....4

2.0 POLICY....4
2.1 IMPORTING PROCESS....4
Vendor Template*....7*

CHAPTER 3 RECORDKEEPING....8

3.0 POLICY....8
3.1 BACKGROUND 8
3.2 RESPONSIBLE PARTY(S) 8
3.3 PROCEDURES AND CONTROLS FOR RECORDKEEPING 9
3.4 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 9
Recordkeeping Checklist*....10*

CHAPTER 4 CLASSIFICATION 11

4.0 POLICY....11
4.1 BACKGROUND 11
4.2 RESPONSIBLE PARTY(S) 11
4.3 PROCEDURES AND CONTROLS FOR CLASSIFICATION OF CURRENT PRODUCTS 11
4.4 PROCEDURES AND CONTROLS FOR CLASSIFICATION OF NEW PRODUCTS 12
4.5 PROCEDURES FOR VERIFYING CLASSIFICATION 13
4.6 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 13
Classification Compliance Checklist*....15*

CHAPTER 5 QUANTITY....16

5.0 POLICY....16
5.1 BACKGROUND 16
5.2 RESPONSIBLE PARTY(S) 16
5.3 PROCEDURES AND CONTROLS FOR QUANTITY 16
5.4 PROCEDURES FOR VERIFYING QUANTITY....17
5.5 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 17

CHAPTER 6 TRANSACTION VALUE 18

6.0 POLICY....18
6.1 BACKGROUND 18
6.2 RESPONSIBLE PARTY(S) 19
6.3 PROCEDURES AND CONTROLS FOR VALUATION OF MERCHANDISE....19
6.3.1 Valuation of Assists *....19*
6.4 PROCEDURES FOR VERIFYING VALUE 20
6.5 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 20
Assist Information *....22*

CHAPTER 7 BASIS OF APPRAISEMENT 23

7.0 POLICY....23
7.1 BACKGROUND 23

7.2 RESPONSIBLE PARTY(S) 23
7.3 PROCEDURES AND CONTROLS FOR BASIS OF APPRAISEMENT 23
7.4 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 24

CHAPTER 8 AMERICAN GOODS RETURNED (9801) 25

8.0 POLICY 25
8.1 BACKGROUND 25
8.2 RESPONSIBLE PARTY(S) 25
8.3 PROCEDURES AND CONTROLS FOR CHAPTER 9801 25
8.4 PROCEDURES FOR VERIFYING 9801 26
8.5 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 27
Manufacturer's Affidavit *28*
Shipper's Declaration *29*
Importer's Declaration *30*

CHAPTER 9 ANTIDUMPING/COUNTERVAILING DUTIES 31

9.0 POLICY 31
9.1 BACKGROUND 31
9.2 RESPONSIBLE PARTY(S) 31
9.3 PROCEDURES AND CONTROLS FOR ADD 31
9.4 PROCEDURES AND CONTROLS FOR ADD DETERMINATION OF NEW PRODUCTS 32
9.5 PROCEDURES FOR VERIFYING ADD 32
9.6 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 33

CHAPTER 10 GENERALIZED SYSTEM OF PREFERENCE 34

10.0 POLICY 34
10.1 BACKGROUND 34
10.1.1 Recordkeeping Requirements *34*
10.2 RESPONSIBLE PARTY(S) 35
10.3 PROCEDURES AND CONTROLS FOR GSP 35
10.4 PROCEDURES FOR VERIFYING CLAIMED GSP 36
10.5 PROCEDURES FOR VERIFYING GSP FOR EXPIRATION AND RENEWAL 36
10.6 COMMON ERRORS 37
10.7 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 37
GSP Eligible Countries or Associations of Countries *38*
GSP Eligibility Requirements *40*

CHAPTER 11 POST ENTRY 42

11.0 POLICY 42
11.1 AMENDMENT OF ENTRY 42
11.2 CF-28 REQUEST FOR INFORMATION 42
11.3 CF-29 NOTICE OF ACTION 43
11.4 PROTEST 43
11.5 RULING REQUEST 44
11.6 PRIOR DISCLOSURE 44
Prior Disclosure Checklist *46*

CHAPTER 12 STAFF TRAINING 47

12.0 POLICY 47
12.1 DIVISION SUPERVISORS TRAINING 47
12.2 NEW EMPLOYEE TRAINING 47
12.3 CURRENT EMPLOYEE TRAINING 48
12.4 IMPORT DEPARTMENT EMPLOYEE TRAINING 48
12.5 DOCUMENTATION 48
12.6 PERIODIC REVIEW TO ENSURE POLICY/OBJECTIVES ARE BEING MET 48

REFERENCE MATERIALS.....49

GLOSSARY.....50

Chapter 1
Introduction

1.0 Background

The Modernization Act of 1993 (Mod Act) fundamentally altered the relationship between importers and Customs. The Mod Act shifted the legal responsibility to the importer for declaring the value, classification, and other information necessary to assess the correct duty rate applicable to entered merchandise. The Mod Act also required importers to use reasonable care to assure Customs is provided accurate and timely data. Finally, the Mod Act increased the maximum civil and criminal penalties for negligent or fraudulent failure to comply with Customs requirements.

This Manual describes the import processes of Phantom Trading Company (PTC) designed to ensure Customs compliance and that personnel in each department understands their role in the overall Customs function.

1.1 Company Information

PTC was incorporated in March 2001 as a wholesaler of phantom widgets and began its business of selling and distributing to original equipment manufacturers in the U.S. PTC is a single business entity having no parent or subsidiary relationships. PTC established its Headquarters in Dallas, TX, with a sales office in Houston, TX and a 10,000-sf. warehouse in Addison, TX. The warehouse is staffed by 25 individuals responsible for inventory, receiving and shipping functions. PTC employs over 200 people in its various Texas locations. PTC's major foreign supplier is Masked Widgets of Brasilia, Brazil. PTC maintains a credit line with Masked Widgets and makes payments by wire transfer.

1.2 Company Organization

To ensure compliance with Customs laws and regulations, PTC has established an Import Department staffed with three employees. One of the three employees holds a broker license. All employees in the Import Department work closely with the Customs broker to ensure compliance and efficient handling of import transactions. The Import/Customs Compliance Manager is the focal point for all information relative to Customs activities.

Complying with Customs laws and regulations requires cooperation between many company departments. Communication and cooperation between the Import, Warehouse, Purchasing, and Engineering Departments are essential to Customs compliance. The following chart depicts the overall company structure with departments and titles.

1.3 Company Customs Policy

It is the express policy of PTC to comply with all applicable laws and regulations of the Customs Service and any other federal agency relating to or governing the importation and exportation of merchandise to/from the United States. Further, PTC seeks to monitor, on a regular basis, compliance with all applicable rules and regulations.

PTC strives to cooperate fully with Customs and promptly report and seek full compliance with applicable rules and regulations. In pursuit of this goal, PTC provides all responsible employees with a copy of this policies and procedures manual and with proper training to promote compliance with these requirements. Finally, PTC seeks technical guidance when needed from third party Customs consultants, authorized Customs brokers, and Customs.

1.4 Purpose of Manual

This manual has been designed to aid employees in ensuring Customs compliance and is not intended to be a substitute for Customs laws and regulations. This manual outlines Customs processes to be used in conjunction with applicable laws and regulations. The policies and procedures outlined in this manual are supported by all levels of management and are expected to be followed by all employees. Noncompliance with Customs laws and regulations may expose PTC to fines, penalties, and liquidated damages.

The following topics are included in this manual: import/entry process, recordkeeping, classification, quantity, transaction value, basis of appraisement, American goods returned, U.S. articles assembled abroad, antidumping/countervailing duties, generalized system of preferences (GSP), post entry processes, staff training, and reference materials.

Following are the primary departments involved in the importation/exportation of merchandise:

- Management
- Import Department
- Accounting
- Warehouse (Shipping/Receiving)
- Purchasing
- Engineering Services

If you have any suggestions for improving the contents of this manual or find any inaccuracies, contact the Import/Customs Compliance Manager at 123-1234. Any questions regarding procedures described in this manual should also be addressed to the Import/Customs Compliance Manager at the aforementioned number or by email at import.manager@ptc.com.

1.5 Periodic Review and Update of Procedures

It is the responsibility of the Import/Customs Compliance Manager to review this manual and update it, as necessary, on an annual basis to ensure that Customs regulation cites are current and to incorporate any procedural changes. This annual review and update (the paperback volume of the CFR is revised each year as of April 1) will take place during the second quarter of the fiscal year. If no updates are considered necessary, the Import/Customs Compliance Manager will write a memo indicating the date of the review and attach it to the back of the Manual. Interim updates or additions to the procedures will be made on an as needed basis. The Import Manager will forward a copy of the revised manual or no change memo to each Department Manager involved in the importation/exportation of merchandise as well as the Personnel Department.

Chapter 2
Import Process

2.0 Policy

PTC has established procedures to ensure that it fully complies with all applicable import requirements and laws. The procedures stated herein ensure compliance and efficient handling of import transactions.

2.1 Importing Process

The following entry procedures (entry type 01) will be followed by those departments involved in the importation of goods into the U.S. (Per Section 1.4)

1. For new vendors, the Purchasing Department will negotiate prices with suppliers/vendors and formalize them by means of a sales contract. PTC buyers will use a Vendor Template (See Exhibit 2.A) when negotiating with new suppliers. This tool is to be used by PTC personnel during the initial contract negotiations to ensure all import compliance objectives are understood by the supplier/vendor. Once the contract has been negotiated, a copy will be maintained in Purchasing Department files, by alphabetical order. For existing vendors, the Purchasing Department will formalize prices by means of a Purchase Order (P.O.).

2. Once the sales contract is signed, PTC's buyer will issue the P.O., which includes the model/part number, HTSUS classification, Antidumping Duty (ADD) order, unit price, and quantity ordered. The buyer, if applicable, obtains the HTSUS classification and ADD order, from the Product Classification Database. The buyer has read only access to the Product Classification Database. The Import Department makes any changes or updates to the Product Classification database (For additional information, see Section 4.4).

3. The buyer will instruct the foreign supplier via the P.O. to place the product HTSUS classification on the commercial invoice. If tooling or payments for tooling were provided by PTC, the buyer will also instruct the vendor to include a statement on the commercial invoice that tooling was provided for the invoiced products (For additional information see Section 6.3.1).

4. The buyer will input the P.O. into the purchasing module and forward a copy to the Import Department. The Import staff will review the P.O. to ensure it contains the HTSUS and will place it in a suspense Import File Folder pending importation of the merchandise.

5. The foreign supplier will send the shipping advice via fax or email to the buyer prior to the arrival of the merchandise at the port of entry.

6. The buyer will send a copy of the shipping advice to the Warehouse to be used for verification when the goods arrive.

7. The foreign supplier will send a copy of the import package (packing list, commercial invoice, bill of lading, and any certificates required for specific imports) to the Import Department. The Import staff will verify the price and quantity on the import package against the P.O. and place the documents in a suspense Import File Folder until the entry documentation (CF-7501, CF-3461, etc.) is received from the Customs broker. If any discrepancies are identified, the Import Department will notify the appropriate buyer. The buyer will be responsible for resolving any discrepancies with the foreign supplier and for maintaining a record of any correspondence on the matter. The supplier will provide revised documents where necessary.

8. The Import Department will send a copy of the commercial invoice found in the import package to the Accounting Department.

9. The Import Department will forward the import package to the authorized Customs broker with any special instructions where necessary.

10. The authorized Customs broker will enter imported merchandise. The Import/Customs Compliance Manager maintains a list of Customs brokers with power of attorney to process Customs entries on PTC's behalf. The Customs broker will file the CF-7501 Entry Summary utilizing the HTSUS classification and value stated on the commercial invoice. The broker will also ensure that the entry package contains shipping documents, release documents and any other documents required for specific imports.

11. The Customs broker will send an arrival notice via carrier to PTC's Warehouse.

12. The Warehouse will make freight arrangements and the merchandise will be transported to PTC's Warehouse facilities in Addison, Texas.

13. The Warehouse will receive the imported merchandise and verify the shipment against the original shipping advice. The goods will be inspected for quality, entered into the receiving module and stored in the Warehouse, unless goods are damaged. Damaged goods will be returned to the supplier/vendor and will not be entered into the receiving module (For additional information, see Section 5.3).

14. The Warehouse will print a copy of the receiving report, attach it to the original shipping advice and keep it on file for a period of five years from the date of receipt of the merchandise. The Warehouse will also forward copies of the receiving report to the Accounting and Import Departments. Receipt of the merchandise into the receiving module will trigger Accounting to issue

payment to the supplier.

15. Accounting Department staff will compare the commercial invoice to the receiving report. If any discrepancies are identified, the Accounting Department will notify PTC's authorized buyer and Import Department of the discrepancy. The buyer will research the discrepancy and notify the Accounting and Import Departments of the resolution. The Import Department, if necessary, will instruct the broker to make proper declaration to Customs. The broker will report the discrepancy to Customs. The Import Department will maintain copies of all correspondence with the broker.

16. The authorized broker will submit the entry package (CF-7501, etc.) to the Import Department with a copy of the broker invoice. Import Department staff will verify the entry package, input the entry information into the Import Database (including commercial invoice number), file the entry documentation in the Import File Folder, and send a copy of the broker's invoice to the Accounting Department.

Vendor Template
Minimum Requirements for International Shipments

1. The **Packing Slip** shall contain, at a minimum, the following:

   - ❑ PTC purchase order number
   - ❑ Part number
   - ❑ Description
   - ❑ Quantity per line item
   - ❑ What box number each line item is in
   - ❑ Total number of boxes in shipment
   - ❑ Dimensions of shipment
   - ❑ Final delivery address
   - ❑ The packing slip shall be put inside the crate and the crate marked on the outside saying packing slip enclosed

2. The **Commercial Invoice** shall contain, at a minimum, the following:

   - ❑ PTC purchase order number
   - ❑ Part number
   - ❑ Description
   - ❑ Quantity per line item
   - ❑ Unit price and extended price on each line
   - ❑ Total value of shipment
   - ❑ Country of origin
   - ❑ HTSUS (to the 8th or 10th digit)
   - ❑ Terms of Sale

3. Is shipment from a GSP eligible country?

   - ❑ Yes
   - ❑ No

4. Is shipment GSP Eligible?

   - ❑ Will merchandise be shipped directly from the supplier in the GSP eligible country to the United States?
   - ❑ Is merchandise manufactured completely of materials from such GSP eligible country?
   - ❑ If third country components are used, is at least 35% value added in the GSP eligible country?

The items listed in 1 and 2 above must be obtained or release of shipments could be delayed by Customs and possibly rejected.

Chapter 3
Recordkeeping

3.0 Policy

PTC will maintain records and information in accordance with Customs recordkeeping requirements. Customs related records and information will be maintained for a period of five years. Failure to maintain or produce entry records may result in the imposition of penalties of up to $100,000 or 75 percent of merchandise value per release.

3.1 Background

Under the Modernization Act of 1993, importers are required to maintain and make available information and records pertaining to Customs related activities. Importers must keep records required by law or regulation for the entry of merchandise, referred to as the "(a)(1)(A) list", and other relevant information thereto. Moreover, 19 CFR §163.4 provides that records shall be kept for five years from the date of entry if the record relates to an entry or five years from the date of the activity that required creation of the record. However, packing lists are only required to be maintained for a period of 60 calendar days from release or conditional release of merchandise, whichever is later.

3.2 Responsible Party(s)

The Import/Customs Compliance Manager, Accounting Department Manager, and Warehouse Manager are primarily responsible for ensuring the maintenance of records and information in accordance with Company policy.

The Import/Customs Compliance Manager is primarily responsible for records supporting import entries filed with Customs, including:

- Entry Summaries (CF-7501)
- Airway bills/bills of lading
- Power of Attorney
- Commercial invoices
- Customs bond
- Product information to support declarations to Customs
- Correspondence pertaining to import issues
- Any other records considered necessary to verify declarations made on Customs Entries.

The Accounting Department Manager is responsible for records supporting Customs Valuation including:

- Invoices
- Payment documents (e.g., accounts payable ledger, canceled checks, wire transfer requests, bank statements)

The Warehouse Manager is responsible for maintaining records to support quantities of goods received, including:

- Receiving reports
- Discrepancy reports
- Shipping Advice

3.3 Procedures and Controls for Recordkeeping

The Import staff will complete a recordkeeping checklist (See Exhibit 3.A) for each entry prepared by the Customs broker to ensure all relevant records were included with the entry package and are on file. If any of the required documents are missing, the Import Staff will contact the appropriate PTC department or the Customs broker and request the missing document(s). The Import Department staff member assigned to review the entry package will initial and date the recordkeeping checklist and file it with the entry package (in the Import File Folder).

3.4 Periodic Review to Ensure Policy/Objectives Are Being Met

On a semi-annual basis the Director Import Department will select 26 entry packages (one from each week in the six-month period) and review them to ensure that the Import staff completed the Customs Entry Checklist in accordance with the above procedures. If systemic problems are identified, the review will be expanded to determine the extent of the problem. The Director Import Department will prepare a memo detailing the review. The memo should at a minimum contain a list of the entries reviewed and the results of the review (positive or negative). A copy of the memo will be sent to the Vice President Administration (See Organizational Chart is Section 1.2). The Director Import Department in conjunction with the Import/Customs Compliance Manager will take appropriate action to correct any problems identified during the review.

On an annual basis the Director Import Department will verify that records are retained in accordance with Customs requirements by randomly selecting 15 archived entry packages for review. The entry packages will be randomly selected from the 5-year retention period. The Director Import Department will ensure that the Customs Entry Checklist as well as all required documents is included in the entry package. The Director Import Department will prepare a memo detailing the review. The memo should at a minimum contain a list of the entries reviewed and the results of the review (positive or negative). The Director Import Department in conjunction with the Import/Customs Compliance Manager will take appropriate action to correct any problems identified during the review.

Recordkeeping Checklist

The Import Department will ensure that the following documents are included with each entry package. Originals should be on file whenever possible. If any of these documents are missing, contact the appropriate PTC department or the Customs broker and request that the document be forwarded to the Import Department.

Document/Information	Yes	No	N/A
Entry Summary (CF-7501)	_____	_____	_____
Entry/Immediate Delivery (CF-3461)	_____	_____	_____
Commercial Invoice	_____	_____	_____
Part/Item Number	_____	_____	_____
Merchandise Description	_____	_____	_____
Quantity	_____	_____	_____
Unit Value	_____	_____	_____
Total Value	_____	_____	_____
Country of Origin	_____	_____	_____
Currency in which transaction made	_____	_____	_____
HTSUS	_____	_____	_____
Terms of Sale	_____	_____	_____
Packing List	_____	_____	_____
	_____	_____	_____
Airway Bill or Bill of Lading	_____	_____	_____
Receiving Report	_____	_____	_____
Importer's Declaration	_____	_____	_____
Shipper's Declaration	_____	_____	_____
Manufacturer's Affidavit	_____	_____	_____
Certificate of Origin	_____	_____	_____
GSP Statement on invoice	_____	_____	_____

Initials of Employee Who Completed the Checklist and Date _____

Chapter 4
Classification

4.0 Policy

PTC will use reasonable care in classifying its imports and ensuring compliance with all classification requirements. Misclassifications can result in the overpayment/underpayment of duties, failure to satisfy import restrictions, and monetary penalties. PTC will promptly notify Customs of any classification discrepancies discovered subsequent to entry filing.

4.1 Background

The Harmonized Tariff Schedule of the United States (HTSUS) is based on the Harmonized Commodity Description and Coding System ("HS"), a single internationally recognized classification system shared by a majority of the major trading nations. HTSUS classifications consist of ten digits. Digits one through six represent the internationally standardized HS classification. Digits seven and eight represent U.S. tariff subdivisions of the international system and the last two digits represent statistical subdivisions.

The HTSUS comprises approximately 5,000 article descriptions and is divided into 99 chapters, arranged in 21 sections. HTSUS Chapters are arranged by product types, beginning in Chapter 1 with crude and natural products continuing in further degrees of complexity by chapter through advanced manufactured goods. Each Chapter contains a broad category of items. Chapter 98 covers the special tariff program for U.S. goods returned, and Chapter 99 addresses temporary legislative actions.

To ensure accurate classification of merchandise, careful consideration must be given to the General Rules of Interpretation, Section Notes, Chapter Notes, and administrative rulings issued by Customs and case law.

4.2 Responsible Party(s)

The Import/Customs Compliance Manager is primarily responsible for ensuring that imported merchandise is classified in accordance with the HTSUS. The Purchasing Department, including Purchasing Manager and Buyers, are responsible for obtaining and providing the Import/Customs Compliance Manager with sufficient product information to properly classify merchandise.

4.3 Procedures and Controls for Classification of Current Products

- For previously imported products, the buyer will search PTC's Product Classification Database according to the model/part number and description to determine the appropriate HTSUS classification and current duty rate. The buyer will supply the HTSUS classification to the foreign supplier via the P.O. with instructions to include it on the commercial invoice.

Chapter 4. Classification

- The Customs broker is required to verify the HTSUS classification on the commercial invoice upon entry by matching it to their copy of the Product Classification Database.

4.4 Procedures and Controls for Classification of New Products

- The Import/Customs Compliance Manager will determine classification of new products prior to entry. The Purchasing Department will provide the Import/Customs Compliance Manager with information on new products utilizing the "Classification Compliance Checklist" (See Exhibit 4.A). The checklist is to be prepared by the buyer and reviewed by the Engineering Department prior to submission to the Import/Customs Compliance Manager. In addition, the Import/Customs Compliance Manager will work closely with the product engineers, buyers, and others as needed to understand the characteristics and function(s) of the product necessary to determine the proper HTSUS classification. If the Import/Customs Compliance Manager is unsure of the classification, guidance will be requested from the Customs broker, the Customs Import Specialist, or Account Manager. If the Import/Customs Compliance Manager has applied PTC's classification procedures and remains uncertain, then a binding ruling request (per 19 CFR §177) and Customs' concurrence to support a classification determination will be obtained.

- The Import/Customs Compliance Manager will maintain a hard copy file with a record of all classification research and updates to the Product Classification Database.

- Once the classification has been determined, the Import/Customs Compliance Manager will enter it into the Product Classification Database and include the following information:

    - Model/part number
    - Short item description
    - Supplier code
    - HTSUS classification
    - Current duty rate
    - Unit of Measure
    - GSP eligibility
    - ADD

- Only the Import/Customs Compliance Manager or Designated Supervisor can update the database.

- The Import/Customs Compliance Manager, or designated Supervisor, is responsible for updating PTC Product Classification Database any time a new product is purchased or a change in the HTSUS is made. The Import/Customs Compliance Manager will provide the Customs broker with updated copies of the Product Classification Database on a quarterly basis and hard copies of changes and updates on a continuing basis. A log will be maintained indicating the date the database was provided to the Customs broker and acknowledgement of receipt by the broker.

4.5 Procedures for Verifying Classification

- The Import staff will review all entries prepared by the Customs broker to ensure that classifications on the CF-7501 were correct. The Import staff will compare the HTSUS found in the Product Classification Database for the specific merchandise with the information listed on the CF-7501.

- The Import staff will add a checkmark (√) above the HTSUS and initial and date the file copy of the CF-7501 to indicate that the entry was reviewed including classification of merchandise. The initials will be added after the Import Department employee has reviewed the entry for compliance in all applicable areas. If the classification on the CF-7501 is in question or requires correction, the Import staff will document correspondence with the broker and resolution of the matter. The Import staff will notify the Import/Customs Compliance Manager of the error and resolution and a copy of this documentation will be attached to the file copy of the related entry package.

4.6 Periodic Review to Ensure Policy/Objectives Are Being Met

On a semi-annual basis the Director Import Department will review the Import/Customs Compliance Manager's files related to research for any classification problems or updates to the Product Classification Database. In addition, the Director Import Department will select 26 entries (same entries selected for the recordkeeping review in Section 3.4) and review them for evidence of the Import staff's actions (initials, date & any follow-up action) in accordance with the above procedures. If systemic problems are identified, the review will be expanded to determine the extent of the problem. The Director Import Department will prepare a memo detailing the review (See Section 3.4). The Director Import Department in conjunction with the Import/Customs Compliance Manager will take appropriate action to correct any problems identified during the review.

On a semi-annual basis the Import/Customs Compliance Manager will randomly select 30 part numbers from the Product Classification Database and determine whether the part classification listed in the database is correct. If any erroneous classifications are found, the Import/Customs Compliance Manager will immediately update the Product Classification Database and inform the Customs broker of the correction. If the cause of the problem is systemic, the

Chapter 4. Classification

Import/Customs Compliance Manager will determine the scope of the problem, implement procedures to correct the problem, and if appropriate, and file a prior disclosure with Customs.

Classification Compliance Checklist

After this form has been completed and reviewed by the Engineering Department, please submit it to the Import/Customs Compliance Manager. If you have any questions about completing this form, contact the Import/Customs Compliance Manager at 123-1234.

Request Submitted By: _____
Telephone Number: _____
Request Date: _____
Request Reviewed By (Engineering): _____
Telephone Number: _____
Review Date: _____

Part/Item number _____
Short Description _____
Name and Address of Supplier _____
_____

Describe product, including main components and uses (also provide descriptive literature, if available).

_____
_____

Did you ask the supplier if this product had been sold to other U.S. purchasers before? _____
If yes, HTSUS previously used: _____
Has PTC imported this product before? _____
When? _____
HTSUS previously used: _____

If you are reporting a situation where you believe the Import Department may have misclassified a product PTC has already imported, please provide the following information.

Part/Item Number _____
HTSUS as found in PTC's database _____
Proposed HTSUS _____
Reason you believe the item was misclassified

_____
_____

Chapter 5
Quantity

5.0 Policy

PTC will take steps to ensure that accurate quantities of imported merchandise are reported to Customs and will promptly notify Customs of any quantity discrepancies discovered subsequent to entry filing as significant quantity variances may have duty impact.

5.1 Background

The Harmonized Tariff Schedule of the United States (HTSUS) establishes the units of measurement to be used to report quantities on Customs entries. In addition, 19 USC 1499(a)(3) and (4) requires that overages and shortages be reported to Customs.

5.2 Responsible Party(s)

The Import/Customs Compliance Manager and Warehouse Manager are primarily responsible for ensuring that accurate quantities are reported to Customs.

5.3 Procedures and Controls for Quantity

- Warehouse personnel will count all merchandise when received and verify the shipment against the original shipping advice.

- If no discrepancies exist between quantities received and the original shipping advice, Warehouse personnel will inspect the merchandise for damage, enter it into the receiving module, and store it in the warehouse. Warehouse personnel will print a copy of the receiving report, initial it, and send it to the Accounting and Import Departments, unless goods are damaged. Damaged goods will be returned to supplier and will not be entered into the receiving module. This will create a discrepancy report on the original shipping advice.

- If a discrepancy exists between the quantities received and the original shipping advice, warehouse personnel will print a Discrepancy Report, initial it, and send it with a copy of the receiving report to PTC's Accounting and Import Departments. A second copy of the Discrepancy Report and receiving report will be sent to the authorized buyer. The buyer will research the discrepancy and notify the Warehouse, Accounting, and Import Departments of the resolution. The buyer will maintain copies of all correspondence with the supplier. The Import Department will instruct the broker to make proper declaration to Customs. The broker will report the discrepancy to Customs as appropriate. The Import Department will maintain copies of all correspondence with the broker.

Chapter 5. Quantity

5.4 Procedures for Verifying Quantity

- The Import Staff will review all entries prepared by the Customs broker to ensure that quantities on the CF-7501 are correct. The staff will compare quantities on the commercial invoice, packing list, and receiving report with the information on the CF-7501.

- The Import staff will add a checkmark (√) above the quantity on the file copy of the CF-7501 to indicate that quantities were reviewed. If the quantity on the CF-7501 is in question or requires correction, the Import staff will document correspondence with the broker and resolution of the matter. The Import staff will notify the Import/Customs Compliance Manager of any errors and resolution and a copy of this documentation will be attached to the file copy of the related entry package.

5.5 Periodic Review to Ensure Policy/Objectives Are Being Met

On a semi-annual basis the Director Import Department will review the Import/Customs Compliance Manager's files related to the research of any quantity discrepancies identified by either Warehouse or Import Department personnel. In addition, the Director Import Department will select 26 entries (same entries selected for the recordkeeping review in Section 3.4) and review them to ensure that the Import staff's actions are in accordance with the above procedures. If systemic problems are identified, the review will be expanded to determine the extent of the problem. The Director Import Department will prepare a memo detailing the review (See Section 3.4). The Director Import Department in conjunction with the Import/Customs Compliance Manager will take appropriate action to correct any problems identified during the review.

Chapter 6
Transaction Value

6.0 Policy

PTC will use reasonable care in declaring accurate and complete values on Customs entries. On occasion, PTC provides tooling to foreign suppliers for purposes of manufacturing imported products. PTC will take steps to ensure that the complete transaction value, including any additions to the price actually paid or payable, is reported to Customs in accordance with applicable laws and regulations. Due to the difficulty involved in identifying assists, efficient interdepartmental communication must be maintained among the Import Department, Purchasing Department, and Accounting Department. In addition, PTC will promptly notify Customs of any value discrepancies discovered subsequent to entry filing. Incorrect values could result in overpayment/underpayment of duties and in monetary penalties.

6.1 Background

When goods are imported into the United States, they must be entered, that is, declared to Customs. As part of the entry process, goods must be classified and their value determined.

PTC's method of valuation is Transaction Value, which is the price actually paid or payable for the imported merchandise. This is the total payment made to the foreign seller, excluding actual international freight and insurance costs. Estimates of freight and insurance cannot be used. This payment may be direct or indirect. An example of an indirect payment is when the seller reduces the price on a current importation to settle a debt owed the buyer. Such indirect payment is part of transaction value.

Transaction value also includes amounts equal to:

A. Packing costs incurred by the buyer.
B. Selling commissions incurred by the buyer.
C. The value, apportioned as appropriate, of any assist (See exhibit 6.A for a definition of assist)
D. Royalties or license fees the buyer is required to pay, directly or indirectly, as a condition of sale.
E. Proceeds of any subsequent resale, disposal, or use of the imported merchandise that accrue, directly or indirectly, to the seller.

These amounts (items A through E) are added only to the extent that they are not included in the price, and are based on information accurately establishing the amount. If sufficient information is not available, then the transaction value cannot be determined and another basis of appraisement must be considered (See Sections 7.1 and 7.3).

Chapter 6. Transaction Value

6.2 Responsible Party(s)

The Import/Customs Compliance Manager and Accounting Manager are primarily responsible for ensuring that correct values, including any assists, are reported to Customs. The Purchasing Department is responsible for informing the Import/Customs Compliance Manager of any tooling or separate tooling payment (i.e. assist) provided to foreign vendors. The Customs Compliance Manager will ensure that the foreign vendor includes assists on invoices and the Customs Broker includes assist values on entries.

6.3 Procedures and Controls for Valuation of Merchandise

- PTC's Import Department will provide the authorized Customs broker with commercial invoice(s) for all shipments of imported merchandise. PTC has instructed its brokers to use the commercial invoice price to make entry of the imported merchandise. If the broker has any questions regarding the value to be on the entry, the broker will contact the Import Department to obtain clarification and ensure the correct value is declared. The Purchasing department should require that the foreign supplier include the appropriate assist charges on the commercial invoice as part of the purchase agreement.

- The Purchasing and Accounting Departments will report any additions to or changes in the invoice price to be paid as a result of quantity discrepancies, revised sales prices, separate payments for tooling, etc. to the Import Department in writing as soon as the change becomes known. The Import Department will notify the Customs broker if entry information is incorrect for appropriate action. The Import Department will update the Import Database to reflect any corrections and maintain hard copies of all related documentation in the Import File Folder.

6.3.1 Valuation of Assists

The following steps should be followed in identifying and determining the value of any assists (For Customs Requirements See Exhibit 6.A):

1. PTC's authorized buyer will add the letter "T" as a suffix to the purchase order (P.O.) Number on any tooling purchases.
2. The buyer will send a copy of the P.O. to the Import/Customs Compliance Manager. The Import Department will maintain an 'Assist Ledger' for any tooling that has been purchased pending production and importation of the merchandise. The tooling P.O. will be maintained in a suspense file until importation of the merchandise.
3. When merchandise is ordered, the buyer will instruct the vendor via the P.O. to include a statement on the commercial invoice that tooling was provided for the invoiced products. The buyer will send a copy of the purchase order to the Import Department. The Import Department will add this information to the 'Assist Ledger' pending receipt of the import package.

4. Once the commercial invoice (with the assist statement) is received, the Import Department communicates to the authorized Customs broker the value of the tooling per imported product (based on the total number products scheduled to be purchased by PTC). The Customs broker will then increase the declared value by the value of provided tooling on each entry of the imported article. The Import Department will also reflect the declarations in the 'Assist Ledger'.

6.4 Procedures for Verifying Value

- The Import staff will review all entries prepared by the Customs broker to verify that the broker correctly reported the value of the imported merchandise and that any assist or additional payments were declared to Customs. The Import staff will verify the value of the assist to the amount calculated and documented in the 'Assist Ledger'. The Import staff will add a checkmark (√) above the declared value on the file copy of the CF-7501 to indicate that the value was reviewed.

- If any errors are noted on the entry documentation, the Import staff will notify the broker to make the appropriate corrections. The Import staff will document correspondence with the broker and resolution of the matter. The Import staff will notify the Import/Customs Compliance Manager of the error and resolution and a copy of the documentation will be attached to the file copy of the related entry package.

6.5 Periodic Review to Ensure Policy/Objectives Are Being Met

- On a semiannual basis the Import/Customs Compliance Manager will coordinate with the Accounting Manager a review of general ledger accounts that may contain tooling or other assists as well as all purchase orders with a "T" suffix. The Accounting Manager will provide the Import/Customs Compliance Manager with a listing of all purchase orders containing a "T" suffix and a copy of the chart of accounts. The Accounting Manager will also identify any general ledger accounts that may contain tooling costs. The Import/Customs Compliance Manager will compare all the purchase orders with a "T" suffix to the 'Assist Ledger' and review general ledger accounts that may contain tooling. The Import/Customs Compliance Manager will document the review and a copy of this documentation will be kept on file. Any additions to the price actually paid or payable identified by the Import/Customs Compliance Manager will be immediately reported to the Customs broker. The Import/Customs Compliance Manager will retain copies of all correspondence with the broker and resulting declaration of the assist to Customs.

- In addition, the Import/Customs Compliance Manager will randomly select five vendors and request that the Accounting Department provides all invoices paid to the five vendors during the preceding six-month period. The

Import/Customs Compliance Manager will trace the paid invoices to corresponding Customs entries. If a payment can not be traced to a Customs entry, the Import/Customs Compliance Manager will contact the Accounting and Purchasing Departments to determine the reason for the payment to determine if the payment was dutiable. If the payment was dutiable, the Import/Customs Compliance Manager will determine why the payment was not posted to the Import Database, decide if the problem is systemic and the extent of the problem, develop procedures to prevent the error from reoccurring, and submit a disclosure to Customs.

- The valuation and reporting of assists will be reviewed as part of the semi-annual internal review of the Customs Function by the Director Import Department. The Director Import Department will review the Import/Customs Compliance Manager's files related to his review of general ledger accounts that may contain tooling. In addition, the Director Import Department will select 26 entries (same entries selected for the recordkeeping review in Section 3.4) and review them to ensure that the Import staff's actions are in accordance with the above procedures. If systemic problems are identified, the review will be expanded to determine the extent of the problem. The Director Import Department will prepare a memo detailing the review (See Section 3.4). The Director Import Department in conjunction with the Import/Customs Compliance Manager will take appropriate action to correct any problems identified during the review, including appropriate disclosures to Customs.

Assist Information

Definition

An assist is defined as any of the following, if supplied directly or indirectly, and free of charge or reduced cost, by the buyer of imported merchandise for use in the production or the sale of merchandise for export to the U.S.

(i) Materials, components, parts and similar items incorporated in the imported merchandise or used in production.
(ii) Tools, dies, molds and similar items used in the production of the imported merchandise.
(iii) Merchandise consumed in the production of the imported merchandise.
(iv) Engineering, development, artwork, design work and plans and sketches that were undertaken elsewhere than in the United States and are necessary for the production of the imported merchandise.

Valuing Assist

The value of assist in categories (i) and (iii) is the cost of acquisition or the cost of production plus any applicable transportation cost to the place of manufacture. The value of assist in category (ii) is the acquisition cost, production, lease, rental cost, etc. plus cost of transportation to the place of production. The value of assist in category (iv) is a) the cost of obtaining copies of the assist, if the assist is available in the public domain; b) the cost of the purchase or lease if the assist was bought or leased by the buyer from an unrelated person; c) the value added outside the United States, if the assist was produced in the United States and one or more foreign countries.

The value of assists used in the production of imported merchandise should be adjusted to reflect use, repairs, modifications, or other factors affecting the value of the assists. Assists of this type include such items as tools, dies, and molds.

Apportioning Assist

The method used to apportion the value of the assist depends on the details. The value of the assist may be allocated over:

- The first shipment if PTC wants to pay duty on the entire value at one time.
- Number of units produced up to first shipment.
- Entire anticipated production.
- Number of years of useful life.

If the entire anticipated production is not destined for the United States, some other method of apportionment will be used that is consistent with generally accepted accounting principles.

Chapter 7
Basis of Appraisement

7.0 Policy

PTC will ensure that transaction value is the proper basis of appraisement for its importations. If any importation does not meet the criteria for transaction value, PTC will take steps to ensure that the proper basis of appraisement is used to value the merchandise. Incorrect basis of appraisement can result in the overpayment/underpayment of duties.

7.1 Background

All merchandise imported into the United States is subject to appraisement. The Trade Agreements Act of 1979 (19 USC 1401a, subsequently referred to as the Act) sets forth the rules for appraisement of imported merchandise. The Act sets forth five different methods of appraisement, and their order of preference. Under the Act, the preferred method of appraisement is transaction value. However, if any of the following limitations are present, transaction value cannot be used as the appraised value:

- Restrictions on the disposition or use of the merchandise.
- Conditions for which a value cannot be determined.
- Proceeds of any subsequent resale, disposal or use of the merchandise, accruing to the seller, for which an appropriate adjustment to transaction value cannot be made.
- Related-party transactions where the transaction value is not acceptable.

In the event the merchandise cannot be appraised on the basis of transaction value, the alternate bases are considered in the following order:

- Transaction Value of Identical and Similar Merchandise
- Deductive Value
- Computed Value (The importer may request the reversal of Deductive Value and Computed Value at the time the entry summary is filed)
- Value if Other Values Cannot be Determined

7.2 Responsible Party(s)

The Import/Customs Compliance Manager is primarily responsible for ensuring the correct basis of appraisement is used for all merchandise imported by PTC.

7.3 Procedures and Controls for Basis of Appraisement

- If any payment other than that set forth in the sales contract is to be made to the seller, PTC's buyer will note the same in the supplier file. The buyer will submit the file to the Purchasing Manager for review. The Purchasing Manager will send a copy of the sales contract to the Import/Customs Compliance Manager. The Import/Customs Compliance Manager will review the contract and purchase order to ensure that none of the transaction value restrictions are present. If any restrictions are present, the Import/Customs

Compliance Manager will consult with the Customs broker and Import Specialist, if necessary, to determine the correct basis of appraisement. The Import/Customs Compliance Manager will maintain copies of all correspondence and documentation on the research conducted.

- In those instances where the purchase price is not definite at the time of importation, or restrictions exist on the disposition or the use of the merchandise, the buyer will notify the Purchasing Manager and the Import/Customs Compliance Manager. The Import/Customs Compliance Manager will consult with the Customs broker and Import Specialist, if necessary, to determine the proper basis of appraisement. The Import/Customs Compliance Manager will maintain copies of all correspondence and documentation on the research conducted. The Import/Customs Compliance Manager will also maintain copies of all documentation supporting whether the transactions met the criteria for use of transaction value.

7.4 Periodic Review to Ensure Policy/Objectives Are Being Met

On a semi-annual basis the Director Import Department will discuss with the Import/Customs Compliance Manager any basis of appraisement issues that have surfaced during the previous six-month period. If no basis of appraisement issues arose during the review period, the Import/Customs Compliance Manager will write a short memo to this effect and the Import Director will include it with the documentation of his review.

Chapter 8
American Goods Returned (9801)

8.0 Policy

PTC will ensure that the strict documentary and procedural requirements imposed on goods entered under subheading 9801.00.10 are met to prevent incorrectly claiming 9801 preference.

8.1 Background

HTSUS 9801.00.10 (American Goods Returned) allows for the duty-free entry of products of U.S. origin if they were not advanced in value or improved in condition while abroad. To obtain the duty exemption the following two conditions must be met:

- Product of the U.S. – For purposes of claiming duty exemption, a product of the U.S. is defined in 19 CFR §10.12(e) as an article manufactured within the Customs territory and may consist wholly of U.S. components or materials, of U.S. and foreign components and materials, or wholly of foreign components or materials. If the article consists wholly or partially of foreign components or materials, the article must have undergone a manufacturing process that substantially transformed it into a new and different article, or have been merged into a new and different article.

- Not advanced in value or improved in condition while abroad – For the purpose of claiming duty exemption, the product must not undergo any processing abroad which results in advancement in value or improvement in condition.

19 CFR §10.14(b) establishes that substantial transformation occurs when, as a result of manufacturing process, a new and different article emerges, having a distinctive name, character, or use, which is different from the original article or material before being subject to the manufacturing process.

8.2 Responsible Party(s)

The Import/Customs Compliance Manager is primarily responsible for ensuring that the documentary and procedural requirements imposed on merchandise entered under 9801 are met.

8.3 Procedures and Controls for Chapter 9801

- If the value of the articles exceeds $2,000, the authorized buyer will be responsible for obtaining a manufacturer's affidavit regarding the U.S. origin of the goods (See Exhibit 8.A) prior to exportation of the merchandise. The buyer will submit the declaration to the Import/Customs Compliance Manager.

- The goods will be physically inspected by shipping/receiving at the time of export to confirm marking as U.S. goods. The warehouse will notify the Import/Customs Compliance Manager of the date the merchandise was inspected and exported. The notification can be done via memo or email.

- The responsible buyer will obtain from the foreign shipper a declaration (Per Exhibit 8.B) regarding the U.S. origin of the goods and the fact that they were not advanced in value or improved in condition while abroad. The buyer will also instruct the foreign shipper to include a statement of U.S. origin and 9801 eligibility on the commercial invoice.

- The buyer will submit the declaration to the Import/Customs Compliance Manager, who will be responsible for submitting the declaration to the Customs broker with instructions to include it with the entry documentation. The declaration will be obtained prior to shipment of the merchandise subject to this regulation.

- The Import/Customs Compliance Manager with the assistance of the responsible buyer, if needed, will prepare the Importer's Declaration (Per Exhibit 8.C). The Import Department will be responsible for submitting the Importer's Declaration to the authorized Customs broker with instructions to include it with the entry package. The Importer's Declaration will be signed by PTC's President, Vice Presidents, or Director Import Department. The Importer's Declaration will be prepared prior to shipment to the U.S. of the merchandise subject to this regulation.

- Once the import package is received from the foreign supplier, the Import Department will inform the authorized Customs broker that the merchandise should be entered as 9801.

- The Customs broker will not claim 9801 preference unless specifically instructed to do so by the Import Department and no entry under 9801 will be made unless PTC has in its files a Shipper's Declaration and an Importer's Declaration covering the merchandise in question.

- The declarations will be attached to the file copy of the related entry package.

8.4 Procedures for Verifying 9801

The Import Staff will review all entries prepared by the Customs broker to ensure complete and adequate documentation of entries filed under 9801. If an entry was incorrectly filed under 9801, the Customs broker will be instructed to amend the entry. The Import staff will notify the Import/Customs Compliance Manager of the error and resolution and a copy of the documentation will be attached to the file copy of the related entry package.

Chapter 8. American Goods Returned (9801)

8.5 Periodic Review to Ensure Policy/Objectives Are Being Met

On a semi-annual basis the Director Import Department will review a random sample representing 10 percent of 9801 entries for the six-month period to confirm the declarations are on file and that the shipment qualified for duty-free treatment. If the review discloses systemic problems, the review will be expanded to identify all products incorrectly claimed under 9801. The Director Import Department will prepare a memo detailing the review (See Section 3.4). The Director Import Department in conjunction with the Import/Customs Compliance Manager will take appropriate action to correct any problems identified during the review.

Manufacturer's Affidavit
19 CFR §10.1(b)

I, _____, certify that part numbers _____ and _____ sold to _____ on _____ were made by _____ in the United States.

Date	Signature
Address	Capacity

Shipper's Declaration
19 CFR §10.1(a)(1)

I, _____, declare that to the best of my knowledge and belief the articles herein specified were exported from the United States, from the port of _____ on or about _____, 20___, and that they are returned without having been advanced in value or improved in condition by any process of manufacture or other means.

Marks	Number	Quantity	Description	Value in U.S. Coin

_____ _____
Date Signature

_____ _____
Address Capacity

Importer's Declaration
19 CFR §10.1(a)(2)

I, _____, declare that the (above) (attached) declaration by the foreign shipper is true and correct to the best of my knowledge and belief, that the articles were manufactured by _____ (name of manufacturer) located in _____ (city and state), that the articles were not manufactured or produced in the United States under subheading 9813.00.05, HTSUS, and that the articles were exported form the United States without benefit of drawback.

Date	Signature
Address	Capacity

Chapter 9
Antidumping/Countervailing Duties

9.0 Policy

PTC will use reasonable care in determining if an import is subject to Antidumping or Countervailing Duty (ADD/CVD). PTC will take steps to ensure strict compliance with procedural and documentary requirements for ADD/CVD and prevent any monetary penalties by Customs.

9.1 Background

Antidumping Duties are assessed on imported merchandise of a class or kind that is sold to purchasers in the United States at a price less than the fair market value. Fair market value of merchandise is the price at which it is normally sold in the manufacturer's home market. Countervailing duties (CVD) are assessed to counter the effects of subsidies provided by foreign governments to merchandise that is exported to the United States. These subsidies cause the price of such merchandise to be artificially low, which causes economic "injury" to the U.S. manufacturers. PTC does not import merchandise subject to CVD.

9.2 Responsible Party(s)

The Import/Customs Compliance Manager and the Purchasing Department, including Purchasing Managers and Buyers, are primarily responsible for ensuring ADD is properly declared.

9.3 Procedures and Controls for ADD

- For previously imported products, the buyer will search PTC's Product Classification Database according to the model/part number and description to determine the correct HTSUS and whether the merchandise is subject to ADD. If the merchandise is subject to ADD, the buyer will add a statement to the Purchase Order to this effect.

- The Customs broker is responsible for querying the database on every entry to obtain the proper classification and determine if the merchandise is subject to ADD. The Customs broker will not change the ADD determination unless specifically instructed to do so by the Import/Customs Compliance Manager.

- The Import/Customs Compliance will maintain a list of all products subject to ADD.

- On a quarterly basis the Import/Customs Compliance Manager will review notices in the Federal Register relating to ADD/CVD. If the notice is for a new ADD/CVD order, the Import/Customs Compliance Manager will determine if the review affects products imported by PTC. If the order affects any product, the Import/Customs Compliance Manager will enter the reference code "A" in

PTC's Product Classification database and inform the Broker (by letter, fax, or email) of the order effective date and the case number.

9.4 Procedures and Controls for ADD Determination of New Products

- Prior to the purchase of merchandise from a foreign supplier, the responsible PTC buyer will inform the Import/Customs Compliance Manager of the product to be sourced and the foreign supplier using the "Classification Compliance Checklist" (See Exhibit 4.A). The Import/Customs Compliance Manager will review the HTSUS classification prior to the purchase of the merchandise. The Import/Customs Compliance Manager will request the Customs broker to determine if the merchandise is subject to ADD by querying the HTSUS number in the Automated Broker Interface (ABI). The Import/Customs Compliance Manager will request the Broker to provide a copy of any potentially applicable antidumping order to confirm if the merchandise is within the scope of the order. The Import/Customs Compliance Manager will consult the Custom Broker and/or Customs Import Specialist if necessary to determine if the product is subject to ADD. If the merchandise is determined to be subject to ADD, the Import/Customs Compliance Manager will enter the reference code "A" in PTC's Product Classification database. The Import/Customs Compliance Manager will maintain a file of all merchandise subject to ADD and the applicable dumping order.

- The Customs broker is required to verify the HTSUS classification and whether the merchandise is subject to ADD upon entry by matching the commercial invoice to their copy of the Product Classification Database.

9.5 Procedures for Verifying ADD

- The import staff will review all entries prepared by the Customs broker to ensure that any required ADD was declared and the ADD declarations were correct. The Import staff will query the Product Classification Database for the specific merchandise and determine if it is subject to ADD. If subject to ADD, the import staff will compare the ADD order number in the Product Classification Database with the information listed on the CF-7501.

- The Import staff will add a checkmark (✓) above the dumping order cited on the CR-7501 and initial and date the file copy of the CF-7501 to indicate that ADD was reviewed.

- If any errors are noted on the entry documentation, the Import staff will notify the broker to make the appropriate corrections. The Import staff will document correspondence with the broker and resolution of the matter. The Import staff will also notify the Import/Customs Compliance Manager of the error and resolution and attach a copy of the documentation to the file copy of the related entry package.

9.6 Periodic Review to Ensure Policy/Objectives Are Being Met

- On a semiannual basis the Director Import Department will review the Import/Customs Compliance Manager files related to any problems pertaining to the declaration of ADD and any additions to the Product Classification Database subject to ADD.

- The Director Import Department will obtain, from the inventory records, the total merchandise imported during the previous six-month period that was subject to ADD. The Director Import Department will compare the total importations per the inventory records to the total merchandise subject to ADD as reported to Customs (per the Import Department Database). The Director Import Department will prepare a memo detailing the review (See Section 3.4). Discrepancies will be discussed with the Import/Customs Compliance Manager with instructions on any required actions.

Chapter 10
Generalized System of Preference

10.0 Policy

PTC will use reasonable care in determining if an import qualifies for duty-free treatment under the Generalized System of Preferences (GSP). PTC will take steps to ensure compliance with procedural and documentary requirements for claiming GSP tariff preference; therefore, assuring that GSP claims are supportable. Customs brokers will not claim GSP on any importation without the express authorization of PTC.

10.1 Background

GSP is a system used by the United States and other countries to help developing nations improve their financial or economic condition through exports. It provides for the duty-free importation of a wide range of products that would otherwise be subject to Customs duty. Approximately 140 countries and territories have been designated as Beneficiary Developing Countries (BDC) and over 4,000 articles designated as eligible for duty-free treatment. The eligible articles are identified in the Harmonized Tariff Schedule of the United States and the designated countries are also listed therein.

10.1.1 Recordkeeping Requirements

The recordkeeping requirements for GSP claims are outlined in 19 CFR 10.171 through 10.178. It is Customs policy that an inability to produce the required records will result in disallowance of GSP preference.

There are two primary factors to be addressed in recordkeeping: the origin of the product and its value. The origin of articles that are wholly the growth, product, or manufacture of the BDC must be supported by documents obtainable by the importer. The supporting documents may *include trip reports, site visits, and quality assurance reports.* Evidence to substantiate the manufacturing origin of articles that are the product or manufacture of the BDC may include *raw materials purchases, proof of factory labor, and support for manufacturing overhead*.

In addition to BDC manufacturing costs, for articles not wholly the growth product or manufacture of that particular BDC for which GSP eligibility is claimed under the 35 percent direct processing costs provision, the exporter or other appropriate and knowledgeable party should be prepared to submit, at the Port Director's request, a declaration setting forth the pertinent facts. The party submitting the declaration must keep supporting documents for five years after submission of the declaration. Evidence may include *product specifications, bill of materials, foreign financial statements, product cost sheets, payment records, overhead allocation schedules, raw material purchases, proof of factory labor, and support for manufacturing overhead*. Production records must establish the

value of the BDC materials used in the imported article on a lot by lot, batch by batch, or shipment by shipment basis.

Finally, if a shipment from a BDC passes through the territory of any other country en route to the U.S., the merchandise must not enter the commerce of the transient country. Documents supporting direct shipment may include *bills of lading, freight or shipping invoices, and air waybills* that show the U.S. as the final destination.

10.2 Responsible Party(s)

The Import/Customs Compliance Manager and the Purchasing Department, including Purchasing Managers and Buyers, are primarily responsible for ensuring the correct determination as to the eligibility of imports under GSP.

10.3 Procedures and Controls for GSP

- Prior to the purchase of merchandise that may be eligible for GSP from a foreign supplier, the responsible PTC buyer will inform the Import/Customs Compliance Manager of the product, the foreign supplier, and the country of origin (See Exhibit 10.A for list of GSP eligible countries). The buyer will also provide any available information as to whether the merchandise (1) can be shipped directly from the supplier in the GSP eligible country to the United States, and (2) is manufactured completely of materials from such GSP eligible country, or if third country components are used, at least 35% value is added in the GSP eligible country.

- The Import/Customs Compliance Manager will verify that the product qualifies for GSP by reviewing the Special Duty Rate column next to the classification in the HTSUS. The Import/Customs Compliance Manager will also verify that the product will be shipped directly to the U.S. or if traveling “In bond”, that the documents indicate U.S. as the final destination. The Import/Customs Compliance Manager will then advise the responsible PTC buyer as to whether the item in question qualifies for GSP treatment.

- If PTC decides to source the item from a supplier producing in a GSP eligible country, the responsible buyer will assure that procurement contracts contain appropriate legal provisions that require the supplier to provide information to support GSP eligibility to Customs on request with appropriate legal provisions for failure to comply. The buyer will instruct the foreign seller via the Purchase Order to include a statement of GSP preference on the commercial invoice. The buyer will also ensure that the foreign vendor understands the requirement for the 35% local value content and the records necessary to support a GSP claim.

- The Import/Customs Compliance Manager will inform the authorized Customs broker that GSP duty status should be claimed for the import. The

Import staff will provide written instructions to the Customs broker to claim GSP via notation on the commercial invoice.

- If the merchandise is not wholly the growth, product or manufacture of the beneficiary developing country, the buyer will request and obtain a GSP Declaration from the supplier. The Declaration will include all relevant detailed information about the manufacture of the product.

- The GSP Declaration does not have to be filed with the Customs entry, but will be maintained by PTC and submitted to Customs if requested by the Import Specialist or any other appropriate Customs official. The Import staff will file the GSP Declaration with the related entry package. In addition, the Import/Customs Compliance Manager will ensure that any other documentary evidence confirming direct shipment, such as shipping documents, invoices, etc. are maintained with the entry file.

- See “Procedures and Controls for Classification of New Products” in Section 4.4. of this Manual.

10.4 Procedures for Verifying Claimed GSP

- The Import staff will review all entries prepared by the Customs broker to ensure adequate documentation of GSP claims. If GSP eligibility was claimed on the CF-7501, the Import staff will verify that either the invoice contains the required supplier statement or a GSP Declaration was obtained.

- If the Import Staff identifies an entry in which the Customs broker claimed GSP eligibility and a supplier statement was not included on the invoice or GSP Declaration obtained, the Import Staff will contact the Customs broker to determine why the claim was made on the entry. The Import staff will also maintain copies of all correspondence with the Customs broker regarding resolution of the matter. If the claim was made in error, the Customs broker will be instructed to amend the entry. The Import staff will notify the Import/Customs Compliance Manager of the error and resolution and a copy of the documentation will be attached to the file copy of the related entry package.

10.5 Procedures for Verifying GSP for Expiration and Renewal

Since GSP preference can change annually with regards to eligible countries, products eligible for benefit or benefits granted, the Import/Customs Compliance Manager must verify GSP eligibility annually. The Import/Customs Compliance Manager will also review Customs Bulletins accompanying GSP expiration/renewal on a retroactive basis for procedures used to handle claims under these circumstances.

Chapter 10. GSP

10.6 Common Errors

- Inability to produce records to support the 35 percent minimum value content provision.
- Foreign manufacturer commingled materials purchased from both BDC & non-BDC suppliers and importer is unable to identify when non-BDC components were used in an imported article.
- U.S. Goods Returned erroneously claimed as imported GSP articles.
- GSP articles erroneously classified and if properly classified, the articles would not be eligible for GSP.
- Articles originated in a GSP ineligible country.
- Importer could not evidence direct shipment of the product from the BDC to the United States when the shipment entered an intermediate country en route to the United States.

10.7 Periodic Review to Ensure Policy/Objectives Are Being Met

On a semi-annual basis the Director Import Department will review a random sample representing 10 percent of total GSP entries for the six-month period to confirm eligibility. If systemic problems are identified, the review will be expanded to determine the extent of the problem. The Director Import Department will prepare a memo detailing the review (See Section 3.4). The Director Import Department in conjunction with the Import/Customs Compliance Manager will take appropriate action to correct any problems identified during the review.

GSP Eligible Countries or Associations of Countries (Per 2001 HTSUS, Rev.1) *

The following countries, territories and associations of countries eligible for treatment as one country (pursuant to section 507(2) of the Trade Act of 1974 (19 U.S.C. 2467(2)) are designated beneficiary developing countries for the purposes of the Generalized System of Preferences, provided for in Title V of the Trade Act of 1974, as amended (19 U.S.C. 2461 et seq.):

Albania
Angola
Antigua and Barbuda
Argentina
Armenia
Bahrain
Bangladesh
Barbados
Belize
Benin
Bhutan
Bolivia
Bosnia and Herzegovina
Botswana
Brazil
Bulgaria
Burkina Faso
Burundi
Cambodia
Cameroon
Cape Verde
Central African Republic
Chad
Chile
Colombia
Comoros
Congo (Brazzaville)
Congo (Kinshasa)
Costa Rica
Cote d'Ivoire
Croatia
Czech Republic
Djibouti
Dominica
Dominican Republic
Ecuador
Egypt
El Salvador
Equatorial Guinea
Eritrea
Estonia
Ethiopia
Fiji
Gabon
Gambia, The
Ghana
Grenada
Guatemala
Guinea
Guinea-Bissau
Guyana
Haiti
Honduras
Hungary
India
Indonesia
Jamaica
Jordan
Kazakhstan
Kenya
Kiribati
Kyrgyzstan
Latvia
Lebanon
Lesotho
Lithuania
Macedonia, Former Yugoslav Republic of
Madagascar
Malawi
Mali
Malta
Mauritania
Mauritius
Moldova
Mongolia
Morocco
Mozambique
Namibia
Nepal
Niger
Nigeria
Oman
Pakistan
Panama
Papua New Guinea
Paraguay
Peru
Philippines
Poland
Romania
Russia
Rwanda
St. Kitts and Nevis
Saint Lucia
Saint Vincent and The Grenadines
Samoa
Sao Tome and Principe
Senegal
Seychelles
Sierra Leone
Slovakia
Slovenia
Solomon Islands
Somalia
South Africa
Sri Lanka
Suriname
Swaziland
Tanzania
Thailand
Togo
Tonga
Trinidad and Tobago
Tunisia
Turkey
Tuvalu
Uganda
Ukraine
Uruguay
Uzbekistan
Vanuatu
Venezuela
Republic of
Yemen
Zambia
Zimbabwe

*Updated annually

Non-Independent Countries and Territories

Anguilla
British Indian Ocean Territory
Christmas Island (Australia)
Cocos (Keeling) Islands
Cook Islands
Falkland Islands (Islas Malvinas)
French Polynesia
Gibraltar
Heard Island and McDonald Islands
Montserrat
New Caledonia
Niue
Norfolk Island
Pitcairn Islands
Saint Helena
Tokelau
Turks and Caicos Islands
Virgin Islands, British
Wallis and Futuna
West Bank and Gaza Strip
Western Sahara

Associations of Countries (treated as one country)

Member Countries Of the Cartagena Agreement (Andean Group)

Consisting of:
Bolivia
Colombia
Ecuador
Peru
Venezuela

Member Countries of the West African Economic and Monetary Union (WAEMU)

Consisting of:
Benin
Burkina Faso
Cote d'Ivoire
Guinea-Bissau
Mali
Niger
Senegal
Togo

Member Countries of the Association of South East Asian Nations (ASEAN)

Currently qualifying:
Cambodia
Indonesia
Philippines
Thailand

Member Countries of the Southern Africa Development Community (SADC)

Currently qualifying:
Botswana
Mauritius
Tanzania

Member Countries of the Caribbean Common Market (CARICOM), except The Bahamas

Consisting of:
Antigua and Barbuda
Barbados
Belize
Dominica
Grenada
Guyana
Jamaica
Montserrat
St. Kitts and Nevis
Saint Lucia
Saint Vincent and the Grenadines
Trinidad and Tobago

GSP Eligibility Requirements

If the symbols “A” or “A*” appear in parentheses in the Special Duty Rate column of the HTSUS, the product is designated to be an eligible article for purposes of GSP pursuant to section 503 of the Trade Act of 1974. However, the following articles are not eligible for GSP:

i. textile and apparel articles which are subject to textile agreements;
ii. watches, except as determined by the President pursuant to section 503(c)(1)(B) of the Trade Act of 1974, as amended;
iii. import-sensitive electronic articles;
iv. import-sensitive steel articles;
v. footwear, handbags, luggage, flat goods, work gloves and leather wearing apparel, the foregoing which were not eligible articles for purposes of the GSP on April 1, 1984;
vi. import-sensitive semimanufactured and manufactured glass products;
vii. any agricultural product of chapters 2 through 52, inclusive, that is subject to a tariff-rate quota, if entered in a quantity in excess of the in-quota quantity for such product; and
viii. any other articles which the President determines to be import-sensitive in the context of the GSP.

The symbol “A” indicates that all beneficiary developing countries (BDC) are eligible for preferential treatment with respect to all articles provided for in the designated provision. The symbol “A*” indicates that certain beneficiary developing countries, specifically enumerated in subdivision (d) of General Note 4(c), are not eligible for such preferential treatment with regard to the article provided for in the designated provision.

To qualify for the duty free treatment a product must meet either of two criteria. Either (1) the product must be the growth, product, or manufacture of a designated beneficiary developing country or (2) the sum of the cost or value of the materials produced in the beneficiary developing country (or any 2 or more countries which are members of the same association of countries entitled to treatment as a BDC) plus the direct costs of processing operations performed in such beneficiary developing country (or member countries) must represent at least 35 percent of the appraised value of the merchandise.

To qualify as GSP material for the 35 percent calculation, the material must either be:

- wholly the growth, product or manufacture of a BDC, or

- substantially transformed in the BDC into a new and different constituent material where the BDC is the country of origin.

No article or material of a BDC will be eligible for such treatment by virtue of having merely undergone simple combining or packing operations, or mere dilution with water or mere dilution with another substance that does not materially alter the characteristics of the article.

Finally, the imported article must be (a) shipped directly to the United States from the beneficiary developing country or (b) shipped through a second foreign country without entering that country's commerce; or (c) shipped through a free trade zone in a second beneficiary developing country where certain very limited operations (e.g., sorting, testing, packing) may have been performed.

Chapter 11
Post Entry

11.0 Policy

PTC will comply with applicable reporting requirements and will promptly respond to inquiries and requests for information by Customs. Failure to respond to Customs inquiries may result in penalties.

PTC will take appropriate steps to report to Customs any errors or omissions related to any importation.

11.1 Amendment of Entry

If an error is identified prior to liquidation of an entry (generally entries are liquidated within one year), the Import Department will notify the Customs broker, who will amend the entry and pay any additional duties/fees owed. The Import Department will maintain a copy of the amended entry with the file copy of the original entry package.

11.2 CF-28 Request for Information

In performing its responsibilities in connection with imports into the United States, Customs will occasionally seek information from importers in addition to that requested in the entry package. These requests may be in writing, in the form of a CF-28, or oral and will generally come from the Import Specialist responsible for PTC's imports or the Account Manager.

- Any employee receiving a Request for Information from any Customs official, whether written or oral, will promptly notify the Import/Customs Compliance Manager. The Import/Customs Compliance Manager will review the request and determine if anyone else in PTC needs to be notified (e.g., Legal Counsel).

- If the Request for Information is in writing, the Import/Customs Compliance Manager, with assistance from the Import Department Staff, will prepare a draft response no later than a week before it is due. The Director Import Department will review the draft response. Any comments will be incorporated into a revised response and sent to Customs so it is received no later than the due date. The submission will also include a "stamp and return" receipt copy for PTC's records. A copy of the CF-28 will be filed with the appropriate entry package as well as in the Customs correspondence file.

- If the Request for Information is made orally, the employee receiving the same will make sure that he/she understands the information being requested. The employee will provide a response if he/she feels that it is a simple technical question to which he/she is certain of the response. Once the employee has provided the response to Customs, he/she will prepare a memorandum to the file setting forth the request, substance of the

conversation with the Customs official and response provided. If the employee is uncertain of the answer, he/she will prepare a memorandum setting forth Customs' request and submit it to the Import/Customs Compliance Manager for response. The memorandums will be maintained in the Customs correspondence file.

11.3 CF-29 Notice of Action

Customs issues a CF-29 when additional duties are owed or a correction is needed. Customs will designate on the notice the type of action being taken that affects duties owed the Government.

Any employee receiving a CF-29 from Customs will promptly submit it to the Import/Customs Compliance Manager. The Import/Customs Compliance Manager will review the CF-29 and seek advice from the Customs broker and/or legal counsel, if considered necessary. If after consulting with the Customs broker and/or legal counsel the Import/Customs Compliance Manager is not in agreement with the notice, he will file a protest within 90 days following the liquidation notice date (See Section 12.4). If the Import/Customs Compliance Manager agrees with the Customs determination, copy of the CF-29 will be filed with the corresponding entry and in the Customs correspondence file.

11.4 Protest

The following decisions of the Customs Port Director may be protested within 90 days of Customs liquidation of the entry:

i. Exclusion of merchandise from entry or delivery
ii. Determination of the value, classification, duty rate, or amount of duty to be applied to an entry
iii. Liquidation or re-liquidation of an entry
iv. Refusal of a claim for duty drawback
v. Refusal to re-liquidate an entry based on clerical error or mistake of fact
vi. Any other charge or exaction within the jurisdiction of the Secretary of the Treasury

When one of these events occurs, the Import/Customs Compliance Manager will determine within two weeks whether a protest should be made. If necessary, the Import/Customs Compliance Manager will seek the advice of the Customs broker and/or legal counsel. He will then assign an employee in the Import Department to gather all relevant information needed for the protest. After the relevant information has been received, the Import/Customs Compliance Manager will prepare the protest on CF-19 pursuant to 19 U.S.C. §1514 and 19 CFR §174, Subpart B. The Import/Customs Compliance Manager will ensure that a copy of the protest is filed in the corresponding entry file and in the Customs correspondence file.

Chapter 11. Post Entry

11.5 Ruling Request

Customs law includes rules under which importers may challenge any aspect of a Customs liquidation of imported merchandise such as valuation, classification, country of origin, or NAFTA eligibility or may seek official guidance on such issues in advance of importation, or after importation but before liquidation.

The following procedures will be followed when requesting a Customs Ruling pursuant to 19 CFR §177:

- The Import/Customs Compliance Manager, with the assistance of the Import Department Staff, will gather all information relevant to the request.
- The Import/Customs Compliance Manager will seek guidance if necessary from the Customs broker, legal counsel, or other sources.
- Once this information has been obtained, the Import/Customs Compliance Manager will prepare a letter (i.e., ruling request) containing all relevant facts relating to the transaction in question, including a detail description of the transaction, names and addressees of interested parties, and name of the port or place at which the article will be entered.
- The draft request will be reviewed by the Director Import. Any comments will be incorporated into a revised ruling request.
- Once the ruling is received, a copy will be maintained in the Customs correspondence file and a copy sent to the Customs broker and the Import Specialist handling the affected importation(s).

11.6 Prior Disclosure

U.S. law provides for reduced civil penalties where a company brings violations of law to the attention of Customs prior to or without knowledge of a Customs investigation having been commenced as defined by 19 CFR 162.74(g).

All PTC employees are expected to promptly report to the Import/Customs Compliance Manager any mistakes he/she may have made in connection with an importation or any circumstances leading the employee to believe an error or omission has occurred regarding information submitted to Customs.

- The Import/Customs Compliance Manager will thoroughly investigate any reports received regarding any errors made in connection with an importation. The Import/Customs Compliance Manager will determine the facts and circumstances surrounding the suspected violation, including:
  1) whether the suspected violation is continuing;
  2) whether the suspected violation involves liquidated or unliquidated entries;
  3) whether there exists evidence of a clerical error or mistakes of fact;
  4) the extent to which PTC and the employees involved in the incident exercised reasonable care or failed to meet their legal responsibilities;

5) any indication that Customs may have commenced an investigation against PTC;
6) any revenue loss to Customs; and
7) whether PTC's procedures need to be adjusted in order to prevent similar situations from reoccurring.

- If the Import/Customs Compliance Manager determines that the error occurred because of deficiencies in control procedures, the practice(s) in question will be immediately terminated and the Import/Customs Compliance Manager will develop necessary procedures to prevent reoccurrence.

- The Import/Customs Compliance Manager will consult with the Director Import and legal counsel, if necessary, to determine whether a violation has occurred, the procedural changes needed to be implemented on a permanent basis to prevent future reoccurrence, and the appropriate approach to use to disclose the violation to Customs.

- If the error or omission involves an unliquidated entry, and clerical error or mistake of fact, PTC will adjust the entry to correct the error.

- If the error involves negligence, gross negligence or fraud and PTC is not aware of the commencement of any investigation by Customs, PTC's Import/Customs Compliance Manager in consultation with the Director Import and other appropriate company officials should make a prior disclosure pursuant to 19 CFR §162.74. The Import/Customs Compliance Manager should use a checklist (See Exhibit 11.A) to ensure the disclosure:

  1) Identifies the class or kind of merchandise involved in the violation.
  2) Identifies the entry number(s) of the importation(s) in question, or the Customs port(s) of entry and the approximate date(s) of entry.
  3) Specifies the material false statement(s) or material omission(s) made.
  4) Describes the true and accurate information or data which should have been provided in the entry documents.
  5) Tenders any loss of duties.
  6) Is sent to the port of entry where the violation occurred.

Any information unknown at the time of the disclosure should be made within 30 days from the date of the initial disclosure and the disclosure should include a statement to that effect.

Prior Disclosure Checklist

The following questions must be answered when completing the prior disclosure submission.

- ❑ Is the prior disclosure addressed to the port Fines, Penalties and Forfeiture (FP&F) Officers for all ports where the violation occurred?

- ❑ Does the prior disclosure identify all the Customs ports where the disclosed violations occurred? (Note: The submission must list all of the concerned ports of entry.)

- ❑ Does the prior disclosure identify the class or kind of merchandise involved in the violation?

- ❑ Does the prior disclosure identify the merchandise by class and kind, the entry number, and the port of entry arrival and approximate date? (Note: The disclosing party defines the scope of the prior disclosure.)

- ❑ Does the prior disclosure specify the material false statements, omissions or acts involved in the disclosed violation? The person making the prior disclosure should explain the how and why behind the occurrences.

- ❑ Does the prior disclosure contain the true and accurate information or data that should have been provided in the entry? (Note: Remember to specify that PTC will provide any unknown information or data within 30 days of the initial disclosure if it is not available at the time of the disclosure. PTC can also ask the concerned Fines, Penalties and Forfeitures Officer for extensions of this 30-day period.)

- ❑ Does the prior disclosure include any loss of duties, taxes and fees due the Government on liquidated entries covered by the disclosure? And, if so, has a check been prepared in the amount of monies owed and made payable to Customs to submit along with the prior disclosure? The regulations provide the option of paying at time of disclosure or within 30 days of Customs notification.

- ❑ If the prior disclosure is to be mailed, have arrangements been made to send it registered or return receipt requested? (Note: Failure to mail the disclosure in this manner will mean that the time of the disclosure will be considered the date of receipt by Customs.)

Chapter 12
Staff Training

12.0 Policy

It is important for all employees to be aware of their responsibilities under the Customs laws and to keep current as to any changes in the legal requirements applicable to imports. The Import Department will develop training programs for PTC employees.

12.1 Division Supervisors Training

Supervisors for the following Departments will receive yearly refresher training on Customs Compliance procedures:

- Upper Level Management
- Accounting
- Purchasing
- Shipping/Receiving
- Engineering

The training will be coordinated by the Personnel Department and provided by the Import Department.

12.2 New Employee Training

All new employees will receive a minimum of two hours of Customs Compliance Training. The training will be coordinated and provided by the Personnel Department.

The training will cover at a minimum:

- PTC's organizational structure for Customs activities and its policy regarding Customs compliance;
- The role of the Import Department; and
- Information on how to obtain assistance if a Customs issue or question arises.

In addition, all new employees will receive a copy of this manual, included with the new employee orientation package, and will be reviewed at the Customs training session.

Once new employees have been assigned specific departmental duties, they will receive additional training if they work in one of the following departments:

- Import
- Accounting
- Customer Service
- Purchasing
- Shipping/Receiving
- Engineering

Chapter 12. Staff Training

Department Supervisors will be responsible for notifying the Import Department of the employee's name and duties, and request the training. The training will be provided by the Import Department and will focus on the employee's duties as they relate to the Customs process.

12.3 Current Employee Training

On a yearly basis employees with Customs responsibilities in the following departments will have a refresher Customs Compliance training course:

- Accounting
- Purchasing
- Shipping/Receiving
- Engineering Services

The training will be coordinated by the Personnel Department and provided by the Import Department and will at a minimum cover:

- Any changes in rules, regulations and procedures of Customs;
- Any changes in PTC's Customs compliance procedures; and
- Any problems or concerns identified since the previous training class.

Further, the Import/Customs Compliance Manager will promptly advise employees by written memorandum of any changes in procedures for which dissemination should not be delayed until the next refresher training course.

12.4 Import Department Employee Training

The Import/Customs Compliance Manager will devise individual development plans for current and new employees in the Import Department. They will receive detailed training in the areas relating to their Customs responsibilities such as valuation, classification, etc.

12.5 Documentation

All training sessions will be documented, including a list of attendees, training date(s), and topics covered. In addition, the Import Department will maintain training materials on file for reference.

12.6 Periodic Review to Ensure Policy/Objectives Are Being Met

On an annual basis the Director Import Department will review the Import/Customs Compliance Manager's training files to ensure required training of supervisors and current employees is being conducted.

Appendix I

Reference Materials

Customs has issued a number of "Informed Compliance Publications" which are designed to assist importers in complying with the Customs Laws and Regulations. The following is a list of some of the Informed Compliance Publications available from the Import Department or U.S. Customs and Border Protection Web site:

What Every Member of the Trade Community Should Know About:

- Bona Fide Sales and Sales For Exportation
- Buying And Selling Commissions
- Customs Value
- Tariff Classification
- Proper Deductions for Freight & Other Costs
- Reasonable Care
- Records and Recordkeeping Requirements
- The ABC's of Prior Disclosure

In addition to the above publications, the Import Department has the following publications available for reference:

- Code of Federal Regulations, Title 19, Parts 1 to 199
- Harmonized Tariff Schedule of the United States (with Explanatory Notes)
- Importing Into the United States

Appendix II

Glossary

ABI – Automated Broker Interface

ADD – Antidumping Duties

BDC – Beneficiary Developing Country

CFR – Code of Federal Regulations

CF-3461 – Entry/Immediate Delivery

CF-7501 – Entry Summary

CVD – Countervailing Duties

FP&F – Fines, Penalties and Forfeitures

GSP – Generalized System of Preferences

HS – Harmonized Commodity Description and Coding System

HTSUS – Harmonized Tariff Schedule of the United States

Mod Act –The Modernization Act of 1993 is the popular name given to Title VI of the North American Free Trade Agreement Implementation Act [P.L. 103-182, 107 Stat. 2057], which became effective on December 8, 1993)

P.O. – Purchase Order

PTC – Phantom Trading Company

USC – United States Code

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Common Importer Errors Identified During Assessments and Audits

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The errors listed here are typical of those identified during assessments and audits of importers. Many are caused by a lack of communication between various departments of the importer or between the importer and its broker. For example, the Import Department knows that additional payments to foreign suppliers are dutiable, but another department, such as Contracts, Finance, or Purchasing, may not know they should be reported to Customs. The importer may have no mechanism built into its accounting system to ensure that the Import Department is informed when additional payments are made. Errors also result when importers assume the broker is correctly classifying or valuing imported merchandise, when in fact the broker may have incomplete or incorrect information about the product.

Manufacturing Assists

Manufacturing assists are items such as material components, molds, equipment, tools, and dies that the importer provided to the foreign manufacturer at a reduced cost or free of charge for use in producing the imported merchandise. Design and development costs undertaken in a country outside of the United States are also assists.

Importers may overlook assists because invoices are received after an entry summary is filed with Customs or the department responsible for purchase does not know that the cost of the assist is dutiable.

Additions to Price Actually Paid or Payable

Payments may include direct or indirect payments, after-the-fact adjustments, payments for purchased quota, payments for locally obtained tooling, currency rate fluctuation adjustments pegged to a contract, commissions, or royalties. Like manufacturing assists, these payments may be overlooked because they are not invoiced by the foreign exporter with the imported merchandise.

Nondutiable Costs

Under certain conditions, foreign inland freight and other inland charges incidental to the international shipment of goods are not dutiable. These charges may be nondutiable if they meet certain evidentiary requirements, such as having a through bill of lading or being identified separately, and if they occur after merchandise has been sold for export to the United States and placed with a carrier for through shipment to the United States. Importers may purchase

products “CIF,” which includes the cost of the foreign inland freight and insurance but do not separately identify it on the invoice, or they may not be able to support the accuracy of the nondutiable costs claimed.

Merchandise Classification

When Focused Assessment teams review classification, they often find that “basket provisions” have been incorrectly used for a classification, rather than the applicable specific tariff number.

Claims for duty preference such as the North American Free Trade Agreement (NAFTA), the Generalized System of Preferences (GSP), and the Caribbean Basin Initiative (CBI) are frequently incorrectly classified.

Classification errors also frequently occur because importers provide poor descriptions of merchandise to brokers or because product specifications are changed without notifying the import department or broker.

Special Trade Programs

Importers frequently do not properly monitor their use of special trade programs, including GSP, CBI, and others, and cannot provide evidence of origin, qualifying value content of materials, or proof the imports were wholly produced or a product of the beneficiary developing country.

Errors occur frequently because importers do not verify that the foreign manufacturer or producer of imports can support the claims for the special trade program. Also, the importer may not have contractual agreements with the foreign manufacturer or producer that require it to provide proof of eligibility to Customs on request. As a result, importers have been unable to support claims for special trade programs.

Harmonized Tariff Schedule of the United States (HTSUS) Chapters 9801 and 9802

Under HTSUS 9801 and 9802, requirements are very specific about what portion, if any, of the value of U.S. goods returned may be exempt from duty. Sometimes importers cannot support claims that packing materials or products assembled in foreign plants were in fact of U.S. origin.

In some instances, the importer has incomplete records that do not permit the tracing of the U.S. components. In other instances, importers switch suppliers from U.S. to foreign sources to take advantage of competing lower costs, but neglect to adjust the value of HTSUS 9802 merchandise on subsequent entries. There also may be dual sources for identical components, but a lack of appropriate inventory records precludes proper identification of the U.S.-source items. U.S. and foreign parts may not be commingled under this section. Importers may also fail to obtain proof-of-origin documentation from U.S. manufacturers on U.S. components that are reportedly used by foreign manufacturers in assembling HTSUS 9802.00.80 and 9802.00.90 products. Failure to maintain required declarations may result in the disallowance of claimed nondutiable status.

Related-Party Transactions

Transaction value is the most commonly used basis of appraisement. It is allowable even when the U.S. buyer and the foreign seller are related if the relationship does not influence the transfer price. It is the importer’s responsibility to provide evidence that transaction value is the appropriate basis of appraisement. Importers are sometimes unable to provide evidence such

as faxes, minutes of meetings, and correspondence to document price negotiations with related parties to show that the relationship did not affect the transfer price.

Buying Commissions

Under certain conditions, commissions paid to buying agents may not be included in the value of the imported merchandise. Selling commissions, however, are dutiable costs. Importers sometimes deduct payments for what is claimed to be a buying commission but is in fact a selling commission.

To support that a buying commission is nondutiable, the importer should have evidence of the duties provided by the agent. Evidence should include a signed buying agency agreement that clearly defines the role of the agent and shows the amount of commission to be paid and documentation that the agent is performing the role of a buying agent.

Recordkeeping

Importers are required to maintain and produce timely records required at time of entry (commonly called (a)(1)(A) records) and must also have accounting and financial records that support the value, quantities, classification, and other information shown on Customs entry documents. Failure to provide adequate documentation of entry information may result in payment of additional duties, as well as fines and penalties for failing to retain required records and/or filing false claims.

Questions and Answers

Determination of Focused Assessment Findings and Guidance

Q. What is the basis or status of Customs decisions made relative to individual transactions sampled and reviewed during a Focused Assessment?

A. The decisions (such as the correct merchandise classification or valuation) made relative to individual transactions reviewed during a Focused Assessment represent Customs determinations based on a comprehensive review of the specific facts and information applicable to the particular transactions. The determinations made through the Focused Assessment process, which includes ongoing dialog between Customs and the importer over the correctness of entered transaction information, are based on the information available to Customs at the time of verification.

Q. Do the Customs determinations made relative to individual transactions sampled and reviewed during a Focused Assessment have any legally binding effect?

A. The Customs determinations made relative to individual transactions reviewed during a Focused Assessment *do not* constitute binding rulings. Binding rulings represent Customs' position with respect to the specific facts presented relative to *prospective* transactions. Binding rulings in certain instances may be obtained on transactions if the entry is not finally liquidated. If the entry is liquidated but not final, a protest and application for further review may be filed and the protest decision issued under Part 177 of Customs Regulations. The individual transactions reviewed during a Focused Assessment involve merchandise that has previously been entered by the importer. In

most cases, the corresponding entries have been liquidated.

Q. What is the applicability of the Customs determinations made relative to individual transactions (and merchandise) sampled and reviewed during a focused assessment toward future importations?

A. While the Customs determinations made during a focused assessment *do not* constitute binding rulings, they *may be* applicable to future transactions. The particular facts and circumstances surrounding each transaction are generally different from previous transactions. This may be especially true when comparing the facts and circumstances of current transactions with those related to the transactions reviewed as part of a Focused Assessment that occurred years earlier. A principal objective of the Focused Assessment process is to provide the importer guidance to correct and/or avoid future compliance problems. Accordingly, the importer (having responsibility for exercising reasonable care in reporting import transactions to Customs) is expected to apply the specific determinations and guidance received during a Focused Assessment to future importations *as appropriate*. Further, with respect to future transactions, the importer may seek guidance from Customs and/or from other knowledgeable experts.

Q. With respect to future importations, can the importer cite, and/or claim detrimental reliance on, the Customs determinations made pertinent to individual transactions sampled and reviewed during a focused assessment?

A. Customs strives to treat identical transactions as uniformly as possible. The internal Customs procedures and process involved in a Focused Assessment emphasize coordination and consultation among members of the Customs Focused Assessment team and various Customs personnel, including those in the ports used by the importer. Specifically, consultation will occur concerning individual determinations (before they are rendered). Additionally, the final Focused Assessment report will be shared with all ports in which the importer enters merchandise.

With respect to future importations, the importer *will not* be able to claim detrimental reliance based on Customs determinations resulting from a Focused Assessment. Customs considers each transaction as an individual case, subject to review or verification as deemed appropriate. However, in instances where Customs initiates a verification activity relative to a current transaction and the importer believes Customs previously reviewed issues related to the verification inquiry through the Focused Assessment process, the importer should advise the Customs office conducting the verification activity of Customs previous determination. The office conducting the verification will consider all information presented by the importer, will compare the facts and circumstances related to any previous transaction with those applicable to a current transaction, and may consult with the appropriate national import specialist.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Prior Disclosures During a Focused Assessment

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The submission of prior disclosures by importers and other parties and the subsequent handling of these prior disclosures by the Customs Service continue to be areas of concern for both the importing community and Customs. Importers and other parties are increasingly re-evaluating how and when they should reveal their past violations to Customs. While Customs is responsible for enforcing title 19 United States Code (U.S.C.) 1592 and ensuring compliance with the laws and regulations that govern U.S. imports and exports, it seeks to improve compliance and encourage parties to submit prior disclosures. The purpose of this document is to further communicate the importance of submitting a prior disclosure and to explain the benefits received by parties submitting valid prior disclosures.

One of the most valuable tools available to a party when it discovers commercial noncompliance before the agency does, is the "prior disclosure" provision found in 19 U.S.C. 1592. If the disclosure is complete, accurate, and filed before, or without knowledge of, the commencement of a formal Customs investigation of that violation, the Fines, Penalties, and Forfeitures (FP&F) officer will review the disclosure to determine if it constitutes a prior disclosure. For example, prior disclosures must include:

(1) An identification of the class or kind of merchandise involved in the violation;

(2) An identification of the importation or drawback claim included in the disclosure by entry number, by drawback claim number, or by indicating each concerned Customs port of entry and the approximate dates of entry or dates of drawback claims;

(3) Specific material false statements, omissions, or acts, including an explanation of how and when they occurred;

(4) To the best of the disclosing party's knowledge, the true and accurate information or data that should have been provided in the entry or drawback claim documents and a statement that the disclosing party will provide any information or data unknown at the time of disclosure within 30 days of the initial disclosure date. The disclosing party may request extensions of the 30-day period from the concerned FP&F officer to enable the party to obtain the information or data;

(5) A tender of the loss of duties, fees, and taxes to Customs either at the time of the claimed prior disclosure or within 30 days after Customs notifies the party of Customs calculation of the actual loss of duties, taxes, and fees or actual loss of revenue. When disclosures are determined to be prior disclosures by Customs, the disclosing party will be entitled to significantly reduced penalties.

A prior disclosure may be submitted either in writing or orally. A written prior disclosure should be addressed to the Commissioner of Customs, have conspicuously printed on the face of the envelope the words "prior disclosure," and be presented to a Customs officer at the Customs port of entry of the disclosed violation. An oral disclosure must be confirmed in writing, unless waived by the FP&F officer, within 10 days of the date of the oral disclosure. When the claimed prior disclosure is made to a Customs officer other than the concerned FP&F officer, it is incumbent upon the Customs officer to provide the disclosure to the concerned FP&F officer. Additionally, the receiving Customs officer must notify the Office of Investigations of the disclosure. When a tender is made in connection with the prior disclosure, the Customs officer who receives the tender should ensure that the tender is deposited with the concerned local Customs entry officer. The FP&F officer responsible for the port of entry where the admitted violation took place decides whether the prior disclosure is valid in accordance with 19 CFR 162.74.

When a disclosure is determined to be a prior disclosure, Customs notifies the disclosing party and usually sets forth the reduced penalty treatment in its notice. The notification should provide instructions regarding payment of any reduced penalty, and also serves as the Customs record of the disclosed violation. In accordance with 19 CFR 162.74(g), if prior disclosure treatment is denied on the basis that Customs had commenced a formal investigation of the disclosed violation, and if Customs initiates a penalty action against the disclosing party involving the disclosed violation, a copy of the "writing" evidencing the commencement of a formal investigation of the disclosed violation shall be attached to any required pre-penalty notice issued to the disclosing party pursuant to 19 U.S.C. 1592 or 19 U.S.C. 1593a.

What Is Considered a "Formal Investigation" for Prior Disclosure Purposes?

For prior disclosure purposes under 19 CFR 162.74(g), a "formal investigation" is considered commenced on the date recorded in writing by the Customs Service as the date on which facts and circumstances were discovered or information received that caused Customs to believe that the possibility of a violation of 19 U.S.C. 1592 or 19 U.S.C. 1593a existed. During a Focused Assessment (FA) or other audit, a Customs officer may discover information that provides a reason to believe that the possibility of a section 1592 or 1593a violation exists. When this occurs, the officer dates and documents those findings. The prior disclosure regulations require that formal investigations be evidenced by such a "writing."

If the discovering Customs officer has commenced the investigation by such a "writing," the party should be notified of the findings. Although a “writing” may take many forms, during an FA or other audit a common form may be a sufficiently documented result sheet. Without knowledge of the commencement of a formal investigation, the party may still be able to submit a prior disclosure If the party is notified of such findings before the submission of a claimed prior disclosure, the concerned FP&F officer may determine the subsequent disclosure not to constitute a prior disclosure.

It is also important to remember that prior disclosure is "violation specific" and that disclosure benefits ordinarily are available only for those violations fully disclosed by the prior disclosure. Further, it should be noted that the definition of commencement of a formal investigation as it relates to prior disclosure does not require the active involvement of the Office of Investigations. The writing and recording by any Customs officer of the facts and circumstances indicating the belief of a possible violation "commences" the investigation.

Benefits Received from a Prior Disclosure

Benefits to the Disclosing Party

As mentioned above, parties may receive reduced penalties if a prior disclosure is submitted to Customs. The penalty may be reduced to "zero" if the importation involves unliquidated (i.e., "open") Customs entries and no fraud is involved. If the entries are liquidated (i.e., "closed or finalized") and no fraud is involved, the penalty is the interest on the duties owed. Therefore, the penalty for grossly negligent and negligent violations is reduced to only the interest on any loss of duties, taxes, and fees, which is computed from the date of liquidation at the prevailing rate of interest applied under section 6621 of title 26 as long as such person tenders the unpaid amount of the lawful duties, taxes, and fees at the time of the disclosure or within 30 days after notice by the Customs Service. If a fraudulent violation is disclosed, the penalty is reduced from the normal assessment of the domestic value of the goods to 1 times the loss of duties, taxes, and fees as long as such person tenders the unpaid amount of the lawful duties, taxes, and fees at the time of the disclosure or within 30 days after notice by the Customs Service. If the violation involves no loss of duties, taxes, and fees, the penalty is reduced to 10 percent of the dutiable value of the merchandise.

Prior disclosures can and do save the trade community time and money. In some cases, parties have saved millions of dollars in potential penalties by submitting prior disclosures, but other benefits often accrue to the disclosing party. By conducting periodic self-assessment of importing activities and utilizing this provision of law, a party may be able to detect and correct errors as well as ensure future compliance with Customs laws and regulations. Additional time and money savings often materialize in the form of reduced legal expenses and/or the elimination of lengthy Customs civil penalty proceedings. A good example of this is illustrated in the Prior Disclosure Scenario below.

Benefits to Customs

In this era of increased international trade with limited Customs appropriations and personnel (doing more with less), a prior disclosure can significantly eliminate or reduce expenditures of valuable Customs resources. Because the disclosing party does most of the work in uncovering the violation, the need for comprehensive or lengthy labor-intensive investigations can be reduced or eliminated, and protracted civil administrative or judicial proceedings can be avoided. Virtually every Customs discipline involved in commercial compliance (e.g., special agents, regulatory auditors, inspectors, import specialists, penalties personnel, attorneys, entry specialists) benefits from having the disclosing party do the work for Customs. The time- and resource-saving elements of prior disclosures permit the disciplines to devote greater energy to other compelling Customs enforcement or compliance initiatives.

Prior Disclosure Scenario

The following fictional scenario may have a very familiar ring to those involved in importing or exporting:

"JANE'S STORY" - OR - "HOW I SAVED MY COMPANY $1 MILLION"

Jane is the new compliance manager for a large electronics company on the West Coast. She's responsible for all the Customs and freight matters involved with the thousands of products the company imports and exports. The company imports well over $500 million worth of products each year. One Monday morning, she's going through the mail and comes across a letter from Customs advising her that her company has been selected for an FA review. The letter indicates that the FA team will be visiting, and that the team would like to review company books and records relating to the classification and value of certain 1998 electronic parts imports, as well as the records relating to the company's rather extensive 1998 HTS 9802 assembled VCR imports. The letter goes on to state that it is recommended that the company undertake a "self-assessment" and consider availing itself of the prior disclosure provision as described in the Customs Regulations at 19 CFR 162.74, in the event noncompliance with the Customs laws is discovered. The document ends with contact information and the usual Customs pleasantries.

Jane puts down the letter and remembers reading about FAs on the Customs Web site and vaguely recollects something called prior disclosure. She races to her computer, logs on to www.customs.treas.gov, and searches through the link tied into importing and exporting/informed compliance. There it is--the FA Program (FAP) Kit! She downloads the document and while waiting, scans the site for information on prior disclosure. Bingo! She finds an informed compliance publication called "The ABC's of Prior Disclosure," and readies it for downloading. Jane spends the rest of the day going through the information she retrieved from the Web.

One month later, Jane completes a thorough self-assessment of imports covered by the upcoming FA and discovers why the company hired her in the first place. Jane finds that both the 1997 and 1998 imported electronic parts are undervalued and that not all of the required HTS 9802 costs for the 1998 VCR imports were reported to Customs. Based on her calculations, the company failed to pay Customs about $250,000 in duty After meeting with Jane to review her findings, company executives agree to retain a Customs lawyer they have used on one other occasion. Later on, the lawyer calls Jane and informs her that based on his review of the records, Customs could pursue a section 592 penalty against the company, most likely at the gross negligence level (generally 4 times the duty loss). That would mean that the company could face a penalty of $1,000,000 plus the $250,000 in duty. The lawyer advises the company to file a prior disclosure to limit its liability.

Jane immediately meets with management and explains, "Ladies and gentlemen, with regard to the upcoming Focused Assessment, it's either a $1,000,000 penalty plus $250,000 in duty if we do nothing, or $250,000 in duty plus interest, if we make a disclosure. The choice is yours." Fortunately, the company goes forward with a prior disclosure that is accepted by Customs, and Jane gets a nice little bonus in her paycheck.

COMMENTS: The lawyer gave Jane good advice about filing a prior disclosure. The next step and often the most difficult one for compliance managers is "selling" management on the benefits associated with prior disclosure. The following points may make the compliance manager's job a bit easier:

1. If you find the noncompliance during a self-assessment, it's very likely the FA team will discover it during the FA.

2. Let the money do the talking for you. For example, do what Jane did--determine the potential penalty if Customs discovers the violation and then look at the difference in numbers if you elect to submit a valid prior disclosure. In most cases, the disclosure savings are substantial.

3. It's worth noting that a disclosure will also, in most cases, reduce the intrusiveness and duration of an investigation or audit that could ensue if the company fails to make a disclosure and Customs discovers the infractions.

Exhibit 4D – See Exhibit 3G

U.S. Customs and Border Protection
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Compliance Improvement Plan Framework

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

A Compliance Improvement Plan (CIP) is a written document that details a company's plan to correct each noncompliant area found during the Focused Assessment (FA). It includes a timetable for developing and implementing the company's corrective action. When an FA indicates the need for corrective action by the company to correct deficiencies and ensure future compliance, the related FA report will recommend that the company prepare and implement a CIP. The account manager (AM) or the designated CIP point of contact will work with the importer to help determine the cause and effect of any noncompliance, which will assist the company in developing the CIP.

Procedures

Time Frames

If the Pre-Assessment Survey (PAS) and/or Assessment Compliance Testing (ACT) phase of the FA disclose unacceptable risks to Customs that the company's importing process may result in significant noncompliance with laws and regulations, the company will be asked to develop and implement a CIP. The company will be given a conditional period of 6 months from the date of the report to implement its CIP. If at the end of the 6-month conditional period the company has not implemented the CIP but has demonstrated significant progress, extensions may be granted at the company's request. If the CIP has not been implemented within the 6-month time frame and the company has not demonstrated significant progress, the FA team will consider referring the company to Customs Headquarters for escalated action or possible enforcement action.

CIP Development

The first step in developing the CIP is for the company to determine the cause of any noncompliance. This will involve a thorough review of the company's current internal control structure and a determination of where the breakdown in the internal controls occurred. For example, if the FA disclosed undeclared assists, the company would need to determine why assists were not declared (e.g., the company's Purchasing Department did not inform the Import Department that the importations involved assists).

The second step is for the company to determine the necessary corrective actions to correct the deficiency and ensure future compliance. This may involve trial and error to determine what corrective actions will actually work. Using the example above, the company may determine that its internal control procedures need to be revised to ensure that the Purchasing Department informs the Import Department of any assists. This could involve revising its written procedures

and developing a log of assists that the Purchasing Department provides to the Import Department.

The third step is for the company to outline the corrective actions to be taken and how the system will be changed to accommodate the corrective actions and to provide timeframes for implementation and validation. This plan should include a timetable for developing and implementing the corrective action and the requirements for monitoring and submitting supporting documentation, such as an import procedure manual, internal control manual, or other evidence documenting the corrective action.

The corporate level of the company should transmit the plan in writing to the appropriate AM or the designated CIP point of contact. Upon full implementation, the company should validate whether the corrective action taken was effective.

Upon Customs receipt of the CIP, the company will be notified in writing of the status of the CIP and its related supporting documentation. The letters will inform the company whether the CIP and supporting documentation reasonably address the deficiencies noted on the audit result sheets and/or whether additional information is necessary.

CIP Contents

The CIP should identify the company point of contact, describe the noncompliant area, illustrate the corrective action, and project the completion, implementation, and validation target dates. A suggested format (template) is provided for preparing a CIP.

Responsible Official
The CIP should identify by name and title the person assigned to coordinate the CIP process. That person should be the company's primary point of contact regarding the CIP.

Deficiency Disclosed on the Result Sheet
The CIP should clearly state the deficiencies found during the FA for each noncompliant area and should refer to the result sheet(s) describing the noncompliant condition.

Action Steps
The company should include a full explanation of any corrective action steps taken and/or planned to correct the noncompliant areas. A step-by-step outline is necessary for the integration of each affected department involved with the company's Customs transactions.

Supporting Documentation
Copies of supporting documentation (department operating manuals illustrating the change, policy statements, or other evidence documenting the corrective action for action steps already completed) should be attached to the CIP. The nature of the required action steps should determine the kind of supporting documentation provided.

Target Dates
A target date should be established for each action step required to correct a deficiency. The company should inform Customs when it expects to complete the action steps.

Responsible Department
In some cases, more than one department may be responsible for addressing an action step. The action plan should reference all departments assigned to address each action step.

Validation Action
As the final action step, the company should describe the validation action. It should include the testing methodology to be used, the person who will conduct the testing, the number of transactions to be tested, the dates testing will begin and conclude, and the date the results will be forwarded to Customs. It is important to note that Customs will not normally conduct the follow-up review until the company has completed its validation action.

Approving Official
The CIP should be signed and transmitted at the corporate level and include the name and the position title of the office and the date issued.

Follow-up Review

After the CIP has been fully implemented and a reasonable time has elapsed since its implementation, the FA team will perform a follow-up review to determine whether the corrective actions taken have eliminated the unacceptable risks to Customs. This follow-up may involve a review of the actions taken by the company to correct the problem(s) and tests of the areas previously identified as noncompliant. If the results show that the company has corrected the problems, then the FA team will issue an opinion that the company is an acceptable risk. If the results show that the company has not corrected the problems, then the FA team will issue an opinion that the company is an unacceptable risk. If the results show that the company has not corrected the problems, then the FA team will consider referring the company to Customs Headquarters for escalated action or possible enforcement action.

COMPLIANCE IMPROVEMENT PLAN
(Suggested format)

Company Name	
Date Compliance Improvement Plan Prepared	
CIP CONTENTS	
Name/Title of Responsible Official	

Deficiency Disclosed on the Audit Results Sheet

(should be taken from the "Condition" section of the Results Sheet)

Corrective Action		**Target Date**	**Responsible Department**
(Specific action steps to be taken to correct the deficiency)	*(Supporting documentation to be submitted)*	*(Expected completion date for each action step)*	*(Title of department assigned to address each action step)*

Validation Action
(Description of testing methodology to be used)

Approving Official/Title	**Date**

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

A Guide for Supporting Generalized System of Preferences (GSP) Claims

October 2003

A Guide for Supporting GSP Claims

Table of Contents

Introduction 3

Information Sources/References 3

Focused Assessment Objectives 4

Regulatory Audit Policy (When Does Regulatory Audit Perform GSP Reviews?) 5

Possible Sampling Frames 5

Responsibility for Support of Claims 5

Support Needed for Claims 6

Common Importer Errors Identified 7

Appendices

APPENDIX I GLOSSARY OF TERMS

APPENDIX II EXAMPLES OF DIRECT PROCESSING OPERATION COSTS

APPENDIX III EXAMPLES OF SUGGESTED SOURCE RECORDS TO SUPPORT GSP CLAIMS

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

A Guide for Supporting GSP Claims

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The Generalized System of Preferences (GSP) is a program that provides duty-free treatment for products of developing countries, called beneficiary developing countries (BDCs). The list of designated countries, territories, and association of countries can be found in General Note 4 of the Harmonized Tariff Schedule of the United States (Annotated) (HTSUS). GSP is both country and product specific. Section 10.176 of the Customs Regulations states that to be eligible for GSP, the imported article must be the growth, product, or manufacture of the BDC. However, duty-free entry under GSP may be accorded only if the sum of (1) the cost or value of the materials produced in the BDC plus (2) the direct costs of processing operations performed in the BDC is not less than 35 percent of the appraised value of the merchandise.

BDCs are generally considered as a single country or territory, and all GSP requirements must be met in the one country. However, certain associations of countries are treated as one country. In the case of an association of countries, GSP requirements can be met in any of the countries within the association.

Generally, the specific statutory and regulatory requirements for claiming GSP are as follows:

- The country must be eligible as defined in General Note 4 of the HTSUS.
- Eligible articles shall be imported directly from the BDC in which they were produced to qualify for treatment under GSP.
- Merchandise must be grown, produced, or manufactured in a BDC. Materials that originate in another country must be substantially transformed in the BDC for the merchandise to be considered a “product of” the BDC.

Refer to Appendix I for definitions of specific terms used throughout this guide.

Information Sources/References

Following is a list of sources of information and/or references to regulations and rulings that affect the GSP area.

- GSP statutes and regulatory requirements are set forth in Title V of the Trade Act of 1974 (19 U.S.C. 2461-2465), as amended by the Customs and Trade Act of 1990, and in 19 Code of Federal Regulations (CFR) 10.171 through 10.178.
- Country of Origin Requirements: 19 CFR 10.176(a) and 10.176.
- Substantial Transformation Rule: 19 CFR 10.177(a)(2).
- No article will be considered to have been grown, produced, or manufactured in a BDC by virtue of having merely undergone simple (as opposed to complex or meaningful) combining or packaging operations or mere dilution with water or mere dilution with

another substance that does not materially alter the characteristics of the article: 19 CFR 10.176.

- "Double Substantial Transformation": Customs Service Decision (C.S.D.) 85-25 explains the application of 19 CFR 10.177 and partly overrules Treasury Decision (T.D.) 76-100, which was the basis for the so-called "double substantial transformation" rule. This rule has been applied since the inception of the GSP program and received explicit judicial approval (764F.2d 1563, 3 CAFC 158, 163 (Fed. Cir 1985)).
- Value Requirement: 19 CFR 10.176 through 10.178.
- The Trade and Development Act of 2000 amended the GSP to extend some enhanced benefits to sub-Saharan African countries. This is contained in new section 19 CFR 10.178a.
- Direct Importation Requirement: 19 CFR 10.174 and 10.175.
- Documentation and supporting records: 19 CFR 10.173 and T.D. 94-47. Additional documentation, including a foreign commercial invoice, can be required to verify that the merchandise qualifies for duty-free GSP treatment (C.S.D. 89-55).
- Unallowable general and administrative expenses (i.e., not direct costs of processing): HQ ruling 557087, dated 7/22/93; T.D. 81-282; T.D. 78-399; and C.S.D. 80-208.
- Dual sourcing of material (i.e., material from BDC and nonqualifying country): HQ ruling 556193, dated 12/23/91.
- Recordkeeping requirements for GSP records are outlined in 19 CFR 10.171 through 10.178. These documents shall be submitted within 60 days of the date of the request or such additional period that may be allowed for good cause shown. The Focused Assessment (FA) team may request records directly from the foreign vendor in accordance with 19 CFR 10.173 (a)(1)(i).

Focused Assessment Objectives

One of the first steps that the FA team takes is to determine whether the importer claimed any GSP during the review period. If there was no activity, then a GSP review is not necessary.

When GSP is applicable, it is essential that a good system of internal controls be in place to ensure ongoing compliance with GSP requirements. Focused assessments involve a review of the importer's GSP policies and procedures. The FA team assessment of internal controls consists of two parts: an understanding of the GSP internal control system and an evaluation of how accurately the system processes information. There are several questions importers could ask themselves regarding the controls in place to ensure that their claims qualify for GSP:

- What do I need to do to ensure that articles claimed for GSP are the growth, product, manufacture, or assembly of the BDC or any two or more countries that are members of the same association of countries?
- What assurance do I have that the supplier's value information is complete and accurate to support the GSP claim?
- Am I sure that the manufacturer(s) can provide proof of eligibility and all the required declarations at the time of purchase?
- When was the last time I assessed my GSP policies and procedures to ensure that they were accurate, in compliance with Customs rules and regulations, and working properly?
- Am I sure that the appropriate employees are receiving all updates on Customs laws, regulations, and rulings on GSP?
- In cases where an article claimed for GSP contains components from other than an eligible BDC, am I tracking the value of components separately for both the BDC and the other countries? Do I have access to the bills of materials for both types of components?

- Is an employee who possesses accurate and current knowledge reviewing GSP imports?
- Do I have the proper linking of GSP records as outlined in 19 CFR 10.171 through 10.178 to financial and accounting systems?

Regulatory Audit Policy (When Does Regulatory Audit Perform GSP Reviews?)

On July 23, 1997, U.S. Customs Service, Regulatory Audit Division, established policy for assessing compliance with respect to trade agreements. This policy established trade agreements as a priority issue in the 1997 Trade Enforcement Plan.

Prior to this policy, these trade programs were reviewed as separate audits or as part of the importer audit program. Regulatory Audit began including reviews of trade agreements as part of the Compliance Assessment process starting after October 1, 1997, and continued this practice in the subsequent FA process.

In the Pre-Assessment Survey (PAS) phase of the FA process, the FA team will evaluate the risk to Customs that the company's importing process relating to GSP may result in significant noncompliance with laws and regulations. If unacceptable risks are identified, the FA team will determine whether additional tests are required to quantify the extent of compliance and/or lost revenue.

Possible Sampling Frames

If it is determined that additional tests are required, the FA team may select its sample from the Automated Commercial System (ACS) or importer data, such as a database of GSP parts. The best method to efficiently determine the extent of compliance or loss of revenue should be used.

The FA team will focus on reviewing the accounting and inventory records, which support the ordering, manufacturing or production process, purchase, and shipment needed to support GSP eligibility of imported articles. If appropriate, the auditor will request and receive access to pertinent foreign accounting and inventory records and documentation.

If GSP internal controls are found to pose an unacceptable risk to Customs and/or if the compliance rate falls below 99 percent, GSP is considered noncompliant and the company will be requested to implement a Compliance Improvement Plan (CIP). As always, the FA team will discuss the conclusions with the company officials and obtain comments.

Responsibility for Support of Claims

In a case involving merchandise covered by a formal entry that is not wholly the growth, product, or manufacture of a single BDC, the exporter of the merchandise or other appropriate party having knowledge of the relevant facts shall be prepared to submit directly to the port director, upon request, a declaration setting forth all pertinent detailed information concerning the production or manufacture of the merchandise. *19 CFR 10.173(a)(1)(i)*

The information necessary for preparation of the declaration shall be retained in the files of the party responsible for its preparation and submission for 5 years. In the event that the port director requests submission of the declaration during the 5-year period, it shall be submitted by the appropriate party directly to the port director within 60 days of the date of the request or such additional period as the port director may allow for good cause shown. Failure to submit the declaration in a timely fashion will result in a denial of duty-free treatment. *19 CFR 10.173(a)(1)(ii)*

In developing detailed steps for verification of GSP entries, the GSP regulations require both

the U.S. importer and the BDC exporter to maintain certain information and documentation to substantiate GSP claims. Therefore, an examination of financial books, records, and documentation kept in the BDC may be necessary. As early in the audit as possible, auditors should request initial supporting documents in order to expedite the process. If the unrelated exporter is reluctant to provide the records to the importer, the exporter may be instructed to send the records directly to the FA team.

It will be presumed that the importer's claim for GSP cannot be supported if (1) the importer is unable to provide required supporting documentation within a reasonable time; and/or (2) the foreign producer refuses to provide, or is legally prevented from providing, that information. Any evidence submitted under Section 10.173 shall be subject to such verification as the port director deems necessary. In the event that the port director is prevented from obtaining the necessary verification, the port director may treat the entry as dutiable.

Support Needed for Claims

The importer should establish and implement a system of internal controls that demonstrate that reasonable care was exercised in the claim for duty-free treatment under GSP. These controls should include tests to ensure the accuracy and availability of records that evidence (1) the origin of the article when the imported article is wholly the growth, product, or manufacture of the BDC; or (2) the cost or value of the materials produced in a BDC, plus the direct processing costs in a BDC, is not less than 35 percent of the appraised value of the article at the time of its entry into the United States; and (3) that the article was imported into the United States directly from the BDC.

If the origin of the imported article is wholly the growth, product, or manufacture of a single BDC, then a statement to that effect shall be included on the commercial invoice provided to Customs. However, if the article is made from materials imported into the BDC, then the port director may require a GSP declaration to be prepared.

The GSP declaration identifies the following information:

1. number and date of invoice;

2. description of articles and quantity;

3. if processing operations are performed on articles:

   (a) description of processing operations and country of processing, and

   (b) direct costs of processing operations;

4. if materials are produced in a BDC or members of the same association, then:

   (a) description of material, production process, and country of production, and

   (b) cost or value of materials.

The origin of articles that are wholly the growth, product, or manufacture of the BDC must be supported by documents obtainable by the importer. The supporting documents may include trip reports, site visits, quality assurance reports, health and safety certificates prepared by government officials, and origin certificates prepared by government officials. Articles that are the product or manufacture of the BDC may require additional evidence to substantiate the manufacturing origin. Evidence may include raw materials purchases, proof of factory labor, and

support for manufacturing overhead.

The 35 percent value-content requirement may necessitate the submission of additional evidence of foreign manufacturing costs. Evidence may include product specifications, bills of materials, product cost sheets, payment records, overhead allocation schedules, raw material purchases, proof of factory labor, and support for manufacturing overhead. Production records must establish the value of the BDC materials used in the imported article on a lot-by-lot, batch-by-batch, shipment-by-shipment basis. Documentation and records supporting GSP must be verifiable by linkage to inventory and accounting records including summary records such as monthly production reports and accounts payable records.

Materials imported into a BDC may be included toward the value-content requirement when they undergo a double substantial transformation. In determining whether the value of a material may be counted toward the GSP 35 percent value-content requirement, a distinction must be made between the imported article and the materials of which it is composed. In the case of imported materials, the value of the material may be counted only if the imported material is first substantially transformed into a new and different article of commerce and then used in the BDC to produce the article imported into the United States. The importer's internal control system should include tests to accumulate such information to substantiate that a double substantial transformation occurred. Evidence may include flowcharts and videos of the manufacturing process, product design specifications, bills of materials, product cost sheets, overhead allocation schedules, raw material purchases, proof of factory labor, payment records, and support for manufacturing overhead.

The direct shipment to the United States should be supported by documents obtainable by the importer's internal control system. If a shipment from a BDC passes through the territory of any other country en route to the United States, the merchandise must not enter the commerce of the transient country. Documents supporting direct shipment may include bills of lading, freight or shipping invoices, and air waybills which show the United States as the final destination.

Appendix II identifies those costs of processing operations that are considered direct and those that are considered indirect and therefore not allowable when considering the value content requirement. Appendix III includes examples of source records that may support various cost categories. These lists are not all-inclusive. Importers may maintain different documents to support their claim. Documents used to support their claims depend upon the company’s account and inventory systems.

Common Importer Errors Identified

Since 1997, compliance assessments, which included a separate GSP sample (exceeded the $10 million dollar threshold), have shown that a significant number of companies have been considered noncompliant. Some of the most common errors identified include the following:

- Imported product did not undergo a double substantial transformation.
- Company was unable to produce records to support value-content provision.
- CBI countries are also GSP countries. Importer may claim GSP or CBI.
- Foreign manufacturer commingled materials purchased from both BDC and non-BDC suppliers and importer is unable to identify when non-BDC components were used in an imported article.
- U.S. goods returned were claimed as imported GSP articles.
- GSP articles were erroneously classified, and the correct classification was not eligible for GSP.
- Articles originated in an ineligible country.

- Importer could not provide evidence of direct shipment of the product from the BDC to the United States when the shipment entered a transient country en route to the United States.

Appendix I

Glossary of Terms

Association of Countries--A voluntary association of countries, as identified in the HTSUS, treated as one country for purposes of GSP.

Beneficiary Developing Country (BDC)--Country eligible for duty-free treatment under the GSP, as identified in the HTSUS.

Bill of Materials (BOM)--A list of parts included in a finished product, normally listing the part number, quantity, and cost of each component, in part number order.

Certificate of Origin (Manufacturer's Affidavit)--A written statement signed by a company officer attesting to the country in which the product was manufactured.

Country of Origin--The country of manufacture, production, or growth of any article of foreign origin entering the United States; consisting of the country in which the last "substantial transformation" of the product was effected.

Direct Costs of Processing--Those costs either directly incurred in or which can be reasonably allocated to the growth, production, manufacture, or assembly of the specific merchandise under consideration; not including profit and general expenses such as administrative salaries and marketing expenses.

Double Substantial Transformation--Material from outside the BDC which is substantially transformed in the BDC into a new and different article of commerce which is then used in the production of the final imported item.

Dual Sourcing--Sourcing the same material component from both qualifying and nonqualifying countries; the qualifying material becomes ineligible if commingled in inventory with nonqualifying material.

General and Administrative Costs--Costs that cannot be allocated to individual products and are instead usually allocated to all products over a "cost input base" consisting of total costs for material, labor, and overhead.

General System of Preference (GSP)--A program authorized by the Trade Act of 1974 to provide duty-free treatment for eligible articles imported directly from designated BDCs. Duty-free treatment under the GSP may be accorded to eligible articles that are the growth, product, manufacture, or assembly of a BDC country; imported into the territory of the United States directly from such BDC if the sum of (1) the cost or value of the materials produced in the BDC or any two or more BDCs that are members of the same association of countries, plus (2) the direct costs of processing operations performed in such BDC or member countries is not less than 35 percent of the appraised value of the merchandise.

GSP Declaration--A declaration setting forth all pertinent detailed information concerning the production or manufacture of the merchandise, in the format specified in 19 CFR 10.173(a)(1)(i).

Imported Directly--Direct shipment from a BDC to the United States without passing through the territory of any other country; or if passing through the territory of any other country, the merchandise does not enter into the retail commerce of any other country; and the rules prescribed in 19 CFR 10.175 are followed.

Materials Produced in a BDC--Materials that are wholly the growth, product, or manufacture of a BDC or materials from other countries which were substantially transformed in the BDC into a new and different article of commerce and are incorporated into the GSP article. The cost or value of materials is described in 19 CFR 10.177(c). Also see Double Substantial Transformation.

Overhead Costs--Product costs, other than material and labor, that may reasonably be allocated to individual products.

Produced in the Beneficiary Developing Country--The eligible article is either (1) wholly the growth, product, or manufacture of the BDC or (2) substantially transformed in the BDC into a new and different article of commerce.

Substantial Transformation--Occurs when an article emerges from a manufacturing process with a name, character, and use that differs from those of the original material subjected to the process; determined on a case-by-case basis.

Trial Balance--A list of each general ledger account and its ending balance for the purpose of verifying that total debits and credits balance at the end of the period.

Appendix II

Examples of Direct Processing Operation Costs

Cost Category	**Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282**	**Reference**	**Nonqualifying (Not directly attributable to the specific merchandise or that are not costs of manufacturing the product) T.D. 81-282**	**Reference**
Material	Manufacturer's actual cost for the materials.	19 CFR 10.177		
	When not included in the manufacturer's actual cost for the materials, the freight, insurance, packing, and all other costs incurred in transporting the materials to the manufacturer's plant.	19 CFR 10.177		
	The actual cost of waste or spoilage (material list), less the value of recoverable scrap.	19 CFR 10.177		
	Taxes and/or duties imposed on the materials by the BDC, or an association of countries treated as one country, provided they are not remitted upon exportation.	19 CFR 10.177		
Labor/Personnel	Fringe benefits provided to direct labor employees.	T.D. 78-399 C.S.D. 80-208	Administrative salaries.	T.D. 78-399 C.S.D. 80-208
	On-the-job training for those employees.	C.S.D. 85-25	Salesmen's salaries, commissions, or expenses.	C.S.D. 80-246
	Cost of transportation provided to direct labor employees.	C.S.D. 80-208	Compensation of a plant manager performing only administrative functions.	C.S.D. 80-208
	Expenses incurred in transporting personnel to and from the production facility to render services that are directly related to the production process.	C.S.D. 80-208	Plant security, accounting personnel, office supplies, telephone and telex, automobiles and trucks compensation.	C.S.D. 80-208
	Group insurance provided to production employees as a fringe benefit.	T.D. 78-399	Wages of an office worker who is responsible for the importation of raw materials.	C.S.D. 80-208
	Compensation, including fringe benefits, of material handlers, shipping, and receiving employees to the extent it is for handling of materials used in the production of subassemblies or the finished subassemblies.	T.D. 78-399	Cost of an employee who merely performs general administrative functions related to the shipment of the merchandise.	C.S.D. 80-208

Cost Category	**Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282**	**Reference**	**Nonqualifying (Not directly attributable to the specific merchandise or that are not costs of manufacturing the product) T.D. 81-282**	**Reference**
Labor/Personnel (cont.)	Cost of employees who receive, unload, and stock raw materials in the manufacturer's plant, distribute materials to the assembly, maintain storage areas and raw material inventory records, and pack and prepare the eligible articles for shipment.	C.S.D. 80-208		
	Cost of engineering, supervisory, quality control, and similar personnel.	C.S.D. 80-208		
	Compensation of group leader, quality control supervisors, and manufacturing foremen to the extent these personnel function as first-line supervisors of workers directly involved in the production operation.	C.S.D. 80-208		
	Cost of engineering personnel, including fringe benefits, if directly incurred in the production of the specific merchandise (pro rata portion).	C.S.D. 80-208		
	Facility maintenance expenses, including compensation of maintenance personnel to the extent they relate to the plant area where the subassemblies and articles are produced.	C.S.D. 80-208		
	Cost of production line employees, quality control personnel, and employees who are involved in the handling of raw materials upon receipt in the plant and the handling of goods in the packing and preparation for shipping.	C.S.D. 80-208		
	Plant manager's (or other administrative personnel) compensation, including fringe benefits, to the extent he functions as a first-line production foreman (percentage of such duties).	C.S.D. 80-208		
	Janitorial services costs to the extent incurred in the plant or factory area.	C.S.D. 80-208		
Labor/Personnel (cont.)	Social insurance for these employees (similar to unemployment or social security	C.S.D. 80-208		

Cost Category	**Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282**	**Reference**	**Nonqualifying (Not directly attributable to the specific merchandise or that are not costs of manufacturing the product) T.D. 81-282**	**Reference**
	taxes).			
	Payroll taxes for direct labor, direct supervision, inspection, and inspection supervision.	C.S.D. 80-208		
	Pro rata expense of work permits for U.S. labor for persons involved in production	C.S.D. 80-208		
Equipment	Cost of renting, repairing, maintaining, and modifying production machinery.	C.S.D. 80-246		
	Cost of repairs, parts, and lubricants used to keep the production machinery in running order.	C.S.D. 80-246		
	Dies, molds, tooling, and depreciation on machinery and equipment that are allocable to the merchandise.	T.D. 78-399		
Equipment (cont.)	Depreciation on machinery and equipment used in the production of the subassemblies and eligible article.	T.D. 78-399 C.S.D. 80-246		
	Assists (used in production of the eligible article).	T.D. 78-399		
Quality Control	Research, development, design, engineering, and blueprint costs as they are allocable to the specific merchandise (not undertaken in the United States).	T.D. 81-282		
Packaging	Packaging performed in a BDC and essential for the shipment of an eligible article to the United States.	C.S.D. 80-208		
	Cost of the packaging operation and cost or value of materials that are produced in the BDC, provided the packaging materials are nonreusable shipping containers.	C.S.D. 80-208		
Transportation			Inland freight charges and brokers' fees associated with the raw materials used in the production of the merchandise (okay as cost of raw materials).	T.D. 78-399 C.S.D. 80-208

Cost Category	**Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282**	**Reference**	**Nonqualifying (Not directly attributable to the specific merchandise or that are not costs of manufacturing the product) T.D. 81-282**	**Reference**
			Inland freight charges and brokers' fees associated with raw materials used in the production of the subassemblies (okay as cost of the raw materials).	T.D. 78-399 C.S.D. 80-208
Rent	Rent attributable to that portion of the building space directly used in the processing operations.	T.D. 78-399 C.S.D. 80-208	Rent on that portion of the building used for personnel offices, accounting departments, and other administrative functions.	T.D. 78-399
Taxes and Insurance	Pro rata share of taxes on the part of the building used in the processing operation.	C.S.D. 80-208	Sales taxes.	C.S.D. 80-208
Taxes and Insurance (cont.)	Cost of property insurance covering machinery and equipment used in the production process (with descriptive evidence).	C.S.D. 80-208	Casualty and liability insurance.	C.S.D. 80-208
Utilities	Cost of utilities, such as electricity, fuel, and water, to the extent they are actually used in the production process of the subassemblies and eligible article.	T.D. 78-399 C.S.D. 80-208 C.S.D. 80-246	Cost of electricity used for lighting or air conditioning administrative offices.	T.D. 78-399 C.S.D. 80-208 C.S.D. 80-246
	Heating costs to keep factory workers warm.	T.D. 78-399 C.S.D. 80-208 C.S.D. 80-246		
Other	Telecommunications costs incurred to facilitate the inspection of the merchandise and the first-line supervision of the production process (with proof).	T.D. 78-399 C.S.D. 80-208	Profit.	C.S.D. 84-104
	Pallets used in the storage of raw materials.	C.S.D. 80-208	General expenses of doing business that either are not allocable to the specific merchandise or are not related to the growth, production, manufacture, or assembly of the merchandise.	T.D. 78-399
Other (cont.)			Advertising.	T.D. 78-399
			Maintenance costs incurred for upkeep of administrative offices or other areas of the facility not related to the production area.	T.D. 78-399

Cost Category	**Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282**	**Reference**	**Nonqualifying (Not directly attributable to the specific merchandise or that are not costs of manufacturing the product) T.D. 81-282**	**Reference**
			General office expenses, mail and telecommunication costs.	T.D. 78-399
			Communication expenses without evidence that they bear a direct relation to the production process.	T.D. 78-399
			Cost of automobiles, depreciation on automobiles.	T.D. 78-399
			Office supplies.	C.S.D. 80-208
			Interest expense that has been capitalized.	C.S.D. 84-104
			Accounting services supplied to the foreign manufacturer.	T.D. 78-399
			Research and development, engineering, and blueprint cost undertaken in the United States.	C.S.D. 81-282
			Onsite medical personnel for workers.	C.S.D. 80-208
Notes:				
19 CFR= Part 19 of the Code of Federal Regulations				
T.D.=Treasury Decision				
C.S.D.=Customs Service Decision				
BDC = beneficiary developing country				

Examples of Suggested Source Records to Support GSP Claims

Cost Category	Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282	Source Record(s) This list is designed to provide companies involved in making GSP claims with the records that provide the best support for their claims. However, each company may utilize and maintain different records. Further, proper support may be achieved with a portion of the records mentioned.
Material	Manufacturer's actual cost for the materials.	GSP declaration, cost sheets, bill of materials, cost of goods sold, general ledger, vendor invoices, material price variance accounts, purchase history reports, inventory records, approved vendor listing by part.
	When not included in the manufacturer's actual cost for the materials, the freight, insurance, packing, and all other costs incurred in transporting the materials to the manufacturer's plant.	GSP declaration, cost sheets, bill of materials, cost of goods sold, general ledger, invoices (freight, insurance, and packing).
	Taxes and/or duties imposed on the materials by the BDC, or an association of countries treated as one country, provided they are not remitted upon exportation.	GSP declaration, cost sheets, bill of materials, cost of goods sold, general ledger, tax bills, duty accounts, and broker bills.
	The actual cost of waste or spoilage (material list), less the value of recoverable scrap.	Product yielding reports, sales invoices relating to waste shipments.
Labor/Personnel	Fringe benefits provided to direct labor employees.	GSP declaration, cost sheets, bill of materials. Manufacturing or engineering studies detailing basis for amount of direct labor required to produce product. General ledger detail for direct labor and fringes. Direct labor variance accounts.
	On-the-job training for those employees.	GSP declaration, cost sheets, general ledger detail for job training expense accounts.
	Cost of transportation provided to direct labor employees.	GSP declaration, cost sheets, general ledger detail for transportation of employees' expense accounts.
	Expenses incurred in transporting personnel to and from the production facility to render services that are directly related to the production process.	GSP declaration, cost sheets, general ledger detail for transportation of employees' expense accounts.
	Group insurance provided to production employees as a fringe benefit.	GSP declaration, cost sheets, general ledger detail for insurance expenses, insurance policies, and premium invoices.
Labor/Personnel (cont.)	Compensation, including fringe benefits, of material handling, shipping, and receiving	GSP declaration, cost sheets, bill of materials. Manufacturing or engineering studies detailing basis for amount of indirect labor required to

Cost Category	Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282	Source Record(s) This list is designed to provide companies involved in making GSP claims with the records that provide the best support for their claims. However, each company may utilize and maintain different records. Further, proper support may be achieved with a portion of the records mentioned.
	employees to the extent it is for handling of materials used in the production of subassemblies or the finished subassemblies.	produce product. General ledger detail for indirect labor and fringes. Indirect labor variance accounts.
	Cost of employees who receive, unload, and stock raw materials in the manufacturer's plant, distribute materials to the assembly, maintain storage areas and raw material inventory records, and pack and prepare the eligible articles for shipment.	GSP declaration, cost sheets, bill of materials. Manufacturing or engineering studies detailing basis for amount of indirect labor required to produce product. General ledger detail for indirect labor and fringes. Indirect labor variance accounts.
	Cost of engineering, supervisory, quality control, and similar personnel.	GSP declaration, cost sheets, bill of materials, and support of how factory overhead was identified and allocated to product. The specific general ledger expense accounts that contain qualifying overhead costs must be identified. Further analysis of the accounts includes supporting accounting ledgers and cost accumulation information that detail the specific personnel and how they support the manufacturing operation. This includes job descriptions of the support personnel and the management, engineering, and quality control personnel involved in the direct support of the production process.
	Compensation of group leader, quality control supervisors, and manufacturing foremen to the extent these personnel function as first-line supervisors of workers directly involved in the production operation.	GSP declaration, cost sheets, bill of materials, and support of how factory overhead was identified and allocated to product. The specific general ledger expense accounts that contain qualifying overhead costs must be identified. Further analysis of the accounts includes supporting accounting ledgers and cost accumulation information that detail the specific personnel and how they support the manufacturing operation. This includes job descriptions of the management and supervisory personnel involved in the direct support of the production process.
Labor/Personnel (cont.)	Cost of engineering personnel, including fringe benefits, if directly incurred in the production of the specific merchandise (pro rata portion).	GSP declaration, cost sheets, bill of materials, and support of how factory overhead was identified and allocated to product. The specific general ledger expense accounts that contain qualifying overhead costs must be identified. Further analysis of the accounts includes supporting accounting ledgers and cost accumulation information that detail the specific

Cost Category	Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282	Source Record(s) This list is designed to provide companies involved in making GSP claims with the records that provide the best support for their claims. However, each company may utilize and maintain different records. Further, proper support may be achieved with a portion of the records mentioned.
		personnel and how they support the manufacturing operation. This includes job descriptions of the engineering personnel involved in the direct support of the production process.
	Facility maintenance expenses, including compensation of maintenance personnel to the extent they relate to the plant area where the subassemblies and articles are produced.	GSP declaration, cost sheets, bill of materials, and support of how factory overhead was identified and allocated to product. The specific general ledger expense accounts that contain qualifying overhead costs must be identified. Further analysis of the accounts includes supporting accounting ledgers and cost accumulation information that detail the specific personnel and how they support the manufacturing operation. This includes job descriptions of the support personnel involved in the direct support of the production process.
	Cost of production line employees, quality control personnel, and employees who are involved in the handling of raw materials upon receipt in the plant and the handling of goods in packing and preparation for shipping.	GSP declaration, cost sheets, bill of materials, and support of how factory overhead was identified and allocated to product. The specific general ledger expense accounts that contain qualifying overhead costs must be identified. Further analysis of the accounts includes supporting accounting ledgers and cost accumulation information that detail the specific personnel and how they support the manufacturing operation. This includes job descriptions of the support and quality control personnel involved in the direct support of the production process.
Labor/Personnel (cont.)	Plant manager's (or other administrative personnel) compensation, including fringe benefits, to the extent he functions as a first-line production foreman (percentage of such duties).	GSP declaration, cost sheets, bill of materials, and support of how factory overhead was identified and allocated to product. The specific general ledger expense accounts that contain qualifying overhead costs must be identified. Further analysis of the accounts includes supporting accounting ledgers and cost accumulation information that detail the specific personnel and how they support the manufacturing operation. This includes job descriptions of the management personnel involved in the direct support of the production process.
	Janitorial services costs to the extent incurred in the plant or factory area.	GSP declaration, cost sheets, bill of materials, and support of how factory overhead was identified and allocated to product. The specific general ledger expense accounts that contain qualifying overhead costs must be identified.

Cost Category	Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282	Source Record(s) This list is designed to provide companies involved in making GSP claims with the records that provide the best support for their claims. However, each company may utilize and maintain different records. Further, proper support may be achieved with a portion of the records mentioned.
		Further analysis of the accounts includes supporting accounting ledgers and cost accumulation information that detail the specific personnel and how they support the manufacturing operation. This includes job descriptions of the support personnel involved in the direct support of the production process.
	Social insurance for these employees (similar to unemployment or social security taxes).	GSP declaration, cost sheets, social insurance tax accounts.
	Payroll taxes for direct labor, direct supervision, inspection, and inspection supervision.	GSP declaration, cost sheets, tax bills showing whom taxes are paid for.
	Pro rata expense of work permits for U.S. labor for persons involved in production.	GSP declaration, cost sheets, expense accounts for permits.
Quality Control	Research, development, design, engineering, and blueprint costs as they are allocable to the specific merchandise (not undertaken in the United States).	GSP declaration, cost sheets, bill of materials, and support of how research and development (R&D) was identified and allocated to product. The specific general ledger expense accounts that contain qualifying R&D must be identified. Further analysis of the accounts includes supporting accounting ledgers and cost accumulation information that detail the specific R&D costs.
Equipment	Cost of renting, repairing, maintaining, and modifying production machinery.	Manufacturing studies detailing the equipment utilized in production of the product and time required. General ledger detail listing the rental, repair, maintenance, and modification expense accounts relating to the required equipment.
	Cost of repairs, parts, and lubricant used to keep the production machinery in running order.	Manufacturing studies detailing the equipment utilized in production of the product and time required. General ledger detail listing the repair and maintenance expense accounts relating to the required equipment.
	Dies, molds, tooling, and depreciation on machinery and equipment that are allocable to the merchandise.	Manufacturing studies detailing the equipment utilized in production of the product and time required. General ledger detail listing the depreciation expenses relating to the required equipment.
	Depreciation on machinery and equipment used in the production of the subassemblies and eligible article.	Manufacturing studies detailing the equipment utilized in production of the product and time required. General ledger detail listing the depreciation expenses relating to the required equipment.
	Assists (used in production of the eligible article).	Purchase accounts, general ledger (machinery and equipment accounts), customer contracts,

Cost Category	Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282	Source Record(s) This list is designed to provide companies involved in making GSP claims with the records that provide the best support for their claims. However, each company may utilize and maintain different records. Further, proper support may be achieved with a portion of the records mentioned.
		fixed asset register (records showing location of machinery/equipment).
Rent	Rent attributable to that portion of the building space directly used in the processing operations.	Production space and utilization studies to support the proration of these expenses to the manufacturing operations. Invoices for rent and general ledger detail listing these expenses for the production period.
Taxes and Insurance	Pro rata share of taxes on the part of the building used in the processing operation.	Production space and utilization studies to support the proration of these expenses to the manufacturing operations. Invoices for taxes and insurance and general ledger detail listing these expenses for the production period.
	Cost of property insurance covering machinery and equipment used in the production process (with descriptive evidence).	Production space and utilization studies to support the proration of these expenses to the manufacturing operations. Invoices for insurance and general ledger detail listing these expenses for the production period.
Utilities	Cost of utilities, such as electricity, fuel, and water, to the extent they are actually used in the production process of the subassemblies and eligible article.	Production space and utilization studies to support the proration of these expenses to the manufacturing operations. Invoices for utilities and general ledger detail listing these expenses for the production period.
	Heating costs to keep factory workers warm.	Production space and utilization studies to support the proration of these expenses to the manufacturing operations. Invoices for utilities and general ledger detail listing these expenses for the production period.
Packaging	Packaging performed in a BDC and essential for the shipment of an eligible article to the United States.	Each company has its specific expenses involved in the manufacturing process that are not recorded in the above-mentioned accounts. The support for these expenses would involve detailing how the expenses related to manufacture of the product (job descriptions, product requirements listed in customer contracts) and the amount of the expenses incurred (general ledger detail of amounts recorded as expenses along with supporting invoices if applicable).
	Cost of the packaging operation and cost or value of materials that are produced in the BDC, provided the packaging materials are nonreusable shipping containers.	Each company has its specific expenses involved in the manufacturing process that are not recorded in the above-mentioned accounts. The support for these expenses would involve detailing how the expenses related to manufacture of the product (job descriptions, product requirements listed in customer contracts) and the amount of the expenses incurred (general ledger detail of amounts

Cost Category	Qualifying (Directly incurred in, or reasonably allocated to, the growth, production, manufacture, or assembly of the specific merchandise) T.D. 81-282	Source Record(s) This list is designed to provide companies involved in making GSP claims with the records that provide the best support for their claims. However, each company may utilize and maintain different records. Further, proper support may be achieved with a portion of the records mentioned.
		recorded as expenses along with supporting invoices if applicable).
Other	Telecommunications costs incurred to facilitate the inspection of the merchandise and the first-line supervision of the production process (with proof).	Each company has its specific expenses involved in the manufacturing process that are not recorded in the above-mentioned accounts. The support for these expenses would involve detailing how the expenses related to manufacture of the product (job descriptions, product requirements listed in customer contracts) and the amount of the expenses incurred (general ledger detail of amounts recorded as expenses along with supporting invoices if applicable).
Other (cont.)	Pallets used in the storage of raw materials.	Each company has its specific expenses involved in the manufacturing process that are not recorded in the above-mentioned accounts. The support for these expenses would involve detailing how the expenses related to manufacture of the product (job descriptions, product requirements listed in customer contracts) and the amount of the expenses incurred (general ledger detail of amounts recorded as expenses along with supporting invoices if applicable).

Not Used

Exhibit 4H – See Exhibit 3D

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Importer Quantification
(Formerly Known as Controlled Assessment Methodology)

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The FA program consists of two processes. During the first process, the Pre-Assessment Survey (PAS), the team determines the risk exposure to U.S. Customs and Border Protection (Customs) of an importer's various operations and evaluates the adequacy of the company's internal control to manage the risk. If the FA team identifies risks, it may be necessary for the FA program to proceed to the second process, Assessment Compliance Testing (ACT), to quantify either a revenue loss or the degree of compliance/noncompliance.

Procedures

Because Customs, not the importer, must assess risk, the importer cannot perform the evaluation of risk in the PAS process. However, if Customs determines that additional testing is necessary to quantify compliance or revenue, the importer may choose to do an Importer Quantification. This quantification by the importer would eliminate the need for Customs to do ACT for that issue. Customs will work with the company to determine an appropriate method for quantifying revenue loss or compliance, using statistical sampling designed for the FA process or some other appropriate method cooperatively developed between Customs and the importer. Customs will verify the information developed during the Importer Quantification to the degree considered necessary.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

PAS Internal Control Overview

Introduction

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The Focused Assessment (FA) program is designed to assess a company's risk of noncompliance in Customs activities. The FA program consists of two parts, the Pre-Assessment Survey (PAS) and Assessment Compliance Testing (ACT). In order to assess the risk of noncompliance, an evaluation is made of the company's internal control during the PAS. If it is necessary to quantify the extent of noncompliance or loss of revenue, it may be necessary to proceed to the ACT process. This technical guide identifies tools that have been developed to use in the PAS process.

Internal Control Tools

The following tools, which have been developed to assist in the evaluation of adequacy of internal control for Customs compliance, are available in the FA Program documents:

1. Technical Information for Pre-Assessment Survey (TIPS) (formerly titled PAS Internal Control Technical Guides). These tools are required to be used. They are the primary tools for the PAS process. A separate guide is provided for each review area, classification, value, each special trade program, special duty provision, etc.

2. Guidance for Using Risk Exposure to Determine Review Areas. This is a guidance document. It will help the FA team determine what review areas should be included in the FA. The purpose of the tool is to assure consistent, uniform reviews and limit the use of Customs resources to areas of true risk to Customs.

3. Consideration of Internal Control in a Customs Compliance Audit. This is a guidance document. It provides general guidance for Customs compliance audits of internal control. It includes general information about internal control and specific guidance for Customs auditors to use when evaluating the adequacy of internal control to assure compliance.

4. Internal Control Summary by Component. This tool is not required to be used. It is intended to help auditors evaluate whether internal controls are adequate for each control component for Regulatory Audit Management Information System (RAMIS) reporting.

5. Internal Control Management and Evaluation Tool. This tool is not required to be used. It is intended to help management and evaluators determine how well a company's internal control is designed and functioning, what improvements are needed, and where and how needed improvements may be implemented. This tool may be useful to evaluate internal control, particularly when auditing large, complex organizations that may require more

complex internal control.

6. Guidance for the Internal Control Interviewing Process. This tool is not required to be used. It is a guidance tool that provides example questions that can be used to obtain information needed to evaluate the adequacy of internal controls. The examples are intended to illustrate the type of questions that may be used to evaluate each internal control component and may be used as deemed necessary.

7. Sample Internal Control Manual. This tool is not intended to be all-inclusive or appropriate for all companies. It illustrates how some internal controls can be developed and organized in a typical midsize company.

TRANSACTION VALUE
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 TRANSACTION VALUE GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS 5
A. Red Flags for TV in General 5
B. Red Flags for PAPP.....5
C. Red Flags for Sales Commissions 6
D. Red Flags for Royalties.....6
E. Red Flags for Assists.....6
F. Red Flags for Packing 6
G. Red Flags for Proceeds.....7
2.2 EXAMPLES OF BEST PRACTICES 7
A. Best Practices for TV in General.....7
B. Best Practices for PAPP 7
C. Best Practices for Sales Commissions 8
D. Best Practices for Royalties.....8
E. Best Practices for Assists.....8
F. Best Practices for Packing 8
G. Best Practices for Proceeds 8
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 8

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 9

3.1 RISK 9
A. Preliminary Assessment of Risk.....9
B. Evaluation of Risk Acceptability 9
3.2 INTERNAL CONTROL.....10
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMITS) 11
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....11
3.5 EXAMPLES.....12

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – TRANSACTION VALUE 15

TRANSACTION VALUE
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The objective of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for transaction value and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and the terms in this technical guide are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78*.

PART 2 TRANSACTION VALUE GUIDANCE

19 U.S.C. 1401(a), the Statement of Administrative Action (accompanying the Trade Agreements Act of 1979), 19 CFR 152.103, and the Customs Valuation Encyclopedia are the basic sources of information on transaction value (TV). In addition, research on Customs Rulings and Customs Service Decisions (CSD) and decisions of the Court of International Trade should be considered. The determination of the proper basis of valuation is within the authority of the Office of Field Operations.

19 CFR 152.101(b) provides that merchandise will be appraised on the basis, and in the order, of the following: TV, TV of identical merchandise, TV of similar, deductive value, computed value, and derived value. This technical guide is limited to TV, the first-order of basis of value.

In 19 CFR 152.102(a), "Assist" means any of the following if supplied directly or indirectly, and free of charge or at a reduced cost, by the buyer of imported merchandise for use in connection with the production or the sale for export to the United States of the merchandise:

(i) Materials, components, parts, and similar items incorporated in the imported merchandise.

(ii) Tools, dies, molds, and similar items used in the production of the imported merchandise.

(iii) Merchandise consumed in the production of the imported merchandise.

(iv) Engineering, development, artwork, design work, and plans and sketches that are undertaken elsewhere than in the United States and are necessary for the production of the imported merchandise.

19 CFR	Information Provided
152.103(a) Derivation of price actually paid or payable (PAPP)	Describes how the PAPP is derived as well as elements to be included, such as indirect payments, cost of assembly, rebates, foreign inland freight, and other charges incident to the international shipment of the merchandise.
152.103 (b) Additions to the PAPP	Lists the additions to the PAPP, including packing costs incurred by the buyer, selling commissions incurred by the buyer, assists, royalty or license fees, and proceeds of subsequent resale.
152.103(c) Sufficiency of Information	Specifies that additions to the PAPP will be made only if there is sufficient information to establish the accuracy of the additions and the extent to which they are not included in the price.
152.103(d) Value of Assists	Specifies that if the value of an assist is to be added to the PAPP or to be used as a component of computed value, the port director shall determine the value of the assist and apportion that value to the price of the imported merchandise in the following manner: (1) If the assist consists of materials, components, parts, or similar items incorporated in the imported merchandise, or items consumed in the production of the imported merchandise, acquired by the buyer from an unrelated seller, the value of the assist is the cost of its acquisition. If the assist was produced by the buyer or a person related to the buyer, its value would be the cost of its production. In either case, the value of the assist would include transportation costs to the place of production. (2) If the assist consists of tools, dies, molds, or similar items used in the production of the imported merchandise, acquired by the buyer from an unrelated seller, the value of the assist is the cost of its acquisition. If the buyer or a person related to the buyer produced the assist, its value would be the cost of its production. If the assist has been used previously by the buyer, regardless of whether it had been acquired or produced by him, the original cost of acquisition or production would be adjusted downward to reflect its use before its value could be determined. If the buyer leased the assist from an unrelated seller, the value of an assist would be the cost of the lease. In either case, the value of the assist would include transportation costs to the place of production. Repairs or modifications to an assist may increase its value.
152.103(e) Apportionment Of Assists	Specifies that apportionment of the value of assists will include the following methods when the entire production is destined for the United States: over the first shipment, over the number of units produced up to the first shipment, over the entire anticipated production, or another method requested by the importer that is in accordance with generally accepted accounting principles.

19 CFR	Information Provided
152.103(f) Royalties	Lists criteria for determining the dutiability of royalties or license fees (patents, copyrights and trademarks).
152.103(g) Proceeds	Specifies that the value of proceeds of any subsequent resale, disposal, or use of imported merchandise that accrues directly or indirectly to the seller is considered as an addition to the PAPP.
152.103(h) Reproduction Fees	Specifies that charges for the right to reproduce the imported merchandise in the United States will not be added to the PAPP.
152.103(i) TV Exclusions	TV does not include any reasonable cost or charges of the following, if identified separately from PAPP, that is incurred for construction, erection, assembly, or maintenance technical assistance provided to the merchandise transportation after importation into the United States for Customs duty federal taxes currently payable on the merchandise by reason of its importation.
152.103(j) Limitations on Use of TV	Specifies that limitations on the use of TV of imported merchandise will be the appraised value if (i) there are no restrictions on the disposition or use of the imported merchandise by the buyer other than those imposed or required by law, limit geographical area in which merchandise by be resold, or do not affect substantially the value of the merchandise; (ii) the sale of, or the PAPP for, the imported merchandise is not subject to any condition or consideration for which a value cannot be determined; (iii) no part of the proceeds of any subsequent resale, disposal, or use of the imported merchandise by the buyer will accrue directly or indirectly to the seller, unless an adjustment can be made; and (iv) the buyer and seller are not related, or the buyer and seller are related but transaction value is acceptable.
152.103(j)(2) Related Person Transactions	Specifies that the TV between a related buyer and seller is acceptable if an examination of the circumstances of sale indicates that their relationship did not influence the PAPP, or if the TV of the imported merchandise closely approximates a value in paragraph (A),(B), or (C) of this subsection.
152.103(k) Restrictions and Conditions of Sale	Specifies that a restriction placed on the buyer of the imported merchandise that does not substantially affect its value will not prevent the use of TV as the appraised value.
152.103(l) Related Buyer and Seller	Specifies that in a validation of transaction, the port director shall not disregard a TV solely because buyer and seller are related. The importer or buyer may demonstrate that the TV in a related-person transaction is acceptable by showing that the value “closely approximates” a test value.
152.103(m) Rejection of TV	Specifies that when Customs has grounds for rejecting the TV declared by the importer and when that rejection increases the duty liability, the importer shall be informed. The importer will be afforded 20 days to respond in writing.

2.1 EXAMPLES OF RED FLAGS

The following examples of red flags (conditions that may indicate a potential problem in transaction value) are broken down into seven categories: TV in general, PAPP, sales commissions, royalties, assists, packing, and proceeds.

A. Red Flags for TV in General

- The company has insufficiently documented, poorly defined, or no internal control for accurately declaring value for Customs purposes.
  - ✓ The company does not monitor or interact with the broker on value issues.
  - ✓ The company relies on one employee to handle value issues, and there are poor or no management checks or balances over this employee.
- Company import staff lacks knowledge of Customs valuation.
- The company offers unreasonable explanations to Customs.
- The company fails to cooperate with or respond to Customs.
- The company has a high turnover of people in key positions.
- Significant variance exists between the importer's data and data submitted to Customs.
- Customs (e.g., import specialist, account manager, compliance measurement, prior audit, other profile information) shows a history of problems with value (e.g., assists).
- The transactions are related-party transactions.
- Merchandise is shipped on consignment.
- A large number of prior disclosures (PDs) are based on value issues.
- Transactions are tiered transactions (e.g., Nissho-Iwai).
- Values are abnormally low.
- Interest payments are not attributable to late payment charges.
- Company is subject to a restriction as to disposition or use of the imported merchandise.
- Sales are tie-in sales.
- Invoices have penned and ink changes.
- Company frequently replaces brokers in the same port.

B. Red Flags for PAPP

- Retroactive or renegotiated price adjustments outlined in purchase contracts may make imports ineligible for TV.
- Warranty replacement parts are declared at less than TV.
- Company has currency conversion risk-sharing agreements.
- Unsubstantiated/estimated nondutiable charge deductions are used for entry.
- Advance or supplemental payments/deposits have been made to vendors.
- Company reimburses the foreign vendor for tooling.
- Company frequent uses pro forma invoices or invoices indicating "Customs Use only," "Customs Purposes Only," or "Free-house delivery."
- Company has indirect payment agreements.
- Renegotiated terms such as cost and freight (C&F) are not supported by documentation.
- Invoice terms are CMT (cut, make, and trim) and exclude raw materials (e.g., textile importers may not include the cost of material).
- Company has tolling agreements (e.g., chemical importers may have such transactions that do not include the cost of the raw materials to be processed).

C. Red Flags for Sales Commissions

- Company has specific accounts for recording agent fees or commissions.
- Company does not have formal agreements with agents.
- Sales commissions are not reported on the import invoice.
- A sales office wholly owned by the foreign seller is receiving merchandise at a discount for domestic sale.
- Agent fees are paid to a “buying agent” that is the foreign manufacturer.
- Agent agreements are verbal and not in writing.
- Sales commission agreements either are not in writing or are in writing but incomplete as to essential terms.
- The buying agent does not act for the benefit of the importer, buys on its own account, retains title, and bears the risk of loss for the merchandise.
- The company cannot produce an invoice from the manufacturer/seller.
- The importer has an exclusive agreement with the manufacturer or ultimate consignee.

D. Red Flags for Royalties

- Company has specific accounts for recording royalties, or company does not have a tracking system for royalties.
- Company makes additional payments to the seller for the right to use the import as a condition of sale.
- Company makes payments to a party who is both the seller and a licensor of the technology.
- Company makes payments to a third party that is related to the seller.

E. Red Flags for Assists

- Company has accounts for recording assists, tools, dies, molds, or similar items used in production, or company does not have a tracking system for assists.
- Foreign research and development necessary for production is not included in invoiced value.
- Design, development and engineering charges are necessary for production.
- Merchandise is exported to foreign vendors or manufacturers.
- The importer is a nonmanufacturing importer (e.g., sales office) with manufacturing equipment depreciation or credits to fixed asset accounts (unreported assists).
- Advance or supplemental payments/deposits are made to vendors.
- Assist payments are made to a domestic company with a foreign subsidiary.
- For reported assists, freight and related transportation charges paid by a buyer in connection with shipments of material are not included.
- For reported assists, the value of waste and scrap is deducted from the invoiced value.

F. Red Flags for Packing

- Company has an account for recording packing.
- Foodstuff invoices do not have charges for icing (freezing) or charges for preserving purchased perishable merchandise.

- Additional payments were made to the seller for price tags, labels, and hangtags.
- A “service charge” (e.g., for hanging garments in containers) was necessary to place the goods in shipping condition.
- There are descriptions such as GOH (garments on hangers) charges.
- There are “stuffing charges” for containerization of merchandise.

G. Red Flags for Proceeds

- Company has an account for recording proceeds of sales.
- A “royalty” is paid on the basis of the domestic sale of imported merchandise.
- Profit-sharing agreements between related parties split the profits of a domestic sale.
- Annual payments are based on total sales or purchases of imported merchandise.
- Additional payments are related to currency fluctuations.
- Prices were unusually low at the time of importation.

2.2 Examples of Best Practices

The following best practices are broken down into seven categories: (1) TV in general, (2) PAPP, (3) sales commissions, (4) royalties, (5) assists, (6) packing, and (7) proceeds.

A. Best Practices for TV in General

- Internal controls over Customs matters:
  - ✓ Are in writing,
  - ✓ Include procedures for monitoring and feedback, and
  - ✓ Are monitored by management.
- One manager is responsible for control of the Import Department, including value. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- The company has good interdepartmental communication about Customs matters.
- The company conducts and documents periodic reviews of value and uses the results to make corrections to entries and changes to its import operations as appropriate.
- The company has access to and knowledge of the U.S. Customs Valuation Encyclopedia.
- The company has access to and knowledge of value binding rulings.
- The company attends Customs informed compliance outreach and seminars or Customs-related seminars provided by private vendors regarding value issues.
- The accounting system can link specific purchase orders, invoices, and payment records to Customs entry numbers.

B. Best Practices for PAPP

- The company has good interdepartmental communication about Customs matters.
- The purchase order matches the invoice, or differences are explained with written documentation.

- The company maintains the Informed Compliance publication on value.
- The company consults with Customs and requests binding rulings on complex value issues.
- The company maintains insurance and freight to support cost, insurance, and freight deductions.
- The company has records and/or procedures that explain differences.
- Visa value and terms of sale match the invoice and purchase order, or differences are explained.

C. Best Practices for Sales Commissions

- The company has written agreements with its agents specifying their relationship and roles and flexibility in selecting manufacturers.
- Sales commissions are shown as a separate item on the invoice.

D. Best Practices for Royalties

- The royalty or licensing agreement indicates (1) what the royalties are for (e.g., patents covering a manufacturing process, the use of a copyright or trademark), (2) whether the buyer had to pay them as a condition of the sale, and (3) to whom and under what circumstances they were paid.
- Royalty agreements are on file and readily available.
- The company maintains written records documenting royalty calculation.

E. Best Practices for Assists

- A specific position or management coordinates all assists.
- The company maintains a tracking system for assists.
- The company maintains records of assist details, for example:
  - ✓ How assists are prorated or apportioned on Customs entries
  - ✓ How assists record the transportation costs of assists to the place of production

F. Best Practices for Packing

- The company maintains records showing that:
  - ✓ It incurred charges for containers, coverings, labor, or materials used in placing merchandise in condition to ship to the United States.
  - ✓ No charge was incurred for returnable containers (e.g., heavy returnable containers for shipping auto parts).

G. Best Practices for Proceeds

- The company has procedures in place to ensure that payments for subsequent resale, disposal, or use of imported merchandise that accrues directly or indirectly to the seller are declared.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to value.
- Documentation that supports monitoring and verification of established and/or written internal control for value.
- Other documents affecting value, including purchase orders and confirmations, contracts (both sales contracts and performance contracts such as R&D, contracts), agency agreements, and risk sharing agreements.
- Buying agent agreement.
- Royalty and licensing agreements.
- Value rulings.
- Import Specialists' CF 28s and CF 29s regarding value issues.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company 's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment
   - Risk Assessment
   - Control Activities
   - Information and Communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal controls over value. (Examples of documents and information to review are listed above.)

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence of communication with the broker and company departments on value issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Company-specific rulings requested and evidence that they are followed.
   - Documentary evidence of intercompany communications to ensure correct information is provided to Customs.
   - Training records and materials used to educate staff on Customs matters.
   - Evidence that pricing information is periodically reviewed and updated (The correct basis of appraisement may be an issue.)
   - Evidence that payment accounts accurately reflect Customs activity.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) over Transaction Value in PART 4 of this document.

   Examples of inclusions to TV
   - Basis of appraisement
   - Price actually paid or payable
     - ✓ Currency exchange adjustments
     - ✓ Price adjustments (e.g., rebates, allowances, renegotiations, credits)
     - ✓ Indirect payments (e.g., payment of seller's debt by buyer)
     - ✓ Quota/Visa charges
     - ✓ Transportation costs
   - Statutory additions to the price actually paid or payable:
     - ✓ Packing

- ✓ Selling commissions
- ✓ Assists
- ✓ Royalties and license fees
- ✓ Proceeds for subsequent resale

Note: The internal control assessment should include steps to:

- Identify and understand internal control.
- Determine what is already known about control effectiveness.
- Assess the adequacy of internal control design.
- Determine whether controls are implemented and effective.
- Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMITS)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In such cases, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the TV level that will be reported on. For example, the table does not limit the PAS team to 20 tests for transaction value. The team may test 1 to 20 items to evaluate accuracy of price paid and 1 to 20 items for each of various additions, assists, or other components reportable to Customs.

Evidence of exceptional internal control, such as linking specific purchase orders, invoices, and payment records to Customs entry numbers may decrease the need for substantive tests.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review/ Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over transaction value.

1. Complete the "Worksheet for Evaluating Internal Control Over Transaction Value" to determine whether risk determination is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will help the PAS team determine whether conditions warrant proceeding to ACT:

   Do not proceed to ACT if:
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the value error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   Proceed to ACT if:
   - The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS *are for clarification only*:

Example A: Situation in which the team would not proceed to ACT (Revenue)

The company's written procedures require the Customs Department to provide the broker with regular, timely updates on price changes. The broker in turn notifies Customs of any adjustments to entered value.

To determine whether this control was working, the PAS team:

- ✓ Reviews the company's broker correspondence file for evidence of price adjustment notification
- ✓ Finds several letters notifying the broker of price adjustments over the past 6 months

In reviewing the letters, the PAS team determines that a retroactive price adjustment was not accurately disclosed to the broker or Customs. The PAS team finds that one retroactive price adjustment for $1,200,000 was reported as $120,000. The company agrees that the Customs manager had not been monitoring the situation.

The new procedure is for the Import Department employee to prepare a monthly report identifying all price changes and effective dates. The manager will review the report. The manager will then verify that (1) the broker received notification and (2) any value adjustments to previously entered merchandise were submitted to Customs on a timely basis. The Import Department will perform an analysis to identify all entries understated due to unreported price adjustments and submit the findings for Customs review.

The PAS team is satisfied that this modification to internal control is sufficient to prevent the error in the future. As a result, the team agrees that no further effort is necessary. The team agrees to verify implementation and effectiveness during an FA follow-up. Therefore, PAS does not proceed to ACT (Revenue).

Example B: Situation in which the team would not proceed to ACT (Compliance)

The importer has internal control over selling commissions. These written procedures require that invoices submitted with selling commissions be verified by the Import Department to include the selling commissions in entered value.

To determine whether this control is working, the PAS team Interviews the import department personnel. The Import Department person states that he followed the company procedures but has no documentation to support the claim. The team is not satisfied with the response. The merchandise was duty free and from Canada. The company acknowledges that there is a compliance problem and agrees to take the necessary action. The team verifies that the new controls are implemented to prevent future valuation errors. As a result, the team determines that it does not need to proceed to ACT (Compliance).

Example C: Situation in which the team would proceed to ACT (Revenue)

With the same fact pattern as example A, the team determines that the company's employees are not following the stated internal control procedures, therefore rendering the procedures ineffective in preventing errors. The company discloses that it has retroactive price adjustments and states that it is satisfied that most of the changes were disclosed to its broker and Customs. The company does not produce evidence to support its position.

The team is not satisfied with the response and considers this high risk for significant loss of revenue. The company declined to quantify the loss of revenue. Therefore, the team determines that it must proceed to the ACT (Revenue) phase.

Example D: Situation in which the team would proceed to ACT (Compliance)

The importer pays buying and selling commissions on imported footwear. The company does not have written internal control for reporting selling commissions, but the job description for the Purchasing Department director requires him to notify the Import Department of costs related to imports. Limited testing during PAS discloses that selling commissions are not always reported. The company believes that the occurrences identified in the PAS were isolated incidents and that its controls are adequate. The company does not agree to correct its internal control or to quantify the problem. The PAS team is concerned that the occurrences were not isolated and

that the problem may be significant. In order to determine the compliance level, the team proceeds to ACT (Compliance).

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – TRANSACTION VALUE

PURPOSE: To determine whether Transaction Value risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1-Internal Control Questions

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure that the value of imports is properly declared?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies and procedures periodically?					
4.	Is internal control of value periodically tested and results documented? (This should include post-entry reviews to verify value was properly declared.)					
5.	If the company found weaknesses during internal control testing on declared value, did the company correct internal control procedures and entries when appropriate?					
6.	Do written internal control procedures assign duties for ensuring the accuracy of declared value to a position rather than a person?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does one individual have authority to ensure that internal control procedures are established and followed by all company departments?					
8.	Do personnel responsible for ensuring the accuracy of declared value have adequate knowledge and training in Customs valuation?					
9.	Does the company have adequate interdepartmental communication about Customs value?					
10.	Does the company have procedures to obtain Customs assistance for value issues when needed and is advice followed when given (e.g., requesting binding rulings)?					
11.	Does the company identify, analyze, and manage risks related to value?					
12.	Has the company identified any risks related to value and implemented control mechanisms?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
13.	Does the company have procedures to ensure pro forma invoices are reconciled to actual invoices and corrections are reported to Customs?					
14.	Does the company have procedures to link specific purchase orders, invoices, and payment records to Customs entry numbers?					
15.	Does the company have procedures to ensure that price actually paid or payable is accurately reported, including:					
	Indirect payments?					
	Quota/visa?					
	Price adjustments?					
	Transportation costs?					
	Currency exchange adjustments?					
	All payments to seller?					
16.	Does the company have procedures to ensure that additions to price actually paid or payable are included for:					
	Packing?					
	Assists?					
	Proceeds?					
	Royalties?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	Selling commissions?					
17.	Do the purchasing department, legal department, engineers and others provide adequate information to the Import Department to ensure value is declared correctly?					
18.	Does the company have procedures to ensure that there are no limitations on the use of transaction value?					
19.	Does the company have procedures to ensure that correct conversion rates are used?					
20.	Does the company have procedures to ensure that non-dutiable charges are accurately reported?					
21.	Does the company require the broker to have written approval prior to making changes to value?					
22.	Does the company provide adequate broker oversight?					
23.	List company-specific procedures below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

*If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples related to various costs comprising transaction value are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

COMPUTED VALUE
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 COMPUTED VALUE GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS.....2
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....4

3.1 RISK.....4
A. Preliminary Assessment of Risk.....4
B. Evaluation of Risk Acceptability.....4
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT).....6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....6
3.5 EXAMPLES.....7

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – COMPUTED VALUE.....10

COMPUTED VALUE
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The objective of this document is to provide guidance for performing a Pre-Assessment Survey (PAS) of the company's internal control for computed value and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on Assessing Internal Controls in Performance Audits, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountant's Statement on Auditing Standards No. 78.

PART 2 COMPUTED VALUE GUIDANCE

19 CFR 152.106(a) defines the computed value of imported merchandise as the sum of:

(i) the cost or value of materials and the fabrication and other processing of any kind employed in the production of the imported merchandise;
(ii) an amount for profit and general expenses equal to that usually reflected in sales of merchandise of the same class or kind as the imported merchandise that are made by the producers in the country of exportation for export to the United States;
(iii) any assist, if its value is not included under paragraph (a) (1) or (2) of this section; and
(iv) packing costs.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem with the valuation of merchandise under computed value.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring value for Customs purposes. Examples:
  - ✓ The company does not monitor or interact with the broker on computed value issues.
  - ✓ The company relies on one employee to handle computed value issues, and there are poor or no management checks or balances over this employee.
  - ✓ The company does not have procedures in place to ensure that material costs are actual and not standard costs.
  - ✓ For computed value involving HTSUS 9802.00.80/90,
    - ◊ The company does not have procedures to ensure that computed value amounts trace to supporting documents.
    - ◊ The company does not have procedures to reconcile reported foreign operating expenses to foreign assembler's income statement.
- Company's import staff lacks knowledge of computed value issues.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.

- Consignment merchandise.
- A significant variance exists between total entered value and total computed value.
- Amounts shown on product cost sheets for unallowable costs such as general expenses and profit that are unusually low or nonexistent. [In general, an amount for gross profit (general expenses and profit) of less that 20% of the sales price is low].
- Customs (e.g., import specialist, account manager, compliance measurements, prior audit, other Customs information) shows a history of problems with computed value.
- The company does not maintain and report computed costs in a format that clearly accumulates all dutiable costs.
- Non-manufacturing importer with manufacturing equipment depreciation or credits to fixed asset accounts (unreported assists).
- General ledger accounts indicate dutiable assists that are not reported.
- Use of standard costs without any adjustments for variances.
- For computed value involving HTSUS 9802.00.80/90,
  - ✓ Discrepancies between the foreign assembler's income statement expenses and profits and the expenses and profit reported to Customs.
  - ✓ Allocation basis results in dutiable costs not being proportionally allocated between dutiable and non-dutiable HTSUS.
  - ✓ Non-dutiable material costs are not equal to the HTSUS 9802.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over computed value:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback,
  - ✓ Are monitored by management, and
  - ✓ Mandate that supporting documents for summary computed value documents are clearly identified and retained.
- One manager is ultimately responsible for control of the Import Department, including ensuring merchandise is properly valued. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign Customs related duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about Customs matters.
- Company conducts and documents periodic reviews of computed value, and uses the results to make corrections and changes to their import operations as appropriate.
- Current standard costs are used to value imported merchandise at time of entry.
- The General Ledger system is designed to identify the value and dutiable status of all merchandise purchased for consignment to the foreign assembler.
- The General Ledger system is designed to identify all dutiable assists.
- For computed value involving HTSUS 9802.00.80/90,
  - ✓ The foreign assembler's cost accounting system allocates overhead and General and Administrative (G&A) expenses and profit to products in a reasonable manner.
  - ✓ The foreign assembler compares its rates for profit and general expenses (gross profit) to industry rates in the country of export, and uses industry rates if there are significant differences.
  - ✓ The company calculates computed value using a format that accumulates all reportable costs.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to computed value.
- Documentation that supports monitoring and verification of established and/or written internal control for computed value.
- Documentation that support the computed value such as worksheets showing the calculation and product allocation of overhead, general expenses and profit, financial statements, general ledger, foreign tax reports, and supporting schedules.
- Other documents affecting computed value such as reports of industry rates for gross profit (general expenses and profit) in the country of export, purchase orders, contracts, agency agreements, and risk sharing agreements.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is a sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining if the controls are in operation, how the controls are applied, how consistently they are applied, and who applies them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

    - Control Environment.
    - Risk Assessment.
    - Control Activities.
    - Information and Communication.
    - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over computed value. (Examples of documents and information to review are listed above.)

3. Determine whether the company established and follows procedures. Review:

    - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
    - Documentary evidence of communication between the broker and company on value issues, company testing of broker operations and verification that the broker followed company instructions.
    - Company-specific rulings and evidence that they are followed.
    - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
    - Training records and materials used to educate staff on Customs matters.
    - Evidence, such as a log, that demonstrates the company periodically reviews broker's or the company's values.
    - Evidence that standard costs are periodically reviewed and updated.
    - Evidence that rates used for general expenses and profit (gross profit) are comparable with the industry rates.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for Computed Value in PART 4 of this document.

    Note: The internal control assessment should include steps to:

        - Identify and understand internal control.
        - Determine what is already known about control effectiveness.
        - Assess the adequacy of internal control design.
        - Determine whether controls are implemented and effective.

- Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over computed value.

1. Complete the WEIC for Computed Value to determine whether risk is acceptable or unacceptable and document why. Put the results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist and account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT:

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the value error was due to an isolated incident.

- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

Proceed to ACT if:

- The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS *are for clarification only*:

Example A: Situation in which the team would not proceed to ACT (Revenue)

Company's Policies and Procedures

The company procedures requires that general ledger account transaction detail be downloaded by the foreign subsidiary and provided by the accounting department, to the Compliance Manager within 30 days of the end of each fiscal year. The Compliance Manager (Import Manager) and two Compliance Analysts review the general ledger accounts and select all manufacturing expense accounts and appropriate non-manufacturing accounts (i.e. general operating expenses) for inclusion in the calculation of actual dutiable value (ADV). Once the dutiable accounts are identified, the Compliance Analyst prepares ADV worksheets using general ledger account transaction detail after year-end adjustments are made to standard costs by the accounting department. Standard costs are evaluated every year and are based on the results of the most recently completed annual computed value. Additionally they compare rates used by the foreign assembler for general expenses and profit (gross profit) to industry rates, and use industry rates if there are significant differences.

The company calculates computed value using a format that accumulates all reportable costs. The company calls the report an Actual Cost Report (ACR). Once the ACR is prepared, it is reviewed and signed by the Accounting Manager and the Import Manager. The ACR and supporting schedules and EDP files are filed and maintained by the Import Manager. The Accounting Manager maintains another backup copy.

Differences in estimated and actual entered values are applied to estimated entered values by HTS on schedules prepared by the company's broker in order to determine additional duties due. The Customs broker makes the value allocation based on a ratio of the entered values per HTS to the total entered value for the year. The broker's calculation's are reviewed and signed by the Import Manager and the broker then files the appropriate reconciliation entry. On an

annual basis, the company's internal audit department reviews the cost preparation process, and makes appropriate recommendations as needed.

Monitoring Activities

The Import Compliance Manual established procedures to ensure that values of entered merchandise were accurately reported to Customs. First, the Import Manager and two Compliance Analysts review the general ledger accounts and select all manufacturing expense accounts and appropriate non-manufacturing accounts for inclusion in calculating actual dutiable value. Detailed evaluations of new accounts are conducted with the assistance of the Assistant Controller. In addition, the process of calculating the actual costs is documented in a permanent file that is reviewed and signed by the Import Manager and Accounting Manager. Ratios between the last years estimated and actual costs are compared to the current year ratios for purposes of testing the reasonableness of actual values. The Import Manager and Accounting Manager review the broker's calculations of duties due, and indicate their review by signing each of the broker's worksheets.

Finally, the manual establishes procedures for conducting internal audits on an annual basis. The manual requires that the Import Manager review a sample of 5 transactions from 10 accounts not used in the preparation of actual cost, in order to determine if some of the account transactions should be included in the actual dutiable value. The accounts and the sample items are to be randomly selected.

The Import Manager holds a meeting prior to the preparation of the current ACR, in order to educate those involved in the preparation process of issues or concerns identified in prior years. All meetings, training seminars and discussions regarding the process are documented and filed by the Import Manager. In addition, employees involved in the process of preparing costs for Customs value attend a one-week training session provided by the company's outside counsel.

Pre-Assessment Survey

To determine if the controls were working, the PAS team:

- Interviewed employees engaged in the preparation of ACR's to determine if they were familiar with the procedures established in the Customs Compliance Manual.
- Verified that the trial balance included all general ledger transactions.
- Verified the ACR review process and that they were signed by the Accounting Manager and the Import Manager.
- Selected 10 of the 50 transactions not used in the preparation of actual cost and reviewed by the Import Manager to verify how the review had been conducted.
- Reviewed broker duty calculations to ensure that they were reviewed.
- Compared brokers estimated duty to the PAS teams estimated duty totals.
- Reviewed internal audit reviews of the last two years ACR reviews.
- Reviewed attendee sign-in sheets and course descriptions for periodic training sessions regarding preparation of ACR's.
- Reviewed correspondence between the company and Customs on value related matters.

The PAS indicated that the company's internal controls were in affect and were working with one exception. One dutiable account was omitted from the calculations used to calculate dutiable costs and file the reconciliation entry. The company agreed to file corrective entries to report the additional value and to pay the additional duty. Therefore proceeding to ACT was not considered necessary.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same situation as Example A above. The company agreed to change procedures to include the account in the future. Therefore, it was not necessary to proceed to ACT to calculate a rate for compliance.

Example C: Situation in which the team would proceed to ACT for (Revenue)

Same situation as Example A above, except unreported assists were identified in a material account. Statistical sampling was necessary to separate dutiable assists from material that was used in domestic production.

Example D: Situation in which the team would proceed to ACT (Compliance)

The same situation as Example A above, with the additional finding that the Import department had decided that reviewing all the new general ledger accounts was too cumbersome due to the company's change in accounting system that had occurred early in the audit period. In addition, the company did not agree to take proper corrective action. Proceeding to ACT was considered necessary due to the fact that there were many general ledger accounts not yet reviewed that could impact the ACR.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) –COMPUTED VALUE

PURPOSE: To determine whether Computed Value risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

OBJECTIVES:

Section 1- Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented: • through the interview process and/or requesting evidence from the company • review documents that provide evidence that the company completed the activity.
Section 2 -Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3-Sample sizes	Use the Risk Exposure Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4-Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 –Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls over computed value formally documented?					
2.	Does management approve written policies and procedures?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Are internal controls over computed value tested periodically and results documented? (This should include post-entry reviews to verify accuracy and completeness of value declarations.)					
5.	If the company found weaknesses in computed value review during internal control testing, did the company correct internal control procedures and entries when appropriate?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
6.	Do written internal control procedures assign duties to a position rather than a person?					
7.	Does one individual have authority to ensure that internal control procedures for imports are established and followed by all company departments?					
8.	Do personnel responsible for ensuring the accuracy of declared value have adequate knowledge and training in Customs valuation?					
9.	Does the company have adequate interdepartmental communication about value?					
10.	Does the company have procedures to obtain professional/Customs assistance in resolving value issues (e.g., binding rulings) and is advice followed when given?					
11.	How does the company identify, analyze, and manage risks related to computed value?					
12.	What risks related to computed value has the company identified, and what control mechanisms has it implemented?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
13.	Does the company have procedures to ensure that industry rates for general expenses and profit (gross profit) in the country of export are checked, and used if significantly different than company rates?					
14.	Does the company have procedures to ensure pro forma invoices or standard costs are reconciled to actual costs and corrections are reported to Customs?					
15.	Does the company have procedures to ensure that material costs include transportation costs to the place of production?					
16.	Does the company have procedures to ensure that value of assists and packing costs are included in computed value?					
17	Does the company have procedures to ensure that material costs and other costs are properly allocated between dutiable and non-dutiable tariff numbers?					
18	Does the company have procedures to ensure that freight costs are properly allocated between dutiable and non-dutiable material?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
19	Does the company have procedures to ensure that any internal tax imposed on imported material by the country of exportation, which is refunded at the time of exportation, are excluded from material value?					
20.	Does the company have procedures to ensure that all foreign operating expenses, applicable to the production of exported merchandise, and profit reported on the foreign assembler's income statement are reported as part of computed value?					
21	Does the company have procedures that ensure that material scrap value, less any proceeds from the sale of the scrap, is included in computed value?					
22	Does the company have procedures that ensure that exchange gains are reported and that translation gains are not reported as part of computed value?					
23	Does the company require the broker to have written approval prior to making changes to value?					
24	Does the company provide adequate broker oversight of value issues?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
25	List company-specific procedures below (if applicable**)**					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

*If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples related to various costs comprising computed value are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

CLASSIFICATION
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 CLASSIFICATION GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS 2
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 3

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 4

3.1 RISK 4
A. Preliminary Assessment of Risk.....4
B. Evaluation of Risk Acceptability 5
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 6
3.4 EVALUATAION OF PRE-ASSESSMENT SURVEY TESTING RESULTS 7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - CLASSIFICATION 10

CLASSIFICATION
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The objective of this document is to provide guidance for performing a Pre-Assessment Survey (PAS) of the company's internal control for classification and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountants Statement on Auditing Standards No. 78.

PART 2 CLASSIFICATION GUIDANCE

19 CFR 141.86(a)(3) states that each invoice of imported merchandise shall set forth a detailed description of the merchandise, including the name by which each item is known, the grade or quality, and the marks, numbers, and symbols under which it is sold by the seller or manufacturer to the trade in the country of exportation, together with the marks and numbers of the packages in which the merchandise is packed.

19 CFR 141.87 states that whenever the classification or appraisement of merchandise depends on the component materials, the invoice shall set forth a breakdown giving the value, weight, or other necessary measurement of each component material in sufficient detail to determine the correct duties.

19 CFR 141.89 states that additional invoice information is required for certain classes of merchandise in order to determine admissibility and merchandise classification.

19 CFR 152.11 requires merchandise to be classified in accordance with the Harmonized Tariff Schedule of the United States (HTSUS) (19 U.S.C. 1202) as interpreted by administrative and judicial rulings.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem in classification:

- The company has insufficiently documented, poorly defined, or no internal control for accurately reporting classifications to Customs.
  - ✓ The company does not monitor or interact with the broker on classification issues.
  - ✓ The company relies on one employee to handle classification issues, and there are poor or no management checks or balances over this employee.
- Company import staff lacks knowledge of classification requirements.
- The company offers unreasonable explanations to Customs.
- The company fails to cooperate with or respond to Customs.
- The company has a high turnover of people in key positions.
- Significant variances exist between the importer's data and data submitted to Customs.
- Customs (e.g., import specialist, account manager, compliance measurements, prior audit, other profile information) shows a history of problems with classification.

- The company uses HTSUSs with known or suspected problems as identified by Customs.
- HTSUSs are complex, or merchandise is classified under a broad range of HTSUSs that would require extensive knowledge to classify.
- The company imports a wide variety of merchandise but enters the merchandise under only a few classifications.
- The company's import pattern has changed.
- Competing HTSUSs have a lower duty rate or relaxed admissibility requirements.
- The company has been referred for enforced compliance.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over classification:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import Department, including proper classification of merchandise. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign classification duties and tasks to a position rather than a person.
- The company has good interdepartmental communication about Customs matters.
- The company requests binding rulings and consults with Customs import specialists.
- The company conducts and documents periodic reviews of merchandise classification and uses the results to make corrections to entries and changes to its import operations as appropriate.
- The company requires that vendors provide sufficient descriptions of merchandise on invoices to permit proper classification.
- The company requires periodic training for staff responsible for classifying merchandise.
- The company attends Customs informed compliance outreach and seminars or attends Customs-related seminars provided by private vendors regarding classification issues.
- The company maintains a database of classifications for its product line and requires the classification to be shown on invoices.
- The company requires engineers to obtain the classification for a new part from the Import Department before obtaining a purchase order to buy the part.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures
- The company's responses to the questionnaire
- Interviews with company staff concerning actual procedures and internal control specific to classification
- Documentation that supports monitoring and verification of established and/or written internal control for classification
- Other documents supporting proper classification, such as invoices, engineering drawings, and other descriptive information
- Headquarters and New York rulings issued to the company and/or rulings issued for identical/similar products imported by the company

- Import specialist team files, including CF 28s and CF 29s issued to the company

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and to determine whether there is a sufficient risk to warrant proceeding to Assessment Compliance Testing (ACT).

Using the chart and the guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls are applied, how consistently they are applied, and who applies them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

Preliminary Assessment of Risk Examples

Example A: Low Risk Assessment

The import specialist identifies four possible HTSUSs that should be used for the products imported by the company. The computer audit specialist (CAS) verifies that the company has used only four HTSUSs during the past fiscal year. The duty rates for each of the four HTSUSs are the same. Compliance measurement rates are acceptable. The import specialist and account manager do not have any concerns. Therefore, the preliminary assessment of risk is low.

Example B: High Risk Assessment

The importer imports $450 million in fasteners annually. The import specialist advises that misclassifications are a frequent problem in the fastener industry and that the company has not contacted him for classification guidance. In addition, the company uses numerous classifications for its imports. Because problems frequently occur in this industry, the import specialist has had no interaction with the company regarding classification, and the company uses numerous classifications, the preliminary assessment of risk is high.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment
   - Risk Assessment
   - Control Activities
   - Information and Communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over classification. (Examples of documents and information to review are listed above.)

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence of communication between the broker and company on classification issues, company testing of broker operations, and verification that the broker followed company instructions.
   - Company-specific rulings and evidence that they are followed.
   - Documentary evidence of intercompany communications to ensure that correct information is provided to Customs.
   - Training records and materials used to educate staff on classification issues.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for Classification in PART 4 of this document. If applicable, include quota, antidumping duties, admissibility requirements, and other classification issues.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control

- Determine what is already known about control effectiveness
- Assess the adequacy of internal control design
- Determine whether controls are implemented and effective
- Determine whether transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In such cases, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the classification level that will be reported on. For example, the company may import under numerous classifications, but the PAS team may decide that testing may be necessary only for certain classifications or types of imports that have been identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

Example (Determination of Testing Level)

Based on a review of the profile (Compliance Measurement (CM) rates were high), questionnaire, written procedures, etc., the team concludes that the preliminary risk exposure is moderate.

The company’s internal control procedures manual requires the import manager to review every 50th transaction to ensure that the merchandise is correctly classified and to maintain a “Classification Review Log” to document this process. The import manager documents the transactions she reviews, identifies misclassifications, and files corrected entries. The log shows that misclassified items have been corrected in the company’s classification database and with Customs. The team concludes that the internal control system over classification is strong.

Using the table above (based on a moderate risk exposure and strong preliminary internal control evaluation), the team concludes that it will test five control items. The team judgmentally selects three items from the “Classification Review Log”. The team import specialist verifies that

two classifications were accurate and one incorrect classification had been corrected. The import specialist reviews two additional entries and determines that the classifications were correct. The company's import manager provides evidence that all entries of the incorrectly classified parts had been corrected. The team verifies that the company took action to prevent future misclassification by examining changes to the classification database and by confirming that classifications on subsequent entries were correct.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over classification.

1. Complete the Worksheet for Evaluating Internal Control for Classification to determine whether risk is acceptable or unacceptable and document why. Put the results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist and account manager. The team must evaluate the PAS results based on the specific situation(s).

2. Obtain the PAS import specialist's opinion of the adequacy of controls and the significance of weaknesses identified. Existing guidelines should be used when contacting national import specialists if their assistance is needed.

3. The following will help the PAS team determine whether conditions warrant proceeding to ACT:

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the classification error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   <u>Proceed to ACT if:</u>
   - The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

4. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS are for clarification only:

Example A: Situation in which the team would not proceed to ACT (Revenue)

The company's written procedures require the Customs Department to provide the broker with specific information (specification sheets, rulings, and complete descriptions) for use in classifying merchandise. The company is required to randomly test X percent of broker-filed entries each month to determine whether classifications were correct and to notify the broker by email if corrections are needed. The broker is required to send the company copies of corrected CF 7501s.

The team:

- Determines that 20 items should be tested, based on:
  - ✓ The high preliminary risk exposure level (Congressional interest in import commodity and import specialist concerns).
  - ✓ The adequate preliminary internal control evaluation (there was no procedure to monitor broker corrections).
- Reviews the company's "Classification Audit Log" to verify that the company had tested X percent of the entries during the past few months.
- Identifies five misclassifications that the company had asked the broker to correct and verifies that the broker had corrected the classification but had not notified the company of the correction.
- Selects several entry summaries, judgmentally selects 15 line items, and confirms that classifications were correct.

The company agrees that the import manager will monitor the broker's corrections in the future. The team concludes that proceeding to ACT will not be necessary because:

- The PAS team has verified classifications were corrected and did not result in unpaid duty.
- The company has elevated its monitoring of the broker to a management level.

Example B: Situation in which the team would not proceed to ACT (Compliance***)***

The team does not identify any concerns in the questionnaire, profile, or interviews. The company has implemented its written internal control procedures, which:

- Assign the company's in-house broker the responsibility for classifying imported merchandise
- Require the import manager to review/test classifications used during the month
- Require the import manager to periodically communicate with and train other departments, such as Engineering and Purchasing, on classification requirements

The team concludes that the preliminary risk exposure is low and internal control is strong. The team judgmentally tests four classifications and finds the merchandise is properly classified. Since internal control was implemented and effective and no incorrect classifications are found, the team concludes that there are no unacceptable risk areas and does not proceed to ACT compliance testing.

Example C: Situation in which the team would proceed to ACT for (Revenue)

The team finds the same situations as identified in example B. However, the import specialist determines that the classifications tested were not correct and there was a significant loss of revenue on a number of items. The team proceeds to ACT to determine loss of revenue.

Example D: Situation in which the team would proceed to ACT (Compliance)

In the same situation as example A above, the company stopped reviewing the broker's classifications 2 years before, when a new import manager was hired. PAS testing of 20 classifications shows that three were incorrect. The PAS team considers the breakdown in the company's control system significant enough to proceed to the ACT process to quantify the level of noncompliance.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - CLASSIFICATION

PURPOSE: To determine whether Classification risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure that classification is correctly declared?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies and procedures periodically?					
4.	Is internal control over classification periodically tested and results documented? (This should include post-entry reviews to verify correctness of classification.)					
5.	If the company found weaknesses during internal control testing of classification, did the company correct internal control procedures and entries when appropriate?					
6.	Do written internal control procedures assign classification of merchandise to a position rather than an individual?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does one individual have authority to ensure that internal control procedures for classification of imports are established and followed by all company departments?					
8.	Do personnel responsible for classifying merchandise have adequate knowledge and training in classification?					
9.	Does the company have adequate interdepartmental communication about classification?					
10.	Does the company have procedures to request Customs assistance classifying merchandise when needed and is advice followed when given (e.g., requesting binding rulings)?					
11.	Does the company identify, analyze, and manage risks related to classification?					
12.	Has the company identified any risks related to classification and implemented control mechanisms?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
13.	Do suppliers, engineers, the purchasing department, laboratory and others provide adequate descriptive information to the Import Department to ensure proper classification?					
14.	Does the company have policies and procedures in place to ensure the proper classification of new items?					
15.	Does the company maintain product classifications in a database that is provided to brokers and updated when necessary?					
16.	If the company provides the broker with the classification is the broker required to obtain company concurrence prior to making classification changes?					
17.	Does the company provide adequate broker oversight of classification issues?					
18.	List company-specific procedures below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Risk Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

HTSUS 9801.00.10 – U.S. GOODS RETURNED
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 HTSUS 9801.00.10 GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS.....2
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....3

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....3

3.1 RISK.....4
A. Preliminary Assessment of Risk.....4
B. Evaluation of Risk Acceptability.....4
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TEST (TESTING LIMIT).....6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....7

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) -HTSUS 9801.00.10 (U.S. GOODS RETURNED).....10

HTSUS 9801.00.10 – U.S. GOODS RETURNED
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The objective of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for merchandise entered under HTSUS 9801.00.10 (9801) and in evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this documents are based *on Assessing Internal Controls In Performance Audits,* GAO/OP 4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountants *Statement on Auditing Standard's No. 78*.

PART 2 HTSUS 9801.00.10 GUIDANCE

To qualify for 9801, articles of the United States must be exported and returned without having been advanced in value or improved in condition by any manufacturing process or other means while abroad.

To receive the benefit of these provisions, the importer must also comply with 19 CFR 10.1(a), which states, in part, "Except as otherwise provided for in paragraph.(g), (h), (I) or (j), the following documents shall be filed in connection with the entry of articles in a shipment valued over $2,000 and claimed to be free of duty under subheading 9801.00.10 or 9802.00.20, Harmonized Tariff Schedule of the United States (HTSUS) (1) A declaration by the foreign shipper…(2) A declaration by the owner, importer, consignee, or agent having knowledge of the facts regarding the claim for free entry."

19 CFR 10.1 allows the Port Director to waive these documentation requirements if other information reasonably satisfies the requirements of HTSUS 9801.00.10. Also, 19 CFR 10.1 allows the Port Director to request additional documentation or evidence to substantiate the claim for duty free treatment when necessary.

The following conditions preclude the use of 9801 (except 9801.00.70 and 9801.00.80):

- Drawback has been claimed on the articles. See 19 CFR 10.3.
- The article was manufactured or produced in a Foreign Trade Zone, exported from a bonded warehouse, or entered under a Temporary Importation Bond.
- The articles were subject to internal revenue tax. See 19 CFR 10.3.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem in 9801.00.10.

- The company has insufficiently documented, poorly defined, or no internal control for accurately declaring 9801.00.10 for Customs purposes.
  - ✓ The company does not monitor or interact with the broker on 9801.00.10 issues.
  - ✓ The company relies on one employee to handle 9801 issues, and there are poor or no management checks or balances over this employee.

  - ✓ The company does not maintain documentation, such as certificates of origin and manufacturers' affidavits, to support U.S. origin.
  - ✓ Company Customs staff lack knowledge of 9801.00.10 eligibility requirements.
- The company offers unreasonable explanations to Customs inquiries.
- The company fails to cooperate with or respond to Customs.
- The company has a high turnover of people in key Customs positions.
- Significant variance exists between the importer's data and Customs data.
- Customs (e.g., import specialist, account manager, compliance measurement, prior audit, other profile information) shows a history of problems with 9801.00.10 claims .
- The company has many drawback claims.
- The company has large amounts of merchandise produced in a Foreign Trade Zone, exported from a bonded warehouse, or entered under a Temporary Importation Bond.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over 9801.00.10:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are approved by management.
- One manager is ultimately responsible for control of the Import Department, including ensuring eligibility of merchandise entered under 9801.00.10. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- The company has good interdepartmental communication about Customs matters.
- The company conducts and documents periodic reviews of 9801.00.10 merchandise and uses the results to make corrections to entries and changes to its import operations as appropriate.
- The company obtains documentation supporting U.S. origin prior to claiming 9801.00.10.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Written internal control policies and procedures for ensuring proper 9801.00.10 eligibility
- The company's response to the questionnaire
- Interviews with company staff concerning actual procedures and controls specific to 9801.00.10
- Company documentation that supports monitoring and verification of established and/or written internal control for 9801.00.10, such as:
  - ✓ Manufacturer's affidavit or certificate of origin declaring U.S. origin
  - ✓ Entry documents (e.g., CF 7501, commercial invoice)
  - ✓ Export documents
- Internal and external audit reports

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate how effective internal control is and to determine whether there is a sufficient risk to warrant proceeding to Assessment Compliance Testing (ACT).

Using the Chart and the guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they were applied, and who applies them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

Preliminary Assessment of Risk Examples

Example A: Low Risk Assessment

Account Profile and Customs Automated Commercial System (ACS) data identified a total entered value of $117 million in FY 2000, with $10 million entered under HTSUS 9801.00.10. No problems were reported in the Account Profile or in the team's discussion with the import specialist and account manager. Therefore, the preliminary assessment of risk is low because the value of 9801 imports is low.

Example B: High Risk Assessment

Account Profile and ACS data identified a total entered value of $90 million during the current fiscal year, of which $30 million was declared as American Goods Returned. The Account Profile reported that merchandise entered under HTSUS 9801 increased by about 20 percent over the past 3 years, and compliance measurement (CM) exams resulted in discrepancies surrounding Country of Origin issues. Therefore, the preliminary assessment of risk is high due to the value of the 9801 imports, the increase in claims, and CM discrepancies.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control environment
   - Risk assessment
   - Control activities
   - Information and communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over 9801.00.10. (Examples of documents and information to review are above.)

3. Determine whether the company established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented
   - Documentary evidence of communication with the broker and company departments on 9801 issues, including company testing of broker operations and verification that the broker followed company instructions
   - Documentary evidence that company-specific rulings are requested and followed
   - Documentary evidence of intercompany communications to ensure correct information is provided to Customs
   - Training records and materials used to educate staff on Customs matters
   - Documentary evidence that the company can support the U.S. origin of the imported merchandise
   - Documentary evidence that the merchandise was exported from the United States without payment of drawback
   - Documentary evidence that the merchandise was not produced with materials imported temporarily under bond or manufactured or produced in a Customs bonded warehouse
   - Documentary evidence that the company ensures that the merchandise was not advanced in value or improved in condition while abroad
   - Documentary evidence that the imported merchandise is the same as the exported articles identified

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for 9801.00.10 in PART 4 of this document.

   Note: The internal control assessment should include steps to:

- Identify and understand internal control.
- Determine what is already known about control effectiveness.
- Assess the adequacy of internal control design.
- Determine whether controls are implemented and effective.
- Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TEST (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In such cases, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the HTSUS 9801.00.10 level that will be reported on. For example, the company may import from several foreign companies, but testing may be necessary only for certain companies or only for certain 9801.00.10 declarations that have been identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

Example: Validation of Company Control Activity

One of the company’s internal controls over 9801.00.10 is that it reviews every 15th 9801.00.10 transaction to ensure that 9801.00.10 transactions are properly declared. The company maintains a “9801.00.10 Review Log” to document this review process. To determine internal control effectiveness, the PAS team may decide to verify that the company review procedure identifies incorrectly declared 9801.00.10 and that the company takes appropriate corrective action, including improved procedures to avoid future improperly declared 9801.00.10.

The PAS team may select a limited number of reviewed items from the “9801.00.10 Review Log” to verify that 9801.00.10 was properly reviewed to determine accurate declaration of 9801.00.10, and that any incorrectly declared 9801.00.10 entries were corrected (causes identified and procedures corrected to ensure future compliance) and reported to Customs. In addition, the PAS team should verify that the company took action to avoid future improperly

declared 9801.00.10 after such errors were identified. In order to do this, the PAS team should verify that the same types of improperly declared items were correctly declared on subsequent entries. The following are examples of some of the tests that can be performed to determine whether 9801.00.10 is accurately declared:

- Trace through the importer's inventory, export bill of lading, and importation documents that 9801.00.10 merchandise claimed is eligible.
- Conduct third-party verifications to verify value and origin.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of the company's internal control over 9801.00.10.

1. Complete the WEIC FOR 9801.00.10 to determine whether risk is acceptable or unacceptable and document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will help the PAS team determine whether conditions warrant proceeding to ACT.

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   <u>Proceed to ACT if:</u>
   - The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS are *for clarification purposes only.*

Example A: Situation in which the team would not proceed to ACT (Compliance)

This example is based on the assumption that this merchandise was purchased from a U.S. supplier.

Export of U.S. Merchandise
The company's procedures manual requires the Material Management Department to maintain serial numbers and value of 9801 merchandise in the inventory system. When goods are shipped to a foreign site, the Shipping Department notifies the Customs Department of the merchandise being exported, including the serial number, value, and reason for export. The Customs Department in turn maintains a log of exported parts to match with entries when the entry package is received from the Customs broker.

Import of Previously Exported Merchandise
The company's written procedures require the Customs Department to obtain a declaration from the foreign shipper that the goods are of U.S. origin and were not advanced in value or improved in condition while abroad. The company also requires foreign shippers to include the part's serial number in the commercial invoice and packing list. The Customs Department is also responsible for submitting this declaration to the Customs broker with instructions to include it with the entry package. Finally, the Customs Department reviews all entries filed by the Customs broker to ensure that required documentation was included in the entry package.

Pre-Assessment Survey
To determine whether these controls are working, the PAS team:

- ✓ Interviewed employees to determine whether they are familiar with the procedures established in the Customs Compliance Manual
- ✓ Selected five parts, verified the proof of U.S. origin, and traced the parts through the inventory system from the time of export to the time of import
- ✓ Reviewed the shippers' declarations maintained by the company for the five sample items

Because the PAS team was able to verify that controls are in place and working effectively, proceeding to ACT was not considered necessary.

Example B: Situation in which the team would not proceed to ACT (Revenue)

The circumstances are the same as those in example A above, except that the company failed to maintain manufacturers'/shippers' declarations to prove that the merchandise was of U.S. origin and was not advanced in value or improved in condition while abroad for the past fiscal year. The company agreed with the PAS findings and was able to quantify loss of revenue caused by not being able to support 9801 eligibility. Therefore, proceeding to ACT was not considered necessary.

Example C: Situation in which the team would proceed to ACT (Compliance)

The circumstances are the same as those in example A above, except that the company disagreed with taking proper corrective action. The company was noncompliant with specific Customs regulations, failed to monitor compliance with Customs requirements, and did not

agree to take corrective action. It is necessary to calculate a compliance rate. Thus the audit team proceeded to ACT.

Example D: Situation in which the team would proceed to ACT (Revenue)

The circumstances are the same as in example B above, except that the company was not able to quantify the loss of revenue caused by not being able to support 9801 eligibility. Therefore, proceeding to ACT was considered necessary.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) -HTSUS 9801.00.10 (U.S. Goods Returned)

PURPOSE: To determine whether 9801.00.10 risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure that 9801 is correctly declared?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies and procedures periodically?					
4.	Is internal control over 9801 periodically tested and results documented? (This should include post-entry reviews to verify correctness.)					
5.	If the company found weaknesses during internal control testing of 9801, did the company correct internal control procedures and entries when appropriate?					
6.	Do written internal control procedures assign 9801 to a position rather than an individual?					
7.	Does one individual have authority to ensure that internal control procedures for 9801 imports are established and followed by all company departments?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
8.	Do personnel responsible for 9801merchandise have adequate knowledge and training in classification?					
9.	Does the company have adequate interdepartmental communication about 9801?					
10.	Does the company have procedures to request Customs assistance on 9801 merchandise when needed and is advice followed when given (e.g., requesting binding rulings)?					
11.	Does the company identify, analyze, and manage risks related to 9801?					
12.	Has the company identified any risks related to 9801 and implemented control mechanisms?					
13.	Do suppliers, engineers, the purchasing department, laboratory and others provide adequate descriptive information to the Import Department?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	**Documentation**. Does the company's recordkeeping system include a retention program and identify documents needed to support 9801.00.10 claims?					
15.	**Documentation**. Has the company established a reliable system or procedure to produce any required entry documentation and supporting information?					
16.	**Origin**. Does the importer maintain manufacturers' affidavits or other documentation proving U.S. origin?					
17.	**Origin**. Do commercial invoices include country of origin, value, part number, and serial numbers?					
18.	**Origin**. Are part numbers for U.S.-origin components maintained in a database that is provided to the company's brokers?					
19.	**Advanced or Improved**. Does the importer maintain the assemblers' declarations or other documentation attesting to the fact that the merchandise was not advanced in value or improved in condition?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
20.	**Advanced or Improved**. Are descriptions of the assembly process obtained prior to making 9801.00.10 claims on new or revised products?					
21.	**Usage**. Does the importer have specific identifiers, such as serial numbers, to trace the merchandise through the inventory system?					
22.	**Value**. Does the importer have documentation to support the actual cost of 9801.00.10 claims?					
23.	**Non-qualifying**. Does the company have procedures in place to ensure that merchandise claimed under 9801 was not produced with materials temporarily imported under bond (Temporary Importation Bond) or produced in a bonded warehouse?					
24.	**Non-qualifying**. Does the company have procedures in place to ensure that drawback was not previously claimed on articles entered under 9801.00.10?					
.						
25..	Does the company provide adequate broker oversight to ensure proper 9801.00.10 declarations and data accuracy?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
26.	Does PAS testing verify that control procedures were being performed?					
27.	Do interviews with responsible persons support control procedures?					
28.	Does the company have adequate internal control to address specific issues identified in the profile?					
29.	List company-specific procedures and controls below (if applicable):					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

HTSUS 9802.00.40 and 9802.00.50 – ARTICLES EXPORTED FOR REPAIRS OR ALTERATIONS
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 HTSUS 9802.00.40 AND 9802.00.50 GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS.....2
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....5

3.1 RISK.....5
A. Preliminary Assessment of Risk.....5
B. Evaluation of Risk Acceptability.....5
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT).....6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – HTSUS 9802.00.40 AND 9802.00.50 (ARTICLES EXPORTED FOR REPAIRS OR ALTERATIONS).....11

HTSUS 9802.00.40 and 9802.00.50 – ARTICLES EXPORTED FOR REPAIRS OR ALTERATIONS
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The objective of this document is to provide guidance for performing a Pre-Assessment Survey (PAS) of the company's internal control for merchandise entered under in HTSUS 9802.00.40 and 9802.00.50 and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits,* GAO/OP- 4.1.4 - published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78.*

PART 2 HTSUS 9802.00.40 AND 9802.00.50 GUIDANCE

HTSUS 9802.00.40 merchandise is merchandise that was exported to a foreign country for repairs or alterations pursuant to a warranty and returned to the U.S.

HTSUS 9802.00.50 merchandise is merchandise that was exported for repairs or alternations not covered under a warranty and returned to the U.S.

Regulations governing 9802.00.40 and 9802.00.50 are in 19 CFR Part 10.8(a) through (d). U.S. Note 3 of Subchapter II of Chapter 98 of the Harmonized Tariff of the United States (HTSUS) provides criteria for duty treatment of these articles. The articles, which can be of U.S. origin or foreign, are dutiable on the cost to the importer for the repairs/alterations or if free of charge, the value of the repairs/alternations.

The following conditions preclude the use of 9802.00.40 and 9802.00.50:

- The importer fails to identify the articles as being previously exported.
- The foreign operations caused the identity or HTSUS classification of the exported article to change.
- The foreign operations were limited to minor procedures, such as warehousing, repackaging, sorting, and testing not performed in conjunction with repairs or alterations.
- The exported articles were incomplete for their intended use prior to being exported and the foreign operation constitutes an intermediate processing operation.
- Drawback has been claimed on the exported articles.

2.1 EXAMPLES OF RED FLAGS

The following examples of red flags are conditions that may indicate a potential problem in 9802.00.40/50:

- Company has insufficiently documented, poorly defined, or no internal control for claiming 9802.00.40/50. Examples:
  - ✓ Company does not monitor or interact with the broker on 9802.00.40/50 issues.
  - ✓ Company relies on one employee to handle 9802.00.40/50 issues, and there are poor or no management checks or balances over this employee.
- Company's import staff lacks knowledge of 9802.00.40/50 requirements.
- Company's import staff lacks the knowledge of cost accounting that is necessary to determine whether the value covers all costs and profit for repairs performed by related parties or under warranty, and to ensure that supporting cost records are retained and readily available.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.
- Significant variances exist between the importer's data and Customs' data.
- Customs (e.g., import specialist, account manager, compliance measurement, prior audit, other profile information) shows a history of problems with 9802.00.40/50
- Company has many drawback claims.
- Company has poor internal control to ascertain that the part exported for repair is the same as the part re-imported (i.e., products without unique number as means of tracking such as serial number, lot number, etc.).
- Company does not have written repair contracts explaining how the repair cost of different components is determined.
- The Questionnaire indicated that the company does not have:
  - ✓ Procedures to verify repairer's declarations (see reasonable care – United States v. Golden Ship Trading Company, Joanne Wu and American Motorists Insurance Company, Slip Op. 01-7).
  - ✓ Procedures to review manufacturing operations performed at the foreign plant to determine whether such operations qualify for partial exemption.
  - ✓ Procedures to ensure that the foreign operations do not result in commercially different articles with new properties and characteristics.
  - ✓ Procedures to verify the cost or value of the repairs or alterations actually performed abroad. The cost should include all domestic and foreign articles furnished for the repairs or alterations, not including any of the expenses incurred in this country whether by way of engineering costs, preparation of plans or specifications, furnishing of tools or equipment for doing the repairs or alterations abroad, or otherwise."
- The value of the imports was based on estimated or standard costs.
- Company does not have warranty documentation for articles claimed as 9802.00.40.

Note: Foreign repairs are often performed by the related foreign factories that manufactured the products. When importer and foreign repair sites are related, or work was done under warranty, all elements of cost and profit, including overhead, general expenses and profit may **NOT** be included in the repair value. Consider that Transaction Value may not be acceptable if the repair value does not cover all costs and a reasonable profit.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over 9802.00.40/50:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and

  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import/Export Department, including 9802.00.40/50 matters. That manager has knowledge of Customs matters and the authority to ensure internal control procedures for imports are established and followed by all company departments.
- The Import Manager also has cost accounting knowledge, for control of imports from related parties or under warranty.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about 9802.00.40/50 matters.
- Company conducts and documents periodic reviews of 9802.00.40/50 matters, and uses the results to make corrections to entries and changes to their import operations as appropriate.
- Company has an export log with serial number, invoice number, and other pertinent information to track merchandise.
- Company maintains documentation indicating that foreign costs include all reportable elements.
- Company maintains documentation for foreign operations to ensure that proper repairs and alterations were actually made.
- Company maintains a log that identifies warranty and non-warranty costs.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and internal control specific to 9802.00.40/50.
- Documentation that supports monitoring and verification of established and/or written internal control for 9802.00.40/50.
- Other documents supporting 9802.00.40/50 claims including:
  - ✓ Declaration from the person who performed the repairs/alternations.
  - ✓ Declaration by the owner, importer, consignee or agent having knowledge of the repair.
  - ✓ Export documents (invoices, bill of lading, etc.).
  - ✓ Bills of Materials and/or detailed breakdown of standard material costs.
  - ✓ Repair orders, purchase order, and/or contracts documenting the reason for exportation.
  - ✓ Warranty repair agreement.
  - ✓ Cost sheets from related parties or for repairs under warranty showing the elements of cost and profit for each product repaired.
  - ✓ Supporting labor cost records for products repaired.
  - ✓ Calculation and allocation worksheets for overhead, general expenses and profit for products repaired.
  - ✓ Accounting records.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company's internal controls are effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**, and

2. The **internal control** system, by determining if the controls are in operation, how the controls were applied, how consistently they are applied, and who applies them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.

- Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over 9802.00.40/50 (Examples of documents and information to review are listed above).

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence of communication between the broker and company on 9802.00.40/50 issues, company testing of broker operations, and verification that the broker followed company instructions.
   - Company-specific rulings and evidence that they are followed.
   - Documentary evidence of intra-company communications to ensure that correct information is provided to Customs.
   - Training records and materials used to educate staff on 9802.00.40/50 issues including knowledge of cost accounting standards if foreign repair sites are related or repairs are performed under warranty.
   - Documentary evidence indicating that the company ensured that the merchandise was not advanced in value or improved in condition abroad.
   - Documentary evidence indicating that the company ensured that the imported merchandise was the same as the exported articles.
   - Documentary evidence, including repairer's declaration, of the type of repairs or alterations taking place.
   - Documentary evidence to support that the value of foreign repair includes all elements of cost and profit and that the records to support such costs are retained and readily available.
   - Documents such as cost sheets from related parties or for repairs under warranty, showing that the elements of cost and profit for each product repaired, included material, labor, overhead, general expenses and profit.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for 9802.00.40 and 9802.00.50 in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form

an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the overall 9802 level that will be reported on. For example, the company may import from various foreign entities and from various countries and tests may be designed for areas identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled "Testing Limit" reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over 9802.00.40 and 9802.00.50.

1. Complete the WEIC for 9802.00.40 and 9802.00.50 to determine whether risk is acceptable or unacceptable and to document why. Put the results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will help the PAS team determine whether conditions warrant proceeding to ACT:

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   <u>Proceed to ACT if:</u>

- The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS *are for clarification only:*

Example A: Situation in which the team would not proceed to ACT (Revenue)

Company's Policies and Procedures
The company's Customs Compliance Manual requires the purchasing department to obtain a declaration from the foreign company performing the repairs or alterations. The buyer submits the declaration to the company's Import Branch (a branch in the Import/Export Department) and provides assistance to the Branch in preparing the Importer's Declaration. The Import Branch in turn is responsible for submitting the declarations to the Customs broker with instructions to include them with the entry. The buyer is also responsible for conferring with the foreign companies to ensure that invoices separately identify each repair or alteration performed and include the cost or value of the repairs. The Manual further requires the Import Branch to maintain and have ready for submission, the foreign customs entry, foreign customs invoice, and bill of lading/airwaybill related to the export for repairs and/or alterations in case the U.S. Customs Service should request additional supporting documentation.

Monitoring Activities
The company's Import Branch conducts a cursory review of all entries filed by its broker. The individual reviewing the entry initials and dates the file indicating that the review was done. If an error is identified, the Company sends the broker a letter describing the type of error with instructions to correct the error. In addition, the company reconciles the export quantity to imported quantity on a monthly basis to ensure that materials returned after being exported for repairs/alternations do not exceed the quantity originally exported.

The Manual also requires the Import/Export Compliance Manager to conduct internal audits on a semi-annual basis. It requires the Manager to select 26 entries (one from each week in the six-month period) for detailed review. If the review discloses any entry to be substantially non-compliant, the Manager will check entries made15 days' prior and 15 days after the date of the non-compliant entry. Within two weeks of completing the audit, the Manager is required to prepare a report with findings and recommendations and submit it to the Director of the Import/Export Department.

Pre-Assessment Survey
To determine if the controls were working, the team:

- Interviewed employees in the Purchasing, the Import Branch, and the Import/Export Department to determine if they were familiar with the procedures established in the Customs Compliance Manual.
- Selected six entries from the entries reviewed by the Import/Export Compliance Manager (two for each month in a three month period) and:
  - ✓ Determined if the company had the Repairer and Importer's declarations on file.
  - ✓ Reviewed repair orders to determine the type of work to be conducted by the foreign company.
  - ✓ Determined whether the invoice identified each of the repairs or alterations performed on the merchandise and the cost of the same.
  - ✓ Compared the repair orders to the commercial invoices.
  - ✓ Determined whether the company maintained copies of the foreign customs entry, foreign customs invoice, bill of lading or airway.
- Selected four entries from the company's files for the most current month and:
  - ✓ Determined if the files contained employees' initials indicating that the entries had been reviewed by the Import/Export Department staff.
  - ✓ Determined if the company had the Repairer and Importer's declaration on file.
  - ✓ Reviewed repair orders to determine the type of work to be conducted by the foreign company.
  - ✓ Determined whether the invoice identified each of the repairs or alterations performed on the merchandise and the cost of the same.
  - ✓ Compared the repair orders to the commercial invoices.
  - ✓ Determined if the company maintained copies of the foreign customs entry, foreign customs invoice, bill of lading or airway.
- Selected a small sample of products from related vendors, and those repaired under warranty:
  - ✓ Compared cost sheets for the foreign repairs and other supporting records, as necessary, to determine whether the value included all costs plus profit.
  - ✓ Determined whether the repairs were actually made under warranty.
- Reviewed company correspondence with the Customs broker.
- Reviewed the last three monthly quantity reconciliations performed by the Import/Export Department.
- Reviewed the most current compliance report prepared by the Import/Export Compliance Manager.

The PAS indicated that the company failed to prepare and maintain repairer's declarations to support eligibility for 9802. The PAS team did not find any evidence that the Import/Export Department staff reviewed the entries. The company agreed with the PAS findings and was able to quantify the loss of revenue.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same situation as Example A above, except the PAS team was able to verify that controls were in place and working effectively. Therefore, proceeding to ACT was not considered necessary.

Example C: Situation in which the team would proceed to ACT (Revenue)

Same situation as Example A above, except the company was not able to quantify the loss of revenue caused by not being able to support 9802 eligibility. Therefore, proceeding to ACT was considered necessary.

Example D: Situation in which the team would proceed to ACT (Compliance)

The same situation as Example A above; however, it was found that the Import/Export Compliance Manager only reviews six entries semi-annually instead of 26 as called for in the company's Manual. The Import/Export Compliance Manager refused to follow the company's Manual saying it was too time consuming, and did not take other corrective actions to address this issue. Therefore, the PAS Team would proceed to ACT.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – HTSUS 9802.00.40 and 9802.00.50 (Articles Exported for Repairs or Alterations)

PURPOSE: To determine whether 9802.00.40 and 9802.00.50 risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure that 9802.00.40/50 is correctly declared?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies and procedures periodically?					
4.	Is one department/individual primarily responsible for ensuring compliance with 9802.00.40/50 requirements?					
5.	Do written procedures assign responsibilities to a position rather than a person?					
6.	Does the individual overseeing compliance with 9802.00.40/50 requirements have adequate knowledge and training and authority to ensure that internal control procedures for imports are established and followed by all departments?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does the individual overseeing compliance have adequate cost accounting knowledge, if products are repaired by related vendors, or under warranty?					
8.	Are internal controls over 9802.00.40/50 periodically tested?					
9.	Were the results of the periodic internal control tests documented?					
10.	If weaknesses were found during internal control testing, were corrective actions implemented?					
11.	Does the company identify, analyze, and manage risks related to 9802.00.40 and 50?					
12.	Has the company identified any risks related to 9802.00.40 and 50 and implemented control mechanisms?					
13.	Does the company use the results of testing to correct its import declarations?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Do the company's procedures include a retention program for documents needed to support 9802.00.40/50 claims (e.g. importer's declarations, repairer's declarations, cost sheets and supporting financial documents from related parties and for warranty repairs, etc.)					
15.	Does the company have procedures in place to ensure that the true costs for material, labor, overhead, general expenses and profit were included in the value of repairs performed by related parties, and for warranty work, even if not payable on the part of the importer?					
16.	Does the company have good interdepartmental communication about 9802.00.40/50 matters?					
17.	Do written controls include specific procedures for monitoring eligibility with 9802.00.40/50 requirements?					
18.	Does the company have procedures to ensure that merchandise imported was the same as the merchandise exported?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
19.	Does the company have procedures in place to ensure the foreign operations did not cause the identity or HTSUS classification of the exported article to change?					
20.	Does the company have procedures in place to ensure that drawback was not previously claimed on exported articles?					
21.	Does the company provide adequate broker oversight?					
22.	List company-specific procedures and controls below (if applicable):					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

HTSUS 9802.00.60 – METAL ARTICLES PREVIOUSLY EXPORTED FOR PROCESSING
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 HTSUS 9802.00.60 GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS 3
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 4

3.1 RISK 4
A. Preliminary Assessment of Risk.....4
B. Evaluation of Risk Acceptability 5
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMITS) 6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – HTSUS 9802.00.60 (METAL ARTICLES PREVIOUSLY EXPORTED FOR PROCESSING)....11

HTSUS 9802.00.60 – METAL ARTICLES PREVIOUSLY EXPORTED FOR PROCESSING

TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

Provide guidance for performing a Pre-Assessment Survey (PAS) of the company's internal control for merchandise entered under HTSUS 9802.00.60 and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on Assessing Internal Controls in Performance Audits, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and American Institute of Certified Public Accountants Statement on Auditing Standards No. 78.

PART 2 HTSUS 9802.00.60 GUIDANCE

9802.00.60 constitutes any article of metal (except precious metals) manufactured in the U.S. or subjected to a process of manufacture in the U.S. and exported for further processing, and any article of metal which results from processing outside the U.S. and is then returned to the U.S. for further processing. The returned articles are dutiable on the value of the processing outside the U.S., provided the documentary requirements of 19 CFR 10.9 are met.

Title19 CFR 10.9 states: "Except as otherwise provided for in this section, the following documents shall be filed in connection with the entry of articles which are returned after having been exported for further processing and which are claimed to be subject to duty only on the value of the processing performed abroad under subheading 9802.00.60, Harmonized Tariff Schedule of the United States (HTSUS): (1) A declaration from the person who performed the processing abroad….; and (2) A declaration by the owner, importer, consignee, or agent having knowledge of the pertinent facts…."

Title 19 CFR 10.9(b) states, "The port director may require such additional documentation as is deemed necessary to prove actual exportation of the articles from the United States for processing, such as a foreign customs entry, foreign customs invoice, foreign landing certificate, bill of lading, or an airway bill." Title 19 CFR 10.9(b) states, "If the port director concerned is satisfied, because of the nature of the articles or production of other evidence, that the articles are imported under circumstances meeting the requirements of subheading 9802.00.60, HTSUS, and related section and additional U.S. notes, he may waive submission of the declarations provided for in paragraph (a) of this section."

HTSUS 9802.00.60 imposes a dual "further processing" requirement on qualifying metal articles: foreign processing, and when returned, domestic processing. More specifically, "'further" processing refers to processing that changes the shape of the metal or imparts new and different characteristics, which become an integral part of the metal itself and which did not exist in the metal before processing. Thus, further processing includes machining, grinding, drilling, threading, punching, forming, plating, and the like, but does not include painting or the mere assembly of finished parts by bolting, welding, etc.".

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions, which may indicate a potential problem in 9802.00.60.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring 9802.00.60 for Customs purposes. Examples:
  - ✓ Company does not monitor or interact with the broker on 9802.00.60 issues.
  - ✓ Company relies on one employee to handle 9802.00.60 issues, and there are poor or no management checks or balances over this employee.
- Company Customs staff lacks knowledge of 9802.00.60 eligibility requirements.
- Company's import staff lacks the knowledge of cost accounting that is necessary to determine whether the value covers all costs and profit for processing performed by related parties and to ensure that supporting cost records are retained and readily available.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.
- A significant variance exists between the importer's data and Customs data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with 9802.00.60.
- The Questionnaire indicated that the company does not have procedures to:
  - ✓ Verify processor's declarations (see reasonable care – United States v. Golden Ship Trading Company, Joanne Wu and American Motorists Insurance Company, Slip Op. 01-7).
  - ✓ Review processing operations performed at the foreign plant to determine whether such operations qualify as further processing (i.e., not just assembly).
  - ✓ Establish that further processing in the U.S. occurred.
  - ✓ Verify that the imported articles are the same as the exported articles.
- Company has many drawback claims.
- Article doesn't receive further processing before sale.
- The product goes directly to finished goods inventory.
- Importer and foreign processing sites are related and all elements of cost and profit, including overhead, general expenses and profit, are not included in the processing value. Foreign processing is often performed by the related foreign factories that manufactured the products. Transaction value may not be acceptable if the processing value does not cover all costs and a reasonable profit.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over 9802.00.60:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import Department, including ensuring eligibility of merchandise entered under 9802.00.60. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- The Import Manager also has cost accounting knowledge, for control of imports from related parties.

- Written internal control procedures assign 9802.00.60 related duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about 9802.00.60 matters.
- Company conducts and documents periodic reviews of 9802.00.60 merchandise, and uses the results to make corrections past and present to entries and changes to their import operations as appropriate.
- The importer or the importer's agent visits the plant in the country where the 9802.00.60 products are processed.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures for ensuring proper handling of 9802.00.60.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to 9802.00.60.
- Company's documentation that supports monitoring and verification of established and/or written internal control for 9802.00.60, such as:
  - ✓ Processor's Declarations.
  - ✓ Importer's Declarations.
  - ✓ Entry documents (CF 7501, invoice, etc.).
  - ✓ Export documents (invoices, bills of lading, etc.).
  - ✓ Bills of material and/or detailed breakdown of standard material costs.
  - ✓ Processing orders and contract documenting the reason of exportation; and
  - ✓ Production records.
  - ✓ Cost sheets from related parties performing processing and allocation worksheets for overhead, general expenses, and profit.
- Internal and external audit reports.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**, and

2. The **internal control** system by determining if the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs

based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.
   - Monitoring.

2. Review relevant Customs and company documents to identify and understand relevant internal control over 9802.00.60 entries. (Examples of documents and information to review are listed on the prior page.)

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence (such as a log) of communication with the broker and company departments on 9802.00.60 issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Documentary evidence that company-specific rulings are requested and followed.
   - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
   - Training records and materials relating to 9802.00.60 used to educate staff on Customs matters.
   - Documentary evidence that the company ensures the merchandise was exported from the U.S. without payment of drawback.
   - Documentary evidence (such as certificates of origin or manufacturer's affidavits) that demonstrate that the company ensured that metal articles exported from the U.S. have

been manufactured in the U.S. or, if of foreign origin, were subjected to a process of manufacture in the U.S. before being exported for further processing.
- Documentary evidence that the company ensures that articles imported in their processed condition are the same articles that were exported.
- Documentary evidence, such as engineering drawings, showing that the company ensured the processes performed in foreign country and U.S. are considered further processing.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for 9802.00.60 in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control
   - Determine what is already known about control effectiveness
   - Assess the adequacy of internal control design
   - Determine whether controls are implemented and effective
   - Determine whether transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMITS)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the overall 9802 level that will be reported on. For example, the company may import from various foreign entities and from various countries and tests may be designed for areas identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from Assessing Internal Controls in Performance Audits.
Column titled “Testing Limit” reflects Customs test sizes.

Note:
PAS audit tests for 9802.00.60 should be used to confirm that internal control is reasonably adequate to assure that 9802.00.60 claims are accurately declared.

Example: Validation of Company Control Activity

One of the company's internal controls over 9802.00.60 is that they review every 20th 9802.00.60 transaction to ensure that 9802.00.60 are properly declared. The company maintains a "9802.00.60 Review Log" to document this review process. To determine internal control effectiveness, the PAS team may decide to verify that the company review procedure identifies incorrectly declared 9802.00.60 and the company takes appropriate corrective action, including improved procedures to avoid future improperly declared 9802.00.60.

The PAS team may select a limited number of reviewed items from the "9802.00.60 Review Log" to verify that 9802.00.60 was adequately reviewed to determine accurate declaration of 9802.00.60, and that any incorrectly declared 9802.00.60 entries were corrected (causes identified and procedures corrected to ensure future compliance) and reported to Customs.

In addition, the PAS team should verify that the company took action to avoid future improperly declared 9802.00.60 after such errors were identified. In order to do this, the PAS team should verify that the same types of improperly declared items were correctly declared on subsequent entries. Following are examples of some of the tests that can be performed to determine if 9802.00.60 is accurately declared:

- Review processor's and importer's declarations to verify documentary requirements of 19 CFR 10.9 are met.
- Trace the imported articles through receiving and inventory records into work in process to verify further processing was performed in the U.S.
- Determine types of records (i.e., general ledger accounts, management reports, production reports, etc.) used by importer to determine costs of material, labor, overhead, general and administrative expenses and profit, and cost or value of the processing actually performed abroad and have importer demonstrate how entry information was developed.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over 9802.00.60.

1. Complete the WEIC for 9802.00.60 to determine whether risk is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT.

   <u>Do not proceed to ACT if:</u>

- Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
- The result of review indicated that the error was due to an isolated incident.
- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

Proceed to ACT if:

- The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS are for clarification only.

Example A: Situation in which the team would not proceed to ACT (Revenue)

Company's Policies and Procedures
The company's Customs Compliance Manual (CCM) requires the purchasing department to obtain a declaration from the foreign company performing the processing. The buyer submits the declaration to company's Import Department and provides assistance to the Import Department, if necessary, in preparing the Importer's Declaration. The Import Department in turn is responsible for submitting these declarations to the Customs broker with instructions to include them with the entry. The buyer is also responsible for conferring with the foreign company to make sure that the invoice to be sent to the company sets forth the processing performed and the cost or value of the processing. The production department is required to submit to the Customs Department production records documenting that the metals have been further processed in the U.S. after importation. The CCM further requires the Customs Department to maintain and have ready for submission the foreign customs entry, foreign customs invoice, and bill of lading/air waybill related to the export of the merchandise from the U.S. for processing in case the U.S. Customs Service should request additional supporting documentation.

Monitoring Activities
The CCM also established procedures to verify compliance. First, the company's Customs Department conducts a cursory review of all entries filed by the Customs broker. If an error is identified the Company sends the broker a letter describing the type of error with instructions to

correct the error. In addition, the company reconciles quantities of exported articles to imported articles on a monthly basis to ensure that materials imported do not exceed quantities of materials originally exported.

Finally, the CCM establishes procedures for conducting internal audits on a semi-annual basis. The Manual requires the Import/Export Compliance Manager to select 26 entries (one from each week in the six-month period) for detailed review. If the review discloses any entry to be substantially not compliant, the Manager also checks entries made in the 15 days prior and 15 days after the non-compliant entry was made. Within two weeks of completing the audit, the Manager is required to prepare a report with findings and recommendations and submit it to the Director of the Import/Export Department.

Pre-Assessment Survey
To determine if the controls were working, the team:

- Interviewed employees in the Purchasing Department to determine if they were familiar with the procedures established in the CCM.
- Selected 5 entries from ACS and:
  - ✓ Determined if the company had the Processor's and Importer's declarations on file.
  - ✓ Reviewed processing orders to determine the type of work to be conducted by the foreign company.
  - ✓ Reviewed production records to determine the types of further processing performed in the U.S.
  - ✓ Determined whether the invoice identified the processing performed on the merchandise and the cost of the processing.
  - ✓ Compared the processing orders to the commercial invoices.
  - ✓ Determined if the company maintained copies of the foreign customs entry, foreign customs invoice, bill of lading or airway bill.
- Correspondence file to the Customs brokers.
- Reviewed the most current compliance report prepared by the Import/Export Compliance Manager.

The PAS team determined that the company failed to prepare and maintain processor's declarations, failed to maintain production records verifying that further processing occurred in the U.S. after importation, and stopped conducting the semiannual compliance reviews. However, the company agrees with the PAS findings, agrees to implement corrections, and is able to quantify the actual loss of revenue caused by not being able to support 9802.00.60 eligibility. Therefore, proceeding to ACT was not considered necessary.

Example B: Situation in which the team would not proceed to ACT (Compliance)

The same circumstances, as Example A above, except the PAS team was able to verify that controls were in place and working effectively. Proceeding to ACT was not necessary.

Example C: Situation in which the team would proceed to ACT (Revenue)

The same circumstances, as Example A above, except the company is not able to quantify the loss of revenue caused by not being able to support 9802.00.60 eligibility. Therefore, proceeding to ACT was necessary.

Example D: Situation where the team would proceed to ACT (Compliance)

The same circumstances as Example A above, except the company did not agree to implement corrections and the extent of the noncompliance cannot be determined without substantive testing.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – HTSUS 9802.00.60 (Metal Articles Previously Exported For Processing)

PURPOSE: To determine whether 9802.00.60 risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls over 9802.00.60 formally documented?					
2.	Are written policies and procedures approved by management?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager ultimately responsible for control of the import department, including 9802.00.60?					
5.	Does the individual overseeing compliance possess adequate cost accounting knowledge, if related vendor's process products?					
6.	Does that manager have knowledge of Customs matters and the authority to assure internal control procedures for imports are established and followed by all company departments?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Do written internal control procedures assign 9802.00.60 duties and tasks to a position rather than a person?					
8.	Does company have good interdepartmental communication about 9802.00.60 matters? Is there a reliable communication system in place to ensure employees have access to current 9802.00.60 and other Customs information? (such as rulings)?					
9.	Does the company conduct and document periodic reviews of entries declared under 9802.00.60?					
10.	Does the company use 9802.00.60 periodic review results to make 9802.00.60 corrections to past and presently filed entries?					
11.	Does the company identify, analyze, and manage risks related to 9802.00.60?					
12.	Has the company identified any risks related to classification and implemented control mechanisms?					
13.	Does the company use 9802.00.60 periodic reviews to make changes to their import operations as appropriate?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Does the company provide adequate training for employees responsible for 9802.00.60 matters?					
15.	Does the company's recordkeeping system include a retention program and identify documents needed to support 9802.00.60 claims?					
16.	Has the company established a reliable system or procedure to produce any required entry documentation and supporting information relating to 9802.00.60?					
17.	Does the company have procedures to ensure that merchandise imported was the same as the merchandise exported?					
18.	Does the company have procedures in place to ensure further processing in foreign country and U.S.?					
19.	Does the company have procedures in place to ensure that the true costs for material, labor, overhead, overhead, general expenses and profit were included in the cost of processing performed by related parties?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
20.	Does the company have procedures in place to ensure that drawback was not previously claimed on articles entered under 9802.00.60?					
21.	Does the company provide adequate broker oversight to ensure proper 9802.00.60 declarations and data accuracy?					
22.	Does the company have adequate internal control to address specific issues identified in the profile?					
23.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

HTSUS 9802.00.80 – U.S. ARTICLES ASSEMBLED ABROAD
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 HTSUS 9802.00.80 GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS 2
A. General Red Flags.....3
B. Red Flags for Origin.....3
C. Red Flags for Usage.....3
D. Red Flags for Value.....3
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....4

3.1 RISK 5
A. Preliminary Assessment of Risk.....5
B. Evaluation of Risk Acceptability.....5
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMITS).....6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – HTSUS 9802.00.80 11

HTSUS 9802.00.80 – U.S. ARTICLES ASSEMBLED ABROAD TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The objective of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal controls for merchandise entered under HTSUS 9802.00.80 and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal controls to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on Assessing Internal Controls in Performance Audits, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountants Statement on Auditing Standards No. 78.

PART 2 HTSUS 9802.00.80 GUIDANCE

Subheading 9802.00.80 provides a duty allowance for assembly abroad in whole or in part of fabricated components that are the product of the United States and that (a) were exported in condition ready for assembly without further fabrication; (b) have not lost their physical identity in such articles by change in form, shape, or otherwise; and (c) have not been advanced in value or improved in condition abroad except by being assembled and except by operations incidental to the assembly process, such as cleaning, lubricating and painting. The returned articles are dutiable on the full value of the imported article less the cost or, if no charge is made, the value of such products of the United States, provided the documentary requirements of 19 CFR 10.24 are met.

19 CFR 10.24 states, "The following documents shall be filed in connection with the entry of assembled articles claimed to be subject to the exemption under subheading 9802.00.80, Harmonized Tariff Schedule of the United States (HTSUS)…. (1) A declaration by the person who performed the assembly operations abroad …; and (2) an endorsement by the importer…." Section 10.24 also contains provisions for waiver of specific details and documents, as well as references to previously filed documents, in certain circumstances.

The fabricated components must be in condition ready for assembly without further fabrication at the time of their exportation from the United States to qualify for the exemption. Components will not lose their entitlement to the exemption by being subjected to operations incidental to the assembly (e.g., cleaning, trimming, or filing, but not chemical treatment of components or polishing) either before, during, or after their assembly with other components. Materials undefined in final dimensions and shapes, which are cut into specific shapes or patterns abroad, are not considered fabricated components.

Some assembly operations (e.g., mixing or combining of liquids or chemicals) are not significant enough to qualify.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem for 9802.00.80. The red flags are separated into four categories: (A) General, (B) Origin, (C) Usage, and (D) Value.

A. General Red Flags

- The company has insufficiently documented, poorly defined, or no internal controls for accurately declaring 9802.00.80 for Customs purposes.
  - ✓ The company does not monitor or interact with the broker on 9802.00.80 issues.
  - ✓ The company relies on one employee to handle 9802.00.80 issues, and there are poor or no management checks or balances over this employee.
- Company Customs staff lack knowledge of 9802.00.80 eligibility requirements.
- The company offers unreasonable explanations to Customs inquiries.
- The company fails to cooperate with or respond to Customs.
- The company has a high turnover of people in key Customs positions.
- Significant variance exists between the importer's data and Customs data.
- Customs (e.g., import specialist, account manager, compliance measurement, prior audit, other profile information) shows a history of problems with 9802.00.80.
- U.S. and foreign components are commingled.
- The description of the assembly process for the imported article includes descriptions involving fabrication, completion, or improvement.
- The company has no export documents to show components were shipped to the manufacturer.
- The company has many drawback claims.

B. Red Flags for Origin

- The company has no manufacturers' affidavits, or certificates or affidavits on file are incomplete.
- Certificates of Origin are from a known distributor/wholesaler.
- There is dual sourcing of fungible or commercially interchangeable components.

C. Red Flags for Usage

- The importer cannot provide records to prove the U.S. components were used in production.
- Inventory and accounting records indicate that the quantities of components purchased and shipped are less than the quantities claimed as 9802.00.80.
- The components are not shown on the bill of materials for the imported article.

D. Red Flags for Value

- The import specialist/account manager has had previous experience with the company failing to file cost submissions or preparing inaccurate cost submissions.
- Costs of components deducted from the foreign invoice value were not included in the foreign invoice value.
- Foreign transportation, freight, and insurance costs are inappropriately omitted from the dutiable value.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over 9802.00.80:
  - ✓ Are in writing;

  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are approved by management.
- One manager is ultimately responsible for control of the Import Department, including ensuring eligibility of merchandise entered under 9802.00.80. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- The company has good interdepartmental communication about Customs matters.
- The company conducts and documents periodic reviews of 9802.00.80 merchandise and uses the results to make corrections to entries and changes to its import operations as appropriate.
- The importer obtains manufacturers' affidavits and other documentation supporting U.S. origin prior to claiming 9802.00.80.
- The importer obtains documentation to support the FOB U.S. port of export value of components prior to claiming 9802.00.80.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Written internal control policies and procedures for ensuring proper 9802.00.80 eligibility.
- The company's responses to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to 9802.00.80.
- Company documentation that supports monitoring and verification of established and/or written internal controls over 9802.00.80, such as:
  - ✓ Entry Summary and invoice
  - ✓ Manufacturer's affidavits
  - ✓ Certificates of origin
  - ✓ Cost submission
  - ✓ Production records
  - ✓ Inventory records
  - ✓ Export documents (e.g., Mexican Pedimento, invoice, bill of lading)
  - ✓ Foreign Assembler's Declaration
  - ✓ Endorsement by the importer
  - ✓ Cost sheets
  - ✓ Accounting records
  - ✓ Bills of materials
  - ✓ Specification sheets
- Internal and external audit reports.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate the effectiveness of internal controls and to determine whether there is a sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) phase.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal controls are effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they were applied, and who applies hem.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.
- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.
- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment
   - Risk Assessment
   - Control Activities
   - Information and Communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal controls over 9802.00.80. (Examples of documents and information to review are listed above.)

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.

- Documentary evidence of communication with the broker and company departments on 9802.00.80 issues, including company testing of broker operations and verification that the broker followed company instructions.
- Documentary evidence that company-specific rulings are requested and followed.
- Documentary evidence of intercompany communications to ensure that correct information is provided to Customs.
- Training records and materials used to educate staff on Customs matters.
- Documentary evidence that the company ensures that the merchandise was exported from the United States without payment of drawback.
- Documentary evidence that the company ensures that the merchandise was not advanced in value or improved in condition while abroad.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for 9802.00.80 in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal controls
   - Determine what is already known about control effectiveness
   - Assess the adequacy of internal control design
   - Determine whether controls are implemented and effective
   - Determine whether transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMITS)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In such cases, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the HTSUS 9802.00.80 level that will be reported on. For example, the company may import from several foreign companies, but testing may be necessary only for certain companies or only for certain imports that have been identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate		Low to Moderate Low	1-10

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
		Strong		Very Low	

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled "Testing Limit" reflects Customs test sizes.

Example: (Determination of Testing Level)

One of the company's internal controls over 9802.00.80 is that it reviews every 20th 9802.00.80 transaction to ensure that 9802.00.80 transactions are properly declared. The company maintains a "9802.00.80 Review Log" to document this review process. To determine internal control effectiveness, the PAS team may decide to verify that the company review procedure identifies incorrectly declared 9802.00.80 and that the company takes appropriate corrective action, including improved procedures to avoid future improperly declared 9802.00.80.

The PAS team may select a limited number of reviewed items from the "9802.00.80 Review Log" to verify that 9802.00.80 was properly reviewed to determine accurate declaration of 9802.00.80 and that any incorrectly declared 9802.00.80 entries were corrected and reported to Customs.

In addition, the PAS team should verify that the company took action to avoid future improperly declared 9802.00.80 after such errors were identified. In order to do this, the PAS team should verify that the same types of improperly declared items were correctly declared on subsequent entries. The following are examples of some of the tests that can be performed to determine whether 9802.00.80 are accurately declared.

Origin

- Compare the dates of manufacturers' affidavits to the dates of 9802.00.80 claims.
- Review purchase orders and bills of materials to identify dual sourcing of materials.
- Conduct third-party verifications to verify origin.

Usage

- Using inventory and accounting records identify the quantities of components purchased and shipped compared to the quantities claimed as 9802.00.80.
- Conduct a plant tour.

Value

- Compare the 9802.00.80 value on the cost submission to accounting records.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of the company's internal controls over 9802.00.80.

1. Complete the WEIC (Part 4 of this document) for 9802.00.80 to determine whether risk is acceptable or unacceptable and document why. Put the results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the

import specialist or account manager. The team must evaluate the PAS results based on the specific situation(s).

2. The following will help the PAS team determine whether conditions warrant proceeding to ACT:

   Do not proceed to ACT if:
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   Proceed to ACT if:
   - The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement actions.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS are *for clarification purposes only.*

Example A: Situation in which the team would not proceed to ACT (Compliance)

Company's Policies and Procedures
The company's Customs Compliance Manual requires the buyer to identify U.S.-origin components used in the assembly of imported articles and obtain a declaration from the foreign company performing the assembly. This includes obtaining manufacturers' affidavits from suppliers prior to making the 9802.00.80 claim. The affidavits are compared to the bills of materials for imported articles to identify where a 9802.00.80 claim can be made. The buyer submits the declaration to the company's Customs Department and provides assistance to the Customs Department, if necessary, in preparing the Importer's Declaration. The Customs Department in turn is responsible for submitting these declarations to the Customs broker with instructions to include them with the entry. The buyer is also responsible for conferring with the foreign company to make sure that the invoice to be sent to the company sets forth the cost or value of the articles and the assembly. The Customs Compliance Manual further requires the Customs Department to maintain and have ready for submission the foreign customs entry,

foreign customs invoice, and bill of lading/air waybill related to the export of the merchandise from the United States for assembly in case the U.S. Customs Service should request additional supporting documentation.

Monitoring Activities

The Customs Compliance Manual also includes procedures to verify compliance. First, the company's Customs Department conducts a cursory review of all entries filed by the Customs broker. If an error is identified, the company sends the broker a letter describing the type of error, with instructions to correct the error. In addition, the company reconciles quantities of exported articles to imported articles on a monthly basis to ensure that materials imported do not exceed quantities of materials originally exported.

Finally, the Manual establishes procedures for conducting internal audits on a semiannual basis. The Manual requires the import/export compliance manager to select 26 entries (one from each week in the 6-month period) for detailed review. If the review discloses any entry to be substantially noncompliant, the manager also checks entries made in the 15 days before and 15 days after the noncompliant entry was made. Within 2 weeks of completing the audit, the manager is required to prepare a report with findings and recommendations and submit it to the director of the Import/Export Department.

Pre-Assessment Survey

To determine whether the controls are working, the PAS team:

- Interviewed employees in the Purchasing Department to determine whether they are familiar with the procedures established in the Customs Compliance Manual
- Selected five entries from the Automated Commercial System (ACS) and:
  - ✓ Reviewed the manufacturers' affidavits and compares the part numbers against the bills of materials.
  - ✓ Trace the 9802.00.80 value shown on the bills of materials to the 9802.00.80 claim made at entry.
  - ✓ Identified part numbers on the bills of materials that were not covered by a manufacturer's affidavit.
  - ✓ Determined whether the company had the assembler and importer's declarations on file.
  - ✓ Reviewed assembly orders to determine the type of work to be conducted by the foreign company.
  - ✓ Determined whether the invoice identified the value of the foreign materials, assembly performed on the merchandise, and the cost or the value of the article.
  - ✓ Compared the assembly orders to the commercial invoices.
  - ✓ Determined whether the company maintained copies of the foreign customs entry, foreign customs invoice, and bill of lading or airway bill.
- Reviewed the correspondence file to the Customs brokers.
- Reviewed the most current compliance report prepared by the import/export compliance manager.

Since the PAS team was able to verify that controls are in place and working effectively, proceeding to ACT was not considered necessary.

Example B: Situation in which the team would not proceed to ACT (Revenue)

The circumstances are the same as in example A above, except that the company failed to maintain the assemblers' declarations and manufacturers' affidavits and stopped conducting semiannual compliance reviews. However, the company agreed with the PAS findings and was able to quantify the actual loss of revenue caused by not being able to support 9802.00.80 eligibility. Therefore, proceeding to ACT was not considered necessary.

Example C: Situation in which the team would proceed to ACT (Compliance)

The circumstances are the same as in example B above, except that the company disagreed with taking proper corrective action. The company was noncompliant with a specific Customs Regulation, failed to monitor compliance with Customs requirements, and did not agree to take corrective action. It was necessary to calculate a compliance rate. Thus, the audit team proceeded to ACT.

Example D: Situation in which the team would proceed to ACT (Revenue)

The circumstances are the same as in example B above, except that the company was not able to quantify the loss of revenue caused by not being able to support 9802.00.80 eligibility. Therefore, proceeding to ACT was considered necessary.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – HTSUS 9802.00.80

PURPOSE: To determine whether HTS 9802.00.80 risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Risk Exposure Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1-Internal Control Questions

	Internal Control	Yes	No	Workpaper Reference		Comments
				Internal Control Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	GENERAL QUESTIONS					
1.	Does the company have formally documented internal controls to assure that 9802.00.80 is properly reported?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies and procedures periodically?					
4.	Is internal control over 9802.00.80 periodically tested and results documented? (This should include post-entry reviews to verify correctness of values and classifications.)					
5.	If weaknesses were found during internal control testing, did the company correct internal control procedures and entries when appropriate?					
6.	Do written internal control procedures assign 9802.00.80 responsibilities to a position rather than an individual?					

	Internal Control	Yes	No	Workpaper Reference		Comments
				Internal Control Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does that individual have adequate knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
8.	Does the company have good interdepartmental communication about 9802.00.80 matters? Is a reliable communication system in place to ensure that employees have access to current 9802.00.80 and other Customs information (e.g., rulings)?					
9.	Does the company communicate with its broker to provide updated listings of products eligible for 9802.00.80? Does the company review the broker's use of 9802.00.80?					
10.	Does the company conduct and document periodic reviews of entries declared under 9802.00.80?					
11.	Does the company identify, analyze, and manage risks related to 9802.00.80?					

	Internal Control	Yes	No	Workpaper Reference		Comments
				Internal Control Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
12l	Has the company identified any risks related to 9802.00.80 and implemented control mechanisms?					
13.	Does the company use 9802.00.80 periodic review results to make 9802.00.80 corrections to past and present filed entries?					
14.	Does the company use 9802.00.80 periodic review results to make changes to its import operations as appropriate?					
15.	**Documentation**. Does the company's recordkeeping system include a retention program and identify documents needed to support 9802.00.80 claims?					
16.	**Documentation**. Has the company established a reliable system or procedure to produce any required entry documentation and supporting information?					
17.	**Origin**. Does the company have procedures in place to verify U.S. origin (e.g., suppliers are required to provide manufacturers' affidavits, assemblers' declarations, or other documentation proving U.S.-origin parts)?					

	Internal Control	Yes	No	Workpaper Reference		Comments
				Internal Control Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
18.	**Origin**. Does the company have procedures for follow-up with suppliers to confirm the accuracy of such information? Is documentation maintained to support follow-up of information with suppliers?					
19.	**Origin**. Do commercial invoices include country of origin, value, part number, and serial numbers?					
20.	**Origin**. Are part numbers for U.S.-origin components maintained in a database that is provided to the company's brokers?					
21.	**Origin**. Does the importer maintain manufacturers' affidavits or other documentation proving U.S. origin?					
22.	**Advanced or Improved**. Does the importer maintain assemblers' declarations or other documentation attesting to the fact that the merchandise was not advanced in value or improved in condition?					
23.	**Advanced or Improved**. Are descriptions of the assembly process obtained prior to making 9802.00.80 claims on new or revised products?					

	Internal Control	Yes	No	Workpaper Reference		Comments
				Internal Control Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
24.	**Usage**. Does the importer have specific identifiers, such as serial numbers, to trace the merchandise through the inventory system?					
25.	**Usage**. Are assemblers required to provide a bill of materials and a cost sheet that identify 9802 components and confirm usage of these U.S. components?					
26.	**Value**. Is the cost submission filed in a timely manner, and does it include the actual cost of 9802.00.80 claims, if applicable is reconciliation filed in a timely manner?					
27.	**Value.** Are the Design and Purchasing Departments required to notify the company's Customs Department formally of any design/supplier changes that affect imported products?					
28.	**Value**. Does the company maintain historical data regarding these changes?					
29.	**Non-qualifying**. Does the company have procedures in place to ensure that drawback was not previously claimed on articles entered under 9802.00.80?					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

*If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples related to 9802.00.80 are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have the company do quantification.

HTSUS 9802.00.90 – U.S. FORMED AND CUT TEXTILE FABRIC ASSEMBLED IN MEXICO (FORMERLY MEXICAN SPECIAL REGIME)

TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 HTSUS 9802.00.90 GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS 2
A. General Red Flags 3
B. Red Flags for Origin 3
C. Red Flags for Usage 3
D. Red Flags for Value 3
2.2 EXAMPLES OF BEST PRACTICES.....4
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 4

3.1 RISK 5
A. Preliminary Assessment of Risk.....5
B. Evaluation of Risk Acceptability 5
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TEST (TESTING LIMIT).....6
3.4 EVALUATION OF PRE-ASSESSMENT OF SURVEY TESTING RESULTS 7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – HTSUS 9802.00.90 (US FORMED AND CUT TEXTILE FABRIC ASSEMBLED IN MEXICO) .11

HTSUS 9802.00.90 – U.S. FORMED AND CUT TEXTILE FABRIC ASSEMBLED IN MEXICO (FORMERLY MEXICAN SPECIAL REGIME)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The purpose of this document is to provide guidance for performing a Pre-Assessment Survey (PAS) of the company's internal controls for merchandise entered under HTSUS 9802.00.90 and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal controls to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78*.

PART 2 HTSUS 9802.00.90 GUIDANCE

Subheading 9802.00.90 provides duty-free treatment for textile and apparel goods assembled in Mexico in which all fabric components were wholly formed and cut in the United States, provided that such fabric components, in whole or in part, (a) were exported in condition ready for assembly without further fabrication; (b) have not lost their physical identity in such articles by change in form, shape or otherwise; and (c) have not been advanced in value or improved in condition abroad except by being assembled and except by operations incidental to the assembly process; provided that goods classifiable in chapter 61, 62, or 63 may have been subject to bleaching, garment dyeing, stone-washing, acid-washing, or perma-pressing after assembly. The returned articles are completely nondutiable and are not subject to an absolute quota or to visa requirements.

All fabric components (including linings, pocketing, interfacing, and interlining), with the exception of findings, trimmings, and certain elastic strips (i.e., thread, snaps, bow buds, hooks and eyes, buttons, zippers, lace trim, labels, elastic < 1 inch wide) not exceeding 25 percent of the cost of the components of the assembled product, must be U.S. formed and cut. (Note: The measurement for determining the 25 percent is the cost of the components, not the value of the product as a whole. This means that labor value involved in the assembly operation is irrelevant for the purpose of determining the maximum allowable foreign content.) The same firm must act as the exporter of cut parts and importer of assembled articles.

Generally, griege fabric imported into the United States and then finished in the United States does not qualify.

The product must be assembled in Mexico.

2.1 EXAMPLES OF RED FLAGS

The following examples of conditions that may indicate a potential problem in 9802.00.90) are broken down into four categories: (A) General, (B) Origin, (C) Usage, and (D) Value.

A. General Red Flags

- The company has insufficiently documented, poorly defined, or no internal controls for accurately declaring 9802.00.90 for Customs purposes.
  - ✓ The company does not monitor or interact with the broker on 9802.00.90 issues.
  - ✓ The company relies on one employee to handle 9802.00.90 issues, and there are poor or no management checks or balances over this employee.
- Company Customs staff lack knowledge of 9802.00.90 eligibility requirements.
- The company offers unreasonable explanations to Customs inquiries.
- The company fails to cooperate with or respond to Customs.
- The company has a high turnover of people in key Customs positions.
- Significant variance exists between the importer's data and Customs data.
- Customs (e.g., import specialist, account manager, compliance measurement, prior audit, other profile information) shows a history of problems with 9802.00.90.
- U.S. and foreign components are commingled.
- The description of the assembly process for the imported article includes descriptions involving fabrication, completion, or improvement.
- The company has no export documents to show that components were shipped to the manufacturer.
- The company has many drawback claims.

B. Red Flags for Origin

- The company has no mill invoices, mill certificates, or manufacturers' affidavits (including name of mill and/or manufacturer), or invoices, certificates, or affidavits on file are incomplete.
- The company has no cutting tickets (including name and location of facility, style number, total number being cut, and type of fabric) or incomplete cutting tickets on file.
- Certificates of Origin are from a known distributor/wholesaler.
- The company dual sources fungible or commercially interchangeable components.

C. Red Flags for Usage

- The importer cannot provide records to prove the U.S. components were used in production.
- Inventory and accounting records indicate that the quantities of components purchased and shipped are less than the quantities claimed as 9802.00.90.
- Components are not shown on the bill of materials for the imported article.

D. Red Flags for Value

- The import specialist/account manager have previous experience with the company failing to file cost submissions or preparing inaccurate cost submissions.
- The costs of the components deducted from the foreign invoice value were not included in the foreign invoice value.
- The export value of the components is less than the value associated with the components upon importation as part of the finished article.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over 9802.00.90:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are approved by management.
- One manager is ultimately responsible for control of the Import Department, including ensuring eligibility of merchandise entered under 9802.00.90. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- The company has good interdepartmental communication about Customs matters.
- The company conducts and documents periodic reviews of 9802.00.90 merchandise and uses the results to make corrections to entries and changes to its import operations as appropriate.
- The importer obtains manufacturers' affidavits and other documentation supporting U.S. origin prior to claiming 9802.00.90.
- The importer obtains documentation to support the FOB U.S. port of export value of components prior to claiming 9802.00.90.

2.3 Examples of Documents and Information to Review

- Written internal control policies and procedures for ensuring proper 9802.00.90 eligibility
- The company's responses to the questionnaire
- Interviews with company staff concerning actual procedures and controls specific to 9802.00.90
- Company documentation that supports monitoring and verification of established and/or written internal controls over 9802.00.90, such as:
  - ✓ Entry Summary and invoice
  - ✓ Manufacturer's affidavits
  - ✓ Certificates of Origin
  - ✓ Mill invoice
  - ✓ Cutting ticket
  - ✓ Transportation records from mill to cutting facility to border to assembler
  - ✓ Cost submission
  - ✓ Production records
  - ✓ Inventory records
  - ✓ Export documents (e.g., Mexican Pedimento, bill of lading)
  - ✓ Cost sheets
  - ✓ Accounting records
  - ✓ Bills of materials
  - ✓ Specification sheets
- Internal and external audit reports

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate the effectiveness of internal controls and to determine whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) phase.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal controls are effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment
   - Risk Assessment
   - Control Activities
   - Information and Communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal controls over 9802.00.90. (Examples of documents and information to review are listed above.)

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence of communication with the broker and company departments on 9802.00.90 issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Documentary evidence that company-specific rulings are requested and followed.
   - Documentary evidence of intercompany communications to ensure that correct information is provided to Customs.
   - Training records and materials used to educate staff on Customs matters.
   - Documentary evidence that the company ensures that the merchandise was exported from the United States without payment of drawback.
   - Documentary evidence that the company ensures that the merchandise was not advanced in value or improved in condition while abroad.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) Over 9802.00.90 in PART 5 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal controls.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 Extensiveness of Audit Sample Test (Testing Limit)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In such cases it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the HTSUS 9802.00.90 level that will be reported on. For example, the company may import from several foreign companies, but testing may be necessary only for certain companies or only for certain imports that have been identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled "Testing Limit" reflects Customs test sizes.

Example: Validation of Company Control Activity

One of the company's internal controls over 9802.00.90 is it reviews every 20th 9802.00.90 transaction to ensure that 9802.00.90 transactions are properly declared. The company maintains a "9802.00.90 Review Log" to document this review process. To determine internal control effectiveness, the PAS team may decide to verify that the company review procedure identifies incorrectly declared 9802.00.90 and that the company takes appropriate corrective action, including improved procedures to avoid future improperly declared 9802.00.90.

The PAS team may select a limited number of reviewed items from the "9802.00.90 Review Log" to verify that 9802.00.90 was properly reviewed to determine accurate declaration of 9802.00.90 and that any incorrectly declared 9802.00.90 entries were corrected (causes identified and procedures corrected to ensure future compliance) and reported to Customs.

In addition, the PAS team should verify that the company took action to avoid future improperly declared 9802.00.90 after such errors were identified. In order to do this, the PAS team should verify that the same types of improperly declared items were correctly declared on subsequent entries. The following are examples of some of the tests that can be performed to determine whether 9802.00.90 are accurately declared.

Origin

- Compare the dates of manufacturers' affidavits to the dates of 9802.00.90 claims.
- Compare the dates of cutting tickets to the dates of export of components.
- Review purchase orders and bills of materials to identify dual sourcing of materials.
- Conduct third-party verifications to verify origin.

Usage

- Using inventory and accounting records, identify the quantities of components purchased and shipped compared to the quantities claimed as 9802.00.90.
- Conduct a plant tour.

Value

- Compare the 9802.00.90 value on the cost submission to accounting records.

3.4 Evaluation of Pre-Assessment of Survey Testing Results

The following steps are guidance for determining the effectiveness of the company's internal controls over 9802.00.90.

1. Complete the WEIC to determine whether risk is acceptable or unacceptable and document why. Put the results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situation(s).

2. The following will help the PAS team determine whether conditions warrant proceeding to ACT:

   Do not proceed to ACT if:
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   Proceed to ACT if:
   - The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement actions.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS are *for clarification purposes only.*

Example A: Situation in which the team would not proceed to ACT (Compliance)

Company's Policies and Procedures
The company's Customs Compliance Manual requires the buyer to identify U.S.-origin components used in the assembly of imported articles. This includes obtaining manufacturers' affidavits from suppliers prior to making the 9802.00.90 claim. The affidavits are compared to the bills of materials for imported articles to identify where a 9802.00.90 claim can be made. The buyer is also responsible for conferring with the foreign assembler in Mexico to make sure that the invoice to be sent to the company sets forth the cost or value of the articles and the

assembly. The Customs Compliance Manual further requires the Customs Department to maintain and have ready for submission the Mexico Customs Entry (Pedimento), invoice for Mexico Customs, and bill of lading/air waybill related to the export of the merchandise from the United States for assembly in case the U.S. Customs Service should request additional supporting documentation.

Monitoring Activities

The Customs Compliance Manual also includes procedures to verify compliance. First, the company's Customs Department conducts a cursory review of all entries filed by the Customs broker. If an error is identified, the Company sends the broker a letter describing the type of error, with instructions to correct the error. In addition, the company reconciles quantities of exported articles to imported articles on a monthly basis to ensure that materials imported do not exceed quantities of materials originally exported.

Finally, the Manual establishes procedures for conducting internal audits on a semiannual basis. The Manual requires the import/export compliance manager to select 26 entries (one from each week in the 6-month period) for detailed review. If the review discloses any entry to be substantially noncompliant, the manager also checks entries made in the 15 days before and 15 days after the noncompliant entry was made. Within 2 weeks of completing the audit, the manager is required to prepare a report with findings and recommendations and submit it to the director of the Import/Export Department.

Pre-Assessment Survey

To determine whether the controls were working, the PAS team:

- Interviewed employees in the Purchasing Department to determine whether they are familiar with the procedures established in the Customs Compliance Manual.
- Selected five entries from ACS and:
  - ✓ Reviewed manufacturers' affidavits and compares the part numbers against the bills of materials.
  - ✓ Verified that the fabric was formed and cut in the United States.
  - ✓ Traced the 9802.00.90 value shown on the bills of materials to the 9802.00.90 claim made at entry.
  - ✓ Identified part numbers on the bills of materials that were not covered by a manufacturer's affidavit.
  - ✓ Reviewed assembly orders to determine the type of work to be conducted by the foreign company.
  - ✓ Determined whether the invoice identified the value of the foreign materials, assembly performed on the merchandise, and the cost or the value of the article.
  - ✓ Compared the assembly orders to the commercial invoices.
  - ✓ Determined whether the company maintained copies of the foreign customs entry, foreign customs invoice, and bill of lading or airway bill.
- Reviewed the correspondence file to the Customs brokers.
- Reviewed the most current compliance report prepared by the import/export compliance manager.

Since the PAS team was able to verify that controls were in place and working effectively, proceeding to ACT was not considered necessary.

Example B: Situation in which the team would not proceed to ACT (Revenue).

The circumstances were the same as in example A above, except that the company failed to maintain manufacturers' affidavits and stopped conducting the semiannual compliance reviews. However, the company agreed with the PAS findings and was able to quantify the actual loss of revenue caused by not being able to support 9802.00.90 eligibility. Therefore, proceeding to ACT was not considered necessary.

Example C: Situation in which the team would proceed to ACT (Compliance).

The circumstances were the same as in example B above, except that the company disagreed with taking proper corrective action. Because the company was unable to prove that fabric was formed and cut in the United States, failed to monitor compliance with Customs requirements, and did not agree to take corrective action, it was necessary to calculate a compliance rate. Thus the audit team proceeded to ACT.

Example D: Situation in which the team would proceed to ACT (Revenue).

The circumstances were the same as in example B above, except that the company was not able to quantify the loss of revenue caused by not being able to support 9802.00.90 eligibility. Therefore, proceeding to ACT was considered necessary.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – HTSUS 9802.00.90 (US Formed and Cut Textile Fabric Assembled in Mexico)

PURPOSE: To determine whether 9802.00.90 risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls over 9802.00.90 formally documented?					
2.	Are written policies and procedures approved by management?					
3.	Does the company review and update written policies and procedures periodically?					
4.	Is one manager ultimately responsible for control of the Import Department, including 9802.00.90? Does that manager have knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all company departments?					
5.	Do written internal control procedures assign 9802.00.90 duties and tasks to a position rather than a person?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
6.	Does the company have good interdepartmental communication about 9802.00.90 matters? Is there a reliable communication system in place to ensure that employees have access to current 9802.00.90 and other Customs information (e.g., rulings)?					
7.	Does the company conduct and document periodic reviews of entries declared under 9802.00.90?					
8.	Does the company use 9802.00.90 periodic review results to make 9802.00.90 corrections to past and present filed entries?					
9.	Does the company use 9802.00.90 periodic reviews to make changes to its import operations as appropriate?					
10.	Does the company provide adequate training for employees responsible for Customs matters?					
11.	Does the company identify, analyze, and manage risks related to 9802.00.90?					
12.	Has the company identified any risks related to 9802.00.90 and implemented control mechanisms?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	9802.00.90 Specific					
13.	Documentation. Does the company's recordkeeping system include a retention program and identify documents needed to support 9802.00.90 claims?					
14.	Documentation. Has the company established a reliable system or procedure to produce any required entry documentation and supporting information?					
15.	Origin. Does the company have procedures in place to verify U.S. origin? For example, are suppliers required to provide manufacturers' affidavits, cutting tickets, or other documentation proving the U.S. origin of parts (i.e., that the fabric was U.S. formed *and* cut)?					
16.	Origin. Does the company have procedures for follow-up with suppliers or cutters to confirm accuracy of such information? Is documentation maintained to support follow-up of information with suppliers or cutters?					
17.	Origin. Do commercial invoices include country of origin, value, part number, and serial numbers?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
18.	Origin. Are part numbers for U.S.-origin components maintained in a database that is provided to the company's brokers?					
19.	Origin. Does the importer maintain manufacturers' affidavits or other documentation proving U.S. origin?					
20.	Advanced or Improved. Does the importer maintain assemblers' declarations or other documentation attesting to the fact that the merchandise was not advanced in value or improved in condition?					
21.	Advanced or Improved. Are descriptions of the assembly process obtained prior to making 9802.00.90 claims on new or revised products?					
22.	Usage. Does the importer have specific identifiers, such as serial numbers, to trace the merchandise through the inventory system?					
23.	Usage. Are suppliers required to provide a bill of materials and cost sheet that identify 9802 components and confirm usage of these U.S. components?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
24.	Value. Is the cost submission filed timely, and does it include the actual cost of 9802.00.90 claims?					
25.	Are the Design and Purchasing Departments required to notify the company's Customs Department formally of any design/supplier changes that affect imported products?					
26.	Non-qualifying. Does the company have procedures in place to ensure that drawback was not previously claimed on articles entered under 9802.00.90?					
27.	Does the company provide adequate broker oversight to ensure proper 9802.00.90 declarations and data accuracy?					
28.	Does the company have adequate internal control to address specific issues identified in the profile?					
29.	List company-specific procedures below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

Anti-Dumping Duty/ Countervailing Duty (ADD/CVD)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 ADD/CVD GUIDANCE 2

2.1 EXAMPLES OF RED FLAGS.....3
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....4

3.1 RISK 4
A. Preliminary Assessment of Risk.....4
B. Evaluation of Risk Acceptability 5
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....7

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – ADD/CVD 9

Anti-Dumping Duty/ Countervailing Duty (ADD/CVD)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of a company's internal controls for anti-dumping duty/countervailing duty (ADD/CVD) and evaluating the results.

Generally Accepted Government Auditing Standards require the auditors to obtain a sufficient understanding of internal controls to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on Assessing Internal Controls in Performance Audits, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and American Institute of Certified Public Accountants Statement on Auditing Standards No. 78.

PART 2 ADD/CVD GUIDANCE

ADD's are assessed on imported merchandise of a class or kind that is sold to purchasers in the United States at a price less than the fair market value. Fair market value of merchandise is the price at which it is normally sold in the manufacturer's home market. CVDs are assessed to counter the effects of subsidies provided by foreign governments to merchandise that is exported to the United States. These subsidies cause the price of such merchandise to be artificially low, which causes economic "injury" to U.S. manufacturers.

19 CFR, Chapter III, section 351.211(b)(1) Instructs the Customs Service to assess antidumping duties or countervailing duties (whichever are applicable) on the subject merchandise in accordance with Secretary of Commerce instructions.

ADD/CVD rates are intended to be punitive, and therefore can be quite high. A rate in excess of 100 percent is not unusual. Therefore, the major risk to Customs is that these duties will not be paid, or will not be paid at the proper rate.

An antidumping or countervailing duty order is issued after an ADD/CVD investigation. When an order is issued, deposit rates are established for a specified period. At the end of that period, final rates are determined. The final rates for that period generally become the deposit rates for the next period. Liquidation of entries subject to ADD/CVD is suspended until final rates are determined.

All orders, deposit rates and final rates are published in the Federal Register. Each order is specific as to the commodity, country of origin, and the manufacturer/shipper. An "all other" rate for the specified commodity and country applies to Manufacturers/shippers for which a specific order was not issued. Multiple dumping or countervailing duty orders may be applicable to merchandise imported by a single importer. Orders for the same commodity and country of origin may have different ADD/CVD rates for different manufacturers/suppliers.

The commodities on an ADD/CVD order may be extremely specific. For instance, left-handed widgets may be covered, and right-handed are not. Frequently, there is not a one-to-one match between the commodities covered by an order and a tariff number. The tariff number under which the covered commodity falls may include other merchandise not covered by the ADD/CVD order. Conversely, the merchandise described by the order may be broad enough to be covered under several tariff numbers. The Department of Commerce frequently issues scope rulings to clarify which commodities are covered by an order.

The correct order must be cited on the entry summary. It is therefore important to obtain a copy of all orders related to the importer under audit from the import specialist or the importer.

There are two prongs to auditing ADD/CVD. The first is to verify that the correct order was used on merchandise entered. The second prong is to look for entries that should have been covered by ADD/CVD, but were not.

When sampling to verify the accuracy of declared ADD/CVD, it is important to review the order cited on the entry and the supporting documentation for the purchase to assure that the commodity, country of origin and manufacturer for the imported merchandise agree with the cited order.

When the importer imports merchandise that is potentially subject to ADD/CVD orders, it is important to discuss with the import specialist possible tariff numbers that may cause the importer to improperly declare or fail to declare ADD/CVD. In some instances, importers have tried to use informal entries or FTZ and warehouse entries to avoid payment of ADD/CVD. Testing for potential misclassifications and warehouse and FTZ entries may help determine if ADD/CVD orders are being circumvented.

ADD/CVD orders are issued for specific commodities by manufacturer and country of origin. A list of open orders can be obtained from the ITC web site at www.usitc.gov.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem in ADD/CVD.

- Company has insufficiently documented, poorly defined, or no internal controls for accurately declaring ADD/CVD. Examples:
  - ✓ Company does not monitor or interact with the broker on ADD/CVD issues.
  - ✓ Company relies on one employee to handle ADD/CVD issues, and there are poor or no management checks or balances over this employee.
- Company's Customs staff lacks knowledge of ADD/CVD issues.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.
- Significant variance exists between the importer's data and Customs data relative to ADD/CVD.
- Customs history (import specialist, account manager, compliance measurements, prior audit) shows problems with ADD/CVD.
- Company imports merchandise known or suspected to be subject to ADD/CVD.
- Specific issues are identified in the profile, such as switching trends in Harmonized Tariff System of the United States (HTSUS), country of origin, merchandise description, Manufacturer's Identification (MID).
- Mill certificates are not available upon request (i.e., steel).
- Merchandise enters via unusual entry types such as Temporary Importation Bond (TIB), immediate export, or bonded warehouse.
- Company receives reimbursements (rebates) for ADD/CVD.
- Import department does not have copies of ADD/CVD orders.
- Recently issued order that the company may not be aware of.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over ADD/CVD:
  - ✓ Are in writing,
  - ✓ Include having a copy of all applicable ADD/CVD orders,
  - ✓ Include procedures for monitoring and feedback, and
  - ✓ Are monitored by management.
- One manager ultimately is responsible for control of the import department, including ADD/CVD. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all company departments.
- Internal control procedures assign duties and tasks to a specific position rather than a person.
- Company has good interdepartmental communication about Customs matters.
- Company conducts and documents periodic reviews of ADD/CVD and uses the results to make corrections to entries and changes to its import operations as appropriate.
- Purchasing, Engineering, other departments, and suppliers provide sufficient information for determining whether merchandise is subject to ADD/CVD.
- Company conducts periodic reviews of the ITC web site to identify open orders and other pertinent new information. (www.usitc.gov)

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- ADD/CVD orders.
- Company's responses to the questionnaire.
- Interviews with company staff concerning internal controls specific to ADD/CVD.
- Company documentation that supports monitoring and verification of established and/or written internal controls for ADD/CVD (e.g., reports, process flowchart, and memoranda).
- CF 28, CF 29, and Fines, Penalties, and Forfeitures (FP&F) records.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate the effectiveness of internal controls and to determine if there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) phase.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal controls are effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**, and

2. The **internal controls** system by determining if the controls are in operation, how the controls were applied, how consistently they are applied, and who applies them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available

information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

Preliminary Assessment of Risk Examples

Example A: High Risk Assessment

A company that is a major importer of bearings imports a huge volume of bearings from a manufacturer that is the subject of a specific antidumping order. Automated Commercial System (ACS) records showed the company filed relatively few ADD entries. Therefore, the preliminary assessment of risk is high.

Example B: Low Risk Assessment

A company that is a major importer of pineapples had three imports of bearings that were subject to an ADD order. The bearings were used for replacement parts in the processing plant. These were the only bearing imports by the company. The import specialist did not have any concerns in this area. Therefore, the preliminary assessment of risk is low.

B. Evaluation of Risk Acceptability

After the audit work begins with the company, the team will refine the assessment of risk exposure. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.
- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.
- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consideration should be given to the five components of internal control:

    - Control Environment
    - Risk Assessment
    - Control Activities
    - Information and Communication
    - Monitoring

2. Review relevant Customs and company documents to identify and understand internal controls over ADD/CVD. (Examples of documents and information to review are listed above.)

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence of communication with the broker and company departments on ADD/CVD issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Company-specific rulings requested to determine if they are followed.
   - Documentary evidence of inter-company communications to ensure that correct information is provided to Customs.
   - Training records and materials used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for ADD/CVD in PART 4 of this document

   Note: The internal control assessment should include steps to:

   - Identify and understand internal controls
   - Determine what is already known about control effectiveness
   - Assess the adequacy of internal control design
   - Determine if controls are implemented and effective
   - Determine if transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In such cases, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. The greatest risk related to ADD/CVD is failure to report imports subject to ADD/CVD. Accordingly, the assessment process should emphasize testing of procedures to assure that imports subject to ADD/CVD are reported. Because of the difficulty of accomplishing this with limited testing, this area may require substantive testing if the risk exposure is moderate or high.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled "Testing Limit" reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of a company's internal controls over ADD/CVD.

1. Complete the WEIC for ADD/CVD to determine whether risk is acceptable or unacceptable and document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT.

<u>Do not proceed to ACT if:</u>

- Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
- The result of review indicated that the error was due to an isolated incident.
- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

<u>Proceed to ACT if:</u>

- The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

3. Determine whether referrals should be made for enforcement actions.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS are *for clarification purposes only*.

Example A: Situation in which the team would not proceed to ACT (Revenue)

During the PAS, the team found an item that was subject to ADD/CVD but had not been declared. Although the company's Customs Department had discovered the error and notified the broker, the Customs clerk had not followed up with the broker to make sure the ADD/CVD entries were corrected. The company readily agreed that the merchandise was subject to ADD/CVD. The company agreed to quantify the loss of revenue within 30 days and to tender all monies due.

Example B: Situation in which the team would not proceed to ACT (Compliance)

The same situation in example A above, except that the company agreed that the Customs manager would monitor the clerk's work and broker corrections in the future. Because the company elevated its monitoring of the broker to a management level and the ADD/CVD entries were corrected, the team agreed that the weakness was corrected and the errors did not present an unacceptable internal control risk.

Example C: Situation in which the team would proceed to ACT (Revenue)

The company imports a significant volume of merchandise subject to ADD/CVD. The company is not knowledgeable about ADD/CVD requirements and has no internal controls. A comparison of ACS data and company purchasing records shows a large discrepancy. ACS data showed the company imported $3 million worth of merchandise subject to ADD/CVD from a particular manufacturer. However, the company's accounting records revealed that the importer had actually purchased $6 million worth of merchandise subject to ADD/CVD.

Example D: Situation in which the team would proceed to ACT (Compliance and Revenue)

The company imports merchandise that was subject to a dumping order. The company has not been filing the entries as "03" (dumping entries) but as regular "01" entries. The extent of the problem is unknown, and the company is unwilling to quantify it.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – ADD/CVD

PURPOSE: To determine whether ADD/CVD risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Risk Exposure Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure that ADD/CVD are declared when appropriate and correctly declared?					
2.	Does management approve written policies and procedures for ADD/CVD? Do the written procedures include requiring the company to maintain copies of all ADD/CVD orders?					
3.	Does the company review and update written policies and procedures for ADD/CVD periodically?					
4.	Is internal control over ADD/CVD periodically tested and results documented? (This should include post-entry reviews to verify ADD/CVD was declared when appropriate and were correctly declared.)					
5.	If the company found weaknesses during internal control testing of ADD/CVD, did the company correct internal control procedures and entries when appropriate?					
6.	Do written internal control procedures assign responsibility for ADD/CVD reporting to a position rather than an individual?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does one individual have authority to ensure that internal control procedures for reporting ADD/CVD are established and followed by all company departments?					
8.	Do personnel responsible for reporting ADD/CVD have adequate knowledge and training in ADD/CVD?					
9.	Does the company have adequate interdepartmental communication about ADD/CVD?					
10.	Does the company have procedures to request Customs, Dept. of Commerce or ITC assistance regarding ADD/CVD when needed and is advice followed when given?					
11.	How does the company identify, analyze, and manage risks related to ADD/CVD?					
12.	What risks related to ADD/CVD has the company identified, and what control mechanisms has it implemented?					
13.	Do suppliers, engineers, the purchasing department, laboratory and others provide adequate descriptive information to the Import					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	Department to ensure ADD/CVD is declared when appropriate and declared correctly?					
14.	Does the company have policies and procedures in place to: (1) ensure that new items are reviewed for potential liability for ADD/CVD (2) identify new orders issued and determine if they are applicable to imported articles (3) identify new scope rulings for orders related to imported articles?					
15.	Does the company maintain product information about ADD/CVD in a database that is provided to brokers and updated when necessary?					
16.	If the company provides the broker ADD/CVD information, is the broker required to obtain company concurrence prior to making changes?					
17.	Does the company provide adequate broker oversight of ADD/CVD issues?					
18.	List company-specific procedures below (if applicable).					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have the company do quantification.

FOREIGN TRADE ZONES (FTZ) – MANUFACTURING
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 MANUFACTURING FTZ GUIDANCE 2

2.2 EXAMPLES OF BEST PRACTICES.....4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 6

3.1 RISK 6

A. Preliminary Assessment of Risk.....6

B. Evaluation of Risk Acceptability 6

3.2 INTERNAL CONTROL.....6

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 7

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....8

3.5 EXAMPLES.....9

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – MANUFACTURING FOREIGN TRADE ZONES.....11

FOREIGN TRADE ZONES – MANUFACTURING
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

Note: This guide may also be used for General Purpose Foreign Trade Zones.

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for merchandise entered into and removed from a Manufacturing - Foreign Trade Zone (FTZ) and evaluating the results.

Generally Accepted Government Auditing Standards require the auditors to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

PART 2 MANUFACTURING FTZ GUIDANCE

An FTZ is a secure area operating under the supervision of U.S. Customs and Border Protection, and under the authority of the Foreign Trade Zone. FTZs are generally used to defer payment of duties until merchandise enters the United States commerce.

Manufacturing FTZs are generally single-purpose sites operating as a subzone of the grantee because the general-purpose zone cannot accommodate the manufacturing process. Merchandise in the manufacturing zone can be manipulated, manufactured, destroyed, exhibited, or temporarily removed with the proper permits.

The Foreign Trade Zones Act of 1934 as amended in 19 U.S.C. 81a through 81u establishes how zones are created, administered, and also identifies what may be done in a zone.

Title19 CFR Part 146 establishes Customs requirements over merchandise admission, handling of the merchandise while in the zone, manipulation, manufacture, exhibition, transfer, and exportation from a zone.

The U.S. Customs Foreign Trade Zone Manual (FTZM) provides additional instructions and guidelines on Customs policy and administrative authority on zone operations. The users of the FTZM include import personnel, zone operators, grantees, and other users of the zone.

The Trade and Development Act of 2000, which became law on May 18, 2000, amended the Tariff Act of 1930, to allow all FTZs to file weekly entries for all classes of merchandise, except for merchandise that is prohibited by law. 19 USC 1484(i)

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem within the FTZ operations:

- Company has insufficiently documented, poorly defined, or no internal control over the admission and withdrawal of FTZ merchandise. Examples:
  - ✓ Company does not have a system to review, monitor, or interact with the broker on foreign trade zone issues.

  - ✓ Company relies on one employee to handle FTZ issues, and there are poor or no management checks or balances over this employee.
  - ✓ Company inventory control and recordkeeping system procedures manual is inadequate or inaccurate.
  - ✓ Company does not have control procedures for zone-to-zone transfer.
- Company staff lacks knowledge of FTZ requirements and the manufacturing process of the company.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate or respond to Customs.
- Company has high turnover of people in key positions.
- A significant variance exists between the importer's data submitted to Customs and their imported data.
- Customs (e.g. spot checks, compliance measurement exams, prior audits, import specialist, account manager, and other Customs information) shows history of problems with the company's FTZ operations.
- Operator does not maintain adequate receiving and inventory records or other documentation to support admission, manufacturing, and removal of merchandise from the FTZ.
- The FTZ contains theft-prone merchandise and security over goods within the zone-activated areas is not adequate.
- Company does not conduct physical inventory/cycle counts at scheduled time.
- Company does not do an annual reconciliation of inventory.
- The importer failed to reconcile manifest quantities to CF 214s and report any shortages or overages to Customs.
- The information reported to Customs on CF 214 does not match operator's records and third party records.
- The FTZ operator failed to file a permit (CF 216) for manipulation and manufacturing, or the permit expired.
- The company exports a large volume directly from the FTZ.
- The company has quota/visa, restricted or antidumping/countervailing duty merchandise in the FTZ.
- The FTZ does not have appropriate signs indicating FTZ restricted area.
- The company does not have records to support value of merchandise when exported.
- The company does not have detailed description of FTZ manufacturing operations.
- The company does not document change to the FTZ merchandise.
- Inventory control does not account for domestic merchandise.
- Company does not submit duty payments for inventory shortages or entries for overages to Customs.
- Shortage payments or overage entries are significantly higher or lower than prior years.
- Excessive shortages or overages are shown on the annual reconciliation.
- Few, if any, adjustments are shown on the annual reconciliation.
- Company is unable to explain or provide records supporting adjustments on the annual reconciliation.
- No documentation is prepared or maintained for scrap or destruction.
- Company does not file Manifest Discrepancy Reports (MDRs) for shortages upon receipt into the zone.
- Company utilizes a template weekly entry estimate worksheet and does not review the worksheet to ensure the quantity covered actual production/withdrawals.

- Company co-mingles domestic and foreign merchandise. Potential exists for company to switch expensive foreign merchandise for inexpensive domestic merchandise of the same kind in the zone and to export the domestic merchandise as foreign merchandise.
- Company changes the part/serial number originally admitted into the zone due to engineering changes and retains no audit trail.
- Company requests zone designation status changes from Privilege Foreign (PF) to Non-Privilege Foreign (NPF).
- Merchandise is not removed from the zone within 5 days after the permit/entry is accepted by Customs.
- Company files entry for merchandise when it is in an intermediate stage of processing with a lower duty rate but inventory records showed merchandise was never removed from the zone. Company then admitted the same merchandise as domestic for further processing that is subject to a higher duty rate.
- Operator signed the ticket for delivery into the zone instead of the cartman.
- Company uses multiple inventory systems, including a separate one for FTZ, but does not have procedures to reconcile the various systems for completeness and accuracy.
- Company uses an inventory method not authorized by Customs and did not obtain approval.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over FTZ operations:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback;
  - ✓ Are monitored by management; and
  - ✓ Include flowchart of the manufacturing process.
- One manager is responsible for control of the import department, including FTZ operations. That manager has knowledge of Customs matters and the authority to ensure internal control procedures for zone operations are established and followed by all company departments.
- The department/individual assigned to monitor compliance of the zone has the responsibility as his/her major duties and he/she has designated a backup.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- Company's FTZ administrator has a broad-based knowledge and understanding of the various departments' functions and role in relation to the zone. For example, the zone administrator has a basic understanding of the process that the inventory department used to compile the year-end reconciliation.
- Company documents and keeps records of its annual system review of its inventory control and record keeping systems.
- Company performs internal/external audit or periodic review of zone operations and uses the results to make corrections to entries and changes to their import operations, as appropriate.
- Company has good interdepartmental communication about Customs matters.
- Company official involved with FTZ merchandise participates in continuing education and is provided sufficient information to determine whether merchandise is entered, controlled and removed in compliance with Customs Regulations and the FTZ grant.

- Company provides training in Customs requirements to other departments (receiving, accounting, manufacturing, and inventory) that are directly or indirectly involved in the zone operation.
- Labs, manufacturing, engineering, and other departments provide sufficient descriptions of merchandise to permit proper classification.
- Company updates its foreign trade zone procedural manual and submits to the port director any changes at the time of its implementation.
- Company seeks rulings and assistance from Customs on unfamiliar issues.
- The company's engineering, manufacturing, and inventory departments include the zone administrator in their regular meeting and/or when changes to the bill of materials or processes occurred.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures for proper FTZ operation.
- The company's latest FTZ procedures manual submitted to the Port.
- Company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to the FTZ.
- Grant of Authority from the Foreign Trade Zone Board.
- Special Zone Procedures approved by Customs (i.e., alternative export procedures, inventory methodology).
- Documentation that supports monitoring and verification of established and/or written internal control over FTZ operations, such as:

  - ✓ Documentary evidence of periodic review or testing of internal control procedures.
  - ✓ Documentary evidence of annual internal reviews of inventory control and record keeping systems.
  - ✓ Documentary evidence that the company conducts scheduled cycle counts, physical inventory, and performs an annual reconciliation.
  - ✓ Release Order.
  - ✓ CF 6043 Delivery Ticket (cartage document).
  - ✓ CF 214 Application for Foreign Trade Zone Admission and/or Status Designation.
  - ✓ CF 7512 Transportation Entry and Manifest of Goods Subject to Customs Inspection and Permit (IT, T&E, IE).
  - ✓ CF 216 Application for Manipulation, Manufacture, Exhibit, or Destruction of Merchandise in a Zone.
  - ✓ CF 7525 Shipper's Export Declaration (SED).
  - ✓ CF 3461 Immediate Delivery Application and any amendment used for Weekly Estimated Removals.
  - ✓ CF 7501 Entry Summary.
  - ✓ CF 349 Harbor Maintenance Fee Report.
  - ✓ CF 301 Customs Bond (Activity Code 4).
  - ✓ Pro-forma/Commercial invoices.
  - ✓ Certified letter to the port director of overages and shortages as a result of annual reconciliation and evidence of duty payment for shortages and entries for overages.
  - ✓ Annual Reconciliation Report and supporting inventory count records.
  - ✓ IT or cartage document.
  - ✓ Waste and scrap reports.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company's internal control in place is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.

- Monitoring.

2. Review relevant Customs and company documents to identify and understand relevant internal control over the FTZ. (Examples of documents and information to review are listed on prior page).

3. Determine whether the company established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence, such as a log, of communication with the broker and company departments on FTZ issues. This includes company testing of broker operations and verification that the broker followed company instructions.
   - FTZ procedures manual and all other written procedures.
   - Company FTZ rulings requested. Determine whether they are followed.
   - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
   - Training records and materials used to educate staff on Customs matters.
   - Evidence that the zone operations were in conformance with the FTZ grant of authority or meet Customs approved procedures if modifications were requested.
   - Documentary evidence that the company conducts physical inventory counts and annual reconciliation.
   - Documentary evidence that the importer accounts for waste/scrap and merchandise destruction.
   - Documentation for shortages and overages in the zone, including reports to Customs.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) Over Manufacturing Foreign Trade Zones in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that they probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled "Testing Limit" reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over the FTZ operations.

1. Complete the "Worksheet for Evaluating Internal Control Over Manufacturing - FTZs" to determine whether risk determination is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT.

   - **Do not proceed to ACT (Revenue) if:**
     - ✓ Cost benefit analysis warrants no further effort (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant).
     - ✓ The PAS indicated that the error was due to an isolated incident.
     - ✓ The company agrees with PAS finding(s) and agrees to quantify the actual loss of revenue within an acceptable timeframe.

   - **Do not proceed to ACT (Compliance) if:**
     - ✓ The error was an isolated instance.
     - ✓ The errors were systemic and the importer agreed to develop and implement a compliance improvement plan within an acceptable timeframe.

   - **Proceed to ACT (Revenue) if :**
     - ✓ Company does not have adequate internal control, and PAS indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
     - ✓ Importer will not quantify loss of revenue.

- **Proceed to ACT (Compliance) if:**
  - ✓ The company refuses to take corrective action on systemic errors, and it is necessary to calculate a compliance rate.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS are for clarification purposes only:

Example A: Situation in which the team would not proceed to ACT (Revenue)

The company's consultant included written internal control procedures for admission to the zone in its procedural manual when it applied for activation. Certain areas of the manual were updated periodically. However, the company had several personnel changes. Interviews with company's current administrative personnel found that these individuals were not aware of the internal control procedures.

The auditor requested inventory records for the walk-through transaction using an admission selected from CF 214s. The admission did not appear in the company's inventory records. In addition, the auditor found that there were receipts recorded in the company's system that were not reported to Customs.

The company discovered that the omitted admissions were sample merchandise, merchandise purchased on credit cards, and merchandise sent free of charge. These omissions were of low value.

The auditor and the company added the value for all CF 214s for a period of three months and compared the value to the company's system. It was found that the total value reported to Customs on CF 214s was significantly higher than the total value recorded as receipts in the company's inventory system. Because these receipts were not recorded in the inventory system, no audit trail exists from admission, manufacturing, and withdrawal from the zone. The company performed a 100 percent review of the admission for the last fiscal year and tendered duties for all admissions not entered in its system. Additionally, the company established internal control procedures to ensure all admissions were properly recorded. The company also paid duties for merchandise not reported to Customs. The auditor verified the accuracy and accepted the company's work; therefore the team would not proceed to ACT for revenue.

To determine whether these controls were working, the team:

- Interviewed employees to determine whether they were familiar with the company's written procedures.
- Selected five items from CF 214, Application for Admission and:
  - ✓ Determined whether admissions were recorded in the inventory system;
  - ✓ Traced the selected admissions through the inventory system; from the time they were ordered until they were withdrawn from the zone;
  - ✓ Reviewed export documents to ensure merchandise was withdrawn for exportation.

- ✓ Reviewed Customs entries to determine whether proper value was declared and appropriate duties were paid.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same situation as Example A above, except the audit team was able to verify that controls were in place and working effectively. Therefore, proceeding to ACT was not considered necessary.

Example C: Situation in which the team would proceed to ACT (Revenue)

The same situation as Example A above, except the company was not able to quantify the loss of revenue caused by failure to maintain control over FTZ merchandise. Therefore, proceeding to ACT was considered necessary.

Example D: Situation in which the team would proceed to ACT (Compliance)

Same situation in Example A above except the company disagreed with taking proper corrective action. Since the company failed to monitor compliance with Customs requirements and did not agree to take corrective action, proceeding to ACT was considered necessary.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – MANUFACTURING FOREIGN TRADE ZONES

PURPOSE: To determine whether manufacturing FTZ risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are Internal Controls over FTZ operations formally documented?					
2.	Does management approve written policies and procedures?					
3.	Is one manager responsible for control of the FTZ operations?					
4.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
5.	Do written internal control procedures assign FTZ duties and tasks to a position rather than a person?					
6.	Are written policies and procedures reviewed and updated periodically?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does the company provide a copy of their procedure manual to the port director when changes are made in the FTZ procedure manual?					
8.	Does the company have adequate communication processes related to its FTZ operations?					
9.	Does company conduct and document periodic reviews of the FTZ operations?					
10.	If weaknesses were found during internal control review, were corrective actions implemented?					
11.	Does the company identify, analyze and manager risks related to FTZ operations?					
12.	Has the company identified any risks related to FTZ operations and implemented control mechanisms?					
13.	Does the company use the periodic review results to make corrections to past and present entries?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Did the company perform an annual internal review of the inventory control and record keeping system, as required by 19 CFR 146.25?					
15.	Did the company report to the Port Director any deficiency discovered and corrective actions as a result of the annual internal review, as required by 19 CFR 146.53?					
16.	Does the individual overseeing compliance with FTZ requirements have adequate knowledge and training?					
17.	Does the zone operator (company) have good interdepartmental communication about FTZ matters?					
18.	Does the company record keeping system include a retention program and identify documents needed to support FTZ merchandise transactions?					
19.	Does the company perform scheduled physical inventory cycle counts and annual reconciliation?					
20.	Does the company maintain adequate documentation to support the admission, control and removal of FTZ merchandise?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
21.	Does the company have specific identifiers such as Unique Identifier Number (UIN) or Zone Lot Numbers (ZLN) to trace merchandise through the manufacturing process and withdrawal of the finished goods?					
22.	Does the company's system account for waste, scrap and merchandise destruction?					
23.	Does the company's system identify overages and shortages of merchandise resulting from cycle counts or annual physical inventory and ensure proper reporting to Customs?					
24.	Does the company have controls to trace merchandise from admission through manufacturing process?					
25.	Does the company use an inventory method authorized by Customs? If not, did the company obtain approval from Customs?					
26.	Does the company review CF 214s & entries prepared by brokers to ensure correctness?					
27.	Does the company provide adequate broker oversight to ensure proper FTZ declarations and data accuracy?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
28.	Does the company have adequate internal control to address specific issues identified in the profile?					
29.	List company-specific procedures below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

FOREIGN TRADE ZONES – PETROLEUM
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND 2

PART 2 PETROLEUM FTZ GUIDANCE 2

2.1 EXAMPLES OF RED FLAGS 3
2.2 EXAMPLES OF BEST PRACTICES 5
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 6

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 7

3.1 RISK 7
A. Preliminary Assessment of Risk 7
B. Evaluation of Risk Acceptability 7
3.2 INTERNAL CONTROL 8
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 9
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS 9
3.5 EXAMPLES 10

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – FOREIGN TRADE ZONES-PETROLEUM 13

FOREIGN TRADE ZONES – PETROLEUM
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal controls for merchandise admitted into and removed from a Petroleum - Foreign Trade Zone (FTZ) and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal controls to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on Assessing Internal Controls in Performance Audits, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountant's Statement on Auditing Standards No. 78.

PART 2 PETROLEUM FTZ GUIDANCE

19 CFR Part 146 establishes Customs requirements for merchandise admission, handling of the merchandise while in the zone, manipulation, manufacture, exhibition, transfer, and exportation from a zone. 19 CFR Part 146, Subpart H, beginning at 146.91, applies specifically to petroleum refinery FTZ's in addition to all other provisions set forth in 19 CFR Part 146.

An FTZ is a secure area operating under the supervision of U.S. Customs and Border Protection (Customs). FTZs are considered outside the Customs territory of the United States for the purpose of entry of foreign merchandise and payment of duties. Under zone procedures, the usual Customs entry procedure and payment of duties is not required until the foreign merchandise enters the Customs territory for domestic consumption.

The Foreign Trade Zones Act of 1934 as amended in 19 U.S.C. 81a through 81u establishes how zones are created, administered, and also identifies what may be done in a zone.

The Customs Foreign Trade Zone Manual (FTZM) provides additional instructions and guidelines on Customs policy and administrative authority on zone operations. The users of the FTZM include Customs personnel, zone operators, grantees, and other users of the zone.

The Trade and Development Act of 2000, that became law on May 18, 2000, amended the Tariff Act of 1930, to allow all FTZs to file weekly entries for all classes of merchandise, except for merchandise that is prohibited by law. 19 USC 1484(i)

19 CFR 146.93 describes the attribution methods available to petroleum FTZ's: producibility, actual production records, and other inventory methods.

19 CFR 146.95 refers to producibility and actual production records. Attribution using the producibility method must be based on the industry standards of potential production on a practical operating basis, as published in Treasury Decision (T.D.) 66-16. Attribution using actual refinery records shall be accepted by Customs to the extent that the operator actually uses this convention in its refinery operations.

If an operator wants to change record keeping procedures, he must seek prior approval from the Director, Office of Regulatory Audit in accordance with 19 CFR 146.96.

Appendix to Part 146 is Guidelines for Determining Producibility and Relative Values for Oil Refinery Zones.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem with Petroleum FTZ's.

- Company has insufficiently documented, poorly defined, or no internal controls over the admission and withdrawal of FTZ merchandise. Examples:
  - ✓ The company does not have a system to review, monitor, or interact with the broker on foreign trade zone issues.
  - ✓ The company relies on one employee to handle FTZ issues, and there are poor or no management checks or balances over this employee.
  - ✓ The company inventory control and record keeping system procedures manual does not reflect the company's current zone operations and is inadequate or inaccurate.
  - ✓ The company does not have control procedures for zone-to-zone transfer.
  - ✓ The company does not have procedures in place to monitor and review its inventory control and record keeping set up, including product code and material code set-ups.
- Company's import staff lacks knowledge of FTZ requirements and the basic refinery process.
- Company fails to cooperate or respond to Customs.
- Company has high turnover of people in key positions.
- A significant variance exists between the company's data and Customs data.
- Customs (compliance checks, compliance measurement exams, prior audits, import specialist, account manager, and other Customs information) shows history of problems with the company's FTZ operations.
- Zone Operator does not maintain adequate receiving, inventory and shipment records or other documentation to support the zone operations.
- Security within the zone-activated areas is not adequate.
- Company does not perform scheduled physical inventory reconciliation as prescribed by procedures manual as well as reconciliation of inventory at least monthly.
- The company does not use the most current version of the inventory control and record keeping system software available from its vendor if the software was not developed internally.
- Reconciliation of gauge report to inventory records reflects unreasonable gains, losses, or a cumulative effect over time.
- Operator failed to reconcile discharged quantities to CF 214s and failed to report any gains or losses to Customs.
- Information reported to Customs on CF 214 does not match operator's records and third party records.
- The company maintains restricted merchandise in the zone.
- The company does not have records to support value of merchandise when exported.
- The company requests zone status changes from Privileged Foreign (PF) to Non-Privileged Foreign (NPF) at any time.
- The company requests zone status changes from NPF to PF after production has begun on the receipt.
- The company makes multiple requests to change zone designation status.
- Merchandise is not removed from the zone within 5 days after the permit/entry is accepted by Customs.

- Receipt quantities are established by zone operator and not by an independent inspector.
- The zone uses an inventory method other than producibility.
- Information obtained from Customs sources indicates that the company has violated grant authority during past reviews.
- The company does not have procedures for calculating relative value on PF shipments. See FTZ Manual.
- Custody transfer points (meters) are not self-certified or certified by Customs.
- The company lacks documentation on self-certified meters or does not test meters as prescribed in the Customs regulations.
- The company does not have procedures to review its weekly estimate worksheet to ensure quantity covered actual production/withdrawals.
- Customs Automated Commercial System (ACS) records and company records show little or no duty was paid during the scope period on entered merchandise.
- The company used “dedicated products table” or “category 0” for merchandise in production.
- Foreign receipts within the inventory control and record keeping system cannot be traced to the CF 214 and/or withdrawal from zone (CF 7501, CF 7512, etc).
- Inventory control and record keeping systems do not account for domestic merchandise admitted into the zone.
- The company uses an inventory method other than those authorized by Customs and did not obtain approval.
- CF 214 not properly signed by Customs officials and zone operator.
- Company does not file amended CFs 214 to convert market value to actual value in order to properly calculate HMF.
- FTZ operator failed to file an Application for Manipulation, Manufacture, Exhibit, and Destruction in the zone (CF 216) or the permit expired.
- The company records indicate inconsistency in using a selected method of measurement (weight or volume).
- The company ships and/or admits products and/or feedstock not listed on T.D. 66-16 and did not obtain approval for the T.D. 66-16 table modifications.
- The company does not account for fuel consumed, flared, and/or evaporated.
- The company does not perform the annual reconciliation required by 19 CFR 146.25.
- The company combines receipt and shipment information prior to downloading to FTZ database.
- The company uses standard gravity instead of actual gravity in the zone data.
- The company uses different volume to weight conversion formulas for different feedstocks and products.
- The company routinely reports large amount of known loss.
- The company does not verify crude class against actual gravity.
- The company combines products into a generic name.
- The company does not review entry information against attribution results.
- The company files its own CF 7501 information but does not use an automated brokerage system provided by the FTZ software.
- The company does not submit, to Customs, duty payments for inventory shortages or entries for inventory overages; or shortage payments or overage entries are significantly higher or lower than prior years.
- Excessive shortages or overages are shown on the annual reconciliation.
- Few, if any, adjustments are shown on the annual reconciliation.

- The company is unable to explain or provide records supporting adjustments on the annual reconciliation.
- The company does not file Manifest Discrepancy Reports (MDRs) for shortages upon receipt in the zone.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over FTZ operations:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import department, including FTZ operations. That manager has knowledge of Customs matters and the power to authority to ensure internal control procedures for FTZ operations are established and followed by all company departments.
- The department/individual assigned to monitor for compliance of the FTZ has the responsibility as major duties and has designated a backup.
- Internal control procedures assign duties and tasks to a position rather than a person.
- FTZ administrator has a good understanding of the process that is used to compile the year-end reconciliation.
- The company documents and maintains records of its annual system review of its inventory control and record keeping systems.
- The company performs internal/external audit or periodic review of FTZ operations and uses the results to make corrections to entries and changes to their import operations as appropriate, including:
  - ✓ Performing monthly inventory reconciliation,
  - ✓ Verifying feedstock and intermediate class against actual gravity,
  - ✓ Reviewing entry information against attribution results,
  - ✓ Verifying volume to weight conversion in every receipt and shipment,
  - ✓ Checking procedure to avoid duplication in recording transactions, and
  - ✓ Periodically reviewing the set up of feedstock, intermediates, and products in the material table and the producibility table.
- The company has good interdepartmental communication about Customs matters.
- The company official involved with FTZ merchandise participates in continuing education and is provided sufficient information to determine whether merchandise is entered, controlled, and removed from the FTZ in compliance with Customs Regulations and the FTZ grant.
- The company provides training in Customs requirements to other departments (receiving, accounting, manufacturing, and inventory) that are directly or indirectly involved in the FTZ operation.
- Labs, manufacturing, engineering, and other departments provide sufficient descriptions of merchandise to permit proper classification.
- The company updates its FTZ procedural manual and submits changes to the port director at the time of its implementation.
- The company seeks rulings and assistance from Customs to ensure compliance with Customs regulations.
- The company has identified non-producible receipts, chemical receipts and has applied for T.D. 66-16 table modifications.
- The company obtained prior approval from Customs for record keeping procedures other than those that have been approved by Customs.

- The company utilizes the National Association of Foreign Trade Zones (NAFTZ) formula when calculating volume, weight, or American Petroleum Institute (API) standards.
- The company periodically reviews the set up of feedstock, intermediates, and products in the material table and the producibility table.
- The company performs monthly inventory reconciliation and internal audits of its FTZ operations on an annual basis.
- The company has a procedure to verify feedstock and intermediate class against actual gravity.
- The company reviews entry information against attribution results.
- The company verifies volume to weight conversion in every receipt and shipment.
- The company has a checking procedure to avoid duplication in recording transactions.
- The company utilized the API standards conversion factors to account for gain or loss.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- The company's most current FTZ procedures manual submitted to the Port.
- The company's response to the questionnaire.
- Process map flowchart and narrative.
- Interviews with company staff concerning actual procedures and controls specific to the FTZ.
- Results of any internal or external audits of the FTZ operation.
- Grant of Authority from the Foreign Trade Zone Board.
- Special FTZ Procedures approved by Customs (i.e., alternative export procedures, inventory methodology).
- Company's documentation that supports monitoring and verification of established and/or written internal controls over FTZ operations, including:
  - ✓ Documentary evidence of periodic review or testing of internal control procedures.
  - ✓ Documentary evidence of annual internal reviews of inventory control and record keeping systems.
  - ✓ Documentary evidence that the company consistently conducts scheduled physical inventories, and performs annual reconciliation.
  - ✓ Release Order.
  - ✓ CF 214 Application for Foreign Trade Zone Admission and/or Status Designation.
  - ✓ CF 7512 Transportation Entry and Manifest of Goods Subject to Customs Inspection and Permit (IT, T & E, IE).
  - ✓ CF 216, Application for Manipulation, Manufacture, Exhibit, or Destruction of Merchandise in an FTZ.
  - ✓ CF 7525 Shipper's Export Declaration (SED).
  - ✓ CF 3461 Immediate Delivery Application and any amendment used for Weekly Estimated Removals.
  - ✓ CF 7501 Entry Summary.
  - ✓ CF 349 Harbor Maintenance Fee Report and CF 350 Amended Quarterly Summary Report.
  - ✓ CF 301 Customs Bond (Activity Code 4).
  - ✓ Pro-forma/Commercial invoices.
  - ✓ Certified letter to the Port Director of overages and shortages as a result of annual reconciliation.
  - ✓ Annual Reconciliation Report.

- ✓ Inventory control and record keeping system generated reports that provide an audit trail from receipt to attribution, shipment, withdrawal from the FTZ, and to appropriate entry documentation and duty payments.
- ✓ Independent Inspectors' reports.
- ✓ Documentation on Customs certified or self-certified meters.
- ✓ Meter tickets.
- ✓ Documentation showing flaring, evaporation, and fuel consumed within the FTZ.
- ✓ Calculations of known and unknown gains and losses.
- ✓ Documentation that establishes the manufacturing period.
- ✓ Appropriate records for the attribution methodology used.
- ✓ Calculations supporting relative value.
- ✓ T.D. 66-16 and subsequent approval.
- ✓ Production specification sheets.
- ✓ Calculations supporting relative value.
- ✓ Producibility table in the FTZ database.
- ✓ Material table in the FTZ database.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and to determine whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company's internal controls are effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.
   - Monitoring

2. Review relevant Customs and company documents to identify and understand internal controls over FTZ. (Examples of documents and information to review are listed above.)

3. Determine whether the company established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence, such as a log, of communication with the broker and company departments on FTZ issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Company FTZ rulings requested. Determine if they are followed.
   - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
   - Training records and materials relating to FTZ used to educate staff on Customs matters.
   - Evidence that the zone operations were in conformance with the FTZ grant of authority or meet Customs approved procedures if modifications were requested.
   - Evidence that Customs approved requests for T.D. 66-16 modifications.
   - Documentary evidence that the company conducts physical inventory counts and performs reconciliations at least monthly.
   - Documentary evidences that the company verifies the conversion between volume and weight using proper formula.
   - Documentary evidence that the company verifies the feedstock and intermediate types according to their gravity.
   - Documentary evidences that new feedstock, intermediates are properly identified with reasonable feedstock type and new products have followed American Society for Testing and Materials (ASTM) when applicable in product category designation.
   - Documentary evidences that company verifies entry information against attribution results.
   - Documentary evidences that the company has a procedure for correcting data errors and making adjustments.

- Documentation for shortages and overages in the zone, including reports to Customs.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for Petroleum FTZ in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal controls
   - Determine what is already known about control effectiveness
   - Assess the adequacy of internal control design
   - Determine if controls are implemented and effective
   - Determine if transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from Assessing Internal Controls in Performance Audits.
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of the company's internal controls over FTZ operations.

1. Complete the WEIC to determine whether risk is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems

identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

At a minimum, Petroleum FTZ's tests should include:

- ✓ Determining the validity of the information submitted to Customs on the CF 214;
- ✓ Determining the accuracy and adequacy of the information in the FTZ's inventory control system (including waste products from the refining process etc.); and
- ✓ Determining the accuracy of information submitted to Customs on entries (CF 7501s) and transportation entry and manifest of goods subject to Customs inspection (CF 7512s).

2. The following will help the PAS team determine whether conditions warrant proceeding to ACT.

<u>Do not proceed to ACT if:</u>

- Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
- The result of review indicated that the error was due to an isolated incident.
- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

<u>Proceed to ACT if:</u>

- The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS are for clarification only:

Example A: Situation in which the team would not proceed to ACT (Revenue)

Auditor Example – The team reviewed the annual reconciliation, profile, questionnaire, written procedures, process map narrative and flowchart, and other documents.

The company procedures indicate that the values used to calculate relative value were updated monthly and that the relative value calculation was performed on every PF shipment. Testing was performed on 10 different shipped products that were attributed to PF receipts to determine whether the company updates values monthly and that the relative calculation was

performed on each shipment that was attributed to a PF receipt. The testing showed that although all 10 values were updated monthly, relative values were not calculated for the 10 shipments tested. The company agreed to quantify any revenue loss and implement a Compliance Improvement Plan (CIP) for the deficiency. Since the company agreed to quantify the loss and implement a CIP, the PAS team concluded they should not proceed to ACT.

CAS Example – During the database analysis the CAS found errors that resulted in duty losses. The zone operator agreed to identify the losses and quantify the errors.

The errors include:

- Class error in foreign feedstock designations,
- Unreported dutiable attributions.

Since the company agreed to quantify the loss and implement a CIP, the PAS team concluded they should not proceed to ACT.

Example B: Situation in which team would not proceed to ACT (Compliance).

Auditor Example - Based on a review of the profile, questionnaire, written procedures, process map narrative and flowchart, and other documents, the team concluded that the preliminary risk exposure was low.

Company procedures indicate that the actual API standards are used on all receipts admitted into the zone. A selection of eight receipts resulted in a review of five domestic receipts and three foreign receipts. Of the five domestic receipts reviewed, the operator selected the crude class type (I, II, III, or IV), based on the selection made by the engineer, rather than on the actual API standards. Of the three foreign receipts reviewed, the operator always used the actual API standards. The PAS team reviewed the API standards for the five domestic receipts, and found that the API standards did not relate to the crude class selected, which could result in over or underattribution, and possibly a revenue loss. The company agreed to the issue, and implemented a CIP and additional procedures to correct the error. Therefore the team would not proceed to ACT.

CAS Example – During the database analysis, the CAS found discrepancies in volume to weight conversion. The CAS also found duplications in shipments in the zone data file. The team decided that the risk exposure is low because the duplications in shipments did not involve duty and the size and frequency were small. Also the zone operator agreed to use the correct conversion formula. Therefore the team would not proceed to ACT.

Example C: Situation in which team would proceed to ACT (Revenue).

Auditor Example - The same scenario as Example B above, except that the company stated that the differences in the crude class and API standards was irrelevant based on the way the refinery is set up and its capabilities. Also the crude class ranges established by Customs did not coincide with the refinery's definitions for crude class ranges. Further, the company argued that the receipts in question were domestic, and were not subject to Customs entry procedures. Based on the discrepancies and issues identified the auditors would proceed to ACT.

CAS Example – During the database analysis the CAS found shipment attribution errors that were systemic and frequent. The errors consisted of a set-up error in the producibility table that had non-original producibility values associated with unauthorized feedstock types. Therefore the team proceeded to ACT.

Example D: Situation in which team would proceed to ACT (Compliance)

Auditor Example -The company procedures indicate that monthly inventory reconciliation are performed and follow the hierarchy for attributing unexplained losses: attribute first to available privileged foreign receipts, and then to domestic receipts when privileged foreign receipts are no longer available. The PAS reviewed three monthly reconciliations to verify that there were no privileged foreign receipts available since the company attributed the unexplained losses to domestic receipts. During the review, the PAS discovered that there were foreign receipts available for attribution of the unexplained losses based on the documented company procedures. However, the company refused to quantify the loss of revenue because the company felt it would lose the domestic receipts, which was used to attribute the original unexplained losses. Since the company refused to quantify the loss of revenue, the team would proceed to ACT.

CAS Example – During database analysis, the CAS found errors involving duty losses in the following areas that the zone operator would not quantify:

Discrepancies in value (such as unsupported freight deduction), quantity, classification, and duty.

FTZ setup or attribution errors, such as:

- Gravity class error in foreign feedstock designation,
- Unknown losses attributed to domestic receipts while PF receipts are available for attribution,
- Import of unauthorized NPF products that are not included in the zone grant (penalty assessment),
- Recorded consumption of coke, etc. as known loss and avoid reporting data on an entry, and
- The company uses actual price for relative value calculation and has a price error that involved non-reportable shipment type, such as export.

Since the company refused to quantify the loss of revenue, the team would proceed to ACT.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) –FOREIGN TRADE ZONES-PETROLEUM

PURPOSE: To determine whether Petroleum FTZ risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are Internal Controls over FTZ operations formally documented?					
2.	Does management approve written policies and procedures?					
3.	Is one manager responsible for control of the FTZ operations?					
4.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
5.	Do written internal control procedures assign FTZ duties and tasks to a position rather than a person?					
6.	Are written policies and procedures reviewed and updated periodically?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does the company provide a copy of their procedure manual to the port director when changes are made in the FTZ procedure manual?					
8.	Does the company have adequate communication processes related to its FTZ operations?					
9.	Are internal controls over FTZ operations periodically tested?					
10.	Does the company use the periodic review results to make corrections to past and present entries?					
11.	Does the company identify, analyze, and manage risks related to FTZ operations?					
12.	Has the company identified any risks related to FTZ operations and implemented control mechanisms?					
13.	Does the company use the periodic review results to make corrections to its import operations?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Did the company perform an annual internal review of the inventory control and record keeping system, as required by 19 CFR 146.25?					
15.	Did the company report to the Port Director any deficiency discovered and corrective actions as a result of the annual internal review, as required by 19 CFR 146.53?					
16.	Did the company seek and attain approval for T.D. 66-16 table modifications?					
17.	Does the zone operator (company) have good interdepartmental communication about FTZ matters?					
18.	Does the company record keeping system include a retention program and identify documents needed to support FTZ merchandise transactions?					
19.	Does the company perform scheduled physical inventories and reconciliation?					
20.	Does the company maintain adequate documentation to support the admission, control and removal of FTZ merchandise?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
21.	Does the company have specific identifiers such as Unique Identifier Number (UIN) or receipt transaction numbers to trace merchandise through the manufacturing process and withdrawal of the finished goods?					
22.	Does the company's system account for fuel consumption, flaring, and evaporation?					
23.	Does the company's system identify gains and losses of merchandise resulting from cycle counts or physical inventories?					
24.	Does the company have controls to trace merchandise from admission through the manufacturing process to withdrawal from the zone?					
25.	Does the company operate within the scope of its grant or authority?					
26.	If the company uses commercially generated software for its inventory control and record keeping system, is the company using the most current version of software available?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
27.	Does the company have procedures for adding additional products and feedstock into its material code and product code tables?					
28.	Does the company review CF 214s, CF 7501s, and CF 7512s, prepared by brokers to ensure correctness?					
29.	Does the company use an inventory method authorized by Customs? If not, did the company obtain approval from Customs?					
30.	Does the company periodically review its material code and product code table set-ups for accuracy? If so, does company take corrective action when errors are found?					
31.	Does the company periodically review the setup of feedstock type, product category, and producibility value?					
32.	Does the company verify volume to weight conversion for all transactions and use the formula issued by NAFTZ?					
33.	Does the company verify the CF 7501 data against attribution reports for correctness?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
34.	Does the company file amended CF 214s to convert market value to actual value in order to calculate HMF?					
35.	Does the company have adequate broker oversight?					
36.	Does the company have adequate internal control to address specific issues identified in the profile?					
37.	List company-specific procedures below (if applicable).					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or	Internal Control Level (Weak, Adequate, or Strong)	Testing Limit

	Low)	From Section 2 Above	(1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

TRANSSHIPMENT
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND 2

PART 2 TRANSSHIPMENT GUIDANCE 2

2.1 EXAMPLES OF RED FLAGS 3
2.2 EXAMPLES OF BEST PRACTICES 3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 5

3.1 RISK 5
A. Preliminary Assessment of Risk 5
B. Evaluation of Risk Acceptability 6
3.2 INTERNAL CONTROL 6
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 7
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS 8
3.5 EXAMPLES 8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - TRANSSHIPMENT 10

TRANSSHIPMENT
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control to prevent unlawful transshipment and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

PART 2 TRANSSHIPMENT GUIDANCE

Transshipment is the movement of goods through a second country en-route to the United States. Transshipment is legal and commonly used in the ordinary course of business. However, transshipment of merchandise for the purpose of circumventing trade laws and other trade restrictions applicable to the shipment is unlawful. For Customs purposes, unlawful transshipment involves claiming a false country of origin to circumvent quota, avoid paying higher duties (such as antidumping or countervailing duties), or to receive benefits from Special Trade Programs (e.g., NAFTA, Generalized System of Preferences (GSP)).

Unlawful transshipment can have the following effects:

- Decrease the competitiveness of the receiving country's domestic market;
- Create an unfair competitive edge for the violator;
- Establish an erroneous restraint level on a host country that was based on the level of unlawful transshipped goods; thereby, restricting the trade from legitimate manufacturers;
- Undermine bilateral textile agreements and other trade initiatives; and
- Confer fraudulent country of origin to the consumer.

Section 141.86(a)(10) of 19 CFR requires commercial invoices to include the country of origin for the merchandise. Section 12.130 of 19 CFR covers country of origin requirements for textile and textile products. Sections 10.173 and 10.176 of 19 CFR cover evidence of country of origin for merchandise claimed under GSP and merchandise produced in beneficiary developing countries respectively. See other trade area tech guides for additional country of origin criteria pertaining to those specific areas/programs.

The Federal Register, on a biannual basis (around March and September), issues a list of individuals and foreign entities located outside the Customs territory of the United States that have been issued a penalty claim under U.S.C. 1592 of the Tariff Act for certain violations of the Customs regulations. This list is referred to as the "List of Foreign Entities Violating Textile Transshipment and Country of Origin Rules" (19 U.S.C. 1592a list). The Federal Register is also available on the web at http://www.access.gpo.gov/su_docs/fedreg/frcont01.html.

A comparison of the manufacturers selected for the PAS sample to the Federal Register and the Bulletin Board should be performed to provide assurance that the company's internal control procedures are working.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem with transshipment.

- The company has insufficiently documented, poorly defined, or no internal control for prevention of transshipment of imported merchandise. Examples:
  - ✓ The company does not monitor or interact with the broker on transshipment issues.
  - ✓ The company relies on one employee to handle transshipment issues, and there are poor or no management checks or balances over this employee.
- The company or qualified agent representative does not visit the factory.
- The company does not exercise adequate control over their agents (buying/selling) regarding transshipment.
- The company's import staff lacks knowledge of transshipment issues such as U.S. Rules of Origin.
- Imported merchandise is subject to quota, antidumping duties, or other restrictions.
- Quota class merchandise is imported or admitted to a Foreign Trade Zone from an unlikely country of origin.
- The company makes quota/visa payments to a country other than the country declared to Customs and/or payments have been endorsed to other parties instead of factories.
- The purchase order does not identify the same manufacturer as the one identified in the commercial invoice.
- Freight bills do not identify the same countries of origin or export as the purchase order.
- Payments for the goods to the stated exporting or manufacturing factory could not be verified.
- ACS data showed the same Harmonized Tariff Schedule (HTS) number and manufacturer for entry type code "01" (consumption entry) and "03" (antidumping/countervailing duty (ADD/CVD)).
- ACS data showed a different country of origin and country of export for many of the company's imports and one or both of the countries may have trade restrictions.
- The company offers unreasonable explanations to Customs.
- The company fails to cooperate with or respond to Customs.
- The company has high turnover of people in key positions.
- A significant variance exists between the importer's data and Customs data.
- Customs shows a history of problems with transshipment issues (import specialist, account manager, compliance measurement, prior audit, other profile information).
- Company imports a high volume of merchandise under special duty provisions.
- The company uses factories that have been issued penalties for transshipment or that use many subcontractors.
- The company's import staff does not research the Customs Bulletin Board or the Federal Register for foreign entities violating textile transshipment and country of origin rules.
- Textile declaration is not signed or is missing original signature.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls for the prevention of transshipment:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.

- One manager is responsible for control of the import department, including prevention of transshipment and accurate reporting of country of origin. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- The company has good interdepartmental communication about Customs matters.
- The company conducts and documents periodic reviews of entry summaries and makes corrections to entries and changes to their import operations as appropriate.
- The company requires periodic training for staff responsible for Customs matters.
- The company provides transshipment training to its agents and brokers.
- The company requests binding rulings from Customs on country of origin.
- The company agency agreements (buying and selling), purchase orders, employment contracts, or letters of credit contain clauses specifying transshipment certification requirements and penalty provisions.
- The company's inspection team makes regular unannounced visits to the plant to assure that a factory exists and that merchandise was produced at that factory.
- The company records and tracks visit to the factories along with the evaluation form.
- The company obtains profiles prepared by the factories, which state capacity levels, in order to determine whether proper ratio exists between the number of workers and the quantity produced.
- The company discontinues doing business with or puts factories on probation for failing the inspection and/or denying admission for an inspection by the company or its representative.
- The company provides a Quality Manual to its vendors stating its expectations of the vendor.
- The company's Quality Manual states that its vendors must obtain written approval from the company before making any changes regarding manufacturing facilities.
- The company has a plan of action or system to deal with factories that have been identified on the 19 U.S.C.1592a list.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to transshipment.
- Documentation that supports monitoring and verification of established and/or written internal control for prevention of transshipment.
- Process Map flowchart and narrative.
- Other documentation supporting country of origin and prevention of transshipment:
  - ✓ Receiving and inventory records.
  - ✓ Correspondence.
  - ✓ Factory inspection reports.
  - ✓ Factory profiles.
  - ✓ Quality control inspection sheets.
  - ✓ Sales confirmations, purchase contracts, or purchase orders.
  - ✓ Invoices and payment records (Letter of Credits, wire transfers).
  - ✓ Bills of lading/airway bills.

- ✓ Freight payment or accounting records.
- ✓ Buying/Selling agency agreements.
- ✓ Quota/Visa transfer forms.
- ✓ Quota/Visa payment records.
- ✓ Textile declarations.
- ✓ Quota/Visa charge statements.
- ✓ Binding rulings on country of origin.
- ✓ Antidumping Orders.
- ✓ Exporter's Certificate of Origin (ECO).

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is risk to warrant proceeding to the Assessment Compliance Testing (ACT) phase.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

Preliminary Assessment of Risk Examples

Example A: Low Risk Exposure

A query of ACS data and discussions with import specialists found no import activities from known transshippers or countries suspected of transshipping activity or merchandise subject to quota or antidumping. Since there were no PAS team concerns, the risk exposure level was considered low.

Example B: High Risk Exposure

A query of ACS data by vendors shows import activities from known transshippers. In addition, the profile showed a decrease in imports from Country A with quota restrictions and a corresponding increase from Country B with no quota restrictions. Due to the above concerns, the risk exposure level was considered high.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.
   - Monitoring.

2. Review relevant Customs and company documents to identify and understand internal control for prevention of unlawful transshipment. (Examples of documents and information to review are listed on prior page.)

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence of communication with the broker and company departments on transshipment issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Company-specific rulings requested. Determine if they are followed.
   - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
   - Training records and materials used to educate staff on Customs matters including transshipment issues.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for the Prevention of Unlawful Transshipment in PART 4 of this document.

   Note: The internal control assessment should include steps to:

- Identify and understand internal control.
- Determine what is already known about control effectiveness.
- Assess the adequacy of internal control design.
- Determine whether controls are implemented and effective.
- Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

Example – Determine Testing Level

Based on a review of the profile and discussions with the import specialist, the team concluded that the risk exposure was low.

The company’s internal control manual required factory visits prior to contracting with the factories. During factory visits, the company verified the data in the factory profile. The import manager provided documentation to support the fact that the Customs Bulletin Board and Federal Register are routinely reviewed for known overseas transshippers. Purchase orders and contracts were required to contain specific information to prevent and identify possible transshippers. After completing the Worksheet for Evaluating Internal Control, the team concluded the preliminary review indicated an adequate internal control system.

Using the table above (based on a low-risk exposure and adequate internal control system) the team concluded they would test 10 internal control transactions for the prevention of unlawful transshipment.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control for the prevention of transshipment.

1. Complete the WEIC for the Prevention of Unlawful Transshipment to determine whether risk is acceptable or unacceptable and document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT.

   Do not proceed to ACT if:
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   Proceed to ACT if:
   - The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations might be encountered during the PAS are for clarification purposes only:

Example A: Situation in which the team would not proceed to ACT (Revenue)

The auditor found that the importer has import activities from a company on the 19 U.S.C. 1592a list of known transshippers.

The PAS team reviewed the company's internal control procedures and found that the company has detailed written procedures to monitor factories and to prevent unlawful transshipment. The company also kept records of its visit to the factories and reviews its policy on transshipment with its buying agents. In addition, the import manager also documented the review of the 1592a list and Customs Bulletin Board for known transshippers. The company explained that there were only two purchases from the particular vendor and that the company stopped using the factory after it was found to be on the 1592a list. The PAS team verified that these were isolated incidents and that the importer was committed to following its written internal control procedures.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same as example A, except that the company did check the 1592a list on a regular basis and could show that they had stopped the two purchases mentioned above before they were shipped. During the PAS, the company established written procedures and implemented them.

Example C: Situation in which the team would proceed to ACT (Revenue)

The company does not have written internal control procedures to prevent unlawful transshipment. In reviewing documentation for transshipment, the PAS team found that the country listed on the manifest and bill of lading were from Vietnam and the country of origin declared on the Customs entry was China. The company spoke to the manufacturer and the Chinese manufacturer explained that it had contracted part of the production to its sister plant in Vietnam. Vietnam was subject to a higher duty rate (column 2) at the time.

The PAS team proceeds to ACT to quantify the loss of duty and to determine whether there were other incidents of transshipment. The PAS team also referred the case to the EET for review.

Example D: Situation in which the team would proceed to ACT (compliance)

Same situation as in C, except company refuses to take corrective action to prevent unlawful transshipment.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - TRANSSHIPMENT

PURPOSE: To determine whether Transshipment risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls for the prevention of unlawful transshipment formally documented?					
2.	Does management approve written policies and procedures?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager responsible for control of the Import Department, including transshipment issues?					
5.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
6.	Do written internal control procedures assign transshipment duties and tasks to a position rather than a person?					
7.	Does company have good interdepartmental communication about transshipment matters?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
8.	Does company conduct and document periodic reviews of transshipment?					
9.	Do procedures require the company to constantly review the Federal Register web site to identify factories found to be transshipping or unable to produce production records?					
10.	Do procedures require the company to review the Federal Registers for violators of 1592a?					
11.	Do procedures require the Purchase Orders (PO) to identify the factory producing the garment, quantity, unit prices, and the specific garment style numbers so the commercial invoice with the Customs entry can be verified by any U.S. Customs Officer? POs should indicate if a factory is subcontracting out to another factory and the company must have the authority to approve the changes prior to production.					
12.	Do procedures require Letters of Credit to state the beneficiary manufacturer, state that textile transshipment is prohibited and include penalty provisions in the event transshipment occur?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
13.	Do procedures require suppliers to undergo a thorough approval process prior to the first importation? Documentation should indicate that approval was granted to contract with new factories before importation. Documentation may include a check list or standard approval form indicating quality, quantities, machinery & equipment, and production lead times.					
14.	Do procedures require the company to obtain and analyze Factory Profiles to determine whether the factory can produce the desired quantities? Profiles should be validated during the company's on-site visits.					
15.	Do procedures require factory visits to be unannounced and conducted by different company staff or agents?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
16.	Do procedures require the factory visits to be fully documented? Documentation should include: 1) an observation of all phases of the production process from the receipt of raw materials to the work-in-process of the sewing and cutting operation to the finished goods and sale; and, 2) a comparison of the number of sewers to number of machines in relation to production and the number of sewers to number of packers. The visits and documentation should identify specific styles and all processes must relate back to the purchase order.					
17.	If an import is detained at a port and productions records requested, do procedures require the company to do a complete review of the internal control process that was in place to select this manufacturer?					
18.	If weakness were found during internal control testing, were corrective actions implemented?					
19.	Is one department/individual primarily responsible for the prevention of transshipment and meeting country of origin requirements?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
20.	Does the individual responsible for prevention of transshipment, country of origin have adequate knowledge and training?					
21.	Is Customs assistance sought regarding transshipment or quota (e.g., requesting binding rulings)?					
22.	Do procedures require periodic monitoring of overseas factory's production and review of factory capacities in relation to the company's imports?					
23.	Do procedures include monitoring specific quota closures for specific commodities from certain factories with a past history of transshipping?					
24.	Do procedures require periodic reviews of changes in freight companies used by overseas suppliers?					
25.	Do procedures require periodic review for new manufacturers that appear after country closures of specific categories?					
26.	Do procedures require the importer to evaluate overseas agent activities? Are evaluations documented and updated periodically?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
27.	Do procedures require overseas agents to receive training or demonstrate knowledge regarding transshipment issues?					
28.	Do procedures require suppliers to maintain ISO 9000 certification?					
29.	Do procedures require verification that the foreign company/person completing required documentation (textile declarations, Certifications of Origin) is knowledgeable about Customs requirements?					
30.	Do procedures require review of Outward Processing Agreements (OPA)? OPA is a document which states factories in more than one country are involved in the manufacturing process or subcontract to other factories in other countries than their own.					
31	Do procedures require that commercial invoices contain the same specific and adequate garment styling description as listed on the PO?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
32.	Do procedures require the Cut, Make, and Trim operations to be visited and approved? (Applies to importers whose major programs consist of buying fabrics and sending the fabric for a Cut, Make & Trim operation.)					
33.	Do procedures require that payment be made only to quota holders or manufacturers who are listed as obtaining the quota?					
34.	Do procedures require periodic review of the quota allocations of the factory?					
35.	Does the company have adequate broker oversight?					
38.	Does the company have adequate internal control to address specific issues identified in the profile?					
39.	Does the company identify analyze and manager risks related to transshipment?					
40.	Has the company identified any risks related to transshipment and implemented control mechanisms?					
41.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	**Yes or No**	**Comments**
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

GENERALIZED SYSTEM OF PREFERENCES
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 GENERALIZED SYSTEM OF PREFERENCES GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS 3
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 5

3.1 RISK 5
A. Preliminary Assessment of Risk.....5
B. Evaluation of Risk Acceptability 5
3.2 INTERNAL CONTROL.....6
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT).....6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - GENERALIZED SYSTEM OF PREFERENCES (GSP) 10

GENERALIZED SYSTEM OF PREFERENCES
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The objective of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for Generalized System of Preferences (GSP) and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and the terms in this document are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78*.

PART 2 GENERALIZED SYSTEM OF PREFERENCES GUIDANCE

Title V of the Trade Act of 1974 (19 U.S.C. 2461-2465), as amended, which authorized the President to establish GSP to provide duty-free treatment for eligible articles imported directly from designated beneficiary developing countries (BDCs).

The eligible BDCs are listed in General Note 4 of the Harmonized Tariff Schedule of the United States (HTSUS). General Notes 4(a) and 4(b) provide the list of BDCs, the combinations of BDCs treated as one country and the least developed BDCs eligible for GSP treatment.

General Note 4(c) provides general exceptions by merchandise description to GSP, and 4(d) provides specific exceptions by specific BDC country and HTSUS number not eligible for GSP treatment.

Title 19 CFR 10.171 through 10.178 states the regulations for GSP.

GSP allows duty-free treatment for goods meeting certain eligibility requirements on entry into the United States. To qualify for GSP, goods must meet the following requirements:

- The imported goods must come to the United States directly from the GSP-eligible country; the direct shipment requirements are in 19 CFR 10.174 and 10.175.
- The imported goods must be wholly the growth, product, or manufacture of the BDC, or a new or different article of commerce that has been grown, produced, or manufactured in a BDC, as stated in 19 CFR 10.176 (a).
- The imported goods must meet the value content requirements of 19 CFR 10.176 through 10.178. GSP merchandise that is not wholly the growth, product, or manufacture of a BDC may be accorded duty-free treatment only if the direct costs of processing performed in the BDC plus the cost or value of materials produced in the BDC is not less than 35 percent of the appraised value.

Information can be requested from the producer using the table provided in 19 CFR 10.173(a)(1). The information requested shall be submitted within 60 days of the date of the request or such additional period as may be allowed for good cause shown.

GSP eligibility is reported using the letter A (the letter Q is used where GSP has expired with the possibility that privileges may be reinstated) in the Special Program Indicator column of the Automated Commercial System (ACS) database. Where an imported good is eligible for GSP, the letter A is also listed in special rates of duty part of Column 1 of the HTSUS. Where the HTSUS indicates an A+ in the Column 1 special rates of duty, the duty-free rate applies only to the least developed BDCs listed in General Note 4(b). Where the special rates of duty part of Column 1 of the HTSUS indicates an A* notation for a specific HTS number, certain BDCs listed in General Note 4(d) are not eligible for GSP for the designated HTS number.

Additional guidance is found in the publication "A Guide for Supporting Generalized System of Preferences (GSP) Claims" (FA Kit Exhibit 4F).

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem in GSP.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring GSP for Customs purposes. Examples:
  - ✓ Company does not monitor or interact with the broker on GSP issues.
  - ✓ Company relies on one employee to handle GSP issues, and there are poor or no management checks or balances over this employee.
- Company Customs staff lacks knowledge of GSP eligibility issues.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate or respond to Customs.
- Company has high turnover of people in key positions.
- Significant variance exists between the importer's data and Customs data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with GSP (e.g., GSP eligibility issues or reporting incorrect country of origin).
- One company representative dominates multiple phases of the GSP process without monitoring or management oversight.
- High compliance measurement error rates occur for HTSUS numbers that the company frequently uses regarding GSP.
- The company imports from a specific provider or under an HTSUS number or country of origin that have been identified by Customs because of known or suspected GSP problems.
- The company imports indicate a large number of GSP Manufacturer Identification (MIDs).
- The company imports a large quantity of GSP articles over many HTSUS numbers.
- The company does not monitor of the GSP classification or records process.
- The company imports of GSP increase significantly from a prior period.
- The importer and the GSP producer are related.
- GSP imports have not been previously audited or reviewed by Customs.
- Specific issues are identified in the profile.
- Company does not request, maintain, or review documents supporting the qualification of GSP (e.g., value content qualification).
- The company Imports some GSP articles that may be considered sets, mixtures, or composites (see T.D. 91-7 and HQ ruling 559010, dated 3/14/96) that could preclude GSP eligibility.
- The company imports some GSP articles which, in addition to a value content requirement, may require a "double substantial transformation" (see CSD 85-25, which explains 19 CFR 10.177(a)(2)).
- Value content qualification is marginal, just meeting the 35 percent requirement, increasing the importance of accurate cost computations.
- Direct materials alone are not adequate to meet the 35 percent value content requirement, making accurate direct processing costs particularly important.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over GSP:
  - ✓ Are in writing,
  - ✓ Include procedures for monitoring and feedback, and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import Department, including GSP. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign GSP duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about GSP matters.
- Company conducts and documents periodic reviews of GSP, and uses the results to make corrections past and present to entries and changes to its import operations as appropriate.
- Purchasing, Engineering, other departments and suppliers provide sufficient descriptions of merchandise to permit a determination of GSP eligibility.
- Internal control includes a verification process to determine that the imported merchandise qualifies for GSP.
- Importer has procedures to obtain any required or necessary documentation to support the claim (e.g., a penalty provision on suppliers if GSP information is not provided to Customs on demand).
- Importer maintains a GSP database or listing of imported merchandise that would readily identify GSP transactions.
- The importer (or the importer's agent) visits the plant in the GSP country where the products are produced.
- The importer performs an annual review of changes to GSP.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures for ensuring proper GSP eligibility.
- Company's response to the questionnaire.
- Interviews with company staff concerning general internal control and internal control specific to GSP.
- Company's documentation that supports monitoring and verification of established and/or written internal control for GSP, including:
  - ✓ GSP declaration signed by the person responsible for certifying that all information on the documentation is accurate and complete.
  - ✓ If available from the importer, the GSP costing sheet.
  - ✓ Binding rulings concerning GSP.
  - ✓ Invoices, specification sheets, or other documents providing detailed descriptions of GSP merchandise.
  - ✓ List containing GSP part numbers, descriptions, quantities imported, and unit costs.
  - ✓ Bills of lading or other evidence of direct transport to the United States.
  - ✓ Producer's written attestation that goods are wholly the growth or product of a BDC.
  - ✓ Records from the GSP producer supporting the company's verification for goods not wholly the growth or product of a BDC, such as GSP cost allocation worksheets, bills of materials, product specification sheets, engineering drawings, work-in-process documents, material inventory records, purchase history reports, and/or material supplier lists.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

Examples of Preliminary Assessment of Risk

Example A: Low Risk

The import specialist, the account manager, and the profile did not identify any concerns with this importer's GSP program. The importer stated that all GSP came from one supplier. The import was wholly the growth of the country of export and the country was one of three major exporting countries of the commodity in the world. Because there were no PAS team concerns, the assessment of risk was considered low.

Example B: High Risk

The import specialist, the account manager, and the profile identified specific concerns with this importer's GSP program. GSP merchandise was frequently misclassified and was sometimes not eligible for GSP when it was correctly classified. The company was the 10th largest importer of GSP. For the year of audit, the importer stated that all GSP came from 10 manufacturers. Because non-GSP imports could be incorrectly listed as GSP, the assessment of risk was considered high.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment
   - Risk Assessment
   - Control Activities
   - Information and Communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over GSP. (Examples of documents and information to review are listed above.)

3. Determine whether the company has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence (such as a log) of communication with the broker and company departments on GSP issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Company-specific GSP rulings requested. Determine if they are followed.
   - Documentary evidence of intercompany communications, to ensure that correct information is provided to Customs.
   - Training records and materials relating to GSP used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for Generalized system of Preferences (GSP).

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control
   - Determine what is already known about control effectiveness
   - Assess the adequacy of internal control design
   - Determine whether controls are implemented and effective
   - Determine whether transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it

probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the total GSP level that will be reported on. For example, the company may import from several foreign companies, but testing may be necessary only for certain companies or only for certain imports that have been identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review/ Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over GSP.

1. Complete the WEIC for GSP to determine whether risk is acceptable or unacceptable and document why. Put results of GSP testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT:

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   <u>Proceed to ACT if:</u>

- The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations might be encountered under PAS are for clarification purposes only.

Example A: Situation in which the team would not proceed to ACT (Revenue)

The importer has internal control for GSP. The internal control includes contract provisions in which the exporter agrees to provide documentary support for GSP eligibility to Customs on demand; reviews of foreign facilities to verify foreign production in the BDC; and maintenance of documentary information to support importer reviews and testing of GSP eligibility. In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of GSP eligibility data, including cost data, supported the eligibility of products from all GSP manufacturers except Happy Link. The team concluded that internal control was effective for shipments of all manufacturers except Happy Link. The breakdown in internal control was systemic. The importer had not included the GSP contract provisions in the contract negotiated with Happy Link. When Customs, as part of the limited testing for GSP, required that Happy Link provide support for GSP eligibility for the items sampled, the manufacturer refused. The entries were not liquidated. The importer agreed to quantify and pay the lost revenue on the Happy Link imports and change its internal control procedures. All future contracts will be amended to include GSP requirements *before* merchandise is declared as eligible for GSP. Since there were no other revenue issue and correction was made to avoid future problems, the team does not proceed to ACT for revenue.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same as example A above, except that the importer agrees to amend the contract with Happy Link to include the GSP provisions immediately, and Happy Link sends the requested country of origin information to Customs. Since the importer agreed to correct internal control deficiencies and Happy Link's merchandise was determined to be GSP eligible, there is no reason to proceed to ACT for compliance.

Example C: Situation in which the team would proceed to ACT (Revenue)

Same as example B above, except that preliminary analysis indicates that for some imports, Happy Link provided the data required by the controls; thus, some of the imports from Happy Link may qualify for GSP (and others do not). Imports from Happy Link included a large volume

of low-value items. The importer is unable to quantify the GSP-eligible value in the Happy Link account. The PAS team proceeds to ACT to use statistical sampling to project revenue loss.

Example D: Situation in which the team would proceed to ACT (Compliance)

The same as example C above, except that preliminary analysis indicates that some of the imports from Happy Link may qualify for GSP. The importer agrees to pay duty on imports for the one Happy Link contract found during the PAS as outside GSP internal control. The importer does not want to change its current internal control and believes that it meets an acceptable level of compliance for GSP (i.e., importer indicates that the internal control breakdown was an isolated event). Since the importer will not change its internal control and the level of compliance is unknown, the PAS team proceeds to ACT to determine whether the importer meets the acceptable level of compliance for GSP.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - Generalized System of Preferences (GSP)

PURPOSE: To determine whether GSP risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interview and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 – Sample Sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4-Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 –Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 - Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure that GSP is correctly declared?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies?					
4.	Is internal control over GSP periodically tested and results documented? (This should include post-entry reviews to verify correctness of GSP.)					
5.	When the company identified weaknesses during internal control testing of GSP entries, did the company correct internal control procedures and related entries when appropriate?					
6.	Do written internal control procedures assign responsibility for GSP to a position rather than an individual?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does one individual have authority to ensure that internal control procedures for GSP are established and followed by all company departments?					
8.	Do personnel responsible for ensuring GSP is correct have adequate knowledge and training in GSP?					
9.	Does the company have adequate interdepartmental communication about GSP?					
10.	Does the company have procedures to request Customs assistance concerning GSP when needed and is advice followed when given (e.g., requesting binding rulings)?					
11.	Does the company identify, analyze, and manage risks related to GSP?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
12.	Has the company identified any risks related to GSP and implemented control mechanisms?					
13.	Does the company have policies and procedures in place to ensure that new merchandise is GSP eligible? Specifically:					
	a. Does the company have a verification process to determine that imported merchandise qualifies for GSP?					
	b. Does the importer have procedures to obtain required documentation to support the claim?					
	c. Does the importer (or agent) visit the plant in the BDC where the products are produced?					
	d. Does the company have procedures to ensure that GSP eligible goods were directly imported from a BDC?					
	e. Does the company ensure that only the costs identified in 19 CFR 10.177 and 10.178 are included in the 35 percent calculations?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Does the company conduct and document periodic monitoring of GSP claims?					
	a. Are documents supporting eligibility reviewed for correctness?					
	b. Are classifications reviewed to determine correctness and eligibility?					
	c. Are material and processing costs re-evaluated to determine that they still meet the 35 percent cost requirement?					
	d. Are results of reviews used to make corrections to past and future entries?					
	e. Are results of reviews used to correct internal control system weakness?					
15.	Does the company provide adequate broker oversight of GSP issues?					
	a. Is the broker required to obtain company concurrence prior to making changes to GSP claims/entries?					
	b. Are GSP entries reviewed to determine that broker used correct GSP-eligible classification?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	c. Are GSP entries reviewed to determine that the merchandise was GSP eligible?					
16.	List company-specific procedures below (if applicable).					

Section 2 - Preliminary Internal Control Assessment

Use Information obtained in Section 1 above to make a preliminary assessment of internal control as strong, adequate weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

*If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in Section 3.3 of TIPS to determine the extensiveness of audit test to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
IC is effective to provide reasonable assurance to preclude significant risk.	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable?		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

CARIBBEAN BASIN ECONOMIC RECOVERY ACT & CARIBBEAN BASIN TRADE PARTNERSHIP ACT
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

2.1 CBERA INFORMATION.....2
2.2 CBTPA INFORMATION.....3
2.3 EXAMPLES OF RED FLAGS 4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 6

3.1 RISK 6
A. Preliminary Assessment of Risk.....6
B. Evaluation of Risk Acceptability 6
3.2 INTERNAL CONTROL.....7
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 8
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....8
3.5 EXAMPLES.....9

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - CBERA/CBTPA 11

A …….11

CARIBBEAN BASIN ECONOMIC RECOVERY ACT (CBERA) & CARIBBEAN BASIN TRADE PARTNERSHIP ACT (CBTPA)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for goods entered for preferential treatment as products of the Caribbean Basin Economic Recovery Act (CBERA) also known as Caribbean Basin Initiative (CBI) and products of the Caribbean Basin Trade Partnership Act (CBTPA), and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountant's *Statement on Auditing Standards* No. 78.

PART 2 CBERA AND CBTPA GUIDANCE

The United States Customs Service issued an Informed Compliance Publication on this area in May 2001.

Additional guidance may be found in:

- C.S.D. 85-25 (double substantial transformation);
- Ruling 556193, dated 12/23/91 (dual-sourcing);
- Ruling 557087, dated 7/22/93,T.D. 81-282, T.D. 78-399, and C.S.D. 80-208 (unallowable general and administrative costs); and
- Ruling 559010, dated 3/14/96 and T.D. 91-7 (treatment of components in sets).

2.1 CBERA INFORMATION

Subtitle A, Title II of Public Law 98-67, entitled the CBERA and referred to as the Caribbean Basin Initiative (CBI) authorizes the President to proclaim duty-free treatment for all eligible articles from any beneficiary country. CBERA is codified at 19 U.S.C. 2701-2706. CBERA allows duty-free treatment for all eligible articles from any beneficiary country. General Note 7 of the Harmonized Tariff Schedule of the U.S. (HTSUS) lists the beneficiary countries for purposes of the CBERA. Merchandise subject to CBERA preference appears as "free or at a reduced duty" by HTSUS number in the "Special" rate of duty sub-column followed by the symbol "E" or "E*" in parenthesis.

The duty free requirements of CBERA are listed in 19 CFR Part 10 sections 10.191 through 10.199. Section 10.191(b)(2) describes those items eligible for preferential treatment under the CBERA provisions. To qualify for the CBERA special trade program, goods must meet the following requirements:

- The imported goods must come to the United States directly from the beneficiary country; the direct shipment requirements are in section 10.194.

- The imported goods must meet the country of origin criteria as stated in section 10.195 and either: a) be wholly the growth, product or manufacture of the beneficiary country; or b) be transformed into new or different article that has been grown, produced or manufactured in a beneficiary country.
- The imported goods must meet the value content requirements of section 10.195, specifically, the sum of: (a) the cost or value of the materials produced in a beneficiary country or two or more beneficiary countries, plus (b) the direct costs of processing operations performed in a beneficiary country or countries is not less than 35 percent of the appraised value of the goods at the time it is entered.

2.2 CBTPA INFORMATION

Title II of Public Law 106-200 (114 Stat.251) entitled the CBTPA, amended section 213(b) of the CBERA. CBTPA allows additional trade benefits to countries designated as beneficiary countries. General Note 17 of the HTSUS lists the Beneficiary Countries for purposes of the CBTPA. Merchandise subject to CBTPA preference appears as “free or at a reduced duty” by HTSUS number in the “Special” rate of duty sub-column followed by the symbol “R” in parenthesis. The CBERA preference is claimed on the imported good by using the letter “R” in the special program indicator field of the Automated Commercial System (ACS) database.

Title 19 CFR Part 10, sections 10.221 through 10.237 divides the CBTPA regulations into separate duty free provisions for **textile/apparel** and **non-textile** goods. For purposes of this technical guide the term textile will include textile and apparel covered by the CBTPA regulations.

The duty free requirements for textile goods claiming preferential treatment under CBTPA are in sections 10.221 through 10.227. **Textile** articles described in section 10.223(a) are the textile goods subject to the CBTPA provisions. Section 10.223(b) lists the special rules for fibers and yarns. A specific Certificate of Origin described in section 10.224 is required for CBTPA textile articles. Section 10.227(b)(2) requires the importer to establish and implement internal control, to periodically review the Certificate of Origin and other records of section 10.227. To qualify for the CBTPA, textile and apparel articles must meet the following requirements:

- The imported goods must be wholly formed or assembled entirely in the territory of one or more designated beneficiary countries; the formed/assembled rules are part of section 10.223(a).
- The imported goods must meet the country of origin criteria, the goods description, and the specific manufacturing requirements, as stated in section 10.223(a)(1) through (a)(12) together with the special rules of section 10.223(b) for component materials.
- The imported goods must be imported to the U.S. directly from the CBPTA beneficiary country; the direct shipment requirements are in section 10.223(c).
- The imported goods must be supported by an original Certificate of Origin described in section 10.224.

The duty free requirements for **non-textile** goods claiming preferential treatment under CBTPA are in sections 10.231 through 10.237. **Non-Textile** goods described in section 10.233(a) are the non-textile items subject to the CBTPA provisions. Section 10.237(b)(2) requires the importer to establish and implement internal control to periodically review the Certificate of Origin and other records of section 10.237. To qualify for the CBPTA **non-textile** goods must meet the following requirements:

- The imported goods must (according to section 10.233(b)) meet the NAFTA originating good requirements of General Note 12 (NAFTA) and the Appendix to CFR 19.181 (the NAFTA Rules of Origin);
- The imported goods must be eligible non-textile goods defined in section 10.233(a);
- be imported directly from the CBERA/CBTPA beneficiary country; the direct shipment requirements are in section 10.233(d); and
- The imported goods must be supported by an original Certificate of Origin (CF-450) described in section 10.236(b)(1).

The Trade Act of 2002 (the Act) was signed by President Bush on August 6, 2002 and amended section 213(b)(2)(A) of the Caribbean Basin Economic Recovery Act (19 U.S.C. 2703(b)(2)(A). The Act changed eligibility requirements for apparel articles imported under provisions of CBTPA. Auditors must obtain current information on CBTPA provisions for imports after August 6, 2002.

2.3 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem with CEBRA/CBTPA.

- The company has insufficiently documented, poorly defined, or no internal control for accurately declaring merchandise entered as products of CBERA/CBTPA for Customs purposes. Examples:
  - ✓ The company does not monitor or interact with the broker on merchandise entered as products of CBERA/CBTPA.
  - ✓ The company relies on one employee to handle merchandise entered as products of CBERA/CBTPA, and there are poor or no management checks or balances over this employee.
- The company staff lacks knowledge of the trade program provisions for products of CBERA/CBTPA.
- The responsible person lacks cost accounting knowledge.
- The company offers unreasonable explanations to Customs.
- The company fails to cooperate with or respond to Customs inquiries.
- The company has high turnover of people in key positions.
- A significant variance exists between the importer's data and Customs' data.
- Customs (import specialist, account manager, compliance measurement, prior audit, other profile information) shows history of problems with merchandise entered as products of CBERA/CBTPA.
- The company has not shipped goods directly from a beneficiary country into Customs territory of the United States.
- The goods were not substantially transformed into a new and different article.
- The goods were not wholly obtained or produced entirely in the territory of one or more designated beneficiary countries.
- The material cost and processing qualification is marginal, just above the required minimum percentage, increasing the importance of accurate cost computations.
- The company does not request, maintain, or review documents supporting the qualification of CBERA/CBTPA (e.g. value of material plus the direct cost of processing operations performed).
- Customs has no prior audits or reviews of the company's imports of CBERA/CBTPA.

- Specific issues are identified in the profile.
- CBERA/CBTPA imports increase sharply from a prior period.
- The importer and the CBERA/CBTPA producer are related.
- Amounts on cost sheets for unallowable general expenses and profit appear unusually low, indicating that allowable costs may be overstated.

2.4 EXAMPLES OF BEST PRACTICES

- Internal controls (as required by 19 CFR 10.217(b)(2)) for merchandise entered as products of CBERA/CBTPA:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the import department, including merchandise entered as products of CBERA/CBTPA. That manager has knowledge of Customs matters and the authority to assure internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- The company conducts and documents periodic reviews of merchandise entered as products of CBERA/CBTPA, and uses the results to make corrections to entries and changes to their import operations as appropriate.
- The company has good interdepartmental communication about Customs matters.
- Internal control involves a verification process to determine that the imported merchandise qualifies for CBERA/CBTPA:
  - ✓ Company has proof that the imported merchandise was shipped directly from a beneficiary country(s) to the United States.
  - ✓ Company can itemize the value of the materials and show that the direct cost of processing operations performed in a beneficiary country(s) is not less than the minimum required percentage of the appraised value.
- The company can provide the origin of the materials used in the production of the goods from the CBERA/CBTPA.
- The company can readily provide listing of goods that are products of CBERA/CBTPA.
- Purchasing, Engineering, other departments and suppliers provide sufficient descriptions of merchandise to permit a determination of CBERA/CBTPA eligibility.
- The company visits the plant in the CBERA/CBTPA beneficiary country(s) where the products are produced.

2.5 EXAMPLES OF CBERA/CBTPA DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- The company's response to the Questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to merchandise entered as products of CBERA/CBTPA.
- The company’s documentation that supports monitoring and verification of established and/or written internal control for merchandise entered as products of CBERA/CBTPA.
  - ✓ Documents showing direct shipment from the beneficiary country to the commerce of the United States. (e.g. shipping documents, invoices, or other documents).

- ✓ Producer's written statement, available upon request, on the commercial invoice provided to Customs attesting that the goods are wholly the growth or product of a single beneficiary country.
- ✓ Accounting records supporting product cost sheets, including financial statements, post-closing trial balance, detailed chart of accounts, and general ledger detail.
- ✓ Non-textile Certificate of Origin (CF-450).
- ✓ Declaration of origin signed by the person responsible for certifying that all information on the documentation is accurate and complete.
- ✓ Textile Certificate of Origin for CBTPA.
- ✓ Binding rulings concerning CBERA/CBTPA.
- ✓ The CBERA/CBTPA costing sheet.
- ✓ Country of origin markings on products and components.
- ✓ Bills of material listing country of origin for components, whether foreign vendors are related or unrelated.
- ✓ Manufacturer's affidavits as to country of origin of components.
- ✓ "Where used" reports ("exploded" bills of material) showing that components underwent "double substantial transformation."

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company 's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.
   - Monitoring.

2. Review relevant Customs and company documents to identify and understand relevant internal control over merchandise entered as products of CBERA/CBTPA (Examples of documents and information to review are listed on prior page).

3. Determine whether the company established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence of communication (such as a log) between the broker and company on merchandise entered as products of CBERA/CBTPA issues, including company testing of broker operations and verification that the broker followed company instructions.
   - The company-specific CBERA/CBPTA rulings and evidence that they are followed.
   - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
   - Training records and materials relating to CBERA/CBPTA are used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for CBERA/CBTPA Goods in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that they probably will not be able to form an opinion based on limited PAS testing. In such cases, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that they can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the overall CBERA/CBTPA level that will be reported on. For example, the company may import from various foreign entities and from various countries and tests may be designed for areas identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of the company's internal control over merchandise entered as products of CBERA/CBTPA.

1. Complete the WEIC for CBERA/CBTPA Goods to determine whether risk is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

2. The following will help the PAS team whether conditions warrant proceeding to ACT:

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and

- The result of review indicated that the error was due to an isolated incident.
- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

Proceed to ACT if:

- The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be forwarded for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS are for clarification only.

Example A: Situation in which the team would not proceed to ACT (Revenue)

The importer has internal control for CBERA/CBTPA. The internal control includes contract provisions in which the exporter agrees to provide documentary support for CBERA/CBTPA eligibility to Customs on demand; reviews of foreign facilities to verify foreign production in the beneficiary country(s); maintenance of documentary information to support importer reviews; and testing of CBERA/CBTPA eligibility. In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of CBERA/CBTPA records, including cost data, supported the eligibility of products from all manufacturers except XYZ Electronics. The team concluded that internal control was effective for shipments of all manufacturers with the exception of XYZ Electronics. The breakdown in internal control regarding XYZ Electronics was systemic because the importer had not included the CBERA/CBTPA contract provisions in the XYZ Electronics' contract. When Customs, as part of the limited testing for CBERA/CBTPA, required that XYZ Electronics provide support for CBERA/CBTPA eligibility for the items sampled, the manufacturer refused. The entries were not liquidated. The importer agreed to quantify and pay the lost revenue on the XYZ Electronics imports and change its internal control procedures. All future contracts will be amended to include CBERA/CBTPA requirements *before* merchandise is declared as eligible for CBERA/CBTPA. Since there were no other revenue issues and correction was made to avoid future problems, the team does not proceed to ACT for revenue.

Example B: Situation in which team would not proceed to ACT (Compliance)

Same as example A above, except that the importer agrees to amend the contract with XYZ Electronics to include the CBERA/CBTPA provisions immediately, and XYZ Electronics sends the requested country of origin information to Customs. Since the importer agreed to correct internal control deficiencies and XYZ Electronics' merchandise was determined to be CBERA/CBTPA eligible; there is no reason to proceed to ACT for compliance.

Example C: Situation in which the team would proceed to ACT (Revenue)

Same as example B above, except that preliminary analysis indicates that for some imports, XYZ Electronics provided the data required by the controls; thus, some of the imports from XYZ Electronics may qualify for CBERA/CBTPA (and others do not). Imports from XYZ Electronics included a large volume of low-value items. The importer is unable to quantify the CBERA/CBTPA eligible value in the XYZ Electronics account. The PAS team proceeds to ACT.

Example D: Situation in which the team would proceed to ACT (Compliance)

The same as example C above, except that preliminary analysis indicates that some of the imports from XYZ Electronics may qualify for CBERA/CBTPA. The importer agrees to pay duty on imports found during the PAS review as outside the CBERA/CBTPA internal control. The importer does not want to change its current internal control and believes that it meets an acceptable level of compliance for CBERA/CBTPA (i.e., importer indicates that the internal control breakdown was an isolated event). Since the importer will not change its internal control and the level of compliance is unknown, the PAS team proceeds to ACT to determine whether the importer meets the acceptable level of compliance for CBERA/CBTPA.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - CBERA/CBTPA

PURPOSE: To determine whether CBERA/CBTPA risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls over merchandise entered as products of CBERA/CBTPA formally documented?					
2.	Are written policies and procedures approved by management?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager responsible for control of the Import Department, including CBERA/CBTPA?					
5.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
6.	Does the responsible person have cost accounting knowledge?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Do written internal control procedures assign merchandise entered as products of CBERA/CBTPA responsibility to a position rather than an individual?					
8.	Does the company have good interdepartmental communication about merchandise entered as products of CBERA/CBTPA?					
9.	Does the company conduct and document periodic reviews of CBERA/CBTPA?					
10.	Does the company use the CBERA/CBTPA periodic review results to make corrections to past and present entries?					
11.	Does the company use the CBERA/CBTPA periodic reviews to make changes to its import operations as appropriate?					
12.	Do internal controls involve a verification process to determine that the imported merchandise qualifies for CBERA/CBTPA?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
13.	Is adequate descriptive information provided (by purchasing, engineering, other departments and suppliers) to the Import Department and/or broker to ensure proper CBERA/CBTPA eligibility?					
14.	Does the importer (or the importer's agent) visit the plants in the CBERA/CBTPA countries where the products are produced?					
15.	Does the company perform an annual review of changes to CBERA/CBTPA?					
16.	Does the importer have procedures to obtain any required or necessary documentation to support the claim (e.g. a contract penalty provision if CBERA/CBTPA information is not provided to Customs on demand)?					
17.	Does the company have procedures in place to ensure that the product meets the direct shipment requirements?					
18.	Does the company have procedures in place to ensure that the materials and direct costs of processing operations performed in beneficiary countries exceed the minimum required percentage of the appraised value?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	New CBERA/CBTPA Merchandise					
19.	Does management review the classification and eligibility of new CBERA/CBTPA items?					
20.	Is responsibility for the CBERA/CBTPA eligibility process assigned to one knowledgeable individual or department with management oversight?					
21.	Is adequate descriptive information provided to the Import Department and/or broker by suppliers, engineers, purchasing department, etc. to ensure proper classification?					
22.	Is Customs assistance sought in classifying merchandise (e.g., requesting binding rulings)?					
	Entry Review					
23.	Does the company review entries to verify that correct classifications were used?					
24.	Does the company monitor the entry review process to verify that controls were followed?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
25.	Are exporters required to print the HTSUS numbers provided by the importing company on invoices and/or packing lists?					
26.	Does the individual reviewing merchandise eligibility have adequate knowledge and training of CBERA/CBTPA issues?					
27.	Are HTSUS classifications for CBERA/CBTPA maintained in a database that is provided to brokers?					
28.	Are brokers required to have written company approval to make classification changes?					
29.	Does the company provide adequate broker oversight?					
30.	Does the company identify, analyze, and manage risks related to CBERA/CBTPA?					
31.	Has the company identified any risks related to CBERA/CBTPA and implemented control mechanisms?					
33.	Does the company have internal control to address specific issues identified in the profile?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
34.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

ANDEAN TRADE PREFERENCE ACT (ATPA)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 ATPA GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS 3
2.2 EXAMPLES OF BEST PRACTICES.....4
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....5

3.1 RISK 5
A. Preliminary Assessment of Risk.....5
B. Evaluation of Risk Acceptability 6
3.2 INTERNAL CONTROL.....6
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 7
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - ANDEAN TRADE PREFERENCE ACT (ATPA) 11

ANDEAN TRADE PREFERENCE ACT (ATPA)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

NOTE: The Andean Trade Preference Act (ATPA) expired December 4, 2001. President Bush signed the Trade Act of 2002 into law on August 6, 2002. Title XXXI of the Act provides for the renewal of the ATPA through December 31, 2006.

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for articles entered for preferential treatment as products of ATPA and evaluating the results.

PART 2 ATPA GUIDANCE

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this technical guide are based on *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

Title II of Public Law 102-182 entitled the ATPA. Codified at 19 U.S.C. 3201 through 3206, ATPA is a special trade program that authorized the president to proclaim duty-free treatment for eligible articles of designated beneficiary countries (BCs).

General Note (GN) 11 of the Harmonized Tariff Schedule of the United States (HTSUS) designates the BCs eligible to claim preference under ATPA. The eligibility requirements of ATPA are provided in 19 CFR 10.201 through 10.208. Exceptions by merchandise description to ATPA are provided in GN 11(d) and in 19 CFR 10.202(b).

To qualify for the ATPA, imported articles must meet the following requirements:

- The imported articles must come to the U.S. directly from the ATPA eligible country; the direct shipment requirements are in 19 CFR 10.204.
- The imported articles must meet the country of origin criteria as stated in 19 CFR 10.205 and be wholly the growth, product or manufacture of the BCs; or be transformed into new or different articles of commerce that have been grown, produced or manufactured in a beneficiary country.
- The imported articles must meet the value content requirements of 19 CFR 10.206. ATPA merchandise that is not wholly the growth, product or manufacture of a BC may be accorded duty-free treatment only if the sum of the direct costs of the processing performed in the BC, plus the cost or value of the materials produced in the BC, is not less than 35 percent of the appraised value.

Merchandise subject to the ATPA appears as "Free or at a reduced duty" in the HTSUS "Special" Rate of Duty sub-column followed by the symbol "J" or "J*" in parenthesis. For articles designated with a J* in the duty free column, the exceptions of General Note 11(d) will apply. The ATPA is claimed on the imported articles by using the letter J in the Special Program Indicator field of the Automated Commercial System (ACS) database.

Additional guidance may be found in:

- C.S.D. 85-25 (double substantial transformation);
- Ruling 556193, dated 12/23/91 (dual-sourcing);
- Ruling 557087, dated 7/22/93, T.D. 81-282, T.D. 78-399, and C.S.D. 80-208 (unallowable general and administrative costs); and
- Ruling 559010, dated 3/14/96 and T.D. 91-7 (treatment of components in sets).

The Trade Act of 2002 ("the Act") was signed into law by President Bush on August 6, 2002. Title XXXI of the Act provides for the renewal of the ATPA through December 31, 2006. This title may be cited as the Andean Trade Promotion and Drug Eradication Act (ATPDEA). Customs Automated Commercial System (ACS) has been reprogrammed to accept duty-free entry summaries using the special program indicators (SPI) "J" and "J*".

The Act eliminated 19 USC 3203(c), which provided duty reductions for certain goods. Effective immediately by the signing of the Act on August 6, 2002, ATPA reduced rates of duty no longer apply on certain handbags, luggage, flat goods, work gloves, and leather wearing apparel.

Certain articles that were previously excluded from ATPA preferential treatment may become eligible for preferential treatment under the Andean Trade Promotion and Drug Eradication Act once the President determines that a country is eligible for such treatment. Auditors must obtain current information on ATPDEA provisions for imports after August 6, 2002.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem in ATPA.

- The company has insufficiently documented, poorly defined, or no internal control for accurately declaring merchandise entered as APTA products for Customs purposes. Examples:
  - ✓ The company does not monitor or interact with the broker on ATPA issues.
  - ✓ The company relies on one employee to handle ATPA issues, and there are poor or no management checks or balances over this employee.
- Responsible person lacks cost accounting knowledge.
- The company import staff lacks knowledge of ATPA eligibility requirements.
- The company offers unreasonable explanations to Customs.
- The company fails to cooperate with or respond to Customs.
- The company has high turnover of people in key positions.
- Significant variance exists between the importer’s data and Customs’ data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with ATPA merchandise.
- HTSUS numbers that the company frequently uses regarding ATPA have high compliance measurement error rates.
- Imports from a specific exporter, or under an HTSUS number or country of origin that the company uses have been identified by Customs because of known or suspected APTA problems.
- The company has a large number of ATPA exporters or a large number of goods for which ATPA is claimed.
- The importer does not request, maintain, or review documents supporting the qualification of ATPA imports (e.g. value content requirements).

- The company has a sharp increase of ATPA imports from a prior period.
- The importer claiming ATPA and the exporter are related parties.
- Customs has no prior audits or reviews of the company's ATPA imports.
- The profile identified specific ATPA issues.
- The company dual sources or obtains an interchangeable article from two different countries, where only one of the countries is an APTA country.
- The articles do not have required markings to distinguish the origin.
- A declaration that assembled ATPA articles declared as wholly produced or manufactured in a beneficiary country appears to be doubtful.
- Value content qualification is marginal, just meeting the 35 percent requirement, increasing the importance of accurate cost computations.
- Direct materials alone are not adequate to meet the 35 percent value content requirement, making accurate direct processing costs particularly important.
- Imported textile and apparel articles are subject to textile restrictions.
- Amounts on cost sheets for unallowable general expenses and profit appear unusually low, indicating allowable costs may be overstated.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over merchandise entered as ATPA products:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import Department, including merchandise entered as ATPA. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign ATPA duties and tasks to a position rather than a person.
- The company has good interdepartmental communication regarding ATPA matters.
- The company conducts and documents periodic reviews of merchandise entered as ATPA products, and uses the results to make corrections past and present to entries, and changes to their import operations as appropriate.
- Purchasing, Engineering, other departments, and suppliers provide sufficient descriptions of merchandise to permit a determination of ATPA eligibility.
- Internal control involves a verification process to determine that the imported merchandise qualifies for ATPA.
- The importer has procedures to obtain any required or necessary documentation to support the claim (e.g. penalty provisions if ATPA information is not provided to Customs on demand).
- The importer maintains an ATPA database or listing of imported merchandise that would readily identify ATPA transactions.
- The importer (or the importer's agent) visits the plant in the ATPA country where the products are produced.
- The importer performs an annual review of changes to ATPA.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures for ensuring ATPA eligibility.

- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to ATPA imports.
- A company's documentation that supports monitoring and verification of established and/or written internal control for ATPA, including:
  - ✓ An ATPA declaration signed by the person responsible for certifying that all information on the documentation is accurate and complete.
  - ✓ A list of articles by vendor that are products of ATPA countries.
  - ✓ Invoices, specification sheets, or other documents providing a detailed description and origin of the ATPA merchandise.
  - ✓ Bills of lading or other evidence of direct transport to the United States.
  - ✓ For related parties a bill of materials listing of origin of the products used in production.
  - ✓ Travel documents that show that the company has recently visited the ATPA manufacturer and verified the commodities are manufactured, produced, or wholly grown in the ATPA country.
  - ✓ Records from the ATPA producer supporting the company's verification for articles not wholly the growth or product of a BC (such as, cost allocation worksheets, bills of materials, product specification sheets, engineering drawings, work-in-process documents, material inventory records, purchase history reports, and/or material supplier lists).
  - ✓ Country of origin markings on products and components.
  - ✓ Bills of material listing country of origin for components, whether foreign vendors are related or unrelated.
  - ✓ Manufacturer's affidavits as to country of origin of components.
  - ✓ "Where used" reports ("exploded" bills of material) showing that components underwent "double substantial transformation."
  - ✓ Accounting records supporting product cost sheets, including financial statements, post-closing trial balance, detailed chart of accounts, and general ledger detail.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company 's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available

information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.
   - Monitoring.

2. Review relevant Customs and company documents to identify and understand relevant internal control over entries of ATPA. (Examples of documents and information to review are listed on prior page).

3. Determine whether the company has established and follows procedures by reviewing:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence (such as a log) of communication with the broker and company departments on ATPA issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Company-specific ATPA rulings requested. Determine whether they are followed.
   - Documentary evidence of intra-company communications, to ensure that correct information is provided to Customs.
   - Training records and materials relating to ATPA used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete the appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for ATPA in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that they can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the total ATPA level that will be reported on. For example, the company may import from several foreign companies, but testing may be necessary only for companies or products that have been identified as primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over ATPA.

1. Complete the WEIC for ATPA to determine whether risk is acceptable or unacceptable and document why. Put results of ATPA testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing,

problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

Customs considers risk unacceptable when testing reveals that internal control is not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will help the PAS team determine whether conditions warrant proceeding to ACT.

   Do not proceed to ACT if:
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   Proceed to ACT if:
   - The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate, or revenue loss, can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS are *for clarification only:*

Example A: Situation in which the team would not proceed to ACT (Revenue)

Background
Commodities Inc. (CI) imports a number of manufactured goods from Colombia (none wholly a product of Colombia) entered duty free under the ATPA. The ATPA goods are made from materials obtained from both ATPA and non-ATPA countries. The process starts with the CI purchasing department. All goods indicated by purchasing as potentially duty free under ATPA must undergo an analysis to determine whether the good qualifies for ATPA before shipment. The Import Department reviews the documentation acquired by purchasing and by e-mail advises purchasing that the good qualifies for ATPA preference. Purchasing then, as part of the purchase contract requirements, indicates that the ATPA producer is required to furnish all

necessary value content information to U.S. Customs should U.S. Customs request the information. A provision added to all trade preference purchase contracts, requires payment of duty, by the producer, for any failure to supply U.S. Customs with the required content information (and resulting disallowance of preferential treatment).

Company's Policies and Procedures
CI has a written company policy (in the CI Customs Procedures Manual) that requires the Import Department review the statement from the ATPA producer on the origin of the materials and other costs used to produce the ATPA goods. Because of trade secrets, material supplier pricing, and content secrecy, the ATPA producer agreed to provide a letter that indicates the article meets the ATPA percentage of value content criteria but no specific value information. As a condition of export, a Statement of Manufacture from the ATPA producer indicating that the goods were produced in the beneficiary country is part of the import documents. All shipments are made directly from the ATPA country to the U.S. In order to make a determination on a good's eligibility the Import Department concludes that the country of origin and the direct shipment have been met, but must rely on statements from the ATPA vendor for the value content requirements.

Pre-Assessment Survey
Since internal controls indicated all ATPA goods were the subject of an import department review, to determine whether the controls were working, the team:

- Interviewed employees in the Purchasing, Receiving, Shipping, and Import Departments to determine their understanding of the requirements in the company's Procedures manual.
- Performed a macro-test determining that the entered values for Customs and CI of ATPA products for the year examined mirrored each other in the aggregate and by HTS heading.
- Judgmentally selected 10 items from the purchasing department files and determined if there was evidence of the Import Department approval and verification of the brokers entry preparation. These items represented 50 percent of CI's total ATPA merchandise value and 100 percent of the ATPA vendors.
- Compared the information on the shipping form, supporting Country of Origin statement and manufacturer statements to determine whether the information was accurate and the goods were products of an ATPA beneficiary country.
- Issued a Customs request to the ATPA producers for value content information. Reviewed content specifications of the goods produced depicting the products manufactured into the finish goods.

The PAS indicated that the Import Department failed to review and approve one of the 10 goods reviewed. This one good was a purchasing department modification (change of material specifications) to another already approved good. Since the good had already received Import Department approval, Purchasing failed to initiate the necessary internal control review. A Customs review of the good revealed that because of the change in the material specifications the source of some critical materials had changed (from the U.S.) to a non-ATPA country causing the value content requirements of ATPA to fail.

The company agreed to adopt a compliance improvement plan (CIP). The CIP reinforced all departments following existing procedures for all articles adding the phrase "including modifications to existing Import Department approved goods" to existing controls and stressed better interdepartmental communication. The company also agreed to quantify the loss of

revenue (LOR) caused by the Import Department not reviewing and approving the modification. Because of this error, the Import Department then performed a reconciliation of all ATPA articles initiated by purchasing, against all ATPA articles approved by the Import Department. The results indicated that there was no additional merchandise not reviewed by the Import Department. Since the company agreed to quantify the LOR, there were no other errors, and CI adopted steps to address the error found, proceeding to ACT was considered unnecessary.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same situation as Example A above, except that the one modified item because of specification changes not approved by the Import Department caused the good to be entered for ATPA preference using an incorrect HTS number. The company found that despite the failure of the controls, the good as reclassified using the correct HTSUS number, still qualified for ATPA. The CIP provided training in existing procedures, expanded the existing procedure for sending to the Import Department all new goods including “modifications” to existing goods for approval (and proper classification), and improved interdepartmental communication. Before PAS close, the team was able to confirm there were no additional compliance issues and that controls were in place and working effectively. Therefore, proceeding to ACT was not considered necessary.

Example C: Situation where the team would proceed to ACT (Revenue)

The same controls as Example A above. However, the limited testing of ten goods covered 50 percent of the total ATPA value and 50 percent of the vendors. The PAS review found that the written internal controls were not followed. The IM never determined whether any of the shipments qualified for the ATPA preference. The limited testing showed that 3 of the 10 goods tested (covering 2 vendors) did not meet the ATPA value content requirements, making the three goods dutiable. The two vendors with dutiable merchandise had shipped additional products not tested. Because the company was not compliant with their procedure manual, there was a failure to determine whether any goods qualified for the ATPA trade preference. The company did not agree to quantify the loss of revenue or take corrective action. Since there was a large quantity of untested merchandise and untested vendors the PAS team proceeded to ACT to determine whether there were any additional ineligible ATPA goods, which would result in additional duty.

Example D: Situation in which the team would proceed to ACT (Compliance)

The same controls as Example A above. However, the Import Department did not determine whether the shipments qualified for the ATPA preference. Since the company was not compliant with their Procedures manual, there was a failure to determine whether any of the goods qualified for the ATPA trade preference. Since the PAS team found that the written internal controls were not followed, the decision was made to forego limited testing because ATPA imports represented by merchandise value 60 percent of all imports. The lack of controls for 60 percent of the merchandise value caused the risk exposure to be considered too high for limited testing. Since the company did not agree to or take corrective action, proceeding to ACT using statistical sampling to determine a compliance rate (and possibly a loss of revenue) was considered necessary.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - ANDEAN TRADE PREFERENCE ACT (ATPA)

PURPOSE: To determine whether ATPA risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls over ATPA merchandise formally documented?					
2.	Are written policies and procedures approved by management?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager responsible for control of the Import Department, including ATPA imports?					
5.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
6.	Does the responsible person have cost accounting knowledge?					
7.	Do written internal control procedures assign ATPA duties and tasks to a position rather than a person?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
8.	Does the company have adequate interdepartmental communication about ATPA matters?					
9.	Does the company conduct and document periodic reviews of ATPA?					
10.	Does the company use the ATPA periodic review results to make corrections to its import operations?					
11..	Does the company identify, analyze, and manage risks related to ATPA					
12.	Has the company identified any risks related to ATPA and implemented control mechanisms?					
13.	Does the company use the ATPA periodic reviews to make changes to its import declarations as appropriate?					
14.	Do internal controls involve a verification process to determine that the imported merchandise qualifies for ATPA?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
15.	Is adequate descriptive information provided (by Purchasing, Engineering, other departments, and suppliers) to the Customs Department and/or broker to ensure proper ATPA eligibility?					
16.	Does the importer have procedures to obtain any required or necessary documentation to support the claim (e.g. a contract penalty provision if ATPA information is not provided to Customs on demand)?					
17.	Does the importer maintain an ATPA database or listing of imported merchandise that would readily identify ATPA transactions?					
18.	Does the importer (or the importer's agent) visit the plant in the ATPA country(s) where the products are produced?					
19.	Does the company perform an annual review of changes to ATPA?					
	New ATPA Merchandise					
20.	Does management review the classification and eligibility of new ATPA items?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
21.	Is responsibility for the ATPA eligibility process assigned to one knowledgeable individual or department with management oversight?					
22.	Is adequate descriptive information provided to the Customs Department and/or broker by suppliers, engineers, purchasing department, etc. to ensure proper classification?					
23.	Is Customs assistance sought in classifying merchandise (e.g., requesting binding rulings)?					
	Entry Review					
24.	Does the company review entries to verify that correct classifications were used?					
25.	Does the company monitor the entry review process to verify that controls were followed?					
26.	Are suppliers required to print company provided HTSUS numbers on invoices and/or packing lists?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
27.	Does the individual reviewing merchandise have adequate knowledge and training on ATPA issues?					
28.	Are HTS classifications for ATPA maintained in a database that is provided to brokers?					
29.	Are brokers required to have written company approval to make classification changes?					
30.	Does the company provide adequate broker oversight?					
31.	Does the company have internal control procedures to address specific issues identified in the profile?					
32.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

PRODUCTS OF INSULAR POSSESSIONS
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

2.1 EXAMPLES OF RED FLAGS 3
2.2 EXAMPLES OF BEST PRACTICES.....4
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 5

3.1 RISK 5
A. Preliminary Assessment of Risk.....5
B. Evaluation of Risk Acceptability 5
3.2 INTERNAL CONTROL.....6
3.3 EXTENSIVENESS OF AUDIT SAMPLE TEST (TESTING LIMIT).....6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – PRODUCTS OF INSULAR POSSESSIONS.....10

PRODUCTS OF INSULAR POSSESSIONS
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for merchandise entered as products of insular possessions (IP) and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

PART 2 INSULAR POSSESSION GUIDANCE

Regulations governing IPs are in 19 CFR Part 7. In addition, General Note 3(a)(iv) of the Harmonized Tariff Schedule of the United States (HTSUS) , provides the criteria for preferential treatment of products produced in IPs. For purposes of this technical guide, only sections 7.2, 7.3 and 7.4 of 19 CFR will apply. Additionally there is a Customs Informed Compliance document on IP dated June,1999.

Additional guidance may be found in:

- C.S.D. 85-25 (double substantial transformation);
- Ruling 556193, dated 12/23/91 (dual-sourcing);
- Ruling 557087, dated 7/22/93,T.D. 81-282, T.D. 78-399, and C.S.D. 80-208 (unallowable general and administrative costs); and
- Ruling 559010, dated 3/14/96 and T.D. 91-7 (treatment of components in sets).

Insular possessions of the U.S. include; the U.S. Virgin Islands, Guam, American Samoa, Wake Island, Midway Islands, Johnston Atoll, and the Commonwealth of the Northern Mariana Islands. 19 CFR 7.2(a). Importations into these Insular Possessionsare not governed by the Tariff Act of 1930, as amended. 19 CFR 7.2(b).

To qualify for duty free treatment, products of insular possessions must:

- Be wholly the growth or product of the insular possession; or the good must became a new and different article as a result of manufacture or production in the insular possession, (See section 7.3(b) of 19 CFR)
- Not contain foreign materials that represent more than 70 percent of the goods total value; or in the case of IP goods described in section 213(b) of the Caribbean Basin Economic Recovery Act (19 U.S.C. 2703(b)), more than 50 percent** of the goods total value. (See section 7.3(a)(1)(i) of 19 CFR).
- Come directly to the U.S. from the insular possession; (See sections 7.3(a)(1)(ii) and 7.3(e) of 19 CFR)

**The 50 percent value content requirement for products of IPs applies to the goods listed in section 10.233(a) of 19 CFR.

A producer of an IP product is required to incorporate any foreign material into the good no later than 18 months after importation from the foreign supplier (See section 7.3(c)(3)(ii) of 19 CFR). The following HTSUS provisions provide additional guidance for specific commodities when these commodities are the products of an IP:

- Additional U.S. Note 5 of chapter 91;
- Additional U.S. Note 2 of chapter 96,and except as provided in section 423 of the Tax Reform Act of 1986, as amended (19 U.S.C. 2703 note); and
- Additional U.S. Note 3(e) of chapter 71.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem with the merchandise entered as products of IPs.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring merchandise entered as products of an IPs for Customs purposes. Examples:
  - ✓ Company does not monitor or interact with the broker on IP eligibility issues.
  - ✓ Company relies on one employee to handle IP merchandise, and there are poor or no management checks or balances over this employee.
- Company staff lacks knowledge of IP eligibility issues.
- The company's import manager lacks cost accounting knowledge
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate or respond to Customs.
- Company has high turnover of people in key positions.
- Significant variance exists between the importer's data and Customs' data.
- Customs (import specialist, account manager, compliance measurement, prior audit, profile) shows history of problems with IP merchandise.
- Company has either, never previously imported IP merchandise, or there was a large increase of imports of IP merchandise from a prior period.
- The importing company obtains identical articles from two different countries, where one of the countries is an insular possession and the other is not.
- The IP producer sources materials to produce the IP article from two different countries, where one of the countries is an insular possession the other is not.
- The importer does not request, maintain, or review documents supporting the qualification of IP merchandise (e.g., value content qualification).
- The importer and the IP producer are related.
- There is no prior audit or Customs review of the company's IP imports.
- Company does not monitor the IP classification or records process.
- The goods do not have markings to determine the country of origin.
- The company cannot provide a list of foreign suppliers and the types of goods the supplier provides.
- Amounts on cost sheets for unallowable general expenses and profit appear unusually low, indicating that allowable costs may be overstated.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over merchandise entered as products of IPs:
  - ✓ Are in writing,
  - ✓ Include procedures for monitoring and feedback, and
  - ✓ Are monitored by management.
- One manager is responsible for control of the import department, including merchandise entered as products of IPs. That manager has knowledge of customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- The company conducts and documents periodic reviews of merchandise entered as products of an IP, and uses the results to make corrections to entries and changes to their import operations as appropriate.
- The company has good interdepartmental communication about Customs matters.
- Importer has procedures to obtain any required or necessary documentation from its suppliers to support IP eligibility. (e.g., penalty provisions on the supplier in the purchase order if IP content information is not provided to Customs on demand).
- Importer maintains a database or listing of imported merchandise that would readily identify IP transactions.
- The company has a program in place to prevent transshipment.
- The company can itemize the value of the materials used.
- The company can readily provide listing of goods that are products of IPs.
- The company can provide the origin of the materials used in the production of the goods from the IP.
- The company visits the plant in the IP country where the products are produced.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to merchandise entered as products of IPs.
- Country of origin markings on products and components.
- Company’s documentation that supports monitoring and verification of established and/or written internal control for merchandise entered as products of IPs including:
  - ✓ A declaration by the shipper in the IP.
  - ✓ Certificate of Origin (Customs Form 3229).
  - ✓ Listing of goods that are products of IPs.
  - ✓ Invoices providing a description and origin of the IP products.
  - ✓ Specification sheets, drawings, or bills of material depicting the products of the insular possession that are included in the produced goods.
  - ✓ Bills of Lading that show direct transport from the U.S. to the IP and/or direct transport from the insular possession to the U.S.
  - ✓ Proof that the goods of the IPs have not been claimed for drawback.
  - ✓ Listing of origin of the products used in production.

- ✓ Travel documents that show the company visited the manufacturers or factories to verify that the products were manufactured produced in the IP.
- ✓ Customs Form ITA-361, Request for Refund of Duties on Watches and Watch Movements.
- ✓ Manufacturer's affidavits as to country of origin of components.
- ✓ Bills of material listing country of origin for components, whether foreign vendors are related or unrelated.
- ✓ "Where used" reports ("exploded " bills of material) showing that components underwent "double substantial transformation".
- ✓ Accounting records supporting product cost sheets, including financial statements, post-closing trial balance, detailed chart of accounts, and general ledger detail.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company 's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment
   - Risk Assessment
   - Control Activities
   - Information and Communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over merchandise entered as products of an IP (Examples of documents and information to review are listed on the prior page).

3. Determine whether the company established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence of communication between the broker and company on merchandise entered as products of IP issues, company testing of broker operations and verification that the broker followed company instructions.
   - Company-specific IP rulings and evidence that they are followed.
   - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
   - Training records and materials relating to IP used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for Products of Insular Possessions in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control
   - Determine what is already known about control effectiveness
   - Assess the adequacy of internal control design
   - Determine whether controls are implemented and effective
   - Determine whether transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TEST (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In such cases, it may

be necessary to proceed immediately to the ACT process. If the PAS team believes it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the total IP level that will be reported. For example, the company imports from several foreign companies, but testing may be necessary only for certain companies or only certain products that have been identified as primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over merchandise entered as products of insular possession.

1. Complete the Worksheet for Evaluating Internal Control (WEIC) for Products of Insular Possessions to determine whether risk is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist and account manager. The team must evaluate the PAS results based on the specific situations.
   Customs considers risk to be unacceptable when testing reveals that internal control is not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT.

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.

- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

Proceed to ACT if:

- The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS *are for clarification purposes only:*

Example A: Situation in which the team would not proceed to ACT (Revenue)

Background

The company's Customs compliance manual requires that its import manager obtain a declaration by the shipper for each crude oil shipment prior to importation into the U.S. Before a shipment can be released to the refinery, the company's import classification clerk from the shipping department must sign a shipment release certificate, which indicates whether or not, the shipment qualifies for products of IPs. The clerk determines whether or not the shipment qualifies based on 10.233(a)(3) of 19 CFR that applies specifically to petroleum.

If the goods qualify, a special trade indicator "Y" is stamped on the shipment release certificate. A copy of the shipment release certificate, and declaration by the shipper are submitted to the import manager for review, approval, and filing. The import manager forwards a copy of the approved documents to the broker for use in preparing the entry and filing. Once the Broker prepared the entry, a copy is sent to the import clerk to check for accuracy. The import clerk then sends a copy of the entry to the accounting department. The accounting department prepares a cash disbursement voucher and sends it to the import manager for payment.

The PAS Results

The PAS found that one of the six entries selected for review did not go through the company's review process to ensure it qualifies as a product of an IP. The entry involved crude oil that was not substantially transformed into a new product of the IP and therefore did not qualify. The company agreed with the PAS finding and quantified the loss of revenue. The company subsequently reviewed all entries, found all the untested entries that had not gone through the

review process, and quantified the loss of revenue. Since Customs was able to determine that correction occurred proceeding to ACT was not necessary.

Example B**:** Situation in which the team would not proceed to ACT (Compliance)

Same situation as Example A above, except the PAS team was able to verify that controls were in place and working effectively. All six of the entries selected for review went through the company's review process to ensure the goods qualify for products of IPs. Therefore, proceeding to ACT was not considered necessary.

Example C**:** Situation in which team would proceed to ACT (Revenue)

Same situation as Example A above, except that the PAS found more entries of other commodities that did not go through the company's review process and the company was not able to quantify the loss of revenue. Therefore, proceeding to ACT was considered necessary.

Example D**:** Situation in which team would proceed to ACT (Compliance)

The same situation as Example A above, except that (as stated in its procedures manual) the company did not allow the import classification clerk from the shipping department to review the data and sign a shipment release certificate. The company refused to follow its written procedures or establish new procedures to correct the problems. Proceeding to ACT was considered necessary to determine the extent of the problem.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – PRODUCTS OF INSULAR POSSESSIONS

PURPOSE: To determine whether Products of Insular Possessions risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls to ensure products of IP meet eligibility formally documented?					
2.	Are written policies and procedures approved by management?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager responsible for control of the Import Department, including products of IPs?					
5.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
6.	Does the responsible person have cost accounting knowledge?					
7.	Do written internal control procedures assign IP duties and tasks to a position rather than a person?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
8.	Does company have good interdepartmental communication about IP matters?					
9.	Does company conduct and document periodic reviews of products of IP?					
10.	Does company use the IP periodic review results to make corrections to past and present entries?					
11.	Does the company use the IP periodic reviews to make changes to it import operations as appropriate?					
12.	Do internal controls involve a verification process to determine that the imported merchandise qualifies for IP?					
13.	Is adequate descriptive information provided (by purchasing, engineering, supplier, and other department) to the Customs Department and/or broker to ensure proper IP classification and eligibility?					
14.	Does the importer have procedures to obtain any required or necessary documentation to support the claim (e.g., a contract penalty provision if IP information is not provided to Customs on demand)?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
15.	Does the importer maintain an IP database or listing of imported merchandise that would readily identify IP transactions?					
16.	Does the importer (or its agent) visit the plant in the IP country where the products are produced?					
17.	Does the company perform an annual review of changes to IP?					
18.	Does the individual overseeing compliance with products of insular possession requirements have adequate knowledge and training?					
	NEW IP MERCHANDISE					
19.	Does management review the classification and eligibility of new IP items?					
20.	Is responsibility for the IP eligibility process assigned to one knowledgeable individual or department with management oversight?					
21.	Is Customs assistance sought in classifying merchandise (e.g., requesting binding rulings)?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	ENTRY REVIEW					
22.	Does the company review entries to verify that correct classifications were used?					
23.	Does the company monitor the entry review process to verify that controls were followed?					
24.	Are suppliers required to print company-provided HTSUS on invoices and/or packing lists?					
25.	Does the company provide adequate broker oversight?					
26.	Does the company identify, analyze and manage risks related to Insular Possessions?					
27.	Has the company identified any risks related to Insular Possessions and implemented control mechanisms?					
28.	Does the company have internal control to address specific issues identified in the profile?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
29.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

ISRAEL FREE TRADE ACT (IFTA)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 IFTA GUIDANCE.....2

2.1 EXAMPLES OF RED FLAG.....3
2.2 EXAMPLES OF BEST PRACTICES.....4
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....5

3.1 RISK.....5
A. Preliminary Assessment of Risk.....5
B. Evaluation of Risk Acceptability.....6
3.2 INTERNAL CONTROL.....6
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT).....7
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....7
3.5 EXAMPLES.....8

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – ISRAEL FREE TRADE AREA (IFTA).....11

ISRAEL FREE TRADE ACT (IFTA)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

Provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for goods entered for preferential treatment as products of the Israel Free Trade Area (IFTA) and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, in Performance Audits published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

PART 2 IFTA GUIDANCE

On April 22, 1985, a free trade agreement was established between the Government of the United States of America and the Government of Israel. Public Law 99-47 entitled the U.S.-Israel Free Trade Area Implementation Act of 1985. IFTA is a special trade program authorized by the president to extend trade benefits for eligible articles of Israel for preferential treatment when entered into the U.S. and satisfying the IFTA eligibility requirements. The eligibility requirements for IFTA goods are found in General Notes (GN) 8 and 3(a)(v) of the Harmonized Tariff Schedule of the United States (HTSUS). The GN describes specific rules that are considered for IFTA preference.

GN 8 designates articles produced by Israel and GN 3(a)(v) covers specific entities including the West Bank, the Gaza Strip or a qualifying industrial zone (defined in GN 3(a)(v)(G)) as eligible to claim preference under IFTA.

Merchandise subject to IFTA preference appears in the HTSUS as "Free" in the HTSUS "Special" Rate of Duty subcolumn followed by the symbol "IL" in parenthesis. The Israel Free Trade preference is claimed on the imported good by using the symbol "IL" in the Special Program Indicator field of the Automated Commercial System (ACS) database.

Although GN 8(e) indicates regulations will be issued as necessary, to date there are no formal regulations for the IFTA.

To qualify for preferential treatment merchandise of the IFTA must:

- Be imported to the U.S. directly from Israel, the West Bank, the Gaza Strip or a "qualifying industrial zone". The direct shipment requirements are in GN 8(b)(ii) and 3(a)(v)(B).
- Meet the country of origin criteria and either: a) be merchandise wholly the growth, product or manufacture of Israel, the West Bank, the Gaza Strip or a "qualifying industrial zone"; or b) be merchandise transformed into a new or different article that has been grown, produced or manufactured in Israel, the West Bank, the Gaza Strip or a "qualifying industrial zone". The origin criteria are stated in GN 8(b)(i) and 3(a)(v)(A)(1) & (2).
- Meet the value content requirements where the sum of materials and direct cost of processing must represent not less than 35 percent of the goods' appraised value at the time it is entered. If the article includes cost or value of materials produced in the

customs territory of the United States, an amount not to exceed 15 percent of the appraised value may be applied toward determining the percentage. The percentage value content requirements are stated in GN 8(b)(iii) and 3(a)(v)(A)(2).

The term "Qualifying Industrial Zone" is a term defined in GN 3(a)(v)(G) as "any (designated) area that encompasses portions of the territory of Israel and Jordan, or Israel and Egypt."

Additional guidance may be found in:

- C.S.D. 85-25 (double substantial transformation);
- Ruling 556193, dated 12/23/91 (dual-sourcing);
- Ruling 557087, dated 7/22/93, T.D. 81-282, T.D. 78-399, and C.S.D. 80-208 (unallowable general and administrative costs); and
- Ruling 559010, dated 3/14/96 and T.D. 91-7 (treatment of components in sets).

2.1 EXAMPLES OF RED FLAG

The following examples are conditions that may indicate a potential problem with IFTA merchandise.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring merchandise entered as products of IFTA for Customs purposes. Examples:
  - ✓ Company does not monitor or interact with the broker on IFTA issues.
  - ✓ Company relies on one employee to handle IFTA issues, and there are poor or no management checks or balances over this employee.
- Responsible person lacks cost accounting knowledge.
- Company's import staff lacks knowledge of IFTA eligibility requirements.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.
- Significant variance exists between the importer's data and Customs' data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with merchandise entered as IFTA goods.
- One company representative dominates multiple phases of the IFTA process without monitoring or management oversight.
- HTSUS numbers that the company uses to enter IFTA merchandise have high compliance measurement error rates.
- Company imports from a specific exporter, or under an HTSUS number or country of origin, that have been identified by Customs because of known or suspected IFTA problems.
- Company has a large number of IFTA exporters or a large number of goods for which IFTA is claimed.
- The company does not request, maintain, or review documents supporting the qualification of IFTA imports.
- Company has a sharp increase of IFTA imports from a prior period.
- The importer claiming IFTA and the exporter producing the merchandise are related parties.
- There have been no prior audits or Customs reviews of IFTA imports.
- The profile identifies specific IFTA issues.

- The IFTA producer dual sources or obtains a material from two different countries, where only one material is a product of Israel.
- The merchandise does not have required markings to distinguish the origin.
- A declaration that assembled IFTA goods declared as wholly produced or manufactured in Israel or a “qualifying industrial zone” appears to be doubtful.
- The importer does not request, maintain, or review documents supporting the qualification of IFTA imports (e.g., value content requirements).
- Value content qualification is marginal, just meeting the 35 percent requirement, increasing the importance of accurate cost computations.
- Direct materials alone are not adequate to meet the 35 percent value content requirement, making accurate direct processing costs particularly important.
- Textiles and apparel articles imported are subject to textile restrictions.
- Amounts on cost sheets for unallowable general expenses and profit appear unusually low, indicating that allowable costs may be overstated.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over merchandise entered for preferential treatment under the Israel Free Trade Act (IFTA):
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Were monitored by management.
- One manager is ultimately responsible for control of the import department, including merchandise entered as IFTA goods. That manager has knowledge of Customs matters and the power to assure internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign IFTA duties and tasks to a position rather than a person.
- The company has good interdepartmental communication regarding IFTA matters.
- The company conducts and documents periodic reviews of IFTA merchandise and uses the results to make corrections to past and present entries, and makes changes to their import operations as appropriate.
- Purchasing, Engineering, other departments, and suppliers provide sufficient descriptions of merchandise to permit a determination of IFTA eligibility.
- Internal control involves a verification process to determine that the imported merchandise qualifies for IFTA.
- Importer has procedures to obtain any required or necessary documentation to support the claim (e.g. a penalty provision on the supplier if IFTA information is not provided to Customs on demand).
- Importer maintains a database or listing of imported merchandise that would readily identify IFTA transactions.
- The importer (or the importer’s agent) visits the plant in the IFTA country where the products are produced.
- The importer performs an annual review of changes to IFTA.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures for ensuring IFTA eligibility.
- The company's response to the questionnaire.

- Interviews with company staff concerning actual procedures and controls specific to IFTA imports.
- Documentation that supports monitoring and verification of established and/or written internal control for IFTA imports.
- The company's documentation that supports monitoring and verification of established and written internal control for IFTA including:
  - ✓ An IFTA declaration signed by the person responsible for certifying that all information on the documentation is accurate and complete.
  - ✓ A list of goods by vendor that are products of the IFTA.
  - ✓ Invoices, specification sheets, or other documents providing a detailed description and origin of the IFTA goods.
  - ✓ Bills of Lading or other documents that show direct transport to the U.S.
  - ✓ For related or unrelated foreign vendors, bills of material listing country of origin of the materials used in production of the good.
  - ✓ Travel documents that show that the company has recently visited the IFTA manufacturer and verified the commodities are manufactured, produced, or wholly grown in Israel, the West Bank, the Gaza Strip or a "qualifying industrial zone".
  - ✓ Records from the IFTA producer supporting the company's verification for goods not wholly the growth or product of Israel, such as, cost allocation worksheets, bills of materials, product specification sheets, engineering drawings, work-in-process documents, material inventory records, purchase history reports, and/or material supplier lists.
  - ✓ Country of origin markings on products and components.
  - ✓ Manufacturer's affidavits as to country of origin of components.
  - ✓ "Where used" reports ("exploded" bills of material) showing that components underwent "double substantial transformation".
  - ✓ Accounting records supporting product cost sheets, including financial statements, post-closing trial balance, detailed chart of accounts, and general ledger detail.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company 's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs

based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.
- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.
- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment
   - Risk Assessment
   - Control Activities
   - Information and Communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over entries of IFTA products (examples of documents and information to review are listed on prior pages).

3. Determine whether the company established and follows procedures by reviewing:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence (such as a log) of communication between the broker and the company on IFTA issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Company-specific IFTA rulings, and evidence that they are followed.
   - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
   - Training records and materials relating to IFTA used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for IFTA Goods in Part 4 of this document.

Note: The internal control assessment should include steps to:

- Identify and understand internal control.
- Determine what is already known about control effectiveness.
- Assess the adequacy of internal control design.
- Determine whether controls are implemented and effective.
- Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the total IFTA level that will be reported on. For example, the company may import from several foreign companies, but testing may be necessary only for certain companies or certain products that have been identified as primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over merchandise entered as products of IFTA.

1. Complete the WEIC for IFTA Goods to determine whether risk is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import

specialist or account manager. The team must evaluate the PAS results based on the specific situations.

Customs considers risk unacceptable when testing reveals that internal control is not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will help the PAS team determine whether conditions warrant proceeding to ACT.

   Do not proceed to ACT if:
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   Proceed to ACT if:
   - The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate, or revenue loss, can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether EET thresholds are met, or could be met, and take appropriate action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS are *for clarification only*.

Example A: Situation in which the team would not proceed to ACT (Revenue)

Background
Commodities Inc., (CI) imports a number of articles manufactured in Israel (none are wholly a product of Israel) entered duty free. The exporter has indicated that the IFTA merchandise is produced with materials obtained from both the United States and foreign vendors. The internal control procedures listed in CI procedure manual requires that two conditions be met before purchasing. The two conditions are: 1) the buyer must secure from the IFTA vendor, at the time the purchase order is written, a general written statement regarding the content of the merchandise; and 2) the purchasing department will obtain from the vendor, as part of the purchase order, a statement that the vendor will provide Customs with detailed value content

data on demand. The purchase order statement also indicates any failure to supply Customs with the needed content information will make the IFTA vendor liable for any duty due.

The PAS team requested the IFTA vendors' material costs and allocation of direct costs of processing for eight items. The eight items represented imports from all IFTA vendors and 90 percent of the IFTA merchandise value. The producers were able to provide the requested information because of the conditions set in the purchase orders. An analysis of how the producers allocated the labor and overhead costs revealed that the allocations included some costs that were not part of the direct cost of processing. As a result of the revised allocations, one item failed to meet the 35 percent content requirements.

CI agreed with the PAS finding and quantified the loss of revenue. CI also reviewed the remaining 10 percent of the IFTA merchandise not covered by the PAS and found that they qualified for IFTA treatment. The PAS Team reviewed CI's work and confirmed its accuracy. Therefore, proceeding to ACT was not considered necessary.

Example B: Situation in which the team would not proceed to ACT (Compliance).

Same as Example A above except that the purchase order for one item did not have the IFTA "documents on demand/duty for failure to provide records" provision stated on the purchase order. Although the purchase order procedure was not followed, the article was entered under IFTA preference. The company found that despite their failure to put the provisions on the purchase order, the content information was supplied to Customs on demand and the good was determined to qualify under the IFTA.

The cause for the above error was the lack of communication between departments and internal control procedures in place at the time. The company established a CIP to reinforce existing procedures and to improve communication between the departments. Therefore, proceeding to ACT was not considered necessary.

Example C: Situation in which the team would proceed to ACT (Revenue).

Same internal control procedures as in Example A, except that 16 items (two from each vendor) were selected from eight vendors for review. The PAS sample represented 52 percent of the IFTA entered value and eight of the 10 IFTA vendors.

Two of the eight vendors tested failed to provide Customs with documentary evidence for four of the 16 items. As a result, the duty free treatment for four items was denied.

It was determined that CI did not review the shipments to determine whether they qualified for IFTA preference. The broker was instructed to enter the goods as eligible for IFTA. In addition, the 48 percent of IFTA value that was not covered in the PAS testing included two vendors that were never selected for review, and additional items for the two vendors that previously failed to provide IFTA documentary evidence. CI did not agree with our findings, was unable to quantify the loss of revenue, and did not take corrective actions to ensure that the 48 percent of merchandise value not tested qualified for IFTA. As a result, the PAS team proceeded to ACT to determine potential loss of revenue on ineligible IFTA merchandise.

Example D: Situation in which the team would proceed to ACT (Compliance).

CI has the same controls as Example A above except that prior to limited PAS testing, it was discovered that written internal control procedures were not followed. CI did not follow its procedures to review merchandise for IFTA eligibility. The broker was instructed to enter the goods as eligible for IFTA.

For this example, CI is a mass merchandiser of Middle Eastern goods. CI imports from many vendors covering many HTS numbers. Due to the large volume of IFTA vendors and the broad range of IFTA merchandise, a determination of risk could not be assessed, based on a limited review of 20 items, without going to the ACT phase. Since the company did not agree to, or want to, take corrective action, proceeding to ACT to determine CI level of compliance was considered necessary.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – ISRAEL FREE TRADE AREA (IFTA)

PURPOSE: To determine whether IFTA risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	Overall Controls					
1.	Are internal controls over IFTA merchandise formally documented?					
2.	Does management approve written policies and procedures?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager responsible for control of the Import Department, including IFTA imports?					
5.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
6.	Does the responsible person have cost accounting knowledge?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Do written internal control procedures assign IFTA duties and tasks to a position rather than a person?					
8.	Does the company have good interdepartmental communication about IFTA matters?					
9.	Does the company conduct and document periodic reviews of IFTA?					
10.	Does the company use the IFTA periodic review results to make corrections to its import operations?					
11.	Does the company use the IFTA periodic reviews to make changes to its import declarations as appropriate?					
12.	Do internal controls involve a verification process to determine that the imported merchandise qualifies for IFTA?					
13.	Is adequate descriptive information provided (by Purchasing, Engineering, other departments, and suppliers) to the Import Department and/or broker to ensure proper IFTA eligibility?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Does the importer have procedures to obtain any required or necessary documentation to support the claim (e.g. a contract penalty provision if IFTA information is not provided to Customs on demand)?					
15.	Does the importer maintain an IFTA database or listing of imported merchandise that would readily identify IFTA transactions?					
16.	Does the importer (or the importer's agent) visit the plant in the IFTA country(s) where the products are produced?					
17.	Does the company perform an annual review of changes to IFTA?					
	New IFTA Merchandise					
18.	Does management review the classification and eligibility of new IFTA items?					
19.	Is responsibility for the IFTA eligibility process assigned to one knowledgeable individual or department with management oversight?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
20.	Is adequate descriptive information to ensure proper classification provided to the Import Department and/or broker by suppliers, engineers, purchasing department, etc.?					
21.	Is Customs assistance sought in classifying merchandise (e.g., requesting binding rulings)?					
	Entry Review					
22.	Does the company review entries to verify that correct classifications were used?					
23.	Does the company monitor the entry review process to verify that controls were followed?					
24.	Are suppliers required to print company provided HTSUS numbers on invoices and/or packing lists?					
25.	Does the individual reviewing merchandise have adequate knowledge and training on IFTA issues?					
26.	Are HTS classifications for IFTA maintained in a database that is provided to brokers?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
27.	Are brokers required to have written company approval to make classification changes?					
28.	Does the company provide adequate broker oversight?					
29.	Does the company identify, analyze, and manage risks related to IFTA?					
30.	Has the company identified any risks related to IFTA and implemented control mechanisms?					
31.	Does the company have internal control to address specific issues identified in the profile?					
32.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

AFRICAN GROWTH AND OPPORTUNITY ACT
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

2.1 AGOA TEXTILE ARTICLES.....3
2.2 AGOA NON-TEXTILE ARTICLES 3
2.3 EXAMPLES OF RED FLAGS 3
2.4 EXAMPLES OF BEST PRACTICES.....4
2.5 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 5

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 6

3.1 RISK 6
A. Preliminary Assessment of Risk.....6
B. Evaluation of Risk Acceptability 6
3.2 INTERNAL CONTROL.....6
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 7
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....8
3.5 EXAMPLES.....9

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - AFRICAN GROWTH AND OPPORTUNITY ACT (AGOA) 12

AFRICAN GROWTH AND OPPORTUNITY ACT (AGOA)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for articles entered for preferential treatment as products of the African Growth and Opportunity Act (AGOA) and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits*; GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

PART 2 AGOA GUIDANCE

Title I of the Trade and Development Act of 2000 (Public Law 106-200) entitled the AGOA. Codified at 19 U.S.C. 3721 through 3724, AGOA is a special trade program authorizing the president to extend certain trade benefits for eligible articles of designated beneficiary countries (BCs) in sub-Saharan Africa.

General Note 16 of the Harmonized Tariff Schedule of the United States (HTSUS), designates the BCs eligible to claim preference under AGOA. The merchandise subject to AGOA preference appears as "free or at a reduced rate of duty" by HTSUS number in the HTSUS "Special" Rate of Duty sub-column followed by the symbol D in parenthesis. The African Growth Preference is claimed on the imported good by using the letter D in the Special Program Indicator field of the Automated Commercial System (ACS) database. AGOA **textile/apparel** and **non-textile** article requirements are in separate sections of 19 CFR Part 10. For purposes of this technical guide the term textile will include textile and apparel covered by the AGOA regulations. In addition to the General Note and the Customs regulations there is a Customs Informed Compliance Pamphlet for AGOA dated May 2001.

Additional guidance may be found in:

- C.S.D. 85-25 (double substantial transformation);
- Ruling 556193, dated 12/23/91 (dual-sourcing);
- Ruling 557087, dated 7/22/93,T.D. 81-282, T.D. 78-399, and C.S.D. 80-208 (unallowable general and administrative costs); and
- Ruling 559010, dated 3/14/96 and T.D. 91-7 (treatment of components in sets).

The Trade Act of 2002 ("the Act") was signed by President Bush on August 6, 2002, and substantially expands preferential access for imports from beneficiary Sub-Saharan African countries by modifying certain provisions of the African Growth and Opportunity Act (AGOA).

The Act clarifies and narrowly expands the trade opportunities for Sub-Saharan African countries under AGOA and encourages more investment in the region. AGOA enhancements include revisions requested by many Sub-Saharan African countries. These enhancements maximize the benefits of AGOA. Auditors must obtain current information on AGOA provisions for imports after August 6, 2002.

2.1 AGOA TEXTILE ARTICLES

The eligibility requirements for AGOA **textile** articles (as defined in 19 CFR 10.212) are found in 19 CFR 10.211 through 10.217. Section 10.213(a)(1) through (a)(10) describes those eligible **textile** articles and the specific rules that are considered for AGOA preference. Section 10.213(b) lists the additional special rules for component materials. To qualify for preferential treatment AGOA **textile** and apparel, articles must meet the following requirements:

- The imported goods must come to the United States directly from the sub-Saharan beneficiary country; the direct shipment requirements are in section 10.213(c).
- The imported goods must meet the country of origin criteria, the goods description, and the specific manufacturing requirements, as stated in section 10.213(a)(1) through (a)(10) together with the special rules of section 10.213(b) for component materials.
- The imported goods must be supported by an original Certificate of Origin described in section 10.214.

2.2 AGOA NON-TEXTILE ARTICLES

The AGOA rules for **non-textile** articles, are an extension of the Generalized System of Preferences (GSP) regulations (contained in 19 CFR 10.171 through 10.178). Regular and enhanced GSP benefits for the AGOA countries were extended until September 30, 2008. The GSP treatment of AGOA **non-textile** articles is reported in section 10.178a. Specific AGOA modifications to the GSP regulations are noted in section 10.178a (d) and (e). To qualify for preferential treatment AGOA, **non-textile** articles must meet the following requirements:

- The imported goods must come to the United States directly from the sub-Saharan beneficiary country; the direct shipment requirements are in section 10.178a (e)(4) that refers to the GSP provision of section 10.175.
- The imported goods must meet the country of origin criteria as stated in section 10.178a (e)(2). This section defines the qualified merchandise as either: a) wholly the growth, product or manufacture of the beneficiary country; or b) transformed into new or different article that has been grown, produced or manufactured in a beneficiary country. Section 10.178a (e)(5) refers to the GSP provision of section 10.173.
- The imported goods must meet the value content requirements of section 10.178a (d)(4); the sum of materials and direct cost of processing must represent not less than 35% of the goods' appraised value at the time it is entered.

2.3 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem in AGOA.

- The company has insufficiently documented, poorly defined, or no internal control for accurately declaring AGOA for Customs purposes. Examples:
  - ✓ The company does not monitor or interact with the broker on AGOA issues.
  - ✓ The company relies on one employee to handle AGOA issues, and there are poor or no management checks or balances over this employee.
- The company staff lacks knowledge of AGOA eligibility requirements.
- The company offers unreasonable explanations to Customs.
- The company fails to cooperate with or respond to Customs.

- The company has high turnover of people in key positions.
- Significant variance exists between the importer's data and Customs' data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems AGOA (e.g., AGOA eligibility issues or reporting incorrect country of origin).
- HTSUS numbers that the company frequently uses for AGOA have high compliance measurement error rates.
- Company imports from a specific exporter, or under an HTSUS number or country of origin, that have been identified by Customs because of known or suspected AGOA problems.
- Company has a large number of AGOA exporters or a large number of articles for which AGOA is claimed.
- The importer does not request, maintain, or review documents supporting the qualification of AGOA imports.
- Company has a sharp increase of AGOA imports from a prior period.
- The importer claiming AGOA and the exporter are related parties.
- There have been no prior audits or Customs reviews of AGOA imports.
- The profile identified specific AGOA issues.
- The company dual sources or obtains an identical good from two different countries, where only one of the countries is an AGOA country.
- The articles do not have required markings to distinguish the origin.
- A declaration that assembled AGOA articles declared as wholly produced or manufactured in a beneficiary country appears to be doubtful.
- Value content qualification is marginal, just meeting the 35 percent requirement, increasing the importance of accurate cost computations.
- Direct materials alone are not adequate to meet the 35 percent value content requirement, making accurate direct processing costs particularly important.
- Textile and apparel articles imported are subject to textile restrictions.
- Responsible person lacks cost accounting knowledge.
- Amounts on cost sheets for unallowable general expenses and profit appear unusually low, indicating that allowable costs may be overstated.

2.4 EXAMPLES OF BEST PRACTICES

- Internal controls (required by 19 CFR 10.178a (e)(3) or 10.217(b)(2)) over merchandise entered as AGOA:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Were monitored by management.
- One manager is responsible for control of the Import Department, including AGOA. That manager has knowledge of Customs matters and the power to ensure internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign AGOA duties and tasks to a position rather than a person.
- The company has good interdepartmental communication regarding AGOA matters.
- The company conducts and documents periodic reviews of AGOA, and uses the results to make corrections past and present to entries, and changes to its import operations as appropriate.

- Purchasing, Engineering, other departments, and suppliers provide sufficient descriptions of merchandise to permit a determination of AGOA eligibility.
- Internal control involves a verification process to determine that the imported merchandise qualifies for AGOA.
- The importer has procedures to obtain any required or necessary documentation to support the claim (e.g. penalty provisions on suppliers if AGOA information is not provided to Customs on demand).
- The importer maintains an AGOA database or listing of imported merchandise that would readily identify AGOA transactions.
- The importer (or the importer's agent) visits the plant in the AGOA country where the products are produced.
- The importer performs an annual review of changes to AGOA.

2.5 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures for ensuring AGOA eligibility.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to AGOA.
- The company's documentation that supports monitoring and verification of established and/or written internal control for AGOA including:
  - ✓ For non-textile articles, an AGOA declaration signed by the exporter of the merchandise or other appropriate party having knowledge of the relevant facts.
  - ✓ A list of articles by vendor that are products of AGOA countries.
  - ✓ Invoices, specification sheets, or other documents providing a detailed description and origin of the AGOA articles.
  - ✓ For textiles, a Certificate of Origin with all of the information required by section 10.214.
  - ✓ Bills of lading or other documents that show direct transport to the United States
  - ✓ For related parties, a bill of materials listing the origin of the materials used in production.
  - ✓ Travel documents that show that the company has recently visited the AGOA manufacturer and verified the commodities are manufactured, produced, or wholly grown in the AGOA country.
  - ✓ Records from the AGOA producer supporting the company's verification for articles not wholly the growth or product of Africa, such as, cost allocation worksheets, bills of materials, product specification sheets, engineering drawings, work-in-process documents, material inventory records, purchase history reports, and/or material supplier lists.
  - ✓ Manufacturer's affidavits as to country of origin of components.
  - ✓ "Where used" reports ("exploded" bills of material) showing that components underwent "double substantial transformation."
  - ✓ Accounting records supporting product cost sheets, including financial statements, post-closing trial balance detailed chart of accounts, and general ledger detail.
  - ✓ Examples of Documents and Information to Review – Country of origin markings on products and components.
  - ✓ Bills of material listing country of origin for components, whether foreign vendors are related or unrelated.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company ‘s internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.

- Monitoring.

2. Review relevant Customs and company documents to identify and understand relevant internal control over entries of AGOA. (Examples of documents and information to review are listed on prior page).

3. Determine whether the company has established and follows procedures by reviewing:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence (such as a log) of communication with the broker and company departments on AGOA issues, including company testing of broker operations and verification that the broker followed company instructions.
   - Company-specific AGOA rulings. Determine whether they are followed.
   - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
   - Training records and materials relating to AGOA used to educate staff on Customs matters.
   - The Textile Certificate of Origin required by and described in 19 CFR 10.214 for AGOA textiles.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for AGOA Goods in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the total AGOA level that will be reported on. For example, the company imports from several foreign companies, but testing may be necessary only for certain companies or only certain products that have been identified as primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits*.
Column titled "Testing Limit" reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of the company's internal control over merchandise entered as products of AGOA.

1. Complete the WEIC for AGOA Goods to determine whether risk is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

   Customs considers risk to be unacceptable when testing reveals that internal control is not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will assist the PAS team in determining if conditions warrant proceeding to ACT.

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   <u>Proceed to ACT if:</u>
   - The company does not have adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.

- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate, or revenue loss, can be quickly performed and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether EET thresholds are met or could be met and take appropriate action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS *are for clarification only.*

Example A: Situation in which the team would not proceed to ACT (Revenue)

Commodities Inc (CI). imports a number of **textile** articles from sub-Saharan African countries entered duty free under the African Growth and Opportunity Act. The various AGOA goods are cut and sewn from materials obtained from the United States. All foreign components including findings, trimmings, and interlinings are reviewed and a determination is made that the costs do not exceed the 25 percent of value.

Pre-Assessment Survey
Internal control procedures indicated all AGOA goods were subject of an import department review. To determine whether the controls were working, the PAS team: (1) Selected ten textile articles (representing 50 percent of the total AGOA merchandise value) from the purchasing department files and (2) determined if there was evidence of import department approval. To determine if information was accurate and the goods were products of an AGOA beneficiary country, the purchase order information was compared to the information on the shipping documents, the supporting Certificate of Origin, and the manufacturer's statements. The PAS team also reviewed the engineer's content specifications of the produced articles beginning with the direct materials used in the manufacture of the finished articles together with any component materials.

The PAS team's review of records indicated that the company's import department failed to review and approve one of the selected ten textile articles. This one article was a "modification" of another already approved article. The modification which was not forwarded to the import department called for the application of additional "findings and trimmings". A failure of purchasing to communicate the additional costs of the modification to the import department resulted in a failure to initiate the internal control review for that article.

The PAS team's review of the materials making up this article not approved by the import department revealed that "findings and trimmings" exceeded the 25 percent maximum cost of components. As a result, the textile article no longer met the 19 CFR 10.213(b) requirements causing the article to be dutiable. The company agreed with the PAS finding and was able to determine that purchasing had made changes to an approved article and failed to send the modifications to the import department. The compliance improvement plan (CIP) reinforced all departments following existing procedures for all articles including any "modifications" to existing previously approved articles and called for improved interdepartmental communication. The company also agreed to quantify the loss of revenue (LOR) caused by the import department

not reviewing and approving the modification and would check for any additional modified articles not reviewed by the import department.

The eighteen articles making up the other 50 percent imported value not sampled by the PAS were checked by CI for any additional unauthorized (and not reviewed) modifications and verified by Customs. Of the eighteen AGOA articles, one article was found to have been modified by the purchasing department and not reviewed or approved by the import department. A further review revealed that the modified item still met the AGOA rules for preferential treatment. Since the LOR was quantified in the PAS and there were no indications of additional compliance or revenue issues, proceeding to ACT was considered unnecessary.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same situation as Example A above, except that PAS testing of ten textile articles of sub-Saharan revealed that one Certificate of Origin incorrectly listed a garment's origin under the AGOA rules of section 10.213(a)(1). However, because of the additional processing of the garment (stone washing and perma-pressing), the article did qualify under section 10.213(a)(2). The PAS team checked other records and there were no other additional articles using the incorrect rule of origin.

Although the import department failed to make a proper origin determination, the article still qualified for AGOA. The cause of the incorrect determination was the failure of Purchasing to provide the import manager (IM) all of the information on the garment's production. The subsequent CIP reinforced following the existing procedures, that the IM review all imported AGOA articles. The CIP also improved interdepartmental communication (an annual import department memo to key departments). Prior to PAS closing the team determined (based on the current review of two new AGOA products) that the controls in place were working effectively. Therefore, proceeding to ACT was considered unnecessary.

Example C: Situation in which the team would proceed to ACT (Revenue)

Commodities Inc (CI). imports a number of **non-textile** articles from AGOA designated countries entered duty free under the African Growth and Opportunity Act. In order to make this determination, CI must conclude that the country of origin, the direct shipment, and the percentage of value content criteria have all been met. The AGOA goods are articles assembled from materials obtained from foreign countries. The CI Import Procedures Manual requires the import department review the evidence of origin from the AGOA producer. The review includes questions on the origin of the materials used to produce the AGOA goods. Because of confidentiality concerns each AGOA vendor gives the import department general information about an article's material costs and material origins but discloses no specific information on the materials used, the source of the materials, or material prices.

Company's Policies and Procedures

For AGOA articles CI has a written company policy that the origin information will be obtained prior to the initial entry of the goods. As a condition of export, a Statement of Manufacture from the AGOA producer indicating that the goods were produced in the beneficiary country makes up part of the import documents. Each purchase order states that for goods imported by CI, on the AGOA producer's acceptance of the PO, the producer agrees to supply detailed information on material price and material source directly to Customs on demand when requested.

Pre-Assessment Survey

Internal control procedures indicated all AGOA goods were subject of an import department review. For goods imported by CI the purchase orders were written to state "on the AGOA

producer's acceptance of the PO, the producer agrees to supply detailed information on material price and material source directly to Customs. To determine if the controls were working, the PAS team selected a total of twelve articles from the purchasing department files and determined if there was evidence of import department approval. There were 6 AGOA vendors. Two articles were selected from each vendor. The twelve articles represented 40 percent of the total AGOA merchandise value.

Because the value content requirements were totally reliant on the AGOA producer the PAS team, in the early stages of the PAS decided to test by vendor. The team prepared Customs letters requesting material cost and content data using the format of section 10.173. The Customs letter assured the vendor of Customs confidentially of the records and requested the documents be sent to the Customs Regulatory Audit Office. Although three of the twelve purchase orders tested did not contain the "supply to Customs on demand" language, the necessary information was provided to Customs by the vendor.

At the same time CI contacted the six AGOA producers attesting to the authenticity of the Customs inquiry, reminding the vendor of the information agreement, and reassuring the producer that sensitive information provided to Customs would not be shared with CI. Customs received the value content information and was satisfied with ten responses. One vendor failed to respond, even after additional inquiries by both Customs and CI. The uncooperative AGOA vendor had additional articles not tested by the PAS and a history of exporting to CI beyond the period of the PAS. CI was unable or unwilling to quantify the loss of revenue. Because of the additional time needed to determine the extent of the loss of revenue a decision was made by the PAS team to proceed to ACT to determine a revenue amount.

Example D: Situation in which the team would proceed to ACT (Compliance)

The same situation as Example C above, with the additional finding that the internal control procedures as written by CI were not followed. The IM never determined if any of the non-textile shipments qualified for the AGOA preference. The broker was instructed by the purchasing department to enter all articles from AGOA beneficiary countries as duty free. Non-textile articles entered under the AGOA represented 60 percent of merchandise value of all CI imports.

Pre-Assessment Survey

Although entry documents indicate the articles were produced by and directly shipped from an AGOA eligible sub-Saharan country, CI was not compliant with their procedures manual since the IM failed to make any determination whether the any of the goods qualified for the AGOA trade preference. Since the PAS team was unable to determine compliance with the AGOA and the merchandise value represented a large part of CI's importing activity, the PAS team decided to go directly to ACT to determine compliance rather than limited testing of a system with no internal control. Since the company did not agree to or take corrective action, and denied that there was a problem, the decision to proceed to ACT using statistical sampling was considered necessary.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - AFRICAN GROWTH AND OPPORTUNITY ACT (AGOA)

PURPOSE: To determine whether AGOA risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	Overall Control					
1.	Are internal controls over AGOA merchandise formally documented?					
2.	Are written policies and procedures approved by management?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager responsible for control of the Import Department, including AGOA imports?					
5.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments?					
6.	Does the responsible person have cost accounting knowledge?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Do written internal control procedures assign AGOA duties and tasks to a position rather than a person?					
8.	Does the company have good interdepartmental communication about AGOA matters?					
9.	Does the company conduct and document periodic reviews of AGOA?					
10.	Does the company use the AGOA periodic review results to make corrections to its import operations?					
11.	Does the company use the AGOA periodic reviews to make changes to its import declarations as appropriate?					
12.	Do internal controls involve a verification process to determine that the imported merchandise qualifies for AGOA?					
13.	Is adequate descriptive information provided (by Purchasing, Engineering, other departments, and suppliers) to the Import Department and/or broker to ensure proper AGOA eligibility?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Does the importer have procedures to obtain any required or necessary documentation to support the claim (e.g. a contract penalty provision if AGOA information is not provided to Customs on demand)?					
15.	Does the importer maintain an AGOA database or listing of imported merchandise that would readily identify AGOA transactions?					
16.	Does the importer (or the importer's agent) visit the plant in the AGOA country(s) where the products are produced?					
17.	Does the company perform an annual review of changes to AGOA?					
	New AGOA Merchandise					
18.	Does management review the classification and eligibility of new AGOA items?					
19.	Is responsibility for the AGOA eligibility process assigned to one knowledgeable individual or department with management oversight?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
20.	Is adequate descriptive information provided to the Import Department and/or broker by suppliers, engineers, Purchasing Department, etc. to ensure proper Classification?					
21.	Is Customs assistance sought in classifying merchandise (e.g., requesting binding rulings)?					
	Entry Review					
22.	Does the company review entries to verify that correct classifications were used?					
23.	Does the company monitor the entry review process to verify that controls were followed?					
24.	Are exporters required to print the HTSUS numbers provided by the company on invoices and/or packing lists?					
25.	Does the individual reviewing merchandise have adequate knowledge and training on AGOA issues?					
	Broker Oversight					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
26.	Are HTSUS Classifications for AGOA maintained in a database that is provided to brokers?					
27.	Are brokers required to have written company approval to make classification changes?					
28.	Does the company provide adequate broker oversight?					
29.	Does the company identify, analyze, and manage risks related to AGOA?					
30.	Has the company identified any risks related to AGOA and implemented control mechanisms?					
31.	Does the company have internal control to address specific issues identified in the profile?					
32.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

QUANTITY
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 QUANTITY GUIDANCE 2

2.1 EXAMPLES OF RED FLAGS 2
2.2 EXAMPLES OF BEST PRACTICES.....3
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 4

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE 4

3.1 RISK 4
A. Preliminary Assessment of Risk.....4
B. Evaluation of Risk Acceptability 4
3.2 INTERNAL CONTROL.....5
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 6
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....6
3.5 EXAMPLES.....7

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - QUANTITY 9

QUANTITY
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

NOTE: An extensive review of internal control for quantity should be conducted when some specific risk exists related to quantity. For example, when specific or compound duty rates are based on quantity then quantity may represent a risk that should be addressed. Quantity may be a risk area for imports of petroleum, footwear, alcoholic beverages, watches, commodities subject to quota, and others. If the audit discloses significant unacceptable practices related to quantity, such as routinely declaring numbers of containers rather than number of units, these unacceptable practices should be addressed by the PAS team working with the company in the most efficient, effective manner.

PART 1 BACKGROUND

The objective of this document is to provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for Quantity and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and the terms in this document are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

PART 2 QUANTITY GUIDANCE

Title 19 U.S.C. 1484(f) states that all import entries shall include an accurate statement specifying the quantities of all merchandise imported and the value of the total quantity of each kind of article. This is also required in General Statistical Note 1(a)(xii) to the HTSUS, 19 CFR 141.61(e), and Customs Directive 099-3550-061 (Instructions for Preparation of the CF 7501).

Title 19 CFR 141.86(a)(4) states that each invoice of imported merchandise shall set forth the quantities in the weights and measures of the country or place from which the merchandise is shipped, or in the weights and measures of the United States.

Title 19 CFR 142.6(a)(2) requires the commercial invoice or other acceptable documentation contain the quantities of the merchandise.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem with Quantity.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring correct quantity for Customs purposes. Examples:
  - ✓ Company does not monitor or interact with the broker on quantity issues.
  - ✓ Company relies on one employee to handle quantity issues, and there are poor or no management checks or balances over this employee.
- Company import staff lacks knowledge of quantity issues.

- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.
- Significant variance exists between the importer's data and Customs data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with quantity (e.g., steel kilogram vs. tonnage issue).
- Company imports merchandise subject to restrictions including specific or compound duty rates, admissibility issues, or quota/visa.
- Quantities reported on the invoice, entry, packing slip, and receiving report do not match.
- The company has no receiving reports or documentation of quantities received (parts shipped to Quality Assurance Dept. and not counted).
- Quantity documents report different units of measure than required by Customs (lbs. vs. kg. , carton vs. cases).
- Company has numerous drop shipments for which quantities cannot be verified (shipment directly to the customer).
- The receiving department has authority to override quantity variances between actual receipt and the packing list or other shipping documents.
- The company uses overseas vendor count for quantities received.
- Special handling requirements prohibit accurate count (e.g. silicon wafers require "clean area").
- Merchandise changes quantity because of expansion/contraction of commodities (e.g. petroleum, resins/polymers).

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls over Quantity:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the import department, including correct imported quantity. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- Internal control procedures assign quantity verification duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about quantity matters.
- Company conducts and documents periodic reviews of quantity, and uses the results to make corrections to entries and changes to their import operations as appropriate.
- Company has appropriate controls in place to monitor quantities of merchandise entered under specific or compound duty rates, quota/visa, or other admissibility issues.
- Company has a system to verify quantities reported on the invoice, entry, packing slip, and receiving report, and generates a discrepancy report.
- Quantity discrepancies are recorded in a log and reported to Customs.
- Company has table of conversions for units of measure as required by Customs.
- Override of quantity variances by the receiving department requires authorization by appropriate personnel.
- Company reviews overseas vendor count for quantities received.
- Company uses industry standards for expansion/contraction of commodities (e.g. petroleum, resins/polymers).

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures for ensuring proper reporting of quantities entered under specific or compound duty rates, quota/visa, or other admissibility issues.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to quantity.
- Company's documentation that supports monitoring and verification of established and/or written internal control for quantity such as:
  - ✓ CF 7501 Entry Summary document.
  - ✓ CF 214 if applicable.
  - ✓ Commercial invoice with additional information affecting admissibility.
  - ✓ Bill of lading, packing slip, in-bond documents, and receiving reports.
  - ✓ Purchase Order, contracts or agreements.
  - ✓ Quantity discrepancy reports.
  - ✓ Gauge Report for commodities (e.g. petroleum, resins/polymers).

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company 's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.
   - Monitoring.

2. Review relevant Customs and company documents to identify and understand relevant internal control over quantity. (Examples of documents and information to review are listed on prior pages.)

3. Determine whether the company established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence (such as a log) of communication with the broker and company departments on quantity issues. This includes company testing of broker operations and verification that the broker followed company instructions.
   - Documentary evidence of inter-company communications to ensure correct quantity information is provided to Customs.
   - Training records and materials relating to quantity are used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for Quantity in PART 4 of this document.

   Note: The internal control assessment should include Steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over reporting correct quantity.

1. Complete the WEIC for Quantity to determine whether risk is acceptable or unacceptable and document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.
   Customs considers risk unacceptable when testing reveals that internal control is not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will assist the PAS team in determining if conditions warrant proceeding to ACT.

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and

- The result of review indicated that the quantity error was due to an isolated incident.
- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

Proceed to ACT if:

- The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS *are for clarification purposes only*.

Example A: Situation in which the team would not proceed to ACT (Revenue)

Company A imports textiles subject to quota/visa requirements from a related party located in Hong Kong. The company did not have written internal control procedures for quantity. The receiving department was not aware of any Customs requirements to report quantity variances to the Import department. The company relied on the quantity stated on the invoice/packing list from overseas vendors and did not perform a physical count. A review of the receiving records revealed that the importer received more than the quantity declared to Customs. This discrepancy resulted in a loss of duty. ACS data showed only two previous entries from this vendor with an insignificant value amount. During the review, the company paid the duty and established written internal control procedures to verify quantity received. The PAS team was able to verify that the procedures were effective, therefore, there was no need to proceed to ACT.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same as Situation A, except that after further review, it was determined that the errors were systemic but the importer agreed to develop and implement a compliance improvement plan within two months. Therefore, there was no need to proceed to ACT.

Example C: Situation in which the team would proceed to ACT (Revenue)

Company C imports steel from Lithuania. Steel is sold in tons. The tonnage must be converted to kilograms (kilos) in order to make entry, since duty is assessed on kilos instead of tons. The conversion from tons to kilos made by the company was not verified for accuracy. The conversions were not followed as prescribed in their operations handbook. This resulted in a major understatement of weight for the steel and the proper duty was not paid. After further review, we found problems with the methodology of the formula calculation for conversions. Since the company was unwilling to quantify loss of revenue, the team proceeded to ACT

Example D: Situation in which the team would proceed to ACT (Compliance)

Same as Situation C except that the company refused to establish internal control procedures to ensure that the correct quantity is reported to Customs. Therefore, the team proceeds to the ACT process.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) - QUANTITY

PURPOSE: To determine whether Quantity risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls over quantity formally documented?					
2.	Are written policies and procedures for quantity for specific or compound duty rates, quota/visa, or other admissibility issues approved by management?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Do written internal control procedures assign responsibility for quantity to a position rather than an individual?					
5.	Does the company have good interdepartmental communication concerning quantity issues?					
6.	Is only one department/individual primarily responsible for assuring compliance with quantity requirements?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does the individual overseeing quantity compliance have adequate knowledge and training and the authority to ensure that internal control procedures for quantity are established and followed by all company departments?					
8.	Are internal controls over quantity periodically tested?					
9.	Were the results of the periodic internal control tests documented?					
10.	If weaknesses were found during internal control testing, were corrective actions implemented?					
11.	Does the company use conversions for units of measure as required by Customs?					
12.	Is the quantity variance override authority limited to appropriate personnel?					
13.	Does the company count quantities received and make a record of such counts and discrepancies?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
14.	Are receiving reports retained and readily available?					
15.	Are receiving reports readily traceable to entry summaries?					
16.	Is broker notified of quantity variances in order to amend Customs entry summary information?					
17.	Does the company have internal control procedures to address specific issues identified in the profile?					
18.	Does the company have written procedures to take corrective actions as necessary?					
19.	Does company provide adequate broker oversight?					
20.	Does the company identify, analyze, and mange risks related to quantity?					
21.	Has the company identified any risks related to classification and implemented control mechnisms?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
22.	Does the company have internal control to address specific issues identified in the profile?					
23.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	**Yes or No**
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	**Yes or No**	**Comments**
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

RECONCILIATION
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 RECONCILIATION GUIDANCE.....2

2.1 EXAMPLES OF RED FLAGS 4
2.2 EXAMPLES OF BEST PRACTICES.....5
2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....6

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....6

3.1 RISK 7
A. Preliminary Assessment of Risk.....7
B. Evaluation of Risk Acceptability 7
3.2 INTERNAL CONTROL.....7
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 8
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....9
3.5 EXAMPLES.....10

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – RECONCILIATION.....13

RECONCILIATION
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

PART 1 BACKGROUND

The purpose of this document is to provide guidance in performing a PAS of the company's internal control for the Automated Commercial System (ACS) Reconciliation Prototype procedures.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and the terms in this technical guide are based on the *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

PART 2 RECONCILIATION GUIDANCE

Title VI of the North American Free Trade Agreement Implement Act (NAFTA) contains provisions pertaining to Customs Modernization. Subtitle B of Title VI establishes the National Customs Automation Program (NCAP), which is an automated and electronic system for processing commercial importations. 19 CFR Section 101.9(b) provides to Customs the authority to develop an experimental procedure to streamline commercial importations. The ACS Reconciliation Prototype is a test established pursuant to these regulations. Any party who elects to reconcile entries pursuant to 19 U.S.C. Section 1484(b) must do so through this prototype.

The ACS Reconciliation Prototype procedures were published in the Federal Register dated February 6, 1998 under the title "Revised National Customs Automation Program Test Regarding Reconciliation." They were also published in Customs Bulletin and Decisions Vol. 32, No. 7", dated February 18, 1998. The ACS Reconciliation Prototype Operations Guide, Version 2.0 was published in February 2000. The extension of the Reconciliation Prototype was announced in the Federal Register, dated September 7, 2000.

Reconciliation is the process by which an importer notifies Customs of undeterminable information for post-entry adjustment, and by which the outstanding information is provided to Customs at a later date. Under Reconciliation, the importer is not disclosing a violation, but rather identifying information that is undeterminable and will be provided at a later date. Auditors should be aware of the distinction between a prior disclosure and a Reconciliation entry. A prior disclosure exists when a person concerned discloses the circumstances of a violation pursuant to the Customs Regulations. The person disclosing this information must do so before, or without knowledge of a formal investigation of that violation.

Reconciliation includes entry types for Consumption with entry codes "01", "02 and "06". Type "06" (Consumption - Foreign Trade Zone) entries are allowed only when no Antidumping/Countervailing duty merchandise is included. In addition, if an FTZ entry has NAFTA issues, the importer must ensure that the product underwent no additional processing to make it qualify for NAFTA. The product must have qualified for NAFTA in the same condition as it entered the FTZ.

The importers also retain the right to request extension of liquidation of entry summaries as outlined in 19 CFR 159.12(a)(ii).

Invaluable information is contained in the ACS Reconciliation Prototype Handbook Version 3.0 published March 02, 2002 that is available on the Customs web site at www.Customs.gov/recon.

The ACS Reconciliation Prototype will allow only the following issues to be flagged for Reconciliation.

1. Value – all value issues.
2. HTSUS heading 9802 – The issue is limited to value – e.g., reconciling the estimated to actual costs.
3. NAFTA – NAFTA eligibility can be established after entry by flagging the entry summary for NAFTA. Reconciliations are subject to the obligations of a valid Certificate of Origin at the time of making a NAFTA claim. Presentation of the NAFTA Certificate of Origin is waived for the purposes of this prototype, but the filer must retain this document, which shall be provided to Customs upon request.
4. Classification – Classification issues will be eligible for Reconciliation only when issues have been formally established as the subject of a pending administrative ruling (including pre-classification rulings), protest, or court action.

The underlying entries may be filed at any appropriate port; however, the Reconciliation and supporting documentation must be timely filed to the importer's assigned port. For purposes of the Reconciliation filing at the processing port, the broker permit requirements are waived. If a Reconciliation claim is not filed by the appropriate deadline and at the appropriate port, it will be handled as a liquidated damage claim for "no file."

One surety (signed bond rider) and one continuous bond must cover all underlying entries subject to Reconciliation. Termination of the continuous bond either by Customs, the bond principal, or surety will result in the deactivation of the Reconciliation and additions of further underlying entries until the company notifies Reconciliation Headquarters Officials of the change in bond status.

The importer must submit a "Notice of Intent" which identifies an undeterminable issue that would be resolved by the Reconciliation procedures. The liability for the identified issue is transferred to the Reconciliation, which permits the liquidation of the underlying entry summary as to all issues other than those that are transferred to the Reconciliation. The importer remains responsible for filing Reconciliation entries and remains liable for any duties, taxes, and fees resulting from the filing and/or liquidation of the Reconciliation. The importer may "flag" the underlying entry via ABI indicator, and this serves as the "Notice of Intent". If the importer has a majority of their entries flagged they may send in a "Notice of Intent" stating the period of coverage. Customs will automatically apply the blanket flag to all entry summaries filed by the importer during the specified time period.

The Reconciliation entry will have an entry type of "09" (Reconciliation). This entry must be submitted within 15 months of the date of oldest entry summary flagged for and grouped on the Reconciliation being filed. Transmission of a NAFTA Reconciliation must occur within 12 months of the date of importation of the oldest entry summary flagged for and grouped on the Reconciliation being filed.

Reconciliation entries can be filed on an entry by entry or aggregate basis.

Reconciliation entries may directly affect other audit issues (i.e. 9802).

One reconciliation entry can have as many as 9,999 underlying entries.

Even though an importer may flag up to four issues at once on a given entry summary, a maximum of two reconciliations may be filed covering the same entry summary.

If NAFTA has been flagged, it must be filed by itself.

Issues that are known at the time of entry such as freight and insurance are not reconcilable.

Issues of admissibility are not allowed.

Quantity is not a reconcilable issue since it directly affects admissibility.

An individual flag will override a blanket flag, canceling the blanket flag for that specific entry. Therefore, if an issue initially covered by the blanket flag is still to be reconciled it must be flagged again in the individual flag.

A reconciliation entry must be filed for every entry that is flagged even if there are no changes.

An importer must flag everything they plan to reconcile.

An importer cannot reconcile 9802 if the merchandise was entered during the period without claiming the 9802 provision.

Drawback cannot be claimed on underlying entries until the reconciliation has been filed.

2.1 EXAMPLES OF RED FLAGS

The following examples are conditions that may indicate a potential problem with Reconciliation entries.

- Company has insufficiently documented, poorly defined, or no internal control for accurately reporting Reconciliation entries to Customs. Examples:
  - ✓ Company does not monitor or interact with the broker on Reconciliation entries;
  - ✓ Company relies on one employee to handle ACS Reconciliation Prototype issues and there are poor or no management checks or balances over this employee.
- Company's staff lacks knowledge of the ACS Reconciliation Prototype requirements.
- Company offers an unreasonable explanation or lack of response to Customs inquiries regarding their Reconciliation entries and supporting documentation.
- Company fails to cooperate with or respond to Customs inquiries regarding their Reconciliation entries and supporting documentation.
- Company has a high turnover of employees in key positions.
- Significant variance exists between the importer's Reconciliation data and Customs underlying entry data that may be related to the company's management decision to delay duty payment because of cash flow problems and not related to post-entry issues.
- Customs (e.g., import specialist, account manager, compliance measurement, prior audit) shows history of problems with the company's submissions to Customs.
- Unreasonable changes in the company's import patterns that may impact the company's Reconciliation entries.
- Large refunds requested initially by the company (until Customs has an idea of the size of refunds from a particular company).
- Company cannot identify the underlying flagged entry summaries.
- Lack of audit trail to validate the inclusion of an underlying entry summary being reconciled.
- Reconciliation submissions are not filed timely.
- Historically, company filed annual reports for tooling and/or assists and now company has flagged entries for other value adjustments.
- The company consistently files prior disclosures on Reconciliation entries.
- The company does not have procedures designed to ensure the identification of all flagged entries.
- The company has received numerous no-file penalties for not filing Reconciliations.
- The company has not been given authority to file Reconciliation entries.
- The company nets increases and decreases in the Reconciliation final adjustments.

- The company's Reconciliation submissions include issues not allowed under the Reconciliation prototype (outlined above).
- Analysis of Reconciliation entries shows an unreasonable variance from previous Reconciliation entries or other support documentation.
- Analysis of the Reconciliation entries shows inaccurate supporting documentation.
- The company always files no-change Reconciliation entries; if so, may not need to participate in Reconciliation as there is no undeterminable issue that would be resolved by the Reconciliation prototype procedures.
- The company cannot provide verification of reconciled amounts.
- The company's procedures appear inadequate or inaccurate to ensure that all required information is collected for the underlying entries and are included in the Reconciliation submission. For example, that all proceeds from the sale of imported merchandise that are dutiable on the underlying entries are included in the Reconciliation entry.
- NAFTA Reconciliation entries are rejected by Customs.
- The company, Customs or the surety has terminated the importers continuous bond.
- The company files drawback on the underlying entries before the Reconciliation is accepted by Customs
- The company uses the Reconciliation entry information on their subsequent drawback claims.
- The company is submitting disclosures to Customs on issues that should be included in the Reconciliation summary.
- Review of the company's response to the questionnaire indicates an issue that would require post-entry adjustments but the company is not filing disclosures or Reconciliations. For example, the company has dutiable proceeds that are not known at time of original entry, however, no Reconciliation entry or disclosure was submitted to Customs.
- Imports are under consignments.
- Company has multiple brokers filing reconciliation entries.

2.2 EXAMPLES OF BEST PRACTICES

- Internal controls to ensure that Reconciliations submitted to Customs are accurate and complete:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Were monitored by management.
- One manager is ultimately responsible for control of the import department, including oversight of Reconciliation procedures and submissions. That manager has knowledge of Customs matters and the authority to assure internal control procedures for imports are established and followed by all company departments.
- Written internal control procedures assign duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about Customs matters.
- Company requests binding rulings and consults with Customs import specialists to ensure submitted Reconcilations are in compliance with Customs regulations.
- Company conducts and documents periodic reviews of entry summaries and makes corrections to entries and changes to their import operations as appropriate.
- Company requires their vendors to provide all appropriate information regarding the required post-entry adjustments listed on the Reconciliation.

- Company requires periodic training for staff responsible for Customs matters.
- The company's Import Department staff attends Customs seminars on Reconciliation and other informed compliance outreach programs.
- Company provides Reconciliation training to its agents and brokers.
- Company maintains a software application that tracks the underlying entry information and ensures all underlying entry adjustments are supported.
- Company performs a periodic review to ensure the status of its continuous bond and takes appropriate action if the bond is terminated and another bond is instated.

2.3 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- Company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to Reconciliation procedures.
- Company's documentation that supports monitoring and verification of established and/or written internal control for the Reconciliation procedures.
- Process map flowchart and narrative.
- Directives and rulings from Office of Regulations and Rules regarding implementation of the ACS prototype for Reconciliation.
- Documentation sustaining the Reconciliations entry calculations that adjusts the underlying entries, such as:
  - ✓ Underlying entry and invoice,
  - ✓ Payment verification of imported merchandise,
  - ✓ Reconciliation entry package,
  - ✓ Documents and schedules linking the Reconciliation with underlying entries,
  - ✓ Applicable documentation that formally established the basis for flagging for a classification issue (protests, rulings, etc.),
  - ✓ NAFTA certificate of origin,

  - ✓ Accounting records that substantiate the Reconciliation issues including the financial statements, post-closing trial balance, detailed chart of accounts, and general ledger detail,
  - ✓ Data Loading Sheet, and
  - ✓ General ledger accounts likely to contain undeclared payments and general ledger detail for those accounts (i.e. description, vendor name, amounts, and credit memos)
- CF-28s (Request for Information), CF-29 (Notice of Action) and other Customs communications with company regarding the Reconciliation entry and the underlying entries.

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company 's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment
   - Risk Assessment
   - Control Activities
   - Information and Communication
   - Monitoring

2. Review relevant Customs and company documents to identify and understand internal control over ACS Reconciliation Prototype procedures. (Examples of documents and information to review are listed on prior page.)

3. Determine whether the company established and follows procedures. Review:

- Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
- Documentary evidence of communication with the broker and company departments on ACS Reconciliation Prototype issues, including company testing of broker operations and verification that the broker followed company instructions.
- Company-specific rulings and evidence that they are followed.
- Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
- Training records and materials used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the "Worksheet for Evaluating Internal Control over ACS Reconciliation Prototype Procedures."

   Note: The internal control assessment should include Steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas within Reconciliation. For example, the company may use Reconciliation for imports from several foreign companies but testing may be necessary only for the underlying entry transactions for certain vendors.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*

Column titled “Testing Limit” reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of a company’s controls over Reconciliation submissions.

1. Complete the “Worksheet for Evaluating Internal Control over ACS Reconciliation Prototype Procedures” to determine whether risk determination is acceptable or unacceptable and to document why. Put results of the Reconciliation testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

   Customs considers risk unacceptable when testing reveals that internal control is not sufficient or effective in providing reasonable assurance that accurate, timely and complete declarations are reported to Customs.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT.

   <u>Do not proceed to ACT if:</u>
   - Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   <u>Proceed to ACT if:</u>
   - The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the loss of revenue.
   - The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

   Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under PAS are for clarification purposes only.

Example A: Situation in which the team would not proceed to ACT (Revenue)

To determine whether Reconciliation controls were working the PAS team:

- ✓ Reviewed the profile and questionnaire,
- ✓ Reviewed written procedures, process map narrative and flowchart, and other documents,
- ✓ Concludes that the preliminary risk exposure was low.

The company's internal control manual required the import manager to maintain a record of all underlying entries for the blanket application period. The company indicated that the post-entry adjustment consisted of payments for subsequent proceeds to four foreign vendors. The amount of the proceeds is calculated at 10% of the resale price.

The internal control procedures show how the Import Department calculates these post-entry adjustments to be included in the six-month Reconciliation entry. Every six-months the Import Department is provided a report from the sales department stating the quantity of each of the relevant items sold each month and the standard sale prices for the period. The Import Department calculates the proceeds amount as the percentage of the sale value as listed in the agreement and total standard sale prices (standard sale price x quantity sold). The team concluded the internal control system related to the Reconciliation procedures were moderate because there was no indication of how the standard sale price was established in the company's documentation. There were no procedures in place to adjust the amounts from the calculation using standard price to the actual proceeds paid to the vendors.

Using the table above (based on low risk exposure and moderate preliminary internal control evaluation), the team concluded that they would test 10 sale invoices of the items to determine whether the items were sold at the standard price. The team determined that 4 of the 10 invoices were sold at higher then the annual standard price and 2 were sold below the standard price.

In discussion with the sales department regarding these discrepancies, it was determined that each salesman has the authority to negotiate each sale and to adjust the standard price according to quantity sold, inventory excess or shortage, and other valid business concerns. The standard price list given to the Import Department is a computer-generated calculation showing the average selling price of each item for the prior month. As each sales invoice is entered into the system, the standard sales price is automatically adjusted to reflect the average sales price for each of the items sold. Even though the company uses a price list, the amounts listed in the computer file are based on the actual sales prices as negotiated by the sales department personnel.

The PAS review determined that the Import Department has online access to the sales price list as described above even though the internal control procedures indicate that they get a semi-annual sale price list, which was provided to the PAS team. At time of the post-entry adjustment, the Import Department determines the post-entry adjustment amount by searching for the imported item in the sale price computer file that shows the average sale price. They calculate the post-entry adjustment as:

- Average sale price per unit x imported quantity from the foreign vendor x percentage of proceeds listed in the vendor agreements.

This calculation is also outlined in the vendor agreements and is used by the accounting department to determine the actual proceed payments to the vendors.

As a result of this review, the PAS team informed the Import Department that the internal control procedures did not reflect the actual procedures they used to calculate the proceeds amounts. The Import Department provided the PAS team with an update of the internal control procedures showing their actual calculations of the proceed amount. The PAS team determined that they do not need to proceed to an ACT as the Reconciliation entries would accurately reflect the required post-entry adjustment to the company's underlying entries regarding proceeds paid to a foreign vendor.

Example B: Situation in which the team would not proceed to ACT (Compliance)

An importer submits 9802 entries to Customs from a wholly owned vendor in Mexico. The products are assembled in Mexico and returned to the importer with the reported standard costs determined by the importer annually. The questionnaire shows that 99.9% of the assembled products at the plant in Mexico are returned to the importer. Every six months the importer submits a blanket Reconciliation entry for the post-entry adjustment that converts the standard costs to the actual costs of the imported items. The Import Department calculates these post-entry adjustments based on accounting records showing the total amount paid for the imported items from the assembly plant and the total value reported to Customs on the underlying entries.

To determine whether these controls were working, the PAS team:

- ✓ Interviewed the company’s import Department personnel,
- ✓ Performed a macro test on two post-entry adjustments.

The PAS team determined that the preliminary internal control review indicated moderate risk. The 10 invoices should be traced to the post-entry adjustment to determine whether the adjustment accurately reflected the conversion of standard to actual cost.

The PAS team reviewed the accounting system to determine how the standard costs were established and how the differences between the standard and actual are recorded in the accounting system. The review determined that the adjustments were made in compliance with Generally Accepted Accounting Principles (GAAP). The PAS review also verified that these appropriate adjustments were used to create the post-entry adjustments on the company's underlying entries. The PAS review of the 10 entries indicated that all 10 were included in the 6-month accurate post-entry adjustments submitted to Customs on the blanket Reconciliation entry. The PAS team determined that they do not need to proceed to the ACT phase, as the Reconciliation entries would accurately reflect the required post-entry adjustment to the company's underlying entries.

Example C: Situation in which the team would proceed to ACT (Revenue)

Same situation as above in Example A, however, the Import Department did not have access to the actual sale price file. They were provided a yearly price list based on standard sales price, which was the December 31 average sale price. December was a slow period and the salesmen were providing deep discounts to their customers due to high inventory and overall unstable economic conditions. Additionally, the Import Department was not aware of the negotiation authority of each salesman. Based on this preliminary review, the team determined 10 entries should be reviewed.

The PAS team was provided a copy of the proceeds agreements between the company and the four foreign vendors. The agreements include provisions on the calculation of the proceeds amount. The proceeds calculation is the same as listed above, with the specification that the computer sale price file showing the average sale price for the item would be the average sale price for date of the sale invoice for the item.

The PAS team recalculated the 10 entry invoices based on the agreements and found that six of the entries showed lower proceeds amounts than the company paid to the vendor.

The PAS team discussed the issue with the company representative the requirement for the actual proceeds payments to be included in the Reconciliation entries. The company management reviewed the internal control of the company and reviewed the procedure that the Import Department received the annual sale price list. They informed the Import Department that they were in compliance with the internal control procedures therefore there was no need for additional information. The sales department management considers the database as an internal and confidential record of the sales department and it was not available to the Import Department.

Since the company will not change its internal control to allow the Import Department to use actual proceed payments in their post-entry adjustments on the Reconciliation and the level of compliance is unknown, the PAS team proceeds to ACT to use statistical sampling to project the revenue loss.

Example D: Situation where the team would proceed to ACT (Compliance)

Same situation as above in Example B, however, the accounting department received a weekly statement from the Mexican assembler showing the operating costs that should be paid the following week. The accounting department sends a check to the assembler to cover these costs, which include labor, direct and indirect material costs. The payment from the US parent company is deposited in the assembler cash account and the assembler uses this cash account to fund payroll and various other account payable transactions of the assembling plant related to the assembly process.

The PAS team discussions with the Import Department indicates they were unaware of the accounting department's weekly payment. They indicated that the invoices from the assembler for the imported merchandise were sent to the accounting department for payment. They referred to the above limited review. The Import Department told the auditors that during the Reconciliation period, they received the accounts payable report showing the list of invoices and the amounts paid to the assembler. The Import Department used this report to calculate the post-entry adjustments listed on the Reconciliation entry. The weekly cash payments made by the accounting department to the assembler were not reflected in the Reconciliation entry.

The PAS team discussed the issue with the accounting personal who made the weekly payments. They stated that the payments were not related to any importation and was not within the scope of the Customs review. To prove their point, the accounting department provided to the PAS team the weekly request from the assembler showing that the payments were for manufacturing costs and not related to the assembler invoices for the assembler cost on 9802 merchandise. The PAS team asked the company's Customs Department to provide to them a list of all of the weekly payments to the assembler. The accounting department again refused to provide the list as they considered the information outside the scope of the PAS review.

The PAS team will proceed to ACT to quantify the amount of money that was paid to the assembler that was not reported on the underlying entries or the Reconciliation entry.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – RECONCILIATION

PURPOSE: To determine whether Reconciliation risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	Overall Control					
1.	Are internal controls for Reconciliation procedures formally documented?					
2.	Are written policies and procedures approved by management?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager responsible for control of the import department, including Reconciliation?					
5.	Does that manager have knowledge of Customs matters and the authority to ensure internal control procedures for imports are established and followed by all company departments?					
6.	Do written internal control procedures assign Reconciliation tasks to a position rather than a person?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does the company have good interdepartmental communication regarding the post-entry adjustments that must be submitted to Customs on the Reconciliation entry?					
8.	Does the company conduct and document periodic reviews of Reconciliation entries?					
9.	Do internal controls involve a verification process to determine that the post-entry adjustments are qualified for Reconciliation procedures?					
10.	Do written procedures appear adequate?					
11.	Are the records necessary to test the reconciliation entries readily available?					
12.	Do purchasing, engineering, other departments and suppliers provide adequate information to the Customs Department and/or broker to ensure the correct post-entry adjustments are listed on the Reconciliation entries?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
13.	Does the importer maintain a database or table listing the underlying entries to ensure that all entries with necessary post-entry adjustments are included in the Reconciliation entries?					
14.	Does the company perform an annual review of the post-entry changes listed in the Reconciliation entries?					
15.	Is responsibility for the reconciliation eligibility process assigned to one knowledgeable individual or department with management oversight?					
	Entry Review					
16.	Does the company review entries to verify that the Reconciliation entries are correct?					
17.	Does the company monitor the entry review process to verify that the internal controls are followed?					
18.	Does the individual reviewing the Reconciliation entries have adequate knowledge and training of ACS Reconciliation Prototype procedures?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
	Broker Review					
19.	Does the company monitor the Reconciliation entries that the broker submits to Customs?					
20.	Do procedures ensure that the broker has all information required for the post-entry adjustments listed on the Reconciliation entries?					
21.	Does the company have adequate broker oversight?					
22.	Does the company identify, analyze, and manage risks related to reconciliation?					
23.	Has the company identified any risks related to reconciliation and implemented control mechanisms?					
24.	Does the company have adequate internal control to address specific issues identified in the profile?					
25.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

INTELLECTUAL PROPERTY RIGHTS
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1 BACKGROUND.....2

PART 2 IPR GUIDANCE.....2

2.1 TRADEMARKS AND TRADE NAMES.....2
2.2 COPYRIGHT.....3
2.3 EXCLUSION ORDERS.....4
2.4 PATENTS.....4
2.5 MASK WORK.....4
2.6 EXAMPLES OF RED FLAGS.....5
A. Red Flags for All IPR.....5
B. Red Flags for Importers that may Manufacturer Goods of IPR Merchandise.....6
C. Red Flags for Importers that are Distributors/Wholesalers/Mass Marketers of IPR Merchandise.....6
2.7 EXAMPLES OF BEST PRACTICES.....6
2.8 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW.....7

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE.....7

3.1 RISK.....8
A. Preliminary Assessment of Risk.....8
B. Evaluation of Risk Acceptability.....8
3.2 INTERNAL CONTROL.....8
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT).....9
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS.....10
3.5 EXAMPLES.....11

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – INTELLECTUAL PROPERTY RIGHTS (IPR).....12

INTELLECTUAL PROPERTY RIGHTS (IPR)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

Note: This technical guide should be used where the importer may be subject to Intellectual Property Right (IPR) issues. Identifying potential IPR issues will require additional analysis such as profile information, port information, past enforcement action, or other means that indicate a past history of receipts subject to IPR. Unlike other parts of the PAS the scope and sampling should be performed on entries of current shipments where there is physical inventory to be viewed for verification of IPR

PART 1 BACKGROUND

The purpose of this document is to provide guidance for performing a PAS of the company's internal control for IPR and evaluating the results.

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this document are based on *Assessing Internal Controls in Performance Audits,* GAO/OP- 4.1.4 - published by the United States General Accounting Office, Office of Policy, September 1990, and the American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78.*

PART 2 IPR GUIDANCE

Intellectual property is the tangible product of a person's intellect or creativity. Literary works, musical scores, computer programs, paintings and drawings are a few examples of intellectual property. Depending on the nature of the intellectual property, the owner of that property may protect it from being exploited by others by registering it with the U.S. Copyright Office or the U.S. Patent and Trademark office. U.S. Customs and Border Protection (Customs) has the responsibility for halting the importation of merchandise which violated trade names, registered trademarks, and copyrights when their owners have sought protections by recording their rights with Customs. Customs also enforces exclusion orders issued by the International Trade Commission (ITC).

In most cases importation of genuine articles without consent of the IPR owner is permissible. It is only in the case of certain trademarked items that the mark owner's consent is required for imports. Any IPR work by RAD must be coordinated closely with the Office of Field Operations and the Office of Regulations and Rulings.

Listed below are summaries of each of the IPR protected by Customs.

2.1 TRADEMARKS AND TRADE NAMES

Customs has the authority to exclude articles bearing copying or simulating trademarks and trade names, and certain restricted gray market goods. To obtain protection against such importations, the trademark holder must register the trademark with the U.S. Patent & Trademark Office *and* request Customs to collect and retain information related to the trademark holder's rights for a specific time. Customs monitors imports to prevent the importation of violating articles based on the trademark-holder's request or on Customs

initiative. To receive protection against imports of articles bearing a copying or simulating trade name, the trade name holder must record the trade name with Customs.

19 CFR §§ 133.1 – 133.7 establishes the authority for registered trademarks to be recorded with Customs.

19 CFR § 133.11 – 133.15 establishes the authority for the trade names to be recorded with Customs.

19 CFR § 133.21 establishes the authority for Customs to seize imported articles bearing counterfeit trademarks.

19 CFR § 133.22 establishes the authority of the port director to detain articles bearing a mark or name copying or simulating a recorded mark or name.

19 CFR § 133.23 restricts the importation of "gray market articles". Gray market articles are foreign-made articles bearing a genuine trademark or trade name identical with or substantially indistinguishable from one owned and recorded by a citizen of the United States. Or a corporation or association created or organized within the United States and imported without the authorization of the United States owner.

19 CFR § 133.24 establishes the restrictions on articles accompanying importer and mail imports. However, 19 CFR § 148.55 provides that a person arriving in the United States may import one article of a type bearing an unauthorized protected trademark.

19 CFR § 133.25 establishes the procedures for the detention of articles that possibly violate trademark owner rights.

19 CFR § 133.26 establishes the authority for the port director to demand the redelivery of the articles that violated a copyright owner's interest. If the articles are not redelivered to Customs, a claim of liquidated damages is made in accordance with § 141.113(h) of this chapter.

19 CFR § 133.27 establishes that Customs can file civil fines for those involved in the importation of counterfeit trademark goods.

2.2 COPYRIGHT

In general, a copyright protects original works of authorship, including written music, computer programs, video games, toy designs and the intellectual creations against unauthorized reproductions, derivations, distribution or display. This protection is available to both published and unpublished works. To provide protections against the importation of infringing copies, Customs offers copyright owners an enforcement option. Claims to copyright which have been registered in accordance with the Copyright Act of July 30, 1947, as amended, or the Copyright Act of 1976, as amended, may be recorded with Customs for import protection.

19 CFR §§ 133.31 – 133.37 establishes the authority for the copyright recordation with Customs.

19 CFR § 133.42 establishes the authority for Customs to seize imported articles that are infringing copies or records of works copyrighted in the United States.

19 CFR § 133.43 establishes the procedures for detention of imported articles that possibly violate the copyright owner rights and review of the status of the articles.

19 CFR § 133.44 establishes the authority of the port director to seize the imported article and institute forfeiture proceedings in accordance with part 162 of this chapter.

19 CFR § 133.46 establishes the authority for the port director to demand the redelivery of the articles that are subject to the restrictions or prohibitions relating to copyrighted articles. If the articles are not redelivered to Customs, a claim for liquidated damages shall be made in accordance with § 141.113(h) of this chapter.

2.3 EXCLUSION ORDERS

Under Section 337 of the Tariff Act of 1930, as amended, unfair methods of competition and unfair practices in the importation or sale of articles, the effect or tendency of which is to destroy, substantially injure, or prevent the establishment of an efficiently and economically operated in U.S. industry, or to restrain or monopolize trade and commerce in the United States, are unlawful.

19 CFR § 12.39 authorizes the procedures to restrict imported articles involving unfair methods or competition or practices. The regulation establishes procedures for the enforcement of exclusion orders and seizure and forfeiture orders of the U. S. International Trade Commission (ITC) pursuant to 19 U.S.C. 1337, which prohibits unfair methods of competition in the import trade. The ITC completes an investigation of an alleged violation to determine if the section has been violated. The Exclusion Orders are sent to the President for his final judgment to enforce the Exclusion Order. The approved Exclusion Orders are issued and administrated by the Office of Rules and Regulations, IPR Branch, but are processed by the Office of Field Operations. Once goods have been denied entry pursuant to an exclusion order, the ITC can issue a seizure and forfeiture order directing Customs to seize and forfeit future importations of the same goods by the same importer.

2.4 PATENTS

A patent is a legal monopoly, granted by the U.S. Government, which secures to an inventor for a term of years the exclusive right to make, use, or sell his invention. U.S. Custom's patent enforcement is more limited than the trademark and copyright importation restrictions.

Customs role in enforcing patent infringement has been limited to the enforcement of certain court orders and conducting Patent Import Surveys under 19 CFR §12.39a. Patent Import Surveys are requested through the Office of Regulations & Rules, Intellectual Property Rights (IPR) Branch. When the owner of a patent registered in the United States believes that merchandise is being imported into the United States, which infringes the patent, an application for a survey to assist the patent owner in taking appropriate action may be filed. In order to assist the patent owner, Customs will, for a fee, undertake to monitor importations on a nationwide basis and report to the patent holder, the names and addresses of importers who have imported goods, which appear to infringe upon a particular patent. Regulatory Audit does not become involved in Patent Import Surveys but this information is provided for information and background purposes.

2.5 MASK WORK

19 CFR §12.39(e) mandates that, in compliance with the Semiconductor Chip Protection Act of 1984, if the owner of a mask work registered in the copyright office seeks to have Customs deny entry to any imported semiconductor chip products which infringe on his rights, the owner must obtain a court order enjoining, or an order of the U.S. International Trade Commission (USITC) to cease the importation of such products.

The exclusion orders approved by the ITC and the President are published in the Federal Register and are available at the web address http://www.access.gpo.gov/su_docs/fedreg/frcont01.html. This site groups the Federal Register notices by agency and shows the International Trade Commission publication of all importation restriction orders for each day.

2.6 EXAMPLES OF RED FLAGS

The following examples of red flags (conditions that may indicate a potential IPR problem) are broken down into three categories: red flags for all IPR, red flags for importers that may manufacture goods of IPR merchandise and red flags for importers that are distributors/wholesalers/mass marketers of IPR merchandise.

A. Red Flags for All IPR

- The company has insufficiently documented, poorly defined, or no internal control for prevention of importation of IPR protected merchandise. Examples:
  - ✓ The company does not monitor or interact with the broker on IPR issues.
  - ✓ The company relies on one employee to handle transactions where IPR issues could occur, and there are poor or no management checks or balances over this employee.
- The company does not exercise adequate control over their agents (buying/selling) regarding IPR.
- The company's import staff lacks knowledge of IPR issues.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.
- Customs (e.g., import specialist, account manager, compliance measurements, prior audit, other Customs information) shows a history of problems with IPR merchandise.
- Company imports merchandise that has a readily recognizable trade name, i.e. Disney, Coca-Cola, Tommy Hilfiger, Nike, but the importer does not have a royalty agreement or a license agreement with the trademark's owner.
- The company's records, i.e. purchase orders, invoices, have an IPR identifier in the merchandise description but the company does not maintain a license agreement or a royalty agreement with the IPR's owner or pays no royalties.
- Company is not aware of dutiability of royalty fees
- Profile indicates specific exporters known to have produced counterfeit merchandise in the past are vendors for the importer.
- Importer has a history of enforcement actions for IPR violations.
- Merchandise shipped in small quantities on informal entries.
- Shipment originates from a source country with known IPR problems.
- Unusually vague invoices or invoices lacking model or catalogue numbers.
- Merchandise missing lot numbers, factory codes, expiration dates, dates of manufacture, or other national requirements.
- Merchandise is shipped c.o.d. rather than by letter of credit. (the risk of seizure of the good is borne by the exporter not the importer).
- Shipment is described in vague or unusual terms, such as articles of plastic, metal discs, samples, parts, molds, dies, etc.
- Shipment is declared at an unusually low or high value for the merchandise.
- Merchandise under-insured for goods of that type.
- Merchandise imported from a country not identified by the rights holder as a country where genuine goods are manufactured.

B. Red Flags for Importers that may Manufacture Goods of IPR Merchandise

- Merchandise shipped in small quantities on informal entries.
- Designer or brand merchandise shipped in bulk or component parts rather than in consumer packaging, such as designer perfumes or watches that are not generally shipped in bulk or in parts.
- Shipments of merchandise described as labels, patches, tags, imprinted boxes, or dies.
- Merchandise imported from a country not identified by the rights holder as a country where genuine goods are manufactured.
- Merchandise missing copyright or trademark notice, especially on well-known copyright works or well-known trademarks.

C. Red Flags for Importers that are Distributors/Wholesalers/Mass Marketers of IPR Merchandise

- Merchandise is of a commodity commonly counterfeited or pirated such as CDs and other media, sunglasses, watches, wearing apparel, handbags, toys, etc.
- Invoices with descriptions related to current “fad” items such as “alien doll”, “Mermaid”, or popular designers such as “Duck Logo”.
- Unusual product combinations such as collections of computer programs, video games, sound recordings when each component is a product of a different manufacturer, studio, or artist.
- Compact discs shipped on spindles and compact discs or cassettes not marked with the artist’s name or title of work.
- Compact discs, audiocassettes, or videocassettes, shipped as “blank” or “unfinished”.
- Merchandise fails to conform to country of origin marking requirements, weight designations, ingredient listings, electrical standards, consumer safety standards or other national requirements.
- Merchandise missing copyright or trademark notice, especially on well-known copyright works or well-known trademarks.
- Merchandise shipped in nonstandard packaging (watches in plastic bags rather than boxes, shoes in bags rather than boxes).
- Textile articles not labeled with fiber content or cleaning instructions.
- Clothing or other merchandise of non-standard sizing or sized to the standards of a different country.
- Merchandise is of a commodity commonly counterfeited or pirated such as computer parts.
- International mail shipments (especially of high technology goods).

2.7 EXAMPLES OF BEST PRACTICES

- Internal controls over IPR:
  - ✓ Are in writing,
  - ✓ Include procedures for monitoring and feedback, and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import Department, including ensuring the adherence to IPR laws and guidelines. That manager has knowledge of

Customs matters and the authority to assure internal control procedures for imports are established and followed by all company departments.

- Written internal control procedures assign duties and tasks to a position rather than a specific person.
- Company has good interdepartmental communication about Customs matters, including IPR issues.
- Company and import department has access to IPR laws, guidelines, and procedures governing imported merchandise subject to IPR analysis.
- Company conducts and documents periodic reviews of its imported merchandise, having IPR implications, and uses the results to make corrections to entries and changes to their import operations as appropriate.
- Company receives authorization of the merchandise subject to IPR by appropriate agreements with the owner of the trademark, trade name, copyright or patent prior to the importation.
- Royalties, proceeds, and indirect payments related to the use of the IPR are accounted for, and where applicable included in the price actually paid or payable.
- Import department has access to, and can readily produce:
  - ✓ Detailed description of imported merchandise identifying type of IPR and its specific requirements and issues,
  - ✓ Listing of all imported merchandise having IPR implications,
  - ✓ Contract(s) and/or other formal documentation indicating agreed to IPR importation practices and activities between the company and its foreign supplier(s).

2.8 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to IPR issues.
- Company's documentation that supports monitoring and verification of established and/or written internal control over IPR issues.
- Documentation that identifies IPR to merchandise such as royalty agreements or license agreements with the trademark's owner and financial statements, general ledger, foreign tax reports, and schedules.
- Invoices (should show such items as model numbers, catalog numbers, lots, factory codes, and/or expiration dates).
- Letters of credit.
- Other documents affecting IPR merchandise such as purchase orders, contracts, or other formal documentation indicating agreed to IPR importation practices and activities between the company and its foreign supplier(s).

PART 3 RISK ASSESSMENT AND INTERNAL CONTROL GUIDANCE

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and the guidelines below, determine through limited judgmental testing whether the company 's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. **Risk**; and

2. The **internal control** system, by determining whether the controls are in operation, how the controls were applied, how consistently they are applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.

- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.

- Using the results of the internal control review, develop an opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

   - Control Environment.
   - Risk Assessment.
   - Control Activities.
   - Information and Communication.
   - Monitoring

2. Review relevant Customs and company documents to identify and understand relevant internal control over IPR. (Examples of documents and information to review are listed on prior page).

3. Determine if the company established and follows procedures. Review:

- Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
- Documentary evidence of communication with the broker and company on IPR issues. Including verification that the broker followed company instructions.
- Documentary evidence of inter-company communications to ensure correct information is provided to Customs.
- Training records and materials used to educate and inform staff on IPR.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the Worksheet for Evaluating Internal Control (WEIC) for IPR in PART 4 of this document.

   Note: The internal control assessment should include steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled “Testing Limit” reflects Customs test sizes.

Example: Determine Testing Level

Based on a review of the profile (company is in an industry heavily known for IPR), questionnaire, written procedures, etc. the team concluded that the preliminary risk exposure was considered moderate.

The company's internal control procedures manual required the Import Manager to review a certain number of importations associated with IPR to ensure that royalties are properly declared to Customs. In addition, an IPR review log is maintained to document this review of importations. The Import Manager documented the transactions reviewed and corrected entries as necessary. The team concluded that the internal control system over IPR was strong.

Using the table above (based on moderate risk exposure and strong preliminary internal control evaluation), the team concluded that they would test five control items. The team judgmentally selected importations from the IPR Review Log. The team determined that the importations were not subject to IPR and were correctly reported to Customs.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of company's internal control over IPR.

1. Complete the WEIC for IPR to determine whether risk determination is acceptable or unacceptable and to document why. Put the results of IPR testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

   Customs considers risk unacceptable when testing reveals that internal control is not effective, or not sufficient, in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will assist the PAS team to determine whether conditions warrant proceeding to ACT.

   <u>Do not proceed to ACT if:</u>

   - The result of review indicated that the error was due to an isolated incident.
   - If substantive tests necessary to determine the extent of the problem can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

   <u>Proceed to ACT if:</u>

   - The company does not have an adequate internal control and the review indicated a significant problem that cannot be quantified without statistical sampling or further review.
   - The importer will not quantify the problem.
   - The company refuses to take corrective action on systemic errors and it is necessary to quantify the problem to consider penalty action.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of situations that might be encountered under the PAS *are for clarification purposes only:*

Note: We have only included compliance examples in this section of this technical guide due to the nature of the IPR issue. Revenue could become an issue; however our focus is to determine any potential IPR violation and proceed with the ACT or proceed to further action deemed necessary by our management.

Example A: Situation in which team would not proceed to ACT (Compliance)

Ciscoctomnik Inc., (CI) imports a number of articles manufactured under IPR constraints. The exporter has indicated that the IPR merchandise is produced within the rights of the trademark holder. The internal control procedures listed in CI procedures manual requires that two conditions be met before purchasing. The two conditions are: 1) the buyer must secure from the vendor at the time the purchase order is written, a general written statement regarding the conformity of the merchandise to the trademark stipulations; and 2) the purchasing department will obtain from the vendor as part of the purchase order, a statement that the vendor will provide Customs with details of that adherence to the stipulations of the trademark. The purchase order statement also indicates any failure to supply Customs with the needed information will make the vendor liable.

The PAS process started with the import team requesting trademark information for eight items. The eight items represented all IPR products that CI imports. Due to the conditions set in the purchase orders the documents were promptly available. The PAS Team reviewed CI's documentation that confirmed the vendor's adherence to the trademark stipulations and CI's application of internal control procedures. Therefore, proceeding to ACT was not considered necessary.

Example B**:** Situation in which the team would proceed to ACT (Compliance)

CI has the same controls as in Example A above except that on two of the eight items they could not produce the trademark information. During the limited PAS testing, it was also discovered that written internal control procedures were not always being followed. The PAS team agreed that they would proceed to ACT to perform additional analysis.

PART 4 WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – INTELLECTUAL PROPERTY RIGHTS (IPR)

PURPOSE: To determine whether IPR risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 - Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1 – Internal Control Questions

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Are internal controls over the manufacture or import of IPR products formally documented?					
2.	Are written policies and procedures approved by management?					
3.	Are written policies and procedures reviewed and updated periodically?					
4.	Is one manager responsible for control of the Import Department, including IPR products?					
5.	Does that manager have knowledge of Customs matters and the authority to ensure that internal control procedures for imports of IPR products are established and followed by all company departments?					
6.	Do written internal control procedures assign IPR duties and tasks to a position rather than a person?					
7.	Does company have good interdepartmental communication about IPR matters?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
8.	Does company conduct and document periodic reviews of products of IPR?					
9.	Does company use the IPR periodic review results to make corrections to past and present entries?					
10.	Does the company use periodic review results to make corrections to its import operations?					
11.	Do internal controls involve a verification process to determine that the imported IPR merchandise is correctly labeled or properly marked?					
12.	Is adequate descriptive information provided to the Import Department and/or broker to ensure proper declaration of IPR imports?					
13.	Does the importer have procedures to obtain any required or necessary copyright or trademark documentation?					
14.	Does the importer maintain an IPR database or listing of imported merchandise that would readily identify IPR merchandise?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
15.	Does the company perform an annual review of changes to IPR?					
16.	Does the individual overseeing compliance with products of IPR requirements have adequate knowledge and training?					
17	Does management review the classification and eligibility of new IPR items?					
18	Is responsibility for the IPR eligibility process assigned to one knowledgeable individual or department with management oversight?					
19.	Does the company provide adequate broker oversight?					
20.	Does the company identify, analyze, and manage risks related to IPR?					
21.	Has the company identified any risks related to IPR and implemented control mechanisms?					
22.	Does the company have internal control to address specific issues identified in the profile?					

No.	Internal Control (IC)	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
23.	List company-specific procedures and controls below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

***** If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)

TABLE OF CONTENTS

PART 1. BACKGROUND 2

1.1 OVERVIEW 2
1.2 AUTHORITY TO CONDUCT AUDITS 2
1.3 RISK MANAGEMENT 2
1.4 OBJECTIVE 2
1.5 LEGAL AND REGULATORY PROVISIONS AND REFERENCES 3

PART 2. PROGRAM GUIDANCE 3

2.1 CLAIMS FOR NAFTA PREFERENTIAL TREATMENT 3
2.2 EXAMPLES OF RED FLAGS 4
A. CATEGORY (1) Red Flags: 5
B. CATEGORY (2) Red Flags: 6
2.3 EXAMPLES OF BEST PRACTICES 6
2.4 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW 7

PART 3. RISK AND INTERNAL CONTROL GUIDANCE 8

3.1 RISK 8
A. Preliminary Assessment of Risk 8
B. Evaluation of Risk Acceptability 8
3.2 INTERNAL CONTROL 8
3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT) 9
3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS 10
3.5 EXAMPLES 11

PART 4. REPORT GUIDANCE 14

PART 5. WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – NAFTA 16

PART 1. BACKGROUND

1.1 OVERVIEW

On December 17, 1992, President Bush of the United States, President Salinas of Mexico and Prime Minister Mulroney of Canada entered into the North American Free Trade Agreement (NAFTA).

Public Law 103-182 (H.R. 3450); December 8, 1993 (107 STAT 2057) approved the North America Free Trade Agreement that was entered into by the United States, Canada and Mexico (the "Parties"); and the statement of administrative action to implement the Agreement. The NAFTA entered into force on January 1, 1994.

The NAFTA creates a free trade area consistent with Article XXIV of the General Agreement on Tariffs and Trade (GATT) in which tariff and non-tariff barriers to trade are substantially reduced between the Parties. (NAFTA Article 101)

Trade between the U.S. and its two NAFTA partners account for one third of all U.S. international trade. The U.S. – Canada is the largest trading relationship between any two countries in the world. Recent trade statistics show that trade between the NAFTA Parties is valued at $1.8 billion per day with 62% of that trade conducted under the NAFTA.

1.2 AUTHORITY TO CONDUCT AUDITS

Under 19 U.S.C. 1509 the U.S. Customs and Border Protection may examine records to ascertain the correctness of any entry for determining the liability of any person for duties, taxes or fees which may be due the United States or for ensuring compliance with the laws of the United States administered by the U.S. Customs and Border Protection.

Any person who imported or knowingly caused the importation of merchandise into the customs territory of the United States, exported merchandise, or knowingly caused the exportation of merchandise to a NAFTA country; must provide the records required by law or regulation to the U.S. U.S. Customs and Border Protection within a reasonable time after demand. (See 19 U.S.C. 1509(a)(2)(A)(ii))

1.3 RISK MANAGEMENT

Customs performs its duty in an environment where decisions regarding the allocation of finite resources have become increasingly important. We define risk as the degree of exposure to the chance of non-compliance that would result in loss to the trade, industry or public. Risk management is the integrated process for identifying and managing risk in trade compliance.

1.4 OBJECTIVE

Provide guidance in performing a Pre-Assessment Survey (PAS) of the importer's internal controls for the North American Free Trade Agreement (NAFTA) and evaluating the results.

Note: The evaluation of the importer's internal controls for NAFTA is limited to a determination as to whether the Certificates of Origin as maintained by the importer are timely, accurate and sufficient. The importer's internal controls for NAFTA should address the records requirements to secure and maintain certificates of origin to support the importer's claims for NAFTA preferential treatment.

The Focused Assessment (FA) process does NOT include determining whether the goods referred to in the Certificates of Origin that are held by the importer actually qualify as originating goods under the

NAFTA. Determinations on the origination of the goods and their resulting eligibility for NAFTA preference are made exclusively through the NAFTA verification process.

The NAFTA evaluation should be limited to a determination as to whether the Certificates of Origin as maintained by the importer are accurate and support the NAFTA status of the imported goods. Unlike GSP where a question regarding content would result in a request from the exporter for supporting documents, under NAFTA supporting documents are not to be requested. However, where there is a question of origin or content, consideration should be made as to whether a referral should be prepared for follow-up by a NAFTA verification either through a port-initiated verification or a Joint Verification Team (JVT).

1.5 LEGAL AND REGULATORY PROVISIONS AND REFERENCES

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal controls to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and the terms in this technical information guide are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78*.

Chapter 3 of the NAFTA provides for preferential treatment for originating goods imported from another Party. A good is considered originating if it meets all of the requirements of the NAFTA Chapter 4 rules of origin. Customs procedures concerning claims for preferential treatment for originating goods are set out in Chapter 5 of the Agreement.

The Chapter 4 Rules of Origin are implemented by the Uniform Rules of Origin Regulations (Part 181, App. of the U.S. Customs Regulations [19 CFR 181.131]) and General Note 12 of the Harmonized Tariff Schedule of the United States for imports into the United States. The Uniform Rules of Origin Regulations are trilateral regulations that have been incorporated into the domestic regulations of each of the Parties.

Customs Procedures of Chapter 5 of the NAFTA are implemented in the U.S. by Part 181 of the Customs Regulations (19 CFR 181.1 through 181.122).

The Rules of Origin provided in Part 102 of the Customs Regulations are for the specific purposes of determining the country of origin for goods of NAFTA Parties. Determination of the country of origin is necessary for proper marking of the good and application of the correct staged rate of duty if the duty rate has not been phased out to zero. The rules of origin of Part 102 are not used to determine the originating status of goods.

General definitions applicable to the NAFTA are found in Chapter 2 of the Agreement and in Section 2 of the Rules of Origin Regulations (Part 181, App. of the U.S. Customs Regulations [19 CFR 181.131]). Definitions that are specific to a Chapter, Article or Annex of the Agreement are found at the end of the Chapter, Article or Annex.

PART 2. PROGRAM GUIDANCE

2.1 CLAIMS FOR NAFTA PREFERENTIAL TREATMENT

To claim NAFTA preferential treatment for imported goods the importer must:

1. Make a written declaration based on a valid certificate of origin (Art. 502 NAFTA; 19 CFR 181.21)

    - A written declaration may be made by entering the prefix "CA" or "MX" with the tariff number of originating goods on the CF 7501 entry summary

- Or at any time within one year of the date of importation using the provisions of 19 USC 1520(d)
- When the importer makes a claim for preferential treatment, NAFTA originating goods are entitled to the duty rate in the "special" column that is indicated "CA" or "MX"
- The merchandise processing fee is also waived for NAFTA qualifying merchandise

2. Possess a valid certificate of origin (CO) at the time of the declaration (Art. 502 NAFTA; 19 CFR 181.21; CD No. 3810-014, June 28, 1999)

   - A valid CO:
     - ✓ Has the signature of the exporter or an authorized agent
     - ✓ Is dated and the date of execution is prior to the date of the NAFTA claim
     - ✓ Is in English or the language of the exporting Party (If in Spanish or French, the importer must provide a translation on request from USCS)
     - ✓ Is on Customs Form 434 or an approved alternative
   - A valid CO is required for each importation
   - Description provided on the CO is sufficient to allow an import specialist to identify the goods
   - A CO may be applicable to:
     - ✓ A single importation
     - ✓ Multiple importations of identical goods within a specified period up to one year (Blanket CO)
   - A CO is valid for 4 years from the date of signature
   - Policy Guidelines for the use of the NAFTA CO are established by Customs Directive No. 3810-014, dated June 28, 1999
     - ✓ A CO is valid provided that it is properly completed, signed and dated
     - ✓ If the importer did not possess a valid CO at the time the claim was made, the claim will be denied
     - ✓ A CO that contains inadequate information, is unsigned or is otherwise defective on its face is invalid
       - ➢ CO's that are "Otherwise defective" include those with: incorrect classifications, inadequate descriptions, missing date, wrong blanket period
         - ▪ The importer will be allowed at least 5 working days to submit a corrected CO
3. Maintain documentation in the United States, including the certificate of origin, relating to the importation of the good. (19 USC 1508, Art. 502 NAFTA; 19 CFR 181.22)

   - Importer must maintain the CO for a period of 5 years from the date of importation

4. Provide the certificate of origin to Customs on request (19 USC 1509, Art. 502 NAFTA; 19 CFR 181.22)

5. Promptly make a corrected declaration when warranted (19 USC 1508, Art. 502 NAFTA; 19 CFR 181.22)

2.2 EXAMPLES OF RED FLAGS

The examples provided below may serve as indicators that there are potential compliance problems with the NAFTA claims being submitted by the importer.

Care must be exercised by the auditor to properly identify issues that are compliance problems with the importer's claims vs. the eligibility of the goods to qualify for preferential treatment because they originate in the NAFTA territory. Originating status of the goods can only be verified through the exporter using the NAFTA verification procedure.

The importer is not responsible to maintain documentation that will support the origination of the goods that is certified by the exporter on the NAFTA CO. A request from Customs for information to support the exporter's declaration on the CO will trigger a NAFTA verification and require the procedures that are formalized in the Agreement and the issuance of a determination.

Requesting information about the good from the importer for determining classification, value or admissibility; asking for the NAFTA CO; or asking the importer questions about the NAFTA claim that the importer would have direct knowledge does NOT trigger a verification. The importer may also voluntarily provide information furnished by the exporter or producer in accordance with 19 CFR 181.72(c).

While conducting a FA review the auditor may develop some information that would raise some "red flags" concerning the goods and whether they qualify as originating. These questions can only be addressed through the NAFTA verification process and the auditor should consider making a referral for verification to be conducted by an import specialist or a joint verification team.

The list of "red flags" below are divided into two categories: those listed in category (1) are conditions that may indicate a potential problem that can probably be addressed directly with the importer without the need for information that would be available only from the exporter or producer; the "red flags" listed in category (2) are more likely to necessitate exporter involvement and may need to be addressed outside of an FA; in these cases a referral for a NAFTA verification may be warranted.

A. CATEGORY (1) Red Flags:

- Importer has insufficiently documented, poorly defined, or no internal controls for accurately declaring NAFTA preferences for Customs purposes. Examples:
  - ✓ Importer does not monitor or interact with the broker on NAFTA eligibility issues
  - ✓ Importer relies on one employee to handle NAFTA compliance, and there are poor or no management checks or balances over this employee
  - ✓ Importer Customs staff lacks knowledge of NAFTA eligibility rules and requirements
- Importer offers unreasonable explanations to Customs
- Previous negative determinations, denials or failed verifications on the same merchandise being imported from the same supplier (Is there documentation that indicates that the importer was notified of production changes so that the good now qualifies? If not, is the importer reasonable in his reliance on the CO?)
- Importer fails to cooperate or respond to Customs
- Importer has high turnover of people in key positions
- There is significant variance between the importer's data and Customs data
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with NAFTA claims (e.g., classification problems, inventory control problems for fungible goods, invalid or improperly completed certificates of origin, lacking a certificate of origin for a claim, reporting incorrect country of origin)
- One importer representative dominates NAFTA preference claims procedures and record keeping without monitoring or management oversight
- There is a large number of NAFTA Manufacturer Identifications (MIDs)
- There is a large quantity of NAFTA merchandise over many HTSUS numbers
- There is no monitoring of the classification procedure or records process that serve as the basis for the NAFTA preference claims
- There is a sharp increase of NAFTA imports from a prior period.
- The importer and the NAFTA producer are related
- The importer's reliance on the information certified in the certificate of origin is not reasonable (May be indicated if there are imports of NAFTA merchandise for which the exporting country is an unlikely source)

- Specific issues are identified in the profile
- Importer did not request, maintain, or review Certificates of Origin (Customs form 434) supporting the qualification of merchandise for NAFTA preferential treatment
- The CO is incorrectly prepared i.e. the HTS information is not correct but can be corrected within the requirements of 19 CFR 181.22.
- The blanket CO is signed subsequent to the beginning of the blanket period claimed and the importer has declared NAFTA for imports of the good prior to the signed date.
- Patterns of "type 02" entries and entries with NAFTA claims vary inversely. For example, the merchandise that was previously subject to quotas was subsequently being claimed as NAFTA eligible and not subject to quota restrictions.
- There are significant shifts in importing practices and claims; for example:
  - ✓ Shifts from claims for benefits of HTSUS 9802 to claims for NAFTA preference
  - ✓ A sudden rise in NAFTA claims and corresponding decline in tariff preference level (TPL) claims
- The importer does not clearly differentiate or does not demonstrate an understanding of 9802 benefits vs. preference claims under NAFTA
- There are changes in classifications from one time frame to another for a considerable portion of an importer's imports (This may be especially significant if any of the merchandise is subject to quota or dumping/countervailing duties from non-NAFTA countries; or if there is a shift away from HTSUS numbers that are associated with complex rules of origin or require RVC calculations.)

B. CATEGORY (2) Red Flags:

(Conditions that may be more appropriately addressed outside of the FA process and may warrant referral for a NAFTA verification)

- There are imports from a specific exporter or under an HTSUS number or country of origin that have been identified by Customs because of known or suspected NAFTA problems
- There are imports of NAFTA merchandise for which the exporting country is an unlikely source
- There are no prior verifications of NAFTA exports from the importer's principal NAFTA suppliers
- There are imports of merchandise where the specific rule of origin provided in HTSUS General Note 12 is very restrictive, complicated, or difficult to meet
- There are imports of merchandise where the applicable specific rule of origin has specific requirements, or requires that certain components originate
- The alternate Normal Trade Relations (NTR) duty rate for the merchandise imported is relatively very high
- There are restrictions imposed on imports of the merchandise from other countries, but not from the NAFTA Parties (e.g. dumping or countervailing duties, visa requirements, quota restrictions, trade sanctions).
- The exporter preparing the CO is not the producer of the good but rather a middleman or warehouse.
- The compliance measurement discrepancy rates are high for HTSUS numbers that importer frequently uses regarding NAFTA; or there are no verifications of the HTSUS numbers
- There are imports from a specific exporter or under an HTSUS number or country of origin that have been identified by Customs because of known or suspected NAFTA problems

2.3 EXAMPLES OF BEST PRACTICES

(Applicable only to the Importer filing claims for NAFTA preference.)

- The importer's Internal controls over NAFTA claims:

  - ✓ Are in writing,
  - ✓ Include procedures for monitoring and feedback, and
  - ✓ Are monitored by management
- One manager is ultimately responsible for control of the Import Department, including NAFTA eligible merchandise. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all importer departments
- Written internal control procedures assign NAFTA duties and tasks to a position rather than a person
- Importer has good interdepartmental communication about NAFTA matters
- Importer conducts and documents periodic reviews of NAFTA, and uses the results to make corrections past and present to entries and changes to its import operations as appropriate
- Suppliers, as well as other departments within the importer's organization such as engineering and purchasing, provide sufficient descriptions of merchandise to the import department to permit accurate classification and resulting determination of NAFTA eligibility
- The importer's internal controls contain prudent business practices (such as designating the material supplier for the NAFTA goods) that are meant to ensure that the importer can reasonably rely on certifications provided by the exporter. E.g. Because of product liability and business arrangements many auto parts producers are required to use customer approved material suppliers)
- The importer's internal controls involve a verification process to determine that the imported merchandise qualifies for NAFTA
- The importer has procedures to obtain certificates of origin from all NAFTA suppliers prior to the initial import date of any of the merchandise covered by the CO
- Internal controls ensure that the CO and related documents are maintained by the importer for the five year required period
- Importer has procedures in place to furnish Customs copies of applicable certificates of origin when requested
- Importer maintains a NAFTA database or listing of imported merchandise that would readily identify transactions that claim NAFTA preference
- The importer (or the importer's agent) visits the plant in the NAFTA country where the products are produced
- The importer performs an annual review of specific rules of origin (General Note 12 of the HTSUSA) that apply to imported merchandise to remain current with any changes to NAFTA requirements.
- The Importer communicates regularly with the filer to keep the filer's information current on what merchandise is NAFTA eligible and which is not.

2.4 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures used to ensure the validity of NAFTA certificates of origin; they should assure that:
  - ✓ Valid CO's are in importer's possession prior to making NAFTA claim
  - ✓ CO's are signed and dated prior to date of importation
  - ✓ CO's pertain (HTS # and description match) to the merchandise imported and claimed for NAFTA
  - ✓ CO's cover each importation on which NAFTA preference was claimed
- Importer's response to the questionnaire
- Interviews with importer staff concerning general internal controls and internal controls specific to NAFTA claims
- Importer's documentation that supports monitoring and verification of established and/or written internal controls for NAFTA, including:
  - ✓ Communications between the person responsible for monitoring NAFTA eligibility and the entry filer
  - ✓ Binding rulings concerning NAFTA eligibility

- ✓ Classification rulings for NAFTA merchandise
- ✓ Invoices, specification sheets, or other documents providing detailed descriptions of NAFTA merchandise
- ✓ Lists containing NAFTA part numbers, descriptions, quantities imported, and unit costs
- ✓ Bills of lading or other evidence of direct transport to the United States
- ✓ Previous positive determinations for the same merchandise
- ✓ Communications between the importer and the exporter concerning NAFTA eligibility of the merchandise.

PART 3. RISK AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate the effectiveness of internal controls and to determine if there is a sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) phase.

Using the chart and guidelines below, determine through limited judgmental testing whether the importer's internal controls are effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. The **risk exposure**, and
2. The **internal control** system by determining if the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.
- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.
- Using the results of the internal control review, develop and opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

- Control Environment
- Risk Assessment
- Control Activities
- Information and Communication
- Monitoring

2. Review relevant Customs and importer documents to identify and understand relevant internal controls over NAFTA. (Examples of documents and information to review are listed above.)

3. Determine whether the importer has established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence (such as a log) of communication with the broker and importer departments on NAFTA issues, Including Importer testing of broker operations and verification that the broker followed importer instructions.
   - Importer-specific NAFTA rulings requested. Determine if they are followed.
   - Documentary evidence of internal communications, to ensure that correct information is provided to Customs.
   - Training records and materials relating to NAFTA used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable importer personnel to complete appropriate sections of the "Worksheet for Evaluating Internal Control (WEIC) - NAFTA."

   Note: The internal control assessment should include steps to:

   - Identify and understand internal controls
   - Determine what is already known about control effectiveness
   - Assess the adequacy of internal control design
   - Determine whether controls are implemented and effective
   - Determine whether transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the total NAFTA level that will be reported on. For example, the importer may import from several NAFTA suppliers, but testing may be necessary only for certain companies or only for certain imports that have been identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review/ Internal Control	=	Extensiveness of Audit Test	Testing Limit

PAR Level	+	Preliminary Review/ Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled "Testing Limit" reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of importer's internal control over NAFTA claims.

1. Complete the "Worksheet for Evaluating Internal Control (WEIC) - NAFTA" to determine whether risk determination is acceptable or unacceptable and document why. Put results of NAFTA testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

   Customs considers risk unacceptable when testing reveals that internal controls were not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT:

<u>Do not proceed to ACT if:</u>

- Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
- The result of review indicated that the error was due to an isolated incident.
- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

<u>Proceed to ACT if:</u>

- The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of scenarios that may be encountered under PAS are provided for clarification purposes only.

Note: Where there are multiple importations of the same merchandise from the same exporter, the importer will most often utilize a blanket CO issued by the exporter to cover imports for a period of one year. The time period where the risk is highest that the importer will not be in possession of a valid CO when claims are made is early in the blanket period or the beginning of the fiscal year.

Example A: Situation in which the team would not proceed to ACT (Revenue)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer’s internal control effectiveness, the PAS team evaluated the importer’s internal control procedures. Specifically, tests of NAFTA claims were supported by valid certificates of origin in the importer's possession except for one item that was imported on multiple entries throughout the year.

The importer imports multiple products from the exporter who provided a blanket certificate of origin covering multiple products. One product was not included in any certificate of origin provided by the exporter.

The importer agreed to quantify and pay duties on the merchandise for which there was no valid certificate of origin and to modify his internal controls to assure that a valid certificate is in his possession prior to making a NAFTA claim.

Since there were no other revenue issues and correction was made to avoid future problems, the team does not proceed to ACT for revenue.

Example B: Situation in which the team would not proceed to ACT (Compliance)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of NAFTA claims were supported by valid certificates of origin in the importer's possession except for one shipment where the invoices indicated that the country of origin was a non-NAFTA country. The NAFTA producer experienced production problems and obtained goods from its parent manufacturing plant in Sweden to fill one of the importer's orders.

The importer agrees to pay the duties and interest due on the one shipment that was not of NAFTA origin and to modify internal controls to assure that NAFTA eligibility is ascertained prior to making claims based on blanket certificates of origin.

Example C: Situation in which the team would not proceed to ACT (Revenue)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of NAFTA claims revealed that two products were consistently misclassified on the certificates of origin and entered under that wrong classification. The correct classification and corresponding rule of origin did not affect the goods originating status and there was, therefore, no revenue impact.

The importer agreed to secure a corrected certificate of origin that was promptly provided by the exporter. The importer also agreed to modify internal controls so that the classification error would not recur.

Example D: Situation in which the team would proceed to ACT (Revenue)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and

testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of NAFTA claims indicated that certificates of origin were on file to support claims for preferential treatment. The importer purchases 4 different models of the product, but only 2 are listed on the CO's provided to the importer by the exporter/producer. Based on the examination of correspondence between the importer and the producer, it is disclosed that the NAFTA producer actually produces 2 of the models in the NAFTA territory and the other 2 are purchased by the exporter from it's parent company located outside of the NAFTA territory. Most of the shipments contain units of all 4 models and the importer claimed NAFTA preference on all models.

In this scenario the importer does not have CO's to support the preference claims on 2 models of the product. Furthermore, the importer will not be able to obtain corrected CO's from the exporter to cover all models. Preferential treatment should be denied. There is no determination of origin of the goods made in this type of scenario and no NAFTA verification. There is a denial of the claim because there is no valid CO for the goods. The PAS team proceeds to ACT to quantify revenue loss.

Example E: Situation in which the team would proceed to ACT (Compliance)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, NAFTA claims are tested and the importer's current inventories are reviewed. A recent shipment is found to contain commingled originating and non-originating goods. Though the origination status for the various goods in the shipment is clearly indicated on the invoices, the importer claimed NAFTA preference on all of the goods in the subject importation.

The importer says that the incident is a one-time occurrence caused by a clerical error and does not want to change internal controls.

The imported goods are used by the U.S. importer as materials for goods that the importer produces and then sells to customers in other NAFTA Parties. The U.S. Company, as the exporter, furnishes NAFTA certificates of origin for the goods that are exported.

Since the importer will not change its internal controls and the level of compliance is unknown, the PAS team proceeds to ACT to determine whether the importer meets the acceptable level of compliance for NAFTA.

In this kind of scenario, NAFTA compliance includes the exported product and the declaration made by the U.S. company on the CO's that it completed for exports to other Parties as well as the import compliance for the goods imported under NAFTA preference and subsequently used as materials. The responsibilities imposed on U.S. importers by 19 USC 1509 are extended to any U.S. exporter who executes a NAFTA certificate of origin. (19 U.S.C. 1509(a)(2)(A)(ii))

If the non-originating goods used as materials in the importer's production affect the origination of the good produced and exported to another NAFTA Party, the declaration made by the U.S. company on the CO's that it completed will be a violation of 19 USC 1509. The Importer/U.S. exporter is subject to the same level of culpability and consequences in this export transaction as it would be for a violation of the same law in an import transaction. Customs also have the same enforcement responsibilities for the violation.

Note*: Based on non-compliance in the NAFTA area, the Team will proceed to ACT only when the actionable non-compliance is based solely on the responsibilities of the importer in the NAFTA transactions. For import transactions, the importer's responsibility is to possess and maintain a valid certificate of origin for each claim for NAFTA preference. If the importer is in possession of a valid CO the NAFTA claim CANNOT be denied without a NAFTA verification. There is never a negative determination on the origin of the goods based on the information provided by the importer. A negative determination on the origin of the goods can only be issued as a result of a verification conducted through the exporter. If the importer cannot produce a valid CO when requested to do so, then NAFTA preference will be denied. In this case, there is a denial of NAFTA benefits; however, there is no determination as to whether or not the goods originate.

PART 4. REPORT GUIDANCE

The Focused Assessment (FA) process does NOT determine the eligibility of the goods for NAFTA preferential treatment. Whether or not the goods qualify for NAFTA treatment by meeting the rules of origin requirements is not an issue that is to be addressed in a FA report.

Rather, the FA process examines and reports on the written internal controls that the importer (not the exporter or producer) has implemented relative to the claims for NAFTA preference that are made on its importations.

The following are examples of statements that might appear in the summary of audit results when the internal controls are found to be sufficient:

"ABC has adequate internal controls over its Customs related transactions which provide reasonable assurance that the importer is compliant with the laws and regulations and is an acceptable risk to Customs. The conclusions for each review area are summarized below:

- "North American Free Trade Agreement (NAFTA) – Our review of ABC's internal controls over its NAFTA importations, disclosed that the controls in place appear to be functioning as intended with no significant risk of non-compliance to Customs. However, our review of ABC's internal controls, is not designed to determine the NAFTA eligibility of the goods imported. The eligibility of the goods imported claiming NAFTA preference can only be determined by a NAFTA Verification."

NOTE:

Although a NAFTA "determination" can never be issued based on a focused assessment report, it does not mean that the importer's claims for NAFTA preference cannot or will not be denied if there are NAFTA claims that cannot be supported by the importer. In order to claim NAFTA preference, the importer must have a valid certificate of origin (CO) at the time the claim is made.

NAFTA preference will be denied:

- If the importer does not have a valid CO that covers the importation and claim for NAFTA preference

  - A valid CO:
    - ✓ Has the signature of the exporter or an authorized agent
    - ✓ Is dated and the date of execution is prior to the date of the NAFTA claim
    - ✓ Is in English or the language of the exporting Party (If in Spanish or French, the importer must provide a translation on request from USCS)
    - ✓ Is on Customs Form 434 or an approved alternative
  - A valid CO is required for each importation
  - Description provided on the CO is sufficient to allow an import specialist to identify the goods
  - A CO may be applicable to:
    - ✓ A single importation
    - ✓ Multiple importations of identical goods within a specified period up to one year (Blanket CO)
  - A CO is valid for 4 years from the date of signature

- If the importer's CO is invalid on its face and the importer cannot produce a corrected CO

  - Policy Guidelines for the use of the NAFTA CO are established by Customs Directive No. 3810-014, dated June 28, 1999
    - ✓ A CO is valid provided that it is properly completed, signed and dated
    - ✓ If the importer did not possess a valid CO at the time the claim was made, the claim will be denied
    - ✓ A CO that contains inadequate information, is unsigned or is otherwise defective on its face is invalid
      - CO's that are "Otherwise defective" include those with: incorrect classifications, inadequate descriptions, missing date, wrong blanket period
        - The importer will be allowed at least 5 working days to submit a corrected CO

- In the normal course of reviewing the importer's books and records, evidence is discovered that their claims for NAFTA preference cannot be supported or there is fraudulent activity on the part of the importer concerning the NAFTA claims

For import transactions, the importer's responsibility is to possess and maintain a valid certificate of origin for each claim for NAFTA preference. If the importer is in possession of a valid CO the NAFTA claim CANNOT be denied without a NAFTA verification. There is never a negative determination on the origin of the goods based on the information provided by the importer. A negative determination on the origin of the goods can only be issued as a result of a verification conducted through the exporter. If the importer cannot produce a valid CO when requested to do so, then NAFTA preference will be denied.

PART 5. WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – NAFTA

PURPOSE: To determine whether Transaction Value risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 – Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample Sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1- Internal Control Questions

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure the validity of all claims for NAFTA preferences?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies and procedures periodically?					
4.	Is internal control of certificates of origin periodically tested and results documented? This should include post-entry reviews to verify certificates of origin for all NAFTA claims.)					
5.	If weaknesses were found during internal control testing of certificates of origin by the company, did the company correct internal control procedures and entries when appropriate?					
6.	Do written internal control procedures assign duties for ensuring that NAFTA claims are supported by valid certificates of origin to a position rather than a person?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does one individual have authority to ensure that internal control procedures for NAFTA certificates of origin are established and followed for all departments?					
8.	Do personnel responsible for ensuring that valid NAFTA certificates of origin are obtained have adequate knowledge and training in Customs valuation?					
9.	Does the company have adequate interdepartmental communication about Customs NAFTA certificates of origin?					
10.	Does the company have procedures to obtain Customs assistance for NAFTA issues when needed and is advice followed when given (e.g., requesting binding rulings)?					
11.	Does the company identify analyze, and manage risk related to NAFTA certificates of origin?					
12.	Has the company identified any risks related to NAFTA certificates of origin and implemented control mechanisms?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
13.	Do internal controls involve a process to determine if reliance on the exporters' certificate of origin is reasonable?					
14.	Does the company have procedures to link specific certificates of origin to Customs entry numbers?					
15.	Do Purchasing, Engineering, other departments, and suppliers provide adequate descriptive information to the Customs Department and/or broker to ensure proper NAFTA classification and eligibility?					
16.	Does the importer have procedures to obtain certificates of origin to support claims for NAFTA preference?					
17.	Does the importer have procedures to track and replace expiring certificates of origin before they expire?					
18.	Does the importer maintain a NAFTA database or listing of imported merchandise that would readily identify NAFTA transactions?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
19.	Does the importer or the importer's agent visit the plant in the NAFTA country where the goods are produced?					
20.	Does the importer perform an annual review of classification, specific rule changes affecting NAFTA?					
21.	Does management review the classification and eligibility of new NAFTA items?					
22.	Do contracts with NAFTA suppliers contain provisions to ensure compliance with NAFTA eligibility requirements?					
23.	Does the importer review entries to verify that correct classifications were used?					
24.	Does the importer verify that certificates of origin are on file for each entry of merchandise for which NAFTA preference is claimed?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
25.	Does the importer review NAFTA certificates of origin to ensure validity of the certificates?					
26.	Does the importer maintain entry documentation and associated NAFTA certificates of origin for 5 years after the date of importation?					
27.	Are HTSUS classifications for NAFTA merchandise maintained in a database that is provided to brokers?					
28.	Are brokers required to have written importer approval to making classification changes?					
29.	Does the importer provide adequate broker oversight?					
30.	**List company-specific procedures below (if applicable)**					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

*If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples related to various costs comprising transaction value are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	

		Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.

U.S. Customs and Border Protection
Office of Strategic Trade
Regulatory Audit Division

Sampling Technical Guide

Introduction and Background

In March 2003, the U.S. Customs Service became part of the U.S. Customs and Border Protection, which will continue to be referenced as Customs in this document.

The high volume of Customs-related transactions makes an examination of all transactions impractical to perform. Sampling transactions allows conclusions to be drawn about an importer's Customs operations without reviewing all transactions. The goal of sampling in regulatory audits is to be as efficient and effective as possible in reviewing those operations and transactions, determining compliance with Customs laws and regulations, and computing any loss of revenue to Customs.

Sampling may be statistical or nonstatistical (judgmental). Statistical sampling is an objective, defensible, reliable method that is commonly used to draw conclusions about an entire population or universe. As discussed in the Government Auditing Standards (Yellow Book), auditors should use statistical sampling and other aspects of quantitative analysis, when appropriate, to accomplish audit objectives. Statistical sampling requires random selection of sample items and statistical evaluation of sample results. Nonstatistical sampling relies on auditor judgment to select sample items and evaluate sample results.

This Exhibit includes 7 appendices and provides guidance for sampling in Focused Assessments as well as other audits.

Appendix I, Sampling Steps – a step by step narrative process for sampling in various Regulatory audits.

Appendix II, Sampling Methodology Diagram – a pictorial quick reference of sampling methodology for sampling in various Regulatory audits.

Appendix III, Focused Assessment (FA) Sampling Methodology Table – a quick reference of sampling methodology for FA audits.

Appendix IV, Sampling Plans – standard sampling plan forms for various types of sampling in various Regulatory audits.

Appendix V, Example Audit Report Tables – examples of tables to be used in any Regulatory audit report to display sampling information.

Appendix VI, Glossary of Sampling Terms – definitions of frequently used sampling terms.

Appendix VII, Reading List for Audit Sampling – references to publications for those wishing to learn more about sampling in audits.

Procedures

Sampling Techniques

1. Nonstatistical (Judgmental) Sampling

   Nonstatistical or judgmental sampling may be used in certain circumstances when statistical results are not needed, there is a high degree of certainty that a conclusion can be drawn without further sampling, and:

   - the purpose is to take a survey in order to determine the necessity for and extent of substantive tests (e.g., FA Pre-Assessment Survey);
   - there is a desire to concentrate audit effort in a specific problem area revealed by a previous sample or other source of information (e.g., FA Follow-Up);
   - the universe is very small and it would be quicker and easier to review all or most of the items in the universe; or
   - the area is very sensitive and there is no room for error (i.e., exact results are required and a 100 percent is review necessary).

   Nonstatistical sampling is the appropriate method for reviewing transactions of particular interest or concern to determine whether more extensive testing is needed. For example, selective limited sampling of items in an account may be used to determine or verify the nature of the account.

2. Statistical Sampling

   Statistical sampling will be used in all other circumstances where nonstatistical sampling is not appropriate.

   Variable sampling will be used in most cases where statistical sampling is appropriate (e.g., most review areas in FA Assessment Compliance Testing). Variable sampling can be physical unit sampling (selecting physical items or transactions) or dollar unit sampling (selecting dollars which are then tied to physical items or transactions for review).

   Attribute discovery sampling may be more appropriate for certain unique audit areas, such as tests for transshipment or undeclared ADD/CVD (anti-dumping duties/counter-veiling duties).

Sample Results Evaluation

1. Compliance

   Compliance determinations for FAs will generally be based on the value of systemic errors found in the sample. Appendix IV of this document and FA Program Exhibit 3F contain specific guidance regarding compliance determinations.

2. Revenue

   Loss of revenue estimates will be based on the most accurate information available (actual amounts if known, statistical projections, etc.).

   If statistical sampling is used, the desired confidence level for revenue projections will be 95 percent. Precision percentages will be calculated to choose the most accurate projection when multiple point estimates are produced. The point estimate with the lowest precision percentage will be used, if the precision percentage is acceptable. If the precision percentages are poor, additional or alternative procedures may be necessary to estimate the revenue due. Appendices I and IV contain guidance on the projection of revenue loss.

   Generally, projections of sample results should be limited to the universe from which the sample was drawn. Items examined in one universe may not be representative of other universes and projecting to other universes would not be statistically defensible. However, auditors may express their opinion and make nonstatistical applications if they believe the results apply to another universe.

3. Enforcement Referrals

   Referral estimates for enforcement will be based on the most accurate information available (actual amounts if known, statistical projections, etc.). Appendices I and IV contain guidance on the enforcement referral estimates.

Sample Documentation

Audit documentation will fully and clearly document all aspects of the sampling that was used. For each sample, the audit documentation will include as a minimum:

- A sampling plan which documents important elements of the sampling methodology and results. (Standard sampling plans are contained in Appendix IV.)
- The sampling frame itself.
- The procedures used to validate and analyze the sampling frame.
- The sample size determination.
- The random numbers/procedure (for statistical samples) or other methodology (for nonstatistical samples) used to select the sample items.

- The selected sample items and the review of the sample items.
- The evaluation of the sample results (conclusions, projections).
- Any other documentation produced during the planning, selection, review, or evaluation of samples.

NOTE: The sampling plans include sections for various phases of the sampling process. The sections of the sampling plans can be separated as necessary and included in audit documentation as each phase of the sampling process is completed. For example one phase might include Sampling Application, Sampling Approach and Universe and Frame Information and Sample Information. The AFD must approve these sample sections before the sample is taken. The sections for Sample Results may be included in another set of documentation. The auditors should develop the various sections of the plan and document sampling phases as they occur but all phases of the sampling process should be documented using all the sections of the sampling plans. This will result in documenting the sampling plans in different sections of the automated documentation. In addition, this will allow supervisors to timely review and approve the planning sections of the sampling plan. As an alternative, the auditor could include the sampling plan in one document and the AFD could sign off on different sections of the sampling plan as he reviews and approves each section.

Appendix I contains guidance for documenting samples.

Reporting Sampling

A table of basic sampling parameters should be included in the audit report for each sample that significantly supports the audit findings. Additional guidance is in Appendix I, Section VII. Example audit report tables are contained in Appendix V.

The audit report will also include the compliance rate, if computed, and the loss of revenue, if applicable.

Sampling Steps

I. PLAN THE SAMPLE

A. Decide whether or not to sample. *(Applies to all circumstances.)*

1. Define the audit objective.

   a) The audit objective usually comes directly from the audit program or is a variation that has been modified by the auditor to fit the specific circumstances. If there is no standard audit program, the auditor must define an audit objective appropriate for the unique audit.

   b) Consider all knowledge available to date. All available information about the company and its Customs transactions should be considered in planning the audit and any required sampling. This information may come from prior audits, historical files, profiles, questionnaires, risk assessment, survey results, input from other Customs disciplines, etc. This information will help in refining the audit objective and the audit tests required to achieve that objective.

   c) Once the audit objective is defined, audit testing can be designed to achieve that objective. The appropriate audit testing will vary depending on the audit objective.

2. Identify the available data, records, and supporting documents.

   a) The available information, its method of storage and retrieval, and its format will directly impact the audit tests that can and should be applied.

   b) For example, if no electronic files are available, this would severely limit the macro analysis that could be performed and would restrict the sampling options as well.

3. Determine if macro analysis is possible and will achieve the audit objective.

   a) Macro analysis is any high-level analysis not involving the review of individual items or transactions. Macro analysis may include such procedures as considering total value balances or total duty paid, calculating potential value or duty impact, extracting and/or comparing data and totals from Customs and importer systems, analyzing variances, analyzing specific characteristics of extracted data, and analyzing relevant data trends.

b) Macro analysis is a key part of assessing risk exposure but may also be used anytime it will help satisfy the audit objectives. It can be more efficient and more precise than sampling and therefore, should be considered first. If macro analysis will achieve the audit objective, then there is no need to perform the remaining sampling steps herein. Thoroughly document all aspects of the macro analysis performed in compliance with audit documentation policies.

c) Micro testing, on the other hand, is the review of individual items or transactions (sampling) usually in order to make conclusions about the population or universe from which they are drawn. The remaining steps pertain to such micro testing or sampling.

B. If macro analysis is not sufficient to achieve the audit objective, decide on nonstatistical (judgmental) or statistical sampling. *(Applies to nonstatistical and statistical sampling.)*

1. Define the sampling objective. The specific sampling objective (i.e., the reason to sample, the question you're trying to answer about the universe, what you're trying to test/measure, the audit statement you need to make, etc.) will help determine whether nonstatistical or statistical sampling is appropriate.

2. Nonstatistical sampling relies on auditor judgment to select the sample items and evaluate the sample results (except in the case of 100% review where actual results are known). Statistical sampling is an objective process for randomly selecting the sample items and statistically evaluating the sample results.

3. There are specific limited circumstances in which nonstatistical sampling is appropriate. Nonstatistical sampling is suitable if statistical results are not needed, there is a high degree of certainty that a conclusion can be drawn without further sampling, and

   a) the purpose is to take a survey in order to determine the necessity for and extent of substantive tests, and/or.

   b) there is a desire to concentrate audit effort in specific problem area revealed by a previous sample or other source of information, and/or

   c) the universe is very small and it would be quicker and easier to review all or most of the items in the universe, and/or

   d) the area is very sensitive and there is no room for error or exact results are needed so all of the items in the universe will be reviewed.

4. It is important to consider the first part of the requirement for nonstatistical sampling (i.e. statistical results are not needed and there is a high degree of certainty that a conclusion can be drawn without further sampling) because it is generally not appropriate to calculate compliance rates or to project dollar impacts (value or revenue) based on results of small nonstatistical samples. Compliance rates and dollar impacts could be based on results of 100% reviews because they represent actual results.

5. If statistical results are needed or you need more than a nonstatistical sample to make a conclusion (e.g., objective results, projections to the universe with measurable precision, or compliance rates), then nonstatistical sampling is not appropriate (unless 100% review is possible).

6. If nonstatistical sampling is chosen, skip to sampling step I.D. If statistical sampling is chosen, continue with sampling step I.C. below.

C. If nonstatistical sampling will not satisfy the sampling objective, decide on which type of statistical sampling (attribute discovery or variable sampling) is appropriate. ***(Applies to statistical sampling.)***

1. Attribute discovery sampling is a special kind of attribute acceptance sampling where the occurrence of even a single error constitutes a failure of the universe. Variable sampling is a form of substantive testing that is quantitative in nature and can be used to determine variance amounts or dollar impacts (e.g., materiality-based compliance rates, revenue due, etc.).

2. Attribute discovery sampling is appropriate when the area of review is sensitive and any systemic error would constitute noncompliance (and potentially fraud). This makes it appropriate for the review of transshipment or undeclared ADD/CVD. Attribute discovery sampling is also appropriate when no error is expected or errors result in penalties rather than revenue due (such as broker or bonded warehouse audits).

3. Variable sampling should be used in all other circumstances where statistical sampling is appropriate. Variable sampling may be physical unit sampling (where individual items or physical units are selected) or dollar unit sampling (where individual dollars are selected).

D. Select the sampling frame and unit. ***(Applies to nonstatistical and statistical sampling.)***

1. Identify available frames, their sampling units, and formats (i.e., electronic, hard copy printout, or physical items).

a) Whether nonstatistical or statistical sampling is used, potential sampling frames and sampling units must be identified. A sampling frame is the physical or electronic representation of the universe from which the sample is selected. The universe is the entire group of items comprising the category or area of interest to the auditor (to be tested). The sampling units are the individual units (e.g., items, transactions, lines, dollars, physical files, etc.) that are selected for review.

b) The available frames and units must be evaluated to determine which will best satisfy the audit and sampling objectives and the best sampling approach to take. An electronic frame is always superior to an identical physical frame or listing because it provides more flexibility and efficiency in the areas of frame analysis, sample selection, and sample results evaluation.

2. Consider the level of summarization of the frame and units and identify the available supporting records/documents and their level of summarization.

a) Frames, units and supporting records and documentation can be at various levels of summarization. They may be at a very high level or a very low level. For example, an entry is made up of many entry/tariff lines, which may be made up of many invoices, which may be made up of many invoice lines, which may be made up of many parts/articles, which may be made up of many styles, which may be made up of many sizes and colors. Importer records and documents may group information similarly or by many other groupings such as by lot, container, purchase order, date received, batch processed, month, supplier, merchandise category, etc.

b) Often, the higher the level of sampling, the more difficult the review because the more items and supporting documents that have to be reviewed. But this is not always the case. It depends on the sample items (nature, level of summarization and number) and the available supporting records and documentation (physical or electronic, level of summarization, and effort required to trace and verify the sample items).

c) The ideal situation is one in which the supporting records and documents are summarized at the same level as the sample items or one in which the sample items are easily traced through and verified by the supporting records and documents. Problems occur or significant extra effort may be required when this is not the case (i.e., the sample items and supporting records and documents are at very different levels and/or the sample items are not easily traced/verified).

d) Also keep in mind the audit and sampling objectives - what is being tested. If the entered/reported data is being tested, then it would not be effective or efficient to sample and verify at a much lower level than that which is reported (e.g., sampling at a level of merchandise color when all colors are properly combined on an entry line for reporting classification, quantity, and value).

3. Based on the available choices, select the best frame and unit to effectively and efficiently accomplish the audit and sampling objectives.

   a) Ask: "If I select this frame and sampling unit, what am I really testing and what procedures will I have to perform? What and how many records and documents will I have to review? What difficulties will I have tracing the sample items through the records and documents? What manual or electronic calculations or summarization will I have to perform in order to trace and verify the sample items? Will this satisfy the audit and sampling objective? Is there a better (more efficient or effective) frame or sampling unit?

   b) An electronic file generally works best with any kind of nonstatistical or statistical sampling. If an electronic file is not available, a printout/listing or a physical item frame can be used for nonstatistical and variable physical unit sampling. A small printout or listing that could easily be typed into EZ-Quant could be used for variable dollar unit sampling.

   c) If nonstatistical sampling is being used, skip to sampling step I.H. If statistical sampling is being used, continue with sampling step I.E. below.

E. Validate the frame. ***(Applies to statistical sampling.)***

1. The purpose of frame validation is to determine if it is an adequate representation of the universe intended for testing

   a) Remove credit/negative items and zero balance items from the frame. Proper sampling requires that duplicate items (e.g., credit/negative items with corresponding debit/positive items) and zero value items that have more than one chance or no chance of selection be removed from the frame – either for separate review (separate sample or 100% review) or for no review.

   b) Compare/reconcile the chosen frame with the intended universe or another potential frame to try to verify that it is a complete and accurate listing suitable for the intended objective.

For example, if the intended universe is all GSP parts received and a frame extracted from an importer parts database is chosen, this frame could be compared to GSP reported to Customs in ACS. Or if the intended universe is all imported value and classifications and a frame of ACS entries is chosen, this frame could be compared to the inventory receipts (all imports) for the year.

2. The primary purpose of these types of comparisons is to ensure that you have good data from which to sample. However, as a form of macro analysis, these reconciliations could also reveal additional risk areas or potential problems, such as potential unreported value, misclassified merchandise, over-declarations of GSP, under-declarations of ADD/CVD, etc.

3. Analyze any variances and adjust the frame, accept the frame, or reject the frame and select another as appropriate.

   a) There are many things that might cause a variance between the frame and universe (or two frames representing the same information). Some common causes of variances are as follows:

      (1) Timing or time frame differences. There are various dates in Customs ACS system (create date, entry date, export date) which are usually different from the dates in the Importer's system (received date, order date, paid date). Therefore, there could be some timing differences when trying to compare ACS data with importer data.

      (2) Excluded items. Due to the complexities of data and data systems and the potential for miscommunication, it is common for whole categories of data to be excluded from one frame or another. This might be data associated with a particular country, vendor, division, importer ID, or broker. Or it might be data assumed to be unique, dissimilar, or irrelevant such as samples, merchandise purchased for use rather than resale, returns, merchandise in transit, drop shipments, consignments, or informal entries.

      (3) Problems with the data source or EDP system. Sometimes data is incomplete because only one partially complete source was accessed when the rest of the data is contained in another file, database, or system.

   b) Various methods can be employed to identify the cause of a variance. Questioning about merchandise receipt timing will help to identify and adjust for timing variances. Computer analyses (such as summing and comparing totals by country, MID and vendor, tariff and merchandise descriptions) may help identify missing categories of data. Grouping queries may show that duplicate records are present.

c) Once the cause has been determined, a decision must be made if the frame can and should be corrected or adjusted, accepted as is, or rejected and another frame used instead. The key will be the audit and sampling objective (the intended universe and testing) and whether adjustments are actually viable.

4. If attribute discovery sampling is being used, skip to sampling step I.H. If variable sampling is being used, continue with sampling step I. F. below.

F. Analyze the frame variability and anticipated/potential errors. ***(Applies to statistical variable sampling.)***

1. Frame variability refers to the differences and similarities among sampling units within the frame, in terms of dollar amounts and characteristics.

2. The degree of frame variability will help determine the required sample size and the best sampling approach.

a) Determine the skewness by calculating the measures of central tendency.

(1) Calculating the mean, median, and mode (AVERAGE, MEDIAN, and MODE functions in Microsoft Excel) will indicate the skewness of the frame. If the mean is greater than the median, then the frame is right skewed, meaning that there are a few high dollar items and many low dollar items. If the mean is less than the median, then the frame is left skewed, meaning there are a few low dollar items and many large dollar items. The greater the difference between the mean and median, the greater the skewness. Skewness is an indication of dollar variability and may also point to the need for horizontal stratification (by dollar amount).

(2) A highly skewed universe (left or right) would point towards a larger stratified physical unit sampling. A highly left skewed universe would point towards a larger dollar unit sampling.

b) Determine the dollar variability by calculating the indices of dispersion (standard deviation and coefficient of variation).

(1) Standard deviation is the average distance of individual values or the extent to which individual values depart from the average. In Microsoft Excel, it can be calculated by using the STDEVP function. The larger the standard deviation, the more variation. (Do not use any other STD functions in Microsoft Excel as will result in a different, incorrect result.)

(2) The coefficient of variation (CV) is the standard deviation expressed as a percentage. The formula is Standard Deviation of the frame /

Mean of the frame * 100. The higher the CV, the more dollar variation in the frame. Generally, a CV < 50% indicates low variation, a CV between 50% and 100% indicates moderate to high variation, and a CV over 100% indicates very high variation.

(3) A higher CV (≥50%) would point towards a larger stratified physical unit sample or a larger dollar unit sample.

c) Determine if there are obvious dollar breaks or groupings (for horizontal stratification). (Applies if the universe is highly skewed and/or the CV ≥ 50%.)

(1) High skewness, standard deviation, and CV indicate high dollar variation and probably a need to stratify – at least horizontally (on dollars) and possibly vertically (on characteristics). Sorting the frame in Microsoft Excel (by dollar amount) may reveal clear divisions or groupings of similar dollar amounts. (This type of analysis may also be performed by creating various tables and reports in Microsoft Access.)

(2) Obvious dollar breaks or groupings would point towards a larger manually stratified physical unit sample. It could also point towards a dollar unit sample with a 100% review high dollar stratum if the obvious dollar break is between high dollars and the rest of the frame.

d) Analyze the characteristics to determine if logical groupings exist (for vertical stratification).

(1) Analyzing the frame in Microsoft Excel (sorting, subtotaling, creating pivot tables, etc.) by description, part number, HTS or tariff number, account number, product lines, size, quantity or any other relevant characteristic may reveal common characteristics or categories that should be grouped together. (This type of analysis may also be performed by creating various tables and reports in Microsoft Access.)

(2) A highly variable frame in terms of characteristics would point towards a larger stratified physical unit sample or multiple dollar unit samples.

e) Identify special, very low risk, or very high risk items and decide whether to leave them in the frame for random sampling or remove them from the frame for no review or 100% review.

(1) These may be, for example, very low dollar items, very high dollar items, informal entries, consignee entries, etc.

(2) Very low dollar items may be eliminated from the frame IF the team agrees that there are no potential significant issues or errors that

could occur. Be cautious about automatically assuming that low dollar items are insignificant. It may not be appropriate to exclude the low dollars if:

(a) the frame contains clusters (the apparently low dollar items may not be low in comparison to the individual items making up the clusters),

(b) they are significant in the aggregate,

(c) they represent sensitive special trade areas, or

(d) the value is known or suspected to be significantly understated.

(3) For example, one company had approximately $350,000 in low dollar sample merchandise out of $65 million total reported value. These were left in the frame and some were chosen in the sample. During the attempt to support the sample merchandise value, the importer discovered they were significantly undervalued and submitted a disclosure for approximately $1.5 million with revenue due of about $300,000. If these low dollar items had been deleted from the frame for no review, the errors would not have been discovered and this loss of revenue would not have been recovered.

3. Define the anticipated or potential errors.

a) The frequency, types, and amounts of the anticipated or potential errors will help to determine the best sampling methodology for the situation.

b) Frequent errors, including small errors, would point towards physical unit sampling. Infrequent large errors would point towards dollar unit sampling.

G. Determine the best variable sampling method (physical unit or dollar unit) based on the results of the frame analysis. *(Applies to statistical variable sampling.)*

1. Physical unit sampling generally works best with:

a) An electronic frame, a printout or listing frame, or a physical item frame.

b) Any amount of frame variability, including one that is highly variable in terms of dollars and characteristics.

c) Sampling units that are individual items or sampling units that are clusters of items where reviewing the entire cluster is acceptable

(i.e., the clusters consist of a few items and/or reviewing whole clusters would not require significant additional effort to trace through the supporting records and documents).

d) The anticipated or potential errors are frequent, including small errors.

2. Dollar unit sampling generally works best with:

a) An electronic frame or a small printout or listing frame that could be typed into EZ-Quant.

b) A frame that is not highly variable or a frame that is highly variable in terms of dollars (especially left skewed) but not in terms of characteristics. (Dollar unit sampling may be used with a frame that is highly variable in terms of characteristics, but it would require multiple dollar unit samples.)

c) Sampling units that are clusters of items where reviewing the entire cluster is not acceptable (i.e., reviewing entire clusters would require significant additional effort to trace through the supporting records and documents).

d) The anticipated or potential errors are infrequent large errors.

H. Establish appropriate sample/strata sizes and sampling parameters. ***(Applies to nonstatistical and statistical sampling.)***

1. Nonstatistical (judgmental) samples.

a) Sample sizes for nonstatistical samples will depend on the type of audit, audit objective, and sample objective.

b) For Focused Assessment (FA) Pre-Assessment Survey (PAS), sample sizes will be 1 to 20 depending on the results of the initial risk exposure and internal control assessment as follows:

(1) Low risk exposure and strong internal controls = low end of 1 to 10 range.

(2) Low risk exposure and adequate internal controls = middle of 1 to 10 range.

(3) Low risk exposure and weak internal controls = high end of 1 to 10 range.

(4) Moderate risk exposure and strong internal controls = low end of 5 to 15 range.

(5) Moderate risk exposure and adequate internal controls = middle of 5 to 15 range.

(6) Moderate risk exposure and weak internal controls = high end of 5 to 15 range.

(7) High risk exposure and strong internal controls = low end of 10 to 20 range.

(8) High risk exposure and adequate internal controls = middle of 10 to 20 range.

(9) High risk exposure and weak internal controls = high end of 10 to 20 range.

c) For most other audits, nonstatistical sample sizes will generally be 100% of the review area. If the review area is much larger than a normal statistical sample size (60 to 100), then statistical sampling should be considered instead of nonstatistical sampling.

2. Attribute discovery samples.

a) Sample sizes for attribute discovery samples are determined by running EZ-Quant ATTDISC (DOS Version 3.10) or Attribute Sample Size Determination Procedure (Windows Version 1.0.1). The procedure will generally result in sample sizes within the range of 59 to 90, depending on the frame size and specified sampling parameters of critical error rate and government risk. The critical error rate is the maximum acceptable error rate in the universe. The government risk is the tolerable level of risk of accepting a faulty universe (one with an actual error rate exceeding the critical error rate).

(1) For circumstances where any systemic error results in noncompliance (e.g. FA Assessment Compliance Testing or Follow-up of transshipment or undeclared ADD/CVD), the appropriate parameters to use are 5% critical error rate and 1% government risk.

(2) For those instances when no errors are anticipated or errors result in penalties rather than revenue due (e.g., broker or bonded warehouse audits), the appropriate parameters to use are 5% critical error rate and 5% government risk.

b) Although the purpose of an attribute discovery sample is to determine if any error exists rather than estimate dollar impacts, there could be situations in which estimating dollar impacts based on the sample results is appropriate or necessary. A desired precision percentage under 100% and confidence level of 95% (same as for variable sampling) should be established for just such a possibility.

The desired precision percentage should be based on auditor judgment of what would be acceptable for the situation. The achieved precision percentage will be compared to the desired precision percentage when determining the acceptability of the projection.

3. Variable samples.

a) Variable sample sizes depend on the variability in the sampling frame. The more variability in the frame (dollars and characteristics), the larger the sample size required to achieve acceptable sample results. Minimum sample size guidelines (based on statistical principles) have been established to assist auditors in determining appropriate variable sample sizes.

(1) Physical unit samples.

(a) If the frame is homogenous, then the minimum sample required is 1 sample with 1 stratum of 60 items. A homogenous frame is one with low variability in dollars and characteristics (i.e. similar dollars and characteristics). Indicators of low dollar variability are low skewness, low standard deviation, low CV (< 50%) and no obvious dollar breaks or groupings. Low characteristic variability would be a frame with no obvious groupings by characteristics.

(b) If the frame is nonhomogenous, then the minimum sample required is 1 sample of 3 random strata plus 1 high dollar 100% review stratum. A nonhomogenous frame is one with high variability in dollars and characteristics (i.e. dissimilar dollars and characteristics). Indicators of high dollar variability are high skewness, high standard deviation, high CV (≥ 50%) and obvious dollar breaks or groupings. High characteristic variability would be a frame with obvious groupings by characteristics. The total sample size should be at least 100 items. Each random stratum should be at least 30 items, except when 30 items would be more than 5% of the items in the entire stratum. In that case, the stratum size can be 5% or 15 items, whichever is greater.

(c) Generally, the larger the total sample size and the more strata, the better the achieved precision will be.

(2) Dollar unit samples.

(a) If the frame is homogenous, then the minimum sample required is 1 sample of 100 units. A homogenous frame is one with low variability in dollars and characteristics (i.e. similar dollars and characteristics). Indicators of low dollar variability

are low skewness, low standard deviation, low CV (< 50%) and no obvious dollar breaks or groupings. Low characteristic variability would be a frame with no obvious groupings by characteristics.

(b) If the frame is nonhomogenous due to high dollar variability, then the minimum sample required is 1 sample of 100 units. Indicators of high dollar variability are high skewness, high standard deviation, high CV (≥ 50%) and obvious dollar breaks or groupings.

(c) If the frame is nonhomogenous due to high characteristic variability, then the minimum samples required are multiple samples of 60 units each (one for each characteristic grouping). High characteristic variability would be a frame with obvious groupings by characteristics. Physical unit sampling is usually better at handling high variability in characteristics. But if clusters are present which would be difficult to review in their entirety and if there only 2 or 3 major characteristic groupings, then dollar unit sampling may still be used.

(d) Generally, the larger the total sample size (or the more samples for characteristic variability), the better the achieved precision will be.

b) Sampling parameters for variable samples will be 95% confidence level and desired precision percentage < 100%. The desired precision percentage should be based on auditor judgment of what is acceptable for the situation. The achieved precision percentage will be compared to the desired precision percentage when determining the acceptability of the projection.

II. SELECT THE SAMPLE

A. Nonstatistical samples.

1. Since nonstatistical sampling is based on auditor judgment, any selection method appropriate for the circumstances may be used. The auditor should keep in mind the audit and sampling objectives when determining the best selection process.

2. Some common techniques are as follows:

   a) Purposive testing is a method that attempts to select sample items with known or suspected problems. This method would be appropriate for the FA PAS, which is a risk-based survey to find problems if they exist. The auditor would select the highest risk areas/items.

b) Cross-section testing is a method that selects sample items from all parts of the area being tested. A common technique is to designate a fixed percentage to test, such as 2%, and then select every nth item to reach the 2%. If this method employed a random start, it would actually be a statistical systematic interval selection. But often, items are just chosen haphazardly across the area being tested until the desired quantity is obtained. This method would be appropriate for FA PAS if there were no identified higher risk areas or items on which to focus

c) Large dollar testing is a method that selects the largest dollar items for review. Emphasis is placed on the materiality of the items selected. This could be appropriate for FA PAS if the higher dollar items are determined to be the highest risk items. However, keep in mind that a breakdown of internal controls is often more pronounced in the lower dollar items.

d) Block testing is a method that selects specific blocks of units. The blocks may be periods of time or consecutive groupings, such as all expense vouchers in June or all invoices with vendor names beginning with the letters M through P. This method would be appropriate for FA PAS only if the selected blocks represent the high risk areas/items.

e) Convenience testing is a method of selecting the most convenient sample items for review. The most readily available items are selected, without reason or randomness, simply because it is expedient. Records that are in storage, in the bottom or back of file drawers, not yet filed, or at another location are excluded when this type of testing is used. This method rarely reflects good auditor judgment, may be manipulated by the auditee, and is not recommended for any audit situation.

B. Attribute discovery and variable physical unit sampling.

1. The same selection methods may be used for both attribute discovery and variable physical unit sampling because both statistical sampling types select physical units for review.

2. The following are sample selection options:

a) EZ-Quant RANUM (DOS Version 3.10) or Random Numbers Generator (Windows Version 1.0.1) is a procedure that generates random numbers that can then be manually or electronically applied (using macros or mini-programs) to a frame to select the sample items. It is suitable for an electronic frame, a numbered printout or listing, or a numbered physical item frame. It could also be used with

a small unnumbered printout/listing or physical items frame, but the frame would have to be manually numbered before the sample items could be selected.

This procedure can be used for manually stratified physical unit samples. If obvious dollar breaks or characteristic breaks were identified during frame analysis, then RANUM may be run for each manually identified stratum to randomly select the sample items.

b) EZ-Quant RASEQ (DOS Version 3.10) or Random Number Sets Generator (Windows Version 1.0.1) is a procedure that generates sets of random numbers that can then be applied to a frame to select the sample items. It is suitable for an unnumbered printout/listing or an unnumbered physical item frame with a hierarchical structure. For example, the first number in the set would represent the page or drawer and the second number in the set would represent the line on the page or the file in the drawer. It can be used when stratification is not necessary, the frame is already stratified, or the frame can be stratified prior to sample selection.

c) EZ-Quant STRAT (DOS Version 3.10) or Physical Unit Sample Selection Procedure (Windows Version 1.0.1) is a procedure that can stratify (on dollars) and randomly select physical units. It is suitable for an electronic frame or a small printout/listing that can be typed into the program.

It can be used for attribute discovery sample selection by specifying 1 random stratum and no high dollar stratum/items.

For variable physical unit samples, the procedure will automatically sort and stratify the frame into equal dollar strata, and then randomly select sample items for each stratum. It works best with a frame that is highly variable in terms of dollars, but not in terms of characteristics. If obvious dollar breaks or characteristic breaks were identified during frame analysis, then EZ-Quant RANUM (Random Numbers Generator), may be used instead to randomly select sample items for each manually identified stratum.

d) Manual systematic interval selection is a procedure for manually selects every nth item with a random start. It should be considered when the only available frame is an unnumbered physical item frame and selecting every nth item would result in a better cross-section of items or would be easier and quicker than using RASEQ. The process is as follows:

(1) Estimate the frame size (if unknown). It is better to underestimate than overestimate.

(2) Compute the interval (frame size / desired sample size). Truncate the result to a whole number.

(3) Run EZ-Quant RANUM (Random Numbers Generator) to get a random start between 1 and the interval. The random start will be the first sample item.

(4) Add the interval to the random start to get the second sample item. Continue adding the interval to select the rest of the sample items.

(5) Do not automatically stop when the desired sample size is achieved. The process is not complete until the end of the frame is reached. To stop before the end of the universe would invalidate the statistical sample because every item would not have an equal chance of selection. The actual sample size may be slightly larger than the initial desired sample size.

(6) The sample may be properly expanded by removing the previously selected sample items from the frame and repeating the above steps (calculating a new interval, running EZ-Quant RANUM Random Numbers Generator to get a new random start, and selecting the additional items from the revised frame).

(7) The sample may be properly decreased by randomly (using EZ-Quant RANUM Random Numbers Generator) selecting items for removal from the entire sample. It would not be proper to merely disregard the last items selected. To do so would invalidate the statistical sample because every item would not have an equal chance of selection.

e) Other computer programs, such as Microsoft Access or SAS, may be used if the electronic frame is too large to fit into Microsoft Excel (for analysis, manual stratification, or application of random numbers) or too large to fit into EZ-Quant STRAT Physical Unit Sample Selection Procedure (for stratification and/or sample selection). Auditors should consult with a CAS if they encounter this situation.

C. Variable dollar unit sampling.

1. Dollar unit sampling is unique in that it randomly selects dollars instead of physical units. The selected dollars (dollar hits) are then tied to physical units which are reviewed.

2. The following selection methods may be used for dollar unit sampling:

a) EZ-Quant DUSSEL (DOS Version 3.10) or Dollar Unit Sample Selection Procedure (Windows Version 1.0.1) is an automated systematic interval selection procedure. It works with an electronic frame or a small printout/listing that can be typed into the program.

The procedure will identify the dollar hits, but if the sampling units are clusters, then the physical items associated with each dollar hit must be identified manually. This is done by calculating cumulative totals for the cluster items and then locating the item within the cluster that contains the dollar hit.

b) Manual systematic interval selection. This method manually selects every nth dollar with a random start. While it is possible for use with a printout or listing, it is generally not recommended for dollar unit sampling due to the amount of effort required to manually select the dollar hits.

c) Other computer programs, such as Microsoft Access or SAS, may be used if the electronic frame is too large to fit into Microsoft Excel (for analysis) or too large to fit into EZ-Quant DUSSEL Dollar Unit Sample Selection Procedure (for sample selection). Auditors should consult with a CAS if they encounter this situation.

III. DOCUMENT ALL ASPECTS OF THE SAMPLE PLANNING AND SELECTION

A. Audit documentation must fully and clearly document all aspects of the sampling that was used. This documentation must be prepared for each sample (nonstatistical and statistical) and must comply with audit documentation policies.

B. The following sample planning and selection items should be included for each sample:

1. A sampling plan that documents the sample planning and selection must be included. Standard sampling plan forms for this purpose are contained in Appendix IV. The sections labeled Sampling Application, Sampling Approach, Universe and Frame Information, and Sample Information pertain to sample planning and selection and should be completed at this point.

2. The sampling frame itself must be included as part of the audit documentation. Electronic frames can be directly incorporated into the automated working papers. If the frame is hard copy, it can be scanned in or maintained separately if too voluminous for scanning. If it is maintained separately, it should be properly explained and referenced in the automated documentation in accordance with audit documentation policies.

3. The procedures used to validate the sampling frame must be documented. Any analysis or file comparisons done in an attempt to validate the frame as an adequate representation of the intended universe must be adequately explained.

4. Analysis of the sampling frame variability must be thoroughly explained and documented. This would include the calculation of measures of central tendency and indices of dispersion (mean, median, mode, standard deviation, and coefficient of variation), the determination of any obvious dollar or characteristic groupings for manual stratification, and identification of special items for separate or no review. These analyses and the related conclusions must be fully and clearly presented.

5. The sample size and how it was determined must be included. For attribute discovery sampling, this would include the EZ-Quant ATTDISC Attribute Sample Size Determination Procedure output. For variable sampling, this may be a conclusion on the frame analysis documentation explaining the application of the sample size guidelines based on the frame variability.

6. The random selection methodology must be documented. This includes the random numbers or random procedure applied for statistical samples or the judgmental procedure and reasoning for nonstatistical samples. EZ-Quant output and its application to the frame (if used) must be included and explained.

7. The selected sample items themselves should be properly documented. This may be accomplished with the sample selection documentation and/or the sample review documentation.

8. Any other documentation produced during the sample planning and selection should be included as appropriate.

IV. REVIEW THE SAMPLE

A. Review each sample item.

1. Perform the review of each sample item based on the established criteria and audit program as required to achieve the audit and sampling objectives.

2. Use the standard RAMIS worksheet and add any additional columns required to perform and document the review.

B. Determine the cause of each error and whether it is systemic/ nonsystemic and recurring/nonrecurring.

1. The cause of the error is critical to understanding the nature of the problem and making appropriate recommendations. The nature of the error is also important for proper computation of compliance rates and projection of dollar impact.

2. Each error will be identified as systemic or nonsystemic AND recurring or nonrecurring for this purpose.

   a) Systemic errors are those caused by a deficiency in the system of internal controls. If the system is corrected or internal controls strengthened, the error should not recur. Clerical or human error (especially if such errors are repetitive) that occurred because there were no internal controls in place to try to prevent or catch such errors (i.e., training, supervision, written instructions, monitoring, checking, etc.) would also be systemic. Systemic errors are also recurring errors, even if only one is found, because they could recur due to the system deficiency. Only systemic errors are included in the determination of compliance.

   b) Nonsystemic errors are those not caused by any apparent weakness in internal controls. Typically these are occasional clerical or human errors that occurred despite adequate internal controls (i.e., training, supervision, written instructions, monitoring, checking, etc.). Nonsystemic errors may also be recurring if they display a pattern or trend that they are likely to recur. For example, repetitive clerical errors may be indicative of some sort of weakness in the internal controls, such as incompetent personnel, inadequate training, lack of supervision or monitoring, etc. The designation of systemic or nonsystemic is required for the determination of compliance. Only systemic errors are included in the computation of compliance rates. Nonsystemic errors are not used when calculating compliance rates

   c) Recurring errors are those that could recur in the frame from which the sample was taken. Typically these are systemic errors. They may also be nonsystemic errors that display a pattern or trend that they are likely to recur (e.g., repetitive clerical errors are recurring errors). The designation of recurring or nonrecurring is required for revenue projection. Only recurring errors are projected. Nonrecurring errors are not projected. However, nonrecurring errors should be added to the projected revenue loss when calculating total revenue loss.

   d) Nonrecurring errors are those that would not be expected to recur in the frame from which the sample was taken. Typically these are nonsystemic, isolated clerical or human errors that occurred despite adequate internal controls (i.e., training, supervision, written instructions, monitoring, checking, etc.). They could also be errors found outside the sampling frame. The designation of recurring or nonrecurring is required for revenue projection. Only recurring errors are projected. Nonrecurring errors are not projected. However, nonrecurring errors should be added to the projected revenue loss when calculating total revenue loss.

V. EVALUATE THE SAMPLE RESULTS

A. Calculate compliance, if applicable.

1. Compliance, when applicable (i.e. the determination of compliance is an audit/sampling objective), will generally be based on the value of systemic errors found in the sample. See Appendix IV of this document and FA Program Exhibit 3F for more guidance on how to compute compliance rates.

2. Remember that it is generally not appropriate to compute compliance rates based on the results of small nonstatistical samples.

B. Calculate the total revenue due.

1. Loss of revenue estimates should be based on the most accurate information available. Actual amounts, if known (e.g. 100% review was performed), would be the first choice. Otherwise, statistical projections or other reasonable means of estimating revenue due may be used.

2. Statistical projections.

   a) EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure may be used to project revenue due for attribute discovery and variable physical unit samples. The procedure projects the sample revenue due to the universe and provides reliability measures for evaluating that projection. It provides two point estimates (one for the ratio method and one for the difference method) along with associated precision dollars and confidence intervals based on the confidence level specified. The confidence level used will be 95%. The point estimate with the lowest precision percentage (precision dollars / point estimate) should be selected.

   b) EZ-Quant DUSAM Dollar Unit Sample Evaluation Procedure may be used to project revenue due for variable physical unit samples. The procedure projects the sample revenue due to the universe and provides reliability measures for evaluating that projection. It provides a point estimate along with associated precision dollars and confidence intervals based on the confidence level specified. The confidence level used will be 95%.

   c) Other computer programs, such as Microsoft Access or SAS, may be used to statistically project and evaluate statistical sample results if electronic files are too large for EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure or EZ-Quant DUSAM Dollar Unit Sample Evaluation Procedure. Auditors should consult with a CAS if they encounter this situation.

d) The achieved precision percentage (precision dollars / point estimate) should be compared to the desired precision percentage from the sampling plan when determining the acceptability of the point estimate. If the achieved precision percentage is ≤ the desired precision percentage, then the projection is acceptable. Otherwise, the sample methodology and sample errors must be reevaluated to determine the appropriate course of action. See the Sample Results – Duty Due section of the sampling plans in Appendix IV for various options.

3. Total revenue due should be compared to thresholds for referral for enforcement and referred as appropriate.

C. Calculate the total value impact.

1. The total value impact is needed for comparison to thresholds for referral for enforcement.

2. The total value impact is a manual ratio calculation projecting the value of the sample errors to the universe. See the Sample Results – Value Impact section of the sampling plans in Appendix IV for detailed calculations.

D. Determine the impact on other years or areas.

1. Auditors should consider the impact of their sample results on other universes, such as other years or areas.

2. Generally, projections of sample results should be limited to the universe from which the sample was drawn. Items examined in one universe may not be representative of other universes and projecting to other universes would not statistically defensible. However, auditors may express their opinion and make nonstatistical applications if they believe the results apply to another universe.

VI. DOCUMENT THE SAMPLE RESULTS EVALUATION

A. Audit documentation must fully and clearly document all aspects of the sampling that was used. This documentation must be prepared for each sample (nonstatistical and statistical) and must comply with audit documentation policies.

B. The following sample results evaluation items should be included for each sample:

1. A sampling plan that documents the sample results evaluation must be included. Standard sampling plan forms for this purpose are contained in Appendix IV. The sections labeled Sample Results – Errors, Sample

Results – Compliance, Sample Results – Duty Due, Sample Results – Value Impact, and Sample Results – Other Years/Areas pertain to sample results evaluation. These sections should be completed at this point.

2. The determination of compliance and how calculated.

3. The total revenue due and its method of calculation. This would include the EZ-Quant input and output if statistical projections are used.

4. The calculation and analysis of the resulting precision percentage and any actions taken for unacceptable precision must be included.

5. The total value impact, how calculated, comparison with thresholds for referral for enforcement, and referral for enforcement if applicable.

6. The impact on other years/areas and how determined.

7. Any other documentation produced during the sample results evaluation should be included as appropriate.

VII. REPORT THE SAMPLE RESULTS

A. A table of sampling information will be included in the audit report for each sample (nonstatistical and statistical) if the sample significantly supports the audit findings. The table will show the sample review area, frame description, sampling approach, why the sampling was chosen, frame size/value/duty, and sample size/value/duty. A table will be used for each statistical sample.

B. The tables will be used for all samples in the Assessment Compliance Testing phase of the Focused Assessment (FA). The tables will be used for the Pre-Assessment Survey (PAS) phase of the FA only if the sample in the PAS included the entire universe because the universe was small. Although sampling tables will not normally be included in PAS reports, the sampling plans in Appendix IV will be developed for all samples, including judgmental samples such as those taken in the PAS audit process and will be included in audit documentation. See Appendix IV for sampling plans and see Appendix V for examples of the tables for audit reports.

C. In addition, the audit reports should include any computed compliance rates and total revenue loss computed.

Sampling Methodology Diagrams

Audit Testing Methods

Macro Analysis
Appropriate Uses

Macro Analysis

Any high level analysis or testing not involving the review of individual items or transactions. This could include analysis of totals, trends, file comparisons, etc.

Focused Assessment (FA) Pre-Assessment Survey (PAS) – Preliminary Assessment of Risk (PAR)

An essential element of assessing risk See the FA PAS audit program for examples of macro risk analyses that can be applied using the Preliminary Assessment of Risk form.

FA PAS – Risk & Assessment Compliance Testing (ACT) Determinations

May be able to use macro analysis during the Risk/ACT Determination to quickly quantify compliance and/or revenue due (without further transaction testing).

FA ACT

May be able to use macro analysis during the ACT phase to quantify compliance and/or revenue due (without further transaction testing).

Follow Up

May be able to use macro analysis during follow up audits to verify CIP implementation or quantify compliance and/or revenue due (without detailed transaction testing).

Other

Can use macro analysis during any other audit when it will achieve the audit objectives without detailed transaction testing.

Nonstatistical Sampling
Appropriate Uses

Nonstatistical Sampling
(Judgmental Sampling)

Judgmental sampling is appropriate when statistical results are not needed and/or there is a high degree of certainty that a conclusion can be reached without further sampling, AND WHEN:

Survey

The purpose is to survey the area in order to determine the necessity for and extent of substantive testing (further transaction testing).

- **FA PAS**
- **Follow up**
- **Any other audit where a survey is appropriate to achieve the audit objectives.**

Known Problem Area

There is a desire to concentrate audit effort in a specific limited problem area revealed by a previous sample or other source of information.

- **FA ACT**
- **Follow up**
- **Any other audit where there is a specific limited problem area.**

Very Small Universe

The universe is very small and it would be quicker and easier to review all or most of the items in the universe.

- **FA ACT**
- **Follow up**
- **Any other audit where the universe is very small.**

Very Sensitive Area

The area is very sensitive and there is no room for error or exact results are needed so all of the items in the universe must be reviewed.

- **Fraud**
- **Any other very sensitive audit where there is no room for error or where exact results are needed.**

Nonstatistical Sampling
Sample Sizes

Nonstatistical Sampling
(Judgmental Sampling)

Nonstatistical sample sizes are generally small and will vary depending on the application and area being reviewed.

FA PAS

Sample sizes will be 1 to 20, depending on the results of the initial risk exposure and internal control assessment.

Low risk exposure and strong internal controls = low end of 1 to 10 range.

Low risk exposure and adequate internal controls = middle of 1 to 10 range.

Low risk exposure and weak internal controls = high end of 1 to 10 range.

Moderate risk exposure and strong internal controls = low end of 5 to 15 range.

Moderate risk exposure and adequate internal controls = middle of 5 to 15 range.

Moderate risk exposure and weak internal controls = high end of 5 to 15 range.

High risk exposure and strong internal controls = low end of 10 to 20 range.

High risk exposure and adequate internal controls = middle of 10 to 20 range.

High risk exposure and weak internal controls = high end of 10 to 20 range.

All Other Audits

Sample sizes will generally be 100% of the review area.

Judgmental sample sizes generally should not significantly exceed a normal statistical sample of 60 to 100.
If the area is much larger than that, then statistical sampling should be considered instead.

Nonstatistical Sampling
Common Selection Methods

Nonstatistical Sampling
(Judgmental Sampling)

Judgmental sampling is a process in which sample items are selected subjectively rather than statistically (i.e. randomly). It relies solely on auditor judgment to appropriately select sample items to accomplish the particular audit and sample objectives.

Cross Section Test

Items from all parts of an area are selected (e.g., 5% sampled by selecting every 10th item or by haphazardly selecting items). This is a good method when there is no knowledge of the area or when it is desirable to get broad representation.

Block Test

A specific section or "block" of items is selected for review (e.g., one month of transactions). This method has limited applicability and may not give a clear picture of the entire area. The results may not be applicable to untested blocks.

Purposive Test

Known or suspected problem items are selected (e.g., all items in the tooling account). This method efficiently focuses resources. Caution must be exercised to avoid overstating the problem when attempting to apply the results to untested areas.

Convenience Test

The easiest or most readily available items are selected (e.g., the items in the office file drawer). This method rarely reflects good audit judgment, can be manipulated by the auditee, and is not recommended.

Large Dollar Test

The largest dollar items are selected (e.g., all items over $100,000). Caution must be exercised when attempting to apply conclusions to untested smaller items. Breakdowns in internal controls are often more pronounced in the smaller dollar area.

Nonstatistical Sampling Evaluation Methods

Nonstatistical Sampling
(Judgmental Sampling)

Judgmental sampling, by definition, relies solely on auditor judgment to evaluate sample results. That is, statistical analysis is not used to evaluate judgmental sample results.

100% Reviews

When the judgmental sample represents 100% of the review area, then the sample results represent actual results for the review area.

If the review area represents only part of the entire area being evaluated/reported on, then the review area results must be analyzed within the context of the entire area under evaluation.

< 100% Reviews

When the judgmental sample does not represent 100% of the review area, then the sample results must be evaluated by the auditor to determine if the audit and sample objectives have been achieved and if an opinion on the review area can be expressed.

It is generally not appropriate to compute compliance rates or project dollar impacts (revenue or value) based on the results of small nonstatistical samples.

Statistical Sampling
Basic Categories

Statistical Sampling
(Probability Sampling)

Statistical sampling is an objective process for testing a limited number of transactions in order to draw a conclusion about a larger universe. It uses a sampling plan in such a way that the laws of probability can be used to make statements or generalizations about the universe.

Statistical sampling is appropriate when the universe is too large to review 100% and statistical results are needed (i.e. to statistically project the sample results to the universe).

Variable Sampling

Variable sampling is a form of substantive testing of dollars that is quantitative in nature and results in better estimates of amounts. Sample items are evaluated for error amounts or variables. Variable sampling answers the question “how much?”

Attribute Sampling

Attribute sampling is a form of compliance testing that is qualitative in nature, can be used to determine the rate of occurrence, and may result in system changes. Sample items are evaluated for compliance or attributes. Attribute sampling answers the question “how many?”

Variable Sampling Types

Variable Sampling

Variable sampling is a form of substantive testing that is quantitative in nature, can be used to determine the amount of variance, and may result in dollar impacts.

There are 2 basic types of variable sampling based on the sampling unit selected.

Physical Unit

Physical unit sampling is a type of variable sampling in which the sampling unit is defined as a physical item or transaction, with each physical item or transaction having an equal chance of selection (or determinable non-zero chance of selection in the case of stratification). Physical unit sampling directly selects physical units (items, transactions, etc.) for examination.

Dollar Unit

Dollar unit sampling is a type of variable sampling in which the sampling unit is defined as an individual dollar, with each dollar having an equal chance of selection. Dollar unit sampling selects individual dollars, which are then tied to physical units (items, transactions, etc.) that are examined.

Variable Sampling
Appropriate Uses

Variable Sampling

Variable sampling is appropriate for substantive testing when the objective is to determine the amount of variance and/or calculate dollar impacts (materiality compliance rates, revenue due, etc.).

FA ACT

Variable sampling is appropriate for the FA ACT phase because the purpose of proceeding to ACT is to determine the extent of compliance in terms of dollar materiality and/or to calculate revenue due. (Exceptions: transshipment; undeclared Anti-Dumping Duties/Counterveiling Duties - DD/CVD; and those cases where acro tests or judgmental sampling will meet the audit objectives.)

Follow Up

Variable sampling is appropriate for follow up audits when macro tests or judgmental sampling will not meet the audit objectives (e.g., the area is too large, the errors are too varied, a compliance rate is needed, etc.).

Drawback

Variable sampling is appropriate for drawback audits because the purpose is to determine the amount of noncompliant duty drawback (not payable to the claimant or due to Customs if already refunded to the importer in accelerated payments).

Other

Variable sampling would be appropriate for any other audit where the objective is substantive testing to determine variance amounts and calculate dollar impacts.

Physical Unit Sampling
Appropriate Uses

Physical Unit Sampling

As a type of variable sampling, physical unit sampling is appropriate for substantive testing when the objective is to determine the amount of variance and calculate dollar impacts (materiality compliance rates, revenue due, etc.).

It is appropriate in the same situations and audits where variable sampling is appropriate. Physical unit sampling works best WHEN:

Frame Format

- An electronic file, or
- A printout or listing, or
- Physical items.

Sampling Units

- No clusters, or
- Clusters and reviewing all items in a cluster is acceptable (i.e., it would not require significant additional effort).

Frame Variability

- Widely variable in terms of dollars (need to stratify horizontally) and/or
- Widely variable in terms of characteristics (need to stratify vertically).

Anticipated Errors

- Frequent errors, and
- Small errors.

Physical Unit Sampling
Minimum Sample Sizes

Physical Unit Sampling

Physical unit sample sizes depend on the variability of the sampling frame. The more variability in the sampling frame, the larger the sample size required to achieve acceptable sample results.

Minimum sample size guidelines (based on statistical principles) have been established to assist the auditors.

Homogenous Frame

A homogenous sampling frame (similar dollars and characteristics) with a coefficient of variation < 50% (standard deviation of frame / frame mean * 100) requires as a minimum:

1 sample with 1 random stratum of 60 items.

Nonhomogenous Frame

A nonhomogenous sampling frame (dissimilar dollars and/or characteristics) with a coefficient of variation ≥ 50% (standard deviation of frame / frame mean * 100) requires as a minimum:

1 sample with 3 random strata plus a 100% (e.g., high dollar) stratum.

The total sample size should be at least 100 items. Each random stratum should be at least 30 items except when 30 items would be more than 5% of the items in the entire stratum. In that case, the stratum size can be 5% or 15 items, whichever is greater.

Physical Unit Sampling Selection Methods

Physical Unit Sampling

Valid statistical methods require that each physical sampling unit (item or transaction) has an equal or determinable nonzero chance of selection and that each sampling unit is randomly selected.

EZ-Quant RANUM

(Random Numbers Generator)

A computer procedure that generates random numbers which can then be used to select sample items. It works with an electronic frame, a numbered printout or listing frame, or a numbered physical frame.

EZ-Quant 3.10 EZ-Quant 1.0.1

EZ-Quant RASEQ

(Random Number Sets Generator)

A computer procedure that generates sets of random numbers which can then be used to select sample items. It works with an unnumbered printout or listing, or an unnumbered physical frame.

EZ-Quant 3.10 EZ-Quant 1.0.1

EZ-Quant STRAT

(Physical Unit Sample Selection Procedure)

A computer procedure that automatically stratifies a universe into equal dollar strata and randomly selects sampling units in each stratum. It requires an electronic frame or small printout/listing that can be typed into the program.

EZ-Quant 3.10 EZ-Quant 1.0.1

Manual Systematic Interval

A manual selection method that selects every nth item by means of a fixed interval with a random start. It should only be used with an unnumbered physical frame when it would produce a better cross-section or would be quicker and easier than using RASEQ.

Other Computer Programs

Other programs, such as Microsoft Access or SAS, may be used if the electronic frame is too large to fit into Microsoft Excel (for analysis, manual stratification, or application of EZ-Quant RANUM) or too large to fit into EZ-Quant STRAT (for stratification and/or sample selection).

Physical Unit Sampling Evaluation Methods

Physical Unit Sampling

An essential phase of statistical sampling, including physical unit sampling, is the statistical evaluation of the sample results.

EZ-Quant SAMPL
(Physical Unit Sample Evaluation Procedure)

A computer procedure that projects the physical unit sample results to the universe and provides reliability measures for evaluating that projection.

The procedure provides two point estimates (one for the ratio method and one for the difference method) along with associated precision dollars and confidence intervals based on the confidence level specified. The point estimate with the lowest precision percentage (precision dollars / point estimate) should be selected and its precision percentage compared to the desired precision percentage from the sampling plan when determining the acceptability of the point estimate.

Sampling parameters should be 95% confidence level and < 100% precision percentage.

Other Computer Programs

Other computer programs, such as Microsoft Access or SAS, may be necessary to statistically project and evaluate the sample results if the electronic file is too large for EZ-Quant SAMPL.

Sampling parameters should be 95% confidence level and < 100% precision percentage.

Dollar Unit Sampling
Appropriate Uses

Dollar Unit Sampling

As a type of variable sampling, dollar unit sampling is appropriate for substantive testing when the objective is to determine the amount of variance and calculate dollar impacts (materiality compliance rates, revenue due, etc.).

It is appropriate in the same situations and audits where variable sampling is appropriate. Dollar unit sampling works best WHEN:

Frame Format

- An electronic file, or
- A small printout or listing that can be typed into EZ-Quant.

Sampling Units

- Clusters and reviewing all items in a cluster is not acceptable (i.e., it would require significant additional effort).

Frame Variability

- Not widely variable, or
- Widely variable in terms of dollars but not in terms of characteristics (especially if left skewed with many high dollar items and few low dollar items).

Anticipated Errors

- Infrequent errors, and
- Large errors.

Dollar Unit Sampling
Minimum Sample Sizes

Dollar Unit Sampling

Dollar unit sample sizes depend on the variability of the sampling frame. The more variability in the sampling frame, the larger the sample size or the more samples required to achieve acceptable sample results.

Minimum sample size guidelines (based on statistical principles) have been established to assist the auditors.

Homogenous Frame

A homogenous sampling frame (similar dollars and characteristics) with a coefficient of variation < 50% (standard deviation of frame / frame mean * 100) requires as a minimum:

1 sample of 60 items.

Nonhomogenous Frame
(High Dollar Variability)

A nonhomogenous sampling frame (dissimilar dollars) with a coefficient of variation ≥ 50% (standard deviation of frame / frame mean * 100) requires as a minimum:

1 sample of 100 items.

Nonhomogenous Frame
(High Characteristic Variability)

A nonhomogenous sampling frame (dissimilar characteristics) with a coefficient of variation >= 50% (standard deviation of frame / frame mean * 100) requires as a minimum:

Multiple samples of 60 items each (one sample for each characteristic group).

Dollar Unit Sampling Selection Methods

Dollar Unit Sampling

Valid statistical methods require that each sampling unit (i.e. dollar) has an equal chance of selection and that each sampling unit is randomly selected.

EZ-Quant DUSSEL
(Dollar Unit Sample Selection Procedure)

A computer procedure that automatically selects dollar units using a systematic interval method. It requires an electronic frame or small printout/listing that can be typed into the program.

Manual Systematic Interval

A manual selection method that selects every nth dollar by means of a fixed interval with a random start. While possible to use with a printout/listing frame, it is generally not recommended due to the amount of effort required to manually select the dollar hits.

Other Computer Programs

Other programs, such as Microsoft Access or SAS, may be used if the electronic frame too large to fit into Microsoft Excel (for analysis) or too large to fit into EZ-Quant DUSSEL (for sample selection).

Dollar Unit Sampling Evaluation Methods

Dollar Unit Sampling

An essential phase of statistical sampling, including dollar unit sampling, is the statistical evaluation of the sample results.

EZ-Quant DUSAM
(Dollar Unit Sample Evaluation Procedure)

A computer procedure that projects the dollar unit sample results to the universe and provides reliability measures for evaluating that projection.

The procedure provides a point estimate along with associated precision dollars and confidence intervals based on the confidence level specified. The achieved precision percentage (precision dollars / point estimate) should be compared to the desired precision percentage from the sampling plan when determining the acceptability of the point estimate.

Sampling parameters should be 95% confidence level and < 100% precision percentage.

Other Computer Programs

Other computer programs, such as Microsoft Access or SAS, may be necessary to statistically project and evaluate the sample results if the electronic file is too large for EZ-Quant DUSAM.

Sampling parameters should be 95% confidence level and < 100% precision percentage.

Attribute Discovery Sampling
Appropriate Uses

Attribute Discovery Sampling

Attribute discovery sampling is a special kind of attribute acceptance sampling where the occurrence of even a single error constitutes a failure of the universe.

Attribute discovery sampling is appropriate when the risk of erroneous rejection of a universe is immaterial, AND:

Any Systemic Error = Noncompliance

The area is sensitive and any systemic error would constitute noncompliance and/or potential fraud.

- **FA ACT Unacceptable Risk Areas of Transshipment and Undeclared ADD/CVD.**
- **Follow Up of Transshipment and Undeclared ADD/CVD.**

No Anticipated Errors and/or Errors Result in Penalties Rather then Revenue Due

No error is expected in the universe (a low risk universe).

- **Broker.**
- **Bonded Warehouse.**

Attribute Discovery Sampling
Sample Sizes

Attribute Discovery Sampling

Attribute discovery sample sizes will vary depending on the universe size and sampling parameters.

The larger the universe and the tighter the sampling parameters (the higher the confidence level, the lower the critical error rate, and the lower the government risk), the larger the required sample size.

EZ-Quant ATTDISC
(Attribute Sample Size Determination Procedure)

A computer procedure that calculates the sample size required to achieve the attribute sample objective based on the universe size and specified sampling parameters.

Sample sizes computed will generally be in the range of 59 to 90.

Sampling parameters when any systemic error results in noncompliance are 5% critical error rate and 1% government risk.

Sampling parameters when no errors are anticipated or errors result in penalties rather than revenue due e 5% critical error rate and 5% government risk

Attribute Discovery Sampling Selection Methods

Attribute Discovery Sampling

Valid statistical methods require that each sampling unit has an equal or determinable nonzero chance of selection and each sampling unit is randomly selected.

EZ-Quant RANUM

(Random Numbers Generator)

A computer procedure that generates random numbers which can then be used select sample items. It works with an electronic frame, a numbered printout or listing frame, or a numbered physical frame.

EZ-Quant RASEQ

(Random Number Sets Generator)

A computer procedure that generates sets of random numbers which can then be used to select sample items. It works with an unnumbered printout or listing, or an unnumbered physical frame.

EZ-Quant STRAT

(Physical Unit Sample Selection Procedure)

A physical unit sample selection computer procedure that may be used for attribute discovery sample selection by specifying 1 stratum and no high dollar stratum items. It requires an electronic frame or small printout/listing that can be typed into the program.

Manual Systematic Interval

A manual selection method that selects every nth item by means of a fixed interval with a random start. It should only be used with an unnumbered physical frame when it would produce a better cross-section or would be quicker and easier than using EZ-Quant RASEQ.

Other Computer Programs

Other programs, such as Microsoft Access or SAS, may be used if the electronic frame is too large to fit into Microsoft Excel (for application of EZ-Quant RANUM) or too large to fit into EZ-Quant STRAT (for sample selection).

Attribute Discovery Sampling Evaluation Methods

Attribute Discovery Sampling

The purpose of attribute discovery sampling is to determine if any error (usually systemic) exists in the universe. Any such sample error would result in a failed universe or determination of noncompliance.

EZ-Quant SAMPL

(Physical Unit Sample Evaluation Procedure)

Since attribute discovery samples are s lected using physical unit procedures, the EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure may be used to project dollar impacts (e.g., value or revenue) when applicable.

Sampling parameters should be 95% confidence level and < 100% precision percentage.

EZ-Quant ATTEVAL1

(Attribute Discovery Acceptance Sample Evaluation Procedure)

If it is necessary to estimate the total error rate in the universe, the EZ-Quant ATTEVAL1 attribute discovery acceptance sample evaluation procedure may be used for this purpose.

The confidence level when any systemic error results in noncompliance is 99%.

The confidence level when no errors are anticipated or errors result in penalties rather than revenue due is 95%.

Other Computer Programs

Other computer programs, such as Microsoft Access or SAS, may be necessary to statistically project and evaluate the sample results if the electronic file is too large for EZ-Quant SAMPL.

Sampling parameters should be 95% confidence level and < 100% precision percentage.

Focused Assessment (FA) Sampling Methodology Table

Audit Action	Sampling Objective	Audit Area	Sampling Frame	Sampling Units	Anticipated Errors	Type of Sampling	Minimum Sample Size	Sampling Parameters	Sample Selection Methods	Sample Evaluation Methods
FA PAS (Pre-Assessment Survey)	To take a survey in order to help determine: (1) the adequacy of internal controls, (2) whether the risk to Customs is acceptable or unacceptable, and (3) if additional testing (FA ACT) is necessary to ascertain the extent of compliance and/or to compute revenue loss.	Any review area.	Any.	Physical units (e.g., items, transactions, files, etc.).	Any.	Nonstatistical (Judgmental)	1 to 20, depending on the initial risk exposure and internal control assessment. Low risk exposure = 1 to 10 items (depending on if internal controls are strong, adequate or weak). Moderate risk exposure = 5 to 15 items (depending on if internal controls are strong, adequate or weak). High risk exposure = 10 to 20 items (depending on if internal controls are strong, adequate or weak).	N/A	Any method appropriate for the circumstances. Purposive selection recommended if possible.	Auditor judgment.

Focused Assessment (FA) Sampling Methodology Table

Audit Action	Sampling Objective	Audit Area	Sampling Frame	Sampling Units	Anticipated Errors	Type of Sampling	Minimum Sample Size	Sampling Parameters	Sample Selection Methods	Sample Evaluation Methods
FA ACT (Assessment Compliance Testing)	To review an identified unacceptable risk area (from FA PAS) in order to ascertain the extent of compliance and/or to compute revenue loss.	Any identified unacceptable risk area that is small enough to review in its entirety.	Any.	Physical units (e.g., items, transactions, files, etc.).	Any.	Nonstatistical (Judgmental)	100% of the identified unacceptable-risk area (generally not more than a typical statistical sample of 60 to 100).	N/A	All items are selected.	Actual results from 100% review.

Focused Assessment (FA) Sampling Methodology Table

Audit Action	Sampling Objective	Audit Area	Sampling Frame	Sampling Units	Anticipated Errors	Type of Sampling	Minimum Sample Size	Sampling Parameters	Sample Selection Methods	Sample Evaluation Methods
FA ACT	To review an identified unacceptable risk area (from FA PAS) in order to ascertain the extent of compliance and/or to compute revenue loss.	Any identified unacceptable risk area that is too large to review 100% (except transshipment and undeclared ADD/CVD).	Electronic file, printout or listing, physical items. Frame may be highly variable in terms of dollars and/or characteristics.	Individual physical units. Clusters of physical units and reviewing entire clusters is acceptable (e.g., clusters consist of small number of items or reviewing whole clusters does not require significant additional effort).	Many errors, including small errors.	Statistical Variable Physical Unit	Homogenous frame (similar dollars and characteristics) with coefficient of variation < 50% (standard deviation of the frame / frame mean * 100) = 1 sample with 1 random stratum of 60 items.	Confidence Level = 95%. Desired Precision < 100%.	EZ-Quant STRAT - Physical Unit Sample Selection Procedure. Provides automatic equal horizontal strata (dollar). Suitable for an electronic frame or a small printout/listing that can be typed in.	EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure.
									EZ-Quant RANUM - Random Numbers Generator. Generates random numbers. Suitable for an electronic frame, a numbered printout/listing, or a numbered physical item frame. Allows control of strata (horizontal/dollars or vertical/characteristics) .	
							Nonhomogenous frame (dissimilar dollars and/or characteristics) with coefficient of variation >= 50% (standard deviation of the frame / frame mean * 100) = 1 sample with 3 random strata of 30 items each plus 1 100% review stratum (e.g., high dollar items).		EZ-Quant RASEQ - Sets of Random Numbers Generator. Generates sets of random numbers. Suitable for unnumbered printout/listing, unnumbered physical item frame with a hierarchical structure. Okay when stratification is not necessary, the frame is already stratified, or the frame can be stratified prior to sample selection.	Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic file is too large for SAMPL.
									Manual Systematic Interval Selection. Suitable for an unnumbered physical item frame where selecting every nth item would result in a better cross-section of items or would be easier and quicker than using RASEQ.	
									Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic frame too large to fit into Microsoft Excel (for analysis, manual stratification, or application of EZ-Quant RANUM) or too large fit into STRAT (for stratification and/or sample selection).	
			Electronic file or small printout or listing. Frame is not highly variable in terms of characteristics but may be highly variable in terms of dollars.	Dollars representing clusters of physical units and reviewing entire clusters is not acceptable (e.g., clusters consist of many items and reviewing all would require significant additional effort).	Few, primarily large errors.	Statistical Variable Dollar Unit	Homogenous frame (similar dollars and characteristics) with coefficient of variation < 50% (standard deviation of the frame / frame mean * 100) = 1 sample of 60 items.	Confidence Level = 95%. Desired Precision < 100%.	EZ-Quant DUSSEL - Dollar Unit Sample Selection Procedure. Suitable for an electronic frame. (Manual systematic interval selection procedures are used to identify the dollar hit items within clusters.)	EZ-Quant DUSAM Dollar Unit Sample Evaluation Procedure.
							Nonhomogenous frame (dissimilar dollars) with coefficient of variation >= 50% (standard deviation of the frame / frame mean * 100) = 1 sample of 100 items. Nonhomogenous frame (characteristics) with coefficient of variation >= 50% (standard deviation of the frame / frame mean * 100) = multiple samples of 60 items each.		Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic frame too large to fit into Microsoft Excel (for analysis) or too large to fit into DUSSEL (for sample selection).	Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic file is too large for DUSAM.

Focused Assessment (FA) Sampling Methodology Table

Audit Action	Sampling Objective	Audit Area	Sampling Frame	Sampling Units	Anticipated Errors	Type of Sampling	Minimum Sample Size	Sampling Parameters	Sample Selection Methods	Sample Evaluation Methods
FA ACT	To review an identified sensitive unacceptable risk area (from FA PAS) in order to verify compliance (i.e., to determine if any systemic error exists) and to compute revenue loss if applicable/ appropriate.	Identified sensitive unacceptable risk areas of transshipment and undeclared ADD/CVD.	Any.	Physical units (e.g., items, transactions, files, etc.).	None.	Statistical Attribute Discovery	Generally 59 to 90, depending on the frame size. Determined by EZ-Quant ATTDISC - Discovery Acceptance Sample Size Procedure.	Confidence Level = 99%. Critical Error Rate = 5%. Government Risk = 1%.	EZ-Quant STRAT - Physical Unit Sample Selection Procedure. May be used for attribute discovery sampling by designating one stratum and no high dollar items.	EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure (if possible, for revenue estimation).
									EZ-Quant RANUM - Random Numbers Generator. Suitable for an electronic frame, a numbered printout/listing, or a numbered physical item frame.	
									EZ-Quant RASEQ - Sets of Random Numbers Generator. Suitable for unnumbered printout/listing, unnumbered physical item frame with a hierarchical structure.	Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic file is too large for SAMPL.
									Manual Systematic Interval Selection. Suitable for an unnumbered physical item frame where selecting every nth item would result in a better cross-section of items or would be easier and quicker than using RASEQ.	
									Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic frame too large to fit into Microsoft Excel (for application of EZ-Quant RANUM) or too large fit into STRAT (for sample selection).	

Focused Assessment (FA) Sampling Methodology Table

Audit Action	Sampling Objective	Audit Area	Sampling Frame	Sampling Units	Anticipated Errors	Type of Sampling	Minimum Sample Size	Sampling Parameters	Sample Selection Methods	Sample Evaluation Methods
Follow-Up	To review an identified unacceptable risk area (from FA PAS), noncompliant area (from FA ACT), and/or importer quantification of compliance/revenue (from FA PAS or FA ACT) in order to: (1) determine if the implemented CIP corrected the internal control deficiencies, (2) ascertain the extent of compliance and/or to compute revenue loss, (3) determine whether the risk to Customs is acceptable or unacceptable, and/or (4) verify any importer quantification of compliance/revenue.	Any identified unacceptable risk area or noncompliant area that is limited in scope and number.	Any.	Physical units (e.g., items, transactions, files, etc.).	Any.	Nonstatistical (Judgmental)	100% of the identified unacceptable risk or noncompliant area (generally not more than a typical statistical sample of 60 to 100) or a sample sufficient to verify internal control adequacy, compliance, and/or revenue due.	N/A	All items are selected or any selection method appropriate for the circumstances.	Actual results from 100% review or auditor judgment from judgmental sample.

Focused Assessment (FA) Sampling Methodology Table

Audit Action	Sampling Objective	Audit Area	Sampling Frame	Sampling Units	Anticipated Errors	Type of Sampling	Minimum Sample Size	Sampling Parameters	Sample Selection Methods	Sample Evaluation Methods
Follow-Up	To review an identified unacceptable risk area (from FA PAS), noncompliant area (from FA ACT), and/or importer quantification of compliance/revenue (from FA PAS or FA ACT) in order to: (1) determine if the implemented CIP corrected the internal control deficiencies, (2) ascertain the extent of compliance and/or to compute revenue loss, (3) determine whether the risk to Customs is acceptable or unacceptable, and/or (4) verify any importer quantification of compliance/ revenue.	Any identified unacceptable risk area or noncompliant area that is broad in scope and/or number (except transshipment and undeclared ADD/CVD).	Electronic file, printout or listing, physical items. Frame may be highly variable in terms of dollars and/or characteristics.	Individual physical units. Clusters of physical units and reviewing entire clusters is acceptable (e.g., clusters consist of small number of items or reviewing whole clusters does not require significant additional effort).	Many errors, including small errors.	Statistical Variable Physical Unit	Homogenous frame (dollars and characteristics) with coefficient of variation < 50% (standard deviation of the frame / frame mean * 100) = 1 sample with 1 random stratum of 60 items.	Confidence Level = 95%. Desired Precision < 100%.	EZ-Quant STRAT - Physical Unit Sample Selection Procedure. Provides automatic equal horizontal strata (dollar). Suitable for an electronic frame or a small printout/listing that can be typed in.	EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure.
									EZ-Quant RANUM - Random Numbers Generator. Suitable for an electronic frame, a numbered printout/listing, or a numbered physical item frame. Allows control of strata (horizontal/dollars or vertical/characteristics) .	
							Nonhomogenous frame (dollars and/or characteristics) with coefficient of variation >= 50% (standard deviation of the frame / frame mean * 100) = 1 sample with 3 random strata of 30 items each plus 1 100% review stratum (e.g., high dollar items).		EZ-Quant RASEQ - Sets of Random Numbers Generator. Suitable for unnumbered printout/listing, unnumbered physical item frame with a hierarchical structure. Okay when stratification is not necessary, the frame is already stratified, or the frame can be stratified prior to sample selection.	Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic file is too large for SAMPL.
									Manual Systematic Interval Selection. Suitable for an unnumbered physical item frame where selecting every nth item would result in a better cross-section of items or would be easier and quicker than using RASEQ.	
									Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic frame too large to fit into Microsoft Excel (for analysis, manual stratification, or application of EZ-Quant RANUM) or too large fit into STRAT (for stratification and/or sample selection).	
			Electronic file or small printout or listing. Frame is not highly variable in terms of characteristics but may be highly variable in terms of dollars.	Dollars representing clusters of physical units and reviewing entire clusters is not acceptable (e.g., clusters consist of many items and reviewing all would require significant additional effort).	Few, primarily large errors.	Statistical Variable Dollar Unit	Homogenous frame (dollars and characteristics) with coefficient of variation < 50% (standard deviation of the frame / frame mean * 100) = 1 sample of 60 items.	Confidence Level = 95%. Desired Precision < 100%.	EZ-Quant DUSSEL - Dollar Unit Sample Selection Procedure. Suitable for an electronic frame.	EZ-Quant DUSAM Dollar Unit Sample Evaluation Procedure.
							Nonhomogenous frame (dollars) with coefficient of variation >= 50% (standard deviation of the frame / frame mean * 100) = 1 sample of 100 items. Nonhomogenous frame (characteristics) with coefficient of variation >= 50% (standard deviation of the frame / frame mean * 100) = multiple samples of 60 items each.		Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic frame too large to fit into Microsoft Excel (for analysis) or too large to fit into DUSSEL (for sample selection).	

Focused Assessment (FA) Sampling Methodology Table

Audit Action	Sampling Objective	Audit Area	Sampling Frame	Sampling Units	Anticipated Errors	Type of Sampling	Minimum Sample Size	Sampling Parameters	Sample Selection Methods	Sample Evaluation Methods
Follow-Up	To review an identified unacceptable risk area (from FA PAS), noncompliant area (from FA ACT), and/or importer quantification of compliance/revenue (from FA PAS or FA ACT) in order to: (1) determine if the implemented CIP corrected the internal control deficiencies, (2) ascertain the extent of compliance and/or to compute revenue loss, (3) determine whether the risk to Customs is acceptable or unacceptable, and/or (4) verify any importer quantification of compliance/revenue.	Identified sensitive unacceptable risk areas or noncompliant areas of transshipment or undeclared ADD/CVD that are broad in scope and number.	Any.	Physical units (e.g., items, transactions, files, etc.).	None.	Statistical Attribute Discovery	Generally 59 to 90, depending on the frame size. Determined by EZ-Quant ATTDISC - Discovery Acceptance Sample Size Procedure.	Confidence Level = 99%. Critical Error Rate = 5%. Government Risk = 1%.	EZ-Quant STRAT - Physical Unit Sample Selection Procedure. May be used for attribute discovery sampling by designating one stratum and no high dollar items.	EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure (if possible, for revenue estimation).
									EZ-Quant RANUM - Random Numbers Generator. Suitable for an electronic frame, a numbered printout/listing, or a numbered physical item frame.	
									EZ-Quant RASEQ - Sets of Random Numbers Generator. Suitable for unnumbered printout/listing, unnumbered physical item frame with a hierarchical structure.	Other computer programs (e.g., Microsoft Access or SAS) may be used if the electronic file is too large for SAMPL.
									Manual Systematic Interval Selection. Suitable for an unnumbered physical item frame where selecting every nth item would result in a better cross-section of items or would be easier and quicker than using RASEQ.	
									Other programs (e.g., Microsoft Access or SAS) may be used if the electronic frame too large to fit into Microsoft Excel (for application of EZ-Quant RANUM) or too large fit into STRAT (for sample selection).	

Sampling Plans

Sampling Plan - Variable Physical Unit Sample

Sampling Application

AUDIT TYPE:	
REVIEW AREA:	
SAMPLING OBJECTIVE:	

Sampling Approach

Type of Sampling:	**Variable Physical Unit Sampling** (A type of variable sampling in which the sampling unit is an item or transaction. Variable sampling is a form of substantive testing that is quantitative in nature, can be used to determine the amount of variance, and may result in dollar impacts.)		
Why Used ? Check All That Apply:		Stratification is desired (for accuracy and/or targeting).	
		Clusters are present, but reviewing all items in a cluster or performing multi-stage sampling is acceptable.	
		An electronic universe is not available.	
		Many errors are expected (including small errors).	
		Other (explain):	
Confidence Level:	95%		
Desired Precision (< 100%):			

Universe and Frame Information

Universe Description:			
Frame Description:			
Frame Size:			
Frame Value:			
Frame Duty:			
Frame Validated?		Yes	
		No (explain):	

Frame Variability Analysis

Dollar Variability:	Mean (Average):		Median:		Mode:	
	Skewed Left (Mean < Median) or Right (Mean > Median)?		Standard Deviation (STDEVP):		Coefficient of Variation (CV = STDEVP / Mean * 100):	
	Dollar Variability of Frame High (High Skewness, High STDEVP, High CV >=50%) or Low (Low Skewness, Low STDEVP, Low CV < 50%?					
Characteristic Variability:	Are there evident categories of sampling units (characteristic groups) which would be expected to have similar types & frequency of errors? (Yes or No)					
	If yes, how many such characteristic groups are identified?					

Sampling Plans

Exhibit 6A
Appendix IV

Sample Information

Sampling Unit Description:	
Sample Size:	
Sample Size Method/Basis:	

Strata Details:	Description	Frame Size	Frame Value	Frame Duty	Sample Size	Sample Value	Sample Duty
100% Review Stratum:							
Random Stratum 1:							
Random Stratum 2:							
Random Stratum 3:							
Random Stratum 4:							
Random Stratum 5:							
Random Stratum 6:							
Random Stratum 7:							
Random Stratum 8:							
Totals:		0	$0	$0.00	0	$0	$0.00

Sample Selection Method:				
		EZ-Quant RANUM - Random Numbers Generator	Random Seed:	
		EZ-Quant RASEQ - Random Number Sets Generator	Random Seed:	
		EZ-Quant STRAT - Physical Unit Sample Selection Procedure	Random Seed:	
		Other:		

Sample Results - Errors

	Total Number	Total Value	Systemic Number	Systemic Value	Recurring Number	Recurring Value
Errors:						

Sampling Plans

Sample Results - Compliance

Actual Compliance Rate If Known:		
Compliance Based on Sample Results		
Absolute Value of All Systemic Errors on Randomly Selected Sample Items (Material Systemic Errors for Classification):	A1	
Absolute Value of All Systemic Errors on Judgmentally Selected or 100% Review Sample Items (Material Systemic Errors for Classification):	A2	
Total Sample Dollars:	B	
Total Frame Dollars:	C	
Total Trade Area Dollars:	D	
1% of Entered Value (for Value Only):	E	
Lessor of 1% of Entered Value or $10,000,000 (for Value Only):	F	

Area and Rule/Formula:	Noncompliant Amount	Total Noncompliant Amount for the Trade Area	Noncompliant Factor	Compliance Rate	Compliant? Y/N
Transshipment or Undeclared ADD/CVD. Any Systemic Error = Noncompliant.	N/A	N/A	N/A	N/A	
Value. If C = D (i.e., the frame represents the entire trade area) then (A1/B *C) + A2 = Noncompliant Amount. If Noncompliant Amount <= F, then Compliant. If Noncompliant Amount > F, then Not Compliant.		N/A	N/A	N/A	
Value. If C < D (i.e., the frame does not represent the entire trade area) then (A1 / B *C) + A2 = Noncompliant Amount for this sample only. Noncompliant Amount for this sample must be added to the Noncompliant Amounts for all other value samples to get the Total Noncompliant Amount for the Trade Area. If Total Noncompliant Amount for the Trade Area <= F, then Compliant. If Total Noncompliant Amount for the Trade Area > F, then Not Compliant.			N/A	N/A	
Other Areas. If C = D (i.e., the frame represents the entire trade area) then (A1 + A2) / B = Noncompliant Factor. 1 - Noncompliant Factor * 100 = Compliance Rate. If Compliance Rate >= 99%, then Compliant. If Compliance Rate < 99%, then Not Compliant.	N/A	N/A			
Other Areas. If C < D (i.e., the frame does not represent the entire trade area) then (A1 / B * C) + A2 = Noncompliant Amount for this sample only. Noncompliant Amount for this sample must be added to Noncompliant Amounts for all other samples to get Total Noncompliant Amount for the Trade Area. Total Noncompliant Amount for the Trade Area / D = Noncompliant Factor. 1 - Noncompliant Factor * 100 = Compliance Rate. If Compliance Rate >= 99%, then Compliant. If Compliance Rate < 99%, then Not Compliant.					

Sampling Plans

Sample Results - Revenue Due

Actual Total Revenue Due if Known (Refer to CEAR Process if > Referral Threshold):	

Revenue Impact Based on Sample Results (Duty or Other Projectable Revenue based on Sample Results)

Initial Projected Revenue Impact of Recurring Errors on Randomly Selected Sample Items from EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure (or Other Computer Program as Applicable).

	Precision Dollars	Initial Point Estimate	Precision Percentage (Precision Dollars/Point Estimate)	Lowest Precision % < Desired Precision %? (Y/N)
Ratio Method:				
Difference Method:				

If Desired Precision Not Met, Course of Action Taken?		Reanalyzed the projectability of the errors and accepted the initial point estimate.	
		Reanalyzed the projectability of the errors and computed revenue due on the sample errors only. Revenue due:	
		Reanalyzed the projectability of the errors, adjusted the errors, and reprojected. (Record results below.)	
		Post-audit stratified and reprojected. (Record results below.)	
		Expanded the sample and reprojected. (Record results below.)	
		Estimated the revenue due by other means. Revenue due:	

Adjusted Projected Revenue Impact of Recurring Errors on Randomly Selected Sample Items from EZ-Quant SAMPL Projection Program (or Other Computer Program as Applicable).

	Precision Dollars	Initial Point Estimate	Precision Percentage (Precision Dollars/Point Estimate)	Lowest Precision % < Desired Precision %? (Y/N)
Ratio Method:				
Difference Method:				

If Desired Precision Not Met, Course of Action Taken? (Check Action Taken.)		Reanalyzed the projectability of the errors and accepted the adjusted point estimate.	
		Reanalyzed the projectability of the errors and accepted the initial point estimate.	
		Reanalyzed the projectability of the errors and computed revenue due on the sample errors only. Revenue due:	
		Estimated the revenue due by other means. Revenue due:	

Summary of Revenue Due Based on Sample Results

Total Revenue Due for All Errors on Judgmentally Selected and 100% Review Sample Items :	
Total Revenue Due for All Recurring Errors on Randomly Selected Sample Items (From Projection or Other):	
Total Revenue Due for All Nonrecurring Errors on Randomly Selected Sample Items:	
Total Revenue Due for This Sample (Refer to CEAR Process if > Referral Threshold):	**$0.00**

Sampling Plans

Sample Results - Value Impact

Actual Total Value Impact If Known (Refer to CEAR Process if > Referral Threshold):		
Value Impact Based on Sample Results		
Absolute Value of All Recurring Errors on Randomly Selected Sample Items:	A1	
Absolute Value of All Nonrecurring Errors on Randomly Selected Sample Items and All Recurring Errors on Judgmentally Selected or 100% Review Sample Items:	A2	
Total Sample Dollars:	B	
Total Frame Dollars:	C	
Total Trade Area Dollars:	D	

Rule/Formula:	Value Impact for Sample	Total Value Impact for Trade Area	Total Value Impact for Trade Area > CEAR Process Referral Threshold? (Y/N. If Y, then Refer)
If C = D (i.e., the frame represents the entire trade area) then (A1 / B * C) + A2 = Total Value Impact.	N/A		
If C < D (i.e., the frame does not represent the entire trade area) then (A1 / B * C) + A2 = Value Impact for this sample only. Value Impact for this sample must be added to the Value Impact for all other samples to get the Total Value Impact for the Trade Area.			

Sample Results - Other Years/Areas

Are Other Years or Areas Outside the Sampling Frame Affected? Do the Sample Results Apply to Other Years or Areas Outside the Sampling Frame?		Yes (Determine how to calculate the revenue due and value impact for the other years/areas.)
		No

Sampling Plans

Sampling Plan - Variable Dollar Unit Sample

Sampling Application

AUDIT TYPE:	
REVIEW AREA:	
SAMPLING OBJECTIVE:	

Sampling Approach

Type of Sampling:	**Variable Dollar Unit Sampling** (A type of variable sampling in which the sampling unit is a dollar. Variable sampling is a form of substantive testing that is quantitative in nature, can be used to determine the amount of variance, and may result in dollar impacts.)	
Why Used ? Check All That Apply:	☐	Desire to emphasize higher dollars and stratification for any other purpose is not needed/desired.
	☐	Clusters are present, and reviewing all items in a cluster or performing multi-stage sampling is not acceptable.
	☐	An electronic universe is available.
	☐	Few errors are expected (primarily large errors).
	☐	Other (explain):
Confidence Level:	95%	
Desired Precision (< 100%):		

Universe and Frame Information

Universe Description:		
Frame Description:		
Frame Size:		
Frame Value:		
Frame Duty:		
Frame Validated?	☐	Yes
	☐	No (explain):

Frame Variability Analysis

Dollar Variability:	Mean (Average):		Median:		Mode:	
	Skewed Left (Mean < Median) or Right (Mean > Median)?		Standard Deviation (STDEVP):		Coefficient of Variation (CV = STDEVP / Mean * 100):	
	Dollar Variability of Frame High (High Skewness, High STDEVP, High CV >=50%) or Low (Low Skewness, Low STDEVP, Low CV < 50%?					
Characteristic Variability:	Are there evident categories of sampling units (characteristic groups) which would be expected to have similar types & frequency of errors? (Yes or No)					
	If yes, how many such characteristic groups are identified?					

Sampling Plans

Exhibit 6A
Appendix IV

Sample Information

Sampling Unit Description:	A Dollar						
Sample Size:							
Sample Size Method/Basis:							
Strata Details:	Description	Frame Size	Frame Value	Frame Duty	Sample Size	Sample Value	Sample Duty
100% Review Stratum:							
Random Stratum:							
Totals:		0	$0	$0.00	0	$0	$0.00
Sample Selection Method:	EZ-Quant DUSSEL - Dollar Unit Sample Selection Procedure					Random Seed:	
	Other:						

Sample Results - Errors

	Total Number	Total Value	Systemic Number	Systemic Value	Recurring Number	Recurring Value
Errors:						

Sampling Plans

Sample Results - Compliance

Actual Compliance Rate If Known:	

Compliance Based on Sample Results		
Absolute Value of All Systemic Errors on Randomly Selected Sample Items (Material Systemic Errors for Classification):	A1	
Absolute Value of All Systemic Errors on Judgmentally Selected or 100% Review Sample Items (Material Systemic Errors for Classification):	A2	
Total Sample Dollars:	B	
Total Frame Dollars:	C	
Total Trade Area Dollars:	D	
1% of Entered Value (for Value Only):	E	
Lessor of 1% of Entered Value or $10,000,000 (for Value Only):	F	

Area and Rule/Formula:	Noncompliant Amount	Total Noncompliant Amount for the Trade Area	Noncompliant Factor	Compliance Rate	Compliant? Y/N
Transshipment or Undeclared ADD/CVD. Any Systemic Error = Noncompliant.	N/A	N/A	N/A	N/A	
Value. If C = D (i.e., the frame represents the entire trade area) then (A1/B *C) + A2 = Noncompliant Amount. If Noncompliant Amount <= F, then Compliant. If Noncompliant Amount > F, then Not Compliant.		N/A	N/A	N/A	
Value. If C < D (i.e., the frame does not represent the entire trade area) then (A1 / B *C) + A2 = Noncompliant Amount for this sample only. Noncompliant Amount for this sample must be added to the Noncompliant Amounts for all other value samples to get the Total Noncompliant Amount for the Trade Area. If Total Noncompliant Amount for the Trade Area <= F, then Compliant. If Total Noncompliant Amount for the Trade Area > F, then Not Compliant.			N/A	N/A	
Other Areas. If C = D (i.e., the frame represents the entire trade area) then (A1 + A2) / B = Noncompliant Factor. 1 - Noncompliant Factor * 100 = Compliance Rate. If Compliance Rate >= 99%, then Compliant. If Compliance Rate < 99%, then Not Compliant.	N/A	N/A			
Other Areas. If C < D (i.e., the frame does not represent the entire trade area) then (A1 / B * C) + A2 = Noncompliant Amount for this sample only. Noncompliant Amount for this sample must be added to Noncompliant Amounts for all other samples to get Total Noncompliant Amount for the Trade Area. Total Noncompliant Amount for the Trade Area / D = Noncompliant Factor. 1 - Noncompliant Factor * 100 = Compliance Rate. If Compliance Rate >= 99%, then Compliant. If Compliance Rate < 99%, then Not Compliant.					

Sample Results - Revenue Due

Actual Total Revenue Due if Known (Refer to CEAR Process if > Referral Threshold):				
Revenue Impact Based on Sample Results (Duty or Other Projectable Revenue based on Sample Results)				
Initial Projected Revenue Impact of Recurring Errors on Randomly Selected Sample Items from EZ-Quant DUSAM Dollar Unit Sample Evaluation Procedure (or Other Compute Program as Applicable).				
	Precision Dollars	Initial Point Estimate	Precision Percentage (Precision Dollars/Point Estimate)	Lowest Precision % < Desired Precision %? (Y/N)
Precision Analysis:				
If Desired Precision Not Met, Course of Action Taken? (Check Action Taken.)		Reanalyzed the projectability of the errors and accepted the initial point estimate.		
		Reanalyzed the projectability of the errors and computed revenue due on the sample errors only. Revenue due:		
		Reanalyzed the projectability of the errors, adjusted the errors, and reprojected. (Record results below.)		
		Expanded the sample and reprojected. (Record results below.)		
		Estimated the revenue due by other means. Revenue due:		
Adjusted Projected Revenue Impact of Recurring Errors on Randomly Selected Sample Items from EZ-Quant DUSAM Projection Program (or Other Computer Program as Applicable).				
	Precision Dollars	Initial Point Estimate	Precision Percentage (Precision Dollars/Point Estimate)	Lowest Precision % < Desired Precision %? (Y/N)
Precision Analysis:				
If Desired Precision Not Met, Course of Action Taken?		Reanalyzed the projectability of the errors and accepted the adjusted point estimate.		
		Reanalyzed the projectability of the errors and accepted the initial point estimate.		
		Reanalyzed the projectability of the errors and computed revenue due on the sample errors only. Revenue due:		
		Estimated the revenue due by other means. Revenue due:		
Summary of Revenue Due Based on Sample Results				
Total Revenue Due for All Errors on Judgmentally Selected and 100% Review Sample Items :				
Total Revenue Due for All Recurring Errors on Randomly Selected Sample Items (From Projection or Other):				
Total Revenue Due for All Nonrecurring Errors on Randomly Selected Sample Items:				
Total Revenue Due for This Sample (Refer to CEAR Process if > Referral Threshold):				**$0.00**

Sampling Plans

Sample Results - Value Impact

Actual Total Value Impact If Known (Refer to CEAR Process if > Referral Threshold):		
Value Impact Based on Sample Results		
Absolute Value of All Recurring Errors on Randomly Selected Sample Items:	A1	
Absolute Value of All Nonrecurring Errors on Randomly Selected Sample Items and All Recurring Errors on Judgmentally Selected or 100% Review Sample Items:	A2	
Total Sample Dollars:	B	
Total Frame Dollars:	C	
Total Trade Area Dollars:	D	

Rule/Formula:	Value Impact for Sample	Total Value Impact for Trade Area	Total Value Impact for Trade Area > CEAR Process Referral Threshold? (Y/N. If Y, then Refer)
If C = D (i.e., the frame represents the entire trade area) then (A1 / B * C) + A2 = Total Value Impact.	N/A		
If C < D (i.e., the frame does not represent the entire trade area) then (A1 / B * C) + A2 = Value Impact for this sample only. Value Impact for this sample must be added to the Value Impact for all other samples to get the Total Value Impact for the Trade Area.			

Sample Results - Other Years/Areas

Are Other Years or Areas Outside the Sampling Frame Affected? Do the Sample Results Apply to Other Years or Areas Outside the Sampling Frame?		Yes (Determine how to calculate the revenue due and value impact for the other years/areas.)
		No

Sampling Plans

Sampling Plan - Attribute Discovery Sample

Sampling Application

AUDIT TYPE:	
REVIEW AREA:	
SAMPLING OBJECTIVE:	

Sampling Approach

Type of Sampling:	**Attribute Discovery Sampling** (A special case of attribute acceptance sampling where the occurrence of even a single error constitutes a failure of the universe. Attribute sampling is a form of compliance testing that is qualitative is nature, can be used to determine the rate of occurrence, and may result in system changes.)		
Why Used ?	The risk of erroneous rejection of a universe is irrelevant, the purpose is not to determine dollar compliance rates or project revenue, and (check those that apply):		
		The area is sensitive and any systemic error would constitute noncompliance (e.g. ADD/CVD, transshipment). [Use Set 1 Parameters below.]	
		No error is expected in the universe. [May use Set 2 Parameters below if only this reason applies.]	
		Other (explain):	
Sampling Parameters for Sample Size and Error Estimation if Applicable (Select the Set that Applies):			
Set 1:		Confidence Level = 99% Critical Error Rate = 5% Government Risk = 1%	
Set 2:		Confidence Level = 99% Critical Error Rate = 5% Government Risk = 1%	
Sampling Parameters for Dollar Estimation if Applicable:			
Confidence Level:	95%		
Desired Precision (< 100%):			

Universe and Frame Information

Universe Description:			
Frame Description:			
Frame Size:			
Frame Value:			
Frame Duty:			
Frame Validated?		Yes	
		No (explain):	

Sampling Plans

Exhibit 6A
Appendix IV

Sample Information				
Sampling Unit Description:				
Sample Size:				
Sample Value:				
Sample Duty:				
Sample Size Method/Basis:	EZ-Quant ATTDISC - Discovery Acceptance Sample Size Procedure			
Sample Selection Method:		EZ-Quant RANUM - Random Numbers Generator	Random Seed:	
		EZ-Quant RASEQ - Random Number Sets Generator	Random Seed:	
		Other:		

Sample Results - Errors						
	Total Number	Total Value	Systemic Number	Systemic Value	Recurring Number	Recurring Value
Errors:						

Sample Results - Compliance			
Compliant?			
Transshipment or Undeclared ADD/CVD (Any Systemic Error = Noncompliant):		Yes	
		No	
Other Area:		Yes. (Rate & Calculation):	
		No. (Rate & Calculation):	
		N/A (Explain):	

Sampling Plans

Sample Results - Revenue Due (If Applicable)

Actual Total Revenue Due if Known (Refer to CEAR Process if > Referral Threshold):	

Revenue Impact Based on Sample Results (Duty or Other Projectable Revenue based on Sample Results)

Initial Projected Revenue Impact of Recurring Errors on Randomly Selected Sample Items from EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure (or Other Computer Program as Applicable).

	Precision Dollars	Initial Point Estimate	Precision Percentage (Precision Dollars/Point Estimate)	Lowest Precision % < Desired Precision %? (Y/N)
Ratio Method:				
Difference Method:				

If Desired Precision Not Met, Course of Action Taken?		Reanalyzed the projectability of the errors and accepted the initial point estimate.	
		Reanalyzed the projectability of the errors and computed revenue due on the sample errors only. Revenue due:	
		Reanalyzed the projectability of the errors, adjusted the errors, and reprojected. (Record results below.)	
		Post-audit stratified and reprojected. (Record results below.)	
		Expanded the sample and reprojected. (Record results below.)	
		Estimated the revenue due by other means. Revenue due:	

Adjusted Projected Revenue Impact of Recurring Errors on Randomly Selected Sample Items from EZ-Quant SAMPL Projection Program (or Other Computer Program as Applicable).

	Precision Dollars	Adjusted Point Estimate	Precision Percentage (Precision Dollars/Point Estimate)	Lowest Precision % < Desired Precision %? (Y/N)
Ratio Method:				
Difference Method:				

If Desired Precision Not Met, Course of Action Taken? (Check Action Taken.)		Reanalyzed the projectability of the errors and accepted the adjusted point estimate.	
		Reanalyzed the projectability of the errors and accepted the initial point estimate.	
		Reanalyzed the projectability of the errors and computed revenue due on the sample errors only. Revenue due:	
		Estimated the revenue due by other means. Revenue due:	

Summary of Revenue Due Based on Sample Results

Total Revenue Due for All Errors on Judgmentally Selected and 100% Review Sample Items :	
Total Revenue Due for All Recurring Errors on Randomly Selected Sample Items (From Projection or Other):	
Total Revenue Due for All Nonrecurring Errors on Randomly Selected Sample Items:	
Total Revenue Due for This Sample (Refer to CEAR Process if > Referral Threshold):	**$0.00**

Sampling Plans

Sample Results - Value Impact

Actual Total Value Impact If Known (Refer to CEAR Process if > Referral Threshold):		
Value Impact Based on Sample Results		
Absolute Value of All Recurring Errors on Randomly Selected Sample Items:	A1	
Absolute Value of All Nonrecurring Errors on Randomly Selected Sample Items and All Recurring Errors on Judgmentally Selected or 100% Review Sample Items:	A2	
Total Sample Dollars:	B	
Total Frame Dollars:	C	
Total Trade Area Dollars:	D	

	Value Impact for Sample	Total Value Impact for Trade Area	Total Value Impact for Trade Area > CEAR Process Referral Threshold? (Y/N. If Y, then Refer)
If C = D (i.e., the frame represents the entire trade area) then (A1 / B * C) + A2 = Total Value Impact.	N/A		
If C < D (i.e., the frame does not represent the entire trade area) then (A1 / B * C) + A2 = Value Impact for this sample only. Value Impact for this sample must be added to the Value Impact for all other samples to get the Total Value Impact for the Trade Area.			

Sample Results - Error Rate (If Applicable)

Average Error Rate for the Frame (Number of Errors / Sample Size OR Point Estimate or Sample Occurrence Rate from EZ-Quant ATTEVAL1 Attribute Discovery Acceptance Sample Evaluation Procedure):	
Maximum Error Rate for the Frame (Upper Limit or Upper Precision Limit from EZ-Quant ATTEVAL1 Attribute Discovery Acceptance Sample Evaluation Procedure):	

Sample Results - Other Years/Areas

Are Other Years or Areas Outside the Sampling Frame Affected? Do the Sample Results Apply to Other Years or Areas Outside the Sampling Frame?		Yes (Determine how to calculate the revenue due and value impact for the other years/areas.)
		No

Sampling Plans

Sampling Plan - Nonstatistical (Judgmental) Sample

Sampling Application

AUDIT TYPE:	
REVIEW AREA:	
SAMPLING OBJECTIVE:	

Sampling Approach

Type of Sampling:	**Nonstatistical (Judgmental) Sampling** (Any selection procedure in which the test items are determined by judgment or other than random methods.)	
Why Used ? Check All That Apply:	Statistical results are not needed, there is a high degree of certainty that a conclusion can be drawn without further sampling, and (check those that apply):	
		The purpose is to take a survey in order to determine the necessity for and extent of substantive tests.
		There is a desire to concentrate audit effort in specific problem area revealed by a previous sample or other source of information.
		The universe is very small and it would be quicker and easier to review all or most of the items in the universe.
		The area is very sensitive and there is no room for error or exact results are needed so all of the items in the universe will be reviewed.

Universe and Frame Information

Universe Description:	
Frame Description:	
Frame Size:	
Frame Value:	
Frame Duty:	

Sampling Plans

Exhibit 6A
Appendix IV

Sample Information	
Sampling Unit Description:	
Sample Size:	
Sample Value:	
Sample Duty:	
Sample Selection Method & Reason:	
Example Sample Selection Methods:	**Purposive test -** units are selected based on known or suspected problems (e.g. units from accounts with suspect names are selected). Exercise caution to avoid overstating the problem by applying results to untested areas.
	Cross-section test - units from all parts of an area are selected (e.g. 5% to be sampled by selecting approximately every 10th item or by haphazardly selecting items here and there).
	Large dollar test - the largest dollar units are selected (e.g. the top 10 dollar value transactions). Exercise caution when attempting to apply conclusions to smaller dollar units. Also, keep in mind that the smaller dollar items are often a better indicator of weaknesses in controls and procedures.
	Block test - a specific section or block of units is selected for review (e.g. all transactions in a particular month). Exercise caution when applying conclusions to untested blocks.
	Convenience test - the most readily available units are selected (e.g. units in the auditee's office file drawers, rather than units in off-site storage). This method rarely reflects good auditor judgment, may be manipulated by the auditee, and is not recommended.

Sample Results - Errors						
	Total Number	Total Dollars	Systemic Number	Systemic Dollars	Recurring Number	Recurring Dollars
Errors:						

Sampling Plans

Sample Results - Compliance			
Compliant?			
100% Review Sample:		Yes. (Rate & Calculation):	
		No. (Rate & Calculation):	
< 100% Review Sample:		N/A because the purpose was not to calculate compliance. Comments:	
		Other. Explain:	

Sample Results - Revenue Due		
Revenue Due:		
How Calculated:		
Revenue Due > CEAR Process Referal Threshold?		Yes. (Refer to CEAR Process)
		No.

Sample Results - Value Impact		
Total Value Impact:		
How Calculated:		
Total Value Impact > CEAR Process Referal Threshold?		Yes. (Refer to CEAR Process)
		No.

Sample Results - Other Years/Areas		
Are Other Years or Areas Outside the Sampling Frame Affected? Do the Sample Results Apply to Other Years or Areas Outside the Sampling Frame?		Yes (Determine how to calculate the revenue due and value impact for the other years/areas.)
		No

Example Audit Report Tables

NOTE: These examples are designed to illustrate sample tables for Focused Assessment audits. These sample tables should be adjusted as appropriate and used in all audit reports when substantive testing is done.

Example for ACT:

Sample Design	
Area	Classification
Approach:	Judgmental Sampling
Why Chosen:	There is a desire to concentrate audit effort in a specific problem area revealed by a previous sample or other source of information. In addition, the sampling frame is very small and therefore, it is possible to review most of the frame value without statistical sampling. The sample results can be used to determine the level of compliance and amount of revenue loss.
Frame:	All ACS Entry Lines with High Risk Classifications for Fiscal Year Ended December 31, 2003
Frame Size:	132
Frame Value:	$11,895,002
Frame Duty:	$375,447
Sample Size:	101
Sample Value:	$10,755,954
Sample Duty:	$353,112

Example for Follow-up:

Sample Design	
Area	Classification
Approach:	Judgmental Sampling
Why Chosen:	There is a desire to concentrate audit effort in a specific problem area revealed by a previous sample or other source of information. In addition, the sampling frame is very small and therefore, it is possible to review the entire frame. The sample results can be used to determine the level of compliance and amount of revenue loss.
Frame:	All ACS Entry Lines with High Risk Classifications for the 6 Months Ended February 29, 2004 (the Period after CIP Implementation)
Frame Size:	63
Frame Value:	$5,852,334
Frame Duty:	$190,225
Sample Size:	63
Sample Value:	$5,852,334
Sample Duty:	$190,225

Example for ACT or Follow-up:

Sample Design	
Area	9802.00.80
Approach:	Variable Dollar Unit Sampling
Why Chosen:	The testing is substantive in nature and the sample results can be used to compute the level of compliance and project revenue loss.
Frame:	9802.00.80 ACS Entry Lines for Fiscal Year Ended December 31, 2003
Frame Size:	2,295
Frame Value:	$23,876,544
Frame Duty:	$0
Sample Size:	65
Sample Value:	$689,742
Sample Duty:	$0

Example for ACT or Follow-up:

Sample Designing Parameters	
Area	Classification
Approach:	Variable Physical Unit Sampling Stratified by Value (4 Strata)
Why Chosen:	The testing is substantive in nature and the sample results can be used to compute the level of compliance and project revenue loss.
Frame:	ACS Entry Lines for the Fiscal Year Ended December 31, 2003
Frame Size:	12,988
Frame Value:	$163,931,095
Frame Duty:	$7,165,083
Sample Size:	104
Sample Value:	$1,455,194
Sample Duty:	$64,721

Example for ACT or Follow-up:

Sample Design	
Area	ADD/CVD
Approach:	Attribute Discovery Sampling
Why Chosen:	The area is very sensitive and any error would constitute a failure of the universe. In addition, if errors exist, the sample results can be used to compute the level of compliance and project revenue loss.
Frame:	ACS Entry Lines With Merchandise Potentially Subject to ADD/CVD for the Fiscal Year Ended December 31, 2003
Frame Size:	3,794
Frame Value:	$48,982,005
Frame Duty:	$2,502,980
Sample Size:	89
Sample Value:	$1,182,721
Sample Duty:	$58,308

Example for ACT or Follow-up:

Sample Design	
Area:	Value
Approach:	Variable Physical Unit Sampling Stratified by Expense Account
Why Chosen:	The testing is substantive in nature and the sample results can be used to compute the level of compliance and project revenue loss.
Frame:	Selected General Ledger Expense Accounts
Stratum 1:	Design Samples Expense Account 92500
Stratum 1 Size:	1588
Stratum 1 Value:	$584,662
Sample 1 Size:	30
Sample 1 Value:	$13,405
Stratum 2:	Art Design Expense Account 92700
Stratum 2 Size:	1,390
Stratum 2 Value:	$3,087,712
Sample 2 Size:	45
Sample 2 Value:	$95,823
Stratum 3:	Tool Parts Expense Account 93100
Stratum 3 Size:	637
Stratum 3 Value:	$2,874,144
Sample 3 Size:	35
Sample 3 Value:	$162,426
Stratum 4:	Miscellaneous Expense Account 95500
Stratum 4 Size:	264
Stratum 4 Value:	$653,009
Sample 4 Size:	15
Sample 4 Value:	$37,591

Glossary of Sampling Terms

100% Review Stratum. A stratum of sample items that is selected based on auditor judgment rather than by random means. The purpose of this stratum is to ensure adequate coverage of high dollar and/or sensitive items. Unlike random strata, this stratum is not a subset of a portion of the frame and the audit results for this stratum are not projected.

Attribute Sampling. A type of statistical sampling used for compliance testing whereby sample items are evaluated for compliance or attributes. Items either are or are not (yes or no) in compliance. This type of sampling reaches a conclusion on the frequency of occurrence of a particular attribute in a universe.

Attribute Discovery Sampling. A special case of attribute sampling in which the occurrence of a single error constitutes a failure of the universe. This feature, which produces a sample size that is minimal in general, is achieved by ignoring any risk of erroneously rejecting an acceptable universe. This type of statistical sampling provides an objective method of indicating the risk or probability of locating at least one irregularity or characteristic in question.

Block Test. A nonstatistical method of selecting sample items (usually a judgmental or non-statistical sample) in which specific blocks of units are selected. The blocks may be periods of time or consecutive groupings, such as all expense vouchers in June or all invoices with vendor names beginning with the letters M through P.

Clerical Error. Human processing errors (e.g., transpositions, typo's, etc.). Internal controls should be designed to minimize and catch these (through training, supervision, monitoring, checking, etc.). Isolated clerical errors that slip through despite adequate internal controls designed to prevent and catch them would be nonsystemic, nonrecurring errors. Repetitive clerical errors would be considered to be recurring errors and may be indicative of internal control weaknesses (lack of controls or controls not being followed); in which case they would also be systemic errors.

Clusters. Sample items or units that are made up of clusters or groups of smaller items or units. For example, an ACS (Automated Commercial System) tariff line that is made up several invoice lines, or an invoice line that is made up of several part numbers.

Coefficient of Variation (CV). A measure of dollar dispersion or variability in a frame. It is standard deviation expressed as a percentage (i.e., standard deviation divided by the frame mean multiplied by 100). The higher the CV, the more variation in the frame. General rules of thumb: a CV < 50% indicates low variation and a CV ≥ 50% indicates moderate to high variation.

Confidence Interval (Precision Interval). The range within which the actual error/value in the frame should fall at a given confidence level or assurance. It is also known as tolerance.

Confidence Level. The probability that the true or actual value will be within the corresponding confidence interval. It is sometimes called reliability, assurance, or probability.

Convenience Test. A nonstatistical method of selecting sample items in which convenience is the prime consideration. The most readily available items are selected, without reason or randomness, simply because it is expedient. Records that are in storage, in the bottom of file drawers, not filed or at another location are excluded when this type of testing is used. This method rarely reflects good auditor judgment, can be manipulated by the auditee, and is not recommended.

Critical Error Rate. The maximum universe error rate considered acceptable by the auditor.

Cross-Section Test. A method of selecting sample items in which the auditor attempts to choose items from all parts of the area being tested. It is common under this type of testing to designate a fixed percentage, such as 5%, of items to be selected. Many times the selection is made using a fixed or uniform interval, such as every 10th item, for selection. If this method were used with a random start, the sample generally would meet the selection requirements of a statistical sample. However, it is not uncommon for the auditor, using the cross-section approach, to go through the records and haphazardly select items until the desired quantity is obtained.

Desired Precision (Desired Sampling Error). The amount of sampling error that can be tolerated and still permit the results to be useful.

Dollar Unit Sampling. A type of variable sampling in which the sampling unit is defined as an individual dollar, with each dollar given an equal chance of selection. The selected dollars are then tied to physical units (items or transactions) that are examined.

Error. A sample item in noncompliance with applicable testing criteria (i.e., laws and regulations).

EZ-Quant. A computer program containing statistical analysis audit tools with modules for statistical sampling, regression, and improvement curves. Auditors may use DOS-based Version 3.10 (which combines all modules) or Windows-based Version 1.0.1 (which separates the modules). The two versions do the same analyses, but have different user interfaces and menus for the same procedures.

EZ-Quant ATTDISC Attribute Discovery Sample Size Procedure. A computer procedure that determines sample sizes for attribute discovery samples. In EZ-Quant DOS Version 3.10, it is call ATTDISC. In EZ-Quant Windows Version 1.0.1, the procedure is selected by choosing Discovery Acceptance in the Attribute Sample Size Development window.

EZ-Quant ATTEVAL1 Attribute Discovery Acceptance Sample Evaluation Procedure. A computer procedure that evaluates the results of an attribute discovery sample by estimating the total error rate in the universe. In EZ-Quant DOS Version 3.10, it is called ATTEVAL1. In EZ-Quant Windows Version 1.0.1, the procedure is selected by choosing Discovery Acceptance, One Step Acceptance, or Rate Estimation in the Attribute Sample Evaluation window.

EZ-Quant DUSAM Dollar Unit Sample Evaluation Procedure. A computer procedure that evaluates the results of a dollar unit sample (i.e., projects the sample results to the frame and provides reliability measures for evaluating that projection). In EZ-Quant DOS Version 3.10, the procedure is called DUSAM. In EZ-Quant Windows Version 1.0.1, the procedure is selected by choosing Variable Sampling and Dollar Unit Sample Evaluation in the initial EZ-Quant window.

EZ-Quant DUSSEL Dollar Unit Sample Selection. A computer procedure that statistically selects dollar unit samples. In EZ-Quant DOS Version 3.10, the procedure is call DUSSEL. In EZ-Quant Windows Version 1.0.1, the procedure is selected by choosing Variable Sampling and Dollar Unit Sample Selection in the initial EZ-Quant window.

EZ-Quant RANUM Random Numbers Generator. A computer procedure that generates random numbers that can then be used to randomly select sample items. In EZ-Quant DOS Version 3.10, the procedure is called RANUM. In EZ-Quant Windows Version 1.0.1, the procedure is selected by choosing Variable Sampling and Generate Random Number/Sets in the initial EZ-Quant window.

EZ-Quant RASEQ Random Number Sets Generator. A computer that generates sets of random numbers that can then be used to randomly select sample items. In EZ-Quant DOS Version 3.10, the procedure is called RASEQ. In EZ-Quant Windows Version 1.0.1, the procedure is selected by choosing Variable Sampling and Generate Random Number/Sets in the initial EZ-Quant window.

EZ-Quant SAMPL Physical Unit Sample Evaluation Procedure. A computer procedure that evaluates the results of a physical unit sample (i.e., projects the sample results to the frame and provides reliability measures for evaluating that projection). In EZ-Quant DOS Version 3.10, the procedure is called SAMPL. In EZ-Quant Windows Version 1.0.1, the procedure is selected by choosing Variable Sampling and Physical Unit Sample Evaluation in the initial EZ-Quant window.

EZ-Quant STRAT Physical Unit Sample Selection Procedure. A computer procedure that statistically selects physical unit samples and can automatically stratify a frame into equal dollar strata (the number of strata is specified by the auditor). In EZ-Quant DOS Version 3.10, the procedure is called STRAT. In EZ-Quant Windows Version 1.0.1, the procedure is selected by choosing Variable Sampling and Physical Unit Sample Selection in the initial EZ-Quant window.

Frame (Sampling Frame). A physical or electronic representation of the universe from which a sample will be taken. The sampling frame excludes sample items that are separated or stratified for 100% examination.

Frame Validation. The process of verifying that the chosen sampling frame is an adequate representation of that universe it is intended to represent. This typically involves reconciling the frame to the universe, analyzing any differences, and correcting, adjusting, or accepting those differences.

Frame Variability (Homogeneity). Refers to the degree of differences or similarities of items in a frame in terms of dollar amounts and characteristics. Dollar variability can be measured with indices of dispersion (e.g., standard deviation and coefficient of variation). The degree of variability in the frame will directly impact the sample size and need for stratification. The higher the variability, the larger the sample size should be and the greater the need for stratification.

Government Risk (Risk). The tolerable level of risk of accepting a faulty universe (a universe with an actual error rate exceeding the critical error rate). The government bears this risk of a failure to detect flawed conditions. Risk is the complement of confidence level (probability or assurance).

Horizontal Stratification. Stratifying or separating a frame into subgroups according to dollar values or amounts. The idea is that similar size items will have similar size errors. Horizontal stratification improves sample results (i.e. precision).

Judgmental (Non-statistical) Sampling. See Nonstatistical (Judgmental) Sampling.

Large Dollar Test. A nonstatistical method of selecting sample items in which the largest dollar items are selected. Emphasis is placed on the materiality of the items selected. No examination is made of lesser dollar value items. Conclusions based on the review of the high dollar items may not be applicable to the lesser dollar items. Also, a breakdown of internal controls is generally more pronounced in the lower dollar items.

Macro Analysis. Any high level analysis not involving the review of individual items or transactions (not sampling). Typically this could include analysis of totals, trends, file comparisons, etc. Macro analysis is a key part of assessing risk exposure but may also be used anytime it will satisfy the audit objectives. It is often more efficient and may be more precise than sampling (micro testing) and therefore should be considered first.

Manual Systematic Interval. The manual application of a statistical sample selection procedure using a random start and a fixed interval to select every nth item.

Micro Testing. Review of individual items or transactions (sampling), usually in order to make conclusions about the population from which they are drawn.

Multistage Sampling. A sampling process involving several stages, in which units at each subsequent stage are subsampled from previously selected larger units. For example: in the first stage, 100 ACS tariff lines are selected, and in the second stage, up to 5 invoice lines are selected for each ACS tariff line. This type of sampling is considerably more complex (in selection and evaluation) than simple or single stage sampling and therefore, is recommended only as a last resort.

Nonrecurring Error. An error that would not be expected to recur in the frame from which the sample was taken. Typically these are nonsystemic, isolated clerical or human errors that occurred despite adequate internal controls (monitoring, checking, training, supervision, etc.). They may also be errors found outside the sampling frame. The designation of recurring or nonrecurring is required for revenue projection. Only recurring errors are projected. Nonrecurring errors are not projected. However, nonrecurring errors should be added to the projected revenue loss when calculating total revenue loss.

Nonstatistical Projection. A nonstatistical extrapolation of the sample results to the universe, which cannot be evaluated statistically. Evaluating a sample for the purpose of reaching a conclusion about the universe without using the laws of probability.

Nonstatistical (Judgmental) Sampling. Any sampling process in which the sample items are selected subjectively rather than by a random process.

Nonsystemic Error. An error that is not caused by any apparent weakness in internal controls. Typically these are occasional clerical or human errors that happen despite adequate internal controls (monitoring, checking, training, supervision, etc.). Repetitive clerical errors may be indicative of some sort of weakness in the internal controls, such as incompetent personnel, inadequate training, lack of supervision or monitoring, etc. The designation of systemic or nonsystemic is required for the determination of compliance. Only systemic errors are included in the computation of compliance rates. Nonsystemic errors are not used when calculating compliance rates.

Physical Unit Sampling. A type of variable sampling in which the sampling unit is defined as a physical unit (item or transaction), with each physical unit having an equal chance of selection (or determinable nonzero chance in the case of stratification).

Point Estimate. A single, specific estimate for a universe characteristic or value.

Population (Universe). See Universe (Population).

Post Audit Stratification. Stratifying the sample and frame after the review is complete and projecting "like to like" in order to produce more accurate projections.

Precision (Sampling Error). A measurement of the accuracy of the sample estimate compared to the universe value. It is the magnitude of error or variation in an estimate derived from a random sample. Because the units included in the sample are there by chance, the estimate is subject to chance variation or sampling error. It is a measure of the accuracy of the point estimate determined by how close it is likely to be to the true error or value in the universe. The point estimate plus and minus the precision provides the confidence interval.

Precision Dollars. Precision (sampling error) expressed in dollars (as in a variable sample).

Precision Percentage. Precision expressed as a percentage. For attribute samples, it is the difference between the upper or lower limit and the point estimate. For variable samples, it is the precision divided by the point estimate.

Projection. See Statistical Projection or Nonstatistical Projection.

Purposive Test. A nonstatistical method of selecting sample items in which items with known or suspected problems are selected. This method is not designed to give a cross section of the entire audit area.

Random Seed. An arbitrarily assigned number that activates the random number selection process in a program that generates random numbers or selects random sample items. Using the identical random seed with the same frame allows one to recreate the random numbers or random sample selection. It prevents duplications when additional sample items are needed from the same frame.

Random Stratum. A stratum of sample items that are selected randomly. This stratum is a subset of a portion of the frame and the audit results for this stratum are projected.

Recurring Error. An error that could recur in the frame from which the sample was taken. Typically these are systemic errors. They may also be nonsystemic errors that display a pattern or trend that they are likely to recur (e.g., repetitive clerical errors are recurring errors). The designation of recurring or nonrecurring is required for revenue projection. Only recurring errors are projected. Nonrecurring errors are not projected. However, nonrecurring errors should be added to the projected revenue loss when calculating total revenue loss.

Sample Frame or Sampling Frame. See Frame.

Sample Universe or Sampling Universe. See Universe (Population).

Sampling Error. See Precision (Sampling Error).

Sampling Parameters. Commonly, refers to the basic sampling methodology facts (i.e., sampling approach, frame size, frame value, frame duty, sample size, sample value, and sample duty). Statistically, refers to the mathematical variables used to statistically calculate sample size and evaluate sample results (i.e., confidence level, desired precision percentage, critical error rate, government risk, precision dollars, achieved precision percentage).

Sampling Plan. A document that outlines the detailed sampling methodology to be used and results obtained. It typically contains elements of the sampling approach, universe and frame, sample size and selection, and projection results.

Sampling Unit. The elementary unit in the frame, which is sampled or selected for detailed examination. Valid statistical sampling requires that each sampling unit have an equal chance of selection (or determinable nonzero chance in the case of stratification) and be selected randomly.

Standard Deviation. A measure of the dollar dispersion or variability in a frame. It is the average distance of individual values or the extent to which the individual values depart from the average. In Microsoft Excel, it is the function STDEVP.

Statistical Projection. A statistical extrapolation of the sample results to the frame. It uses the laws of probability to evaluate a sample for the purpose of reaching a conclusion about the universe. A statistical projection gives a point estimate along with the confidence level (reliability, assurance, probability), precision (sampling error), and confidence interval (tolerance, precision interval).

Statistical Sampling (Probability Sampling). Sampling that uses the laws of probability for selecting and evaluating a sample for the purpose of reaching a conclusion about the universe. In statistical sampling each sampling unit is randomly selected and has an equal or known nonzero probability of selection.

Strata. Two or more mutually exclusive subgroups of a frame. The plural of stratum.

Stratum. One of the two or more mutually exclusive subgroups of a frame. The singular of strata.

Stratification. Separating a frame into different subgroups for separate selection, review, and projection of sample items. The goal is to group like items together (e.g. by dollar value, size, category, characteristic, or type), in order to improve sample results (precision).

Stratified Sampling. A statistical sampling technique in which the frame is divided into distinct subgroups of similar items, called strata. Within each stratum, a separate sample is selected from all the sampling units in that stratum. From the sample obtained in each stratum, a separate stratum mean (or other statistic) is computed. These stratum values are properly weighted to form a combined estimate for the entire frame. The standard deviations are also computed separately within each stratum and then properly weighted and added into a combined estimate for the frame. In this way, sampling precision is improved.

Substantive Testing. Quantitative testing such as verifying account balances or cost elements and noting any differences. Variable sampling is appropriate for this type of testing whereby sample items are evaluated for error amounts or variables.

Survey (Probe) Sample. A limited preliminary sample of an area for the purpose of gaining additional information about the area in order to determine whether more extensive testing is needed.

Systematic Interval. A statistical sample selection procedure that uses a random start and a fixed interval to select every nth item.

Systemic Error. An error that could recur due to a system deficiency or a weakness in internal controls. If the system is corrected or internal controls strengthened, the error should not recur. Clerical or human error (especially if such errors are repetitive) that occurred because there were no internal controls in place to prevent or catch such errors (i.e., no monitoring or checking, no supervision, no training, etc.) would also be systemic. The designation of systemic or nonsystemic is required for the determination of compliance. Only systemic errors are included in the computation of compliance rates. Nonsystemic errors are not used when calculating compliance rates.

Universe (Population). An entire group of items/transactions/records to be tested. The items comprising the category or area of interest to the auditor.

Variable Sampling. A type of statistical sampling used for substantive testing whereby sample items are evaluated for error amounts or variables. This type of sampling reaches a conclusion on dollar amounts in a universe and answers the question – how much?

Variable Dollar Unit Sampling. See Dollar Unit Sampling.

Variable Physical Unit Sampling. See Physical Unit Sampling.

Vertical Stratification. Stratifying or separating a frame into subgroups according to category, type, or characteristics of the sampling units. The idea is that similar items will have similar types and frequency of errors. The purpose is to improve sample results (i.e. precision).

Reading List for Audit Sampling

"Statistical Auditing" by Donald Roberts

"Handbook of Sampling for Auditing and Accounting" by Herbert Arkin

"Practical Statistical Sampling for Auditors" by Arthur J. Wilburn

"Sampling Methods for the Auditor, An Advanced Treatment" by Herbert Arkin

"Using Statistical Sampling", General Accounting Office/Program Evaluation & Methodology Division (GAO/PEMD-10.1.6)

"Statistical Methods" by George W. Snedecor and William G. Cochran