

ROLE OF CUSTOMS AUDIT IN THE TRADE FACILITATION PROCESS

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1. Introduction

Living in the current global economic conditions, the socioeconomic well-being of each country is strongly influenced by the customs activities. Globalization has influenced the changes in customs procedures and inspection processes. Customs are engaged not only in the control, breach prevention and administration of duties and taxes, but also carry out the broader tasks, such as security assurance, simplification of trade conditions and protection of the economic interests of the countries.

Nowadays the role of customs seeking to facilitate legitimate trade and to introduce the simplified customs procedures is growing. Globalisation as well as rapidly changing business models and technical progress are presenting new challenges to the effectiveness and efficiency of the customs activities. It is also influenced international trade, the volume of which depends on the efficiency of logistical operations - from the modelling and management of the logistics process, helping to control the flow of goods crossing national borders. The process of the worldwide transportation of goods is very long and complicated. After analysing the flow of goods, it can be stated that a long time required for the customs procedures can be named as one of the international trade's barriers.

It may be noted that there are not a lot of researches in the scientific literature analysing the matters of customs procedures. Therefore, the focus was made on the analysis of the legal acts regulating the provisions of the global trade liberalization and the security of the international supply network. It is important to point out that until 1990 there was almost no information concerning the aspects of the supply network, and the lack of the information concerning the solutions helping to overcome the logistical barriers that inevitably arise during the international trade process. Customs procedures and time required for the inspection - are extremely serious logistical barriers for the enterprises. Later the number of researches in this area has grown rapidly [Whipple, Gentry, 2000; Ellram et al., 2002; Halachimi, 2002; Gutierrez, Hintsa, 2006; Saiz, Bas, Rodriguez, 2007; Morgan, 2007; Bento, White, 2010].

After analysing the works of scientists from different countries on the topics of the audit, it is clear that theoretical and practical aspects of the audit have been analysed by a number of Lithuanian scientists as well as other

scientists from around the world. However, failed to find the works analysing the subject of the customs audit - both foreign and Lithuanian researchers did not investigate this subject in their works. As a result, the uncharted territory of the customs audit's activities and the absence of its conception create a problem that must be solved. The research problem is often being formulated by the question about the research phenomena and their interactions. It is often being caused by the contradictions appearing in the development of any process or phenomenon. The question-problem of this paper could be formulated as follows: what is a customs audit and what role it plays in trade facilitation? In order to solve this problem and to analyse the ongoing changes in the business environment the attention of researchers and practitioners must be concentrated. Research aim is to identify the role and place of the customs audit in the trade facilitation process. In order to achieve the aim of this paper the analysis and sistematisation of the scientific literature and legal acts, the data analysis and the comparison were combined.

2. International trade and customs control

In the European Union customs deal with the policy of duties of the international trade. They are also responsible for the efficient security of the EU financial interests. The global trading system is not secured against the terrorism which can cause a serious damage to the global economy. Being a part of the governmental organisations that monitor and manage a cross-border movement of goods, customs administrations appear in a unique position, as they ensure an increased security of the global supply network as well as contribute to the social and economic development through the revenue collection and the trade facilitation. With the growth of the international terrorism and the increased threats of the weapons, counterfeit and pirated goods as well as hazardous materials to enter the country and thus endanger the international trade and public security, customs are confronted with new challenges. EU customs authorities are to fulfil the basic strategic objectives, focusing on five key areas: 1) a defence of the public and the EU's financial interests, 2) a competitiveness of European enterprises, 3) a facilitation of the legitimate trade, 4) a control of the supply network, 5) a cooperation of the customs and other governmental institutions with business enterprises [*Customs strategic guidelines, 2008*].

The main strategic objective of Lithuanian customs is a defence of the market and the society in the field of the foreign trade while implementing the policy of European Community's taxes and trade. To achieve this objective, one of the main challenges is to implement measures related to the safety and security of the international trade supply and to prevent the terrorism, smuggling, organised crime and other criminalities. The focus is made on the application of the audit-based control measures in order to overcome the

logistical barriers that inevitably arise during the process of the international trade.

International trade has increased and manufacturing has become more global, with developing, emerging and transition economies connecting with international supply and value chains in terms of both their exports and imports. The worldwide distribution and sourcing cycles, along with just-in-time and just-in-sequence logistics services and the emergence of e-business, has created pressure on governments to ensure efficient, fast and reliable border crossing and clearance procedures. Governments started to realize that their export economies heavily depend on efficient import processing, hence the need to have a holistic approach for a more efficient management of end-to-end trade transactions. Lack of transparency about rules and regulations, redundant and lengthy clearance processes, and multiple documents requirements in different formats and with different data elements, increase the costs and time of doing trade. Today these obstacles are seen as posing greater barriers to trade. It is more important than ever to achieve trade facilitation to enhance administrative efficiency and effectiveness, reduce costs and time to markets, and increase predictability in global trade.

The primary goal of trade facilitation is to help make trade across borders (imports and exports) faster, and cheaper and more predictable, whilst ensuring its safety and security. Simplification is the process of eliminating all unnecessary elements and duplications in trade formalities, processes and procedures. Trade facilitation has to encompass the entire trade environment, actors and processes involved in a transaction. A supply chain embraces all activities necessary for goods to be produced and delivered to the final consumer. Such activities include sourcing of raw materials, preparing for transport, requesting an import license, preparing documentation for customs clearance, clearance, payment, and delivery to the consumer. As a minimum, a supply chain involves two parties, the seller and the buyer. In reality, a supply chain involves many different parties.

There are many variants of supply chains. The Buy-Ship-Pay Model (BSP) developed by UN/CEFACT is an example of such a model [Fig. 1]. It presents the supply chain as a sequence of business processes that can be grouped into the high-level domains of Buy, Ship and Pay. For each domain, the model presents key activities, such as the activity “insure cargo” for the step “prepare for export” of the Ship domain. The model can be used in various ways, for example to gain understanding of the processes and actors involved, to identify the impact of given trade facilitation initiatives and instruments.

Trade facilitation has to take place at three levels: at the national, regional and international level. While at the regional and international level standards and agreements are developed and agreed, the operational

implementation of trade facilitation measures including these standards, takes place at the national level.

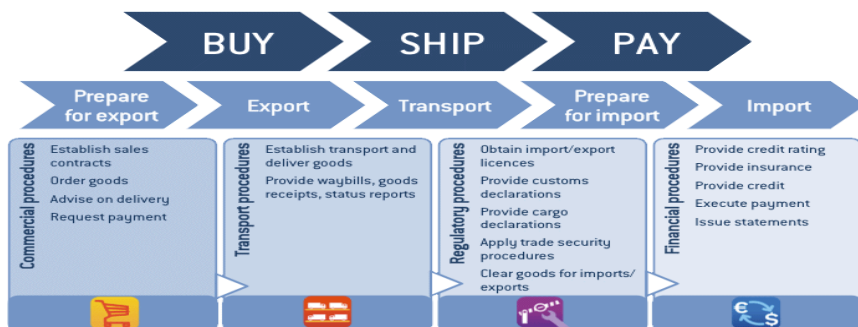


Fig.1. The UN/CEFACT Buy Ship Pay Model

Source: BUY-SHIP-PAY Modeling Guidelines, 2008.

Many trade facilitation measures require a reform and modernization process that depends on an enabling environment, which is built upon strong political support and professional program management and change management capabilities.

3. Overview of the customs audit process

Nowadays the rapidly growing international trade as well as new technologies of the production and transport require the goods to be delivered to the recipient exactly at the time when they are needed. For this reason, customs formalities must be carried out as quickly as possible, without disturbing the flow of goods and at the same time not reducing the efficiency of the customs control. The customs are involved in the procedures of the international trade regulation control. Therefore, inconvenient or inflexible customs procedures have a negative impact on the business competitiveness. While improving their work, customs contribute to the strengthening of the European Union business enterprises' competitiveness in the world markets at the same time imposing resources to the very place they are needed. Here, the important role played audit-based customs control. The increase in customs audit activities should coincide with a commensurate decrease in border controls, based on an adequate risk assessment, it may be considered to reduce the number of staff in ports and border posts and to increase staff in customs audit teams. Customs audit focuses on persons involved in the international movement of goods. It is an effective tool for customs control because it provides a clear and comprehensive picture of the transactions relevant to customs as reflected in the books and records of international

traders. At the same time it enables customs administrations to offer the trader facilitation measures in the form of simplified procedures.

The customs audit is of a great importance in the process of the customs inspection. The control based on the methods of the customs audit assures better opportunities of anti-breaches. Moreover, a faster flow of goods traffic at the external border of the European Union is assured while carrying out the most inspections at the companies' residences. Therefore, it is important to improve the customs audit combining this process with the changing business environment. This also has to do with the ongoing market processes. Recently, the customs of the EU countries began appreciating the activities of the business enterprises, seeking to gain the status of the authorised economic operator (AEO). In order to implement this, the need of the exploration of business enterprises activities' evaluation appeared, at the same time paying attention to the aspects of the international trade supply network.

The legal framework of customs audit is being regulated by of the Community Customs Code [1992]. The accomplished comprehensive analysis of scientific and practical literature helped to identify the customs audit and its place in the audit system. Customs audit is defined as a process, allowing customs officials to qualify the following entities: 1) checking the information correctness of customs declarations, entity's accounting documents and registers, business systems and all the commercial documents being of a great importance to the customs – documents belonging to companies (individuals) and that are directly or indirectly related to the activities carried out during customs procedures, 2) determining the agreement with certain criteria. The main objectives of the customs audit are the following: 1) to check the data accuracy and comprehensiveness indicated in the customs declarations, 2) to define the breaches – on the basis of which duties and other taxes are being counted - and errors of the data in the documents provided by the importers and exporters as well as other persons accepting the customs obligations, 3) to evaluate the entities' activities and compliance with the requirements.

Customs audit process consists of 5 stages: planning and selection, preparation, realization, execution and review (Fig. 2). The objectives of the preparatory process is to identify and analyze specific risk areas of the audittee's systems and to draft a specific audit plan that includes audit scope, methods and assignment of auditor/team members. The selection of persons/companies for audit should be based on risk profiles. Audits should generally be conducted for compliance verification purposes in the areas of valuation, origin, tariff classification, duty relief/ drawback/remission programmes, etc., but other areas should be targeted as necessary. Audit planning should take place every year, taking into account the availability of the auditor or audit team, in relation to work in progress and the start of new audits. Each audit area could be assigned standard hours of completion and

each available auditor or audit team hour could be calculated in order to determine how many audits can be performed by each auditor or audit team in a given year. Customs audit places great emphasis on professionalism in the conduct of a review and the examination of the auditees' books and records. From pre-audit planning to completion, it is essential to maintain communication and co-ordination with the auditee and with other interested parties in customs. A report should be produced to ensure that all findings and other relevant issues are fully shared and discussed. Follow-up visits may be needed.

Comparing all the types of the audit it is clear that the customs audit has many features in common with other types of the audit. There is a special correlation between the customs audit and financial, operational as well as management audit. The customs audit having common features with other types of the audit has also its own differences; its different goal has its own special features. Customs procedures, goods' customs value, goods' classification, origin and other things can become the inspected areas of business enterprises' activities and the items to be assessed.

The customs audit can be regarded as an interim/pre-audit or an audit passing the goods away after customs execution. Under the competitive market's conditions, it is important to evaluate the business enterprises' activities. One of the key tools here is the customs audit, giving an opportunity to identify the efficiency, economy, effectiveness and continuity of business activities. The assessment of the enterprises' activities can also be referred to the interim audit. During this assessment the enterprise submits an application to customs asking for receiving the AEO (*Authorised Economic Operator*) status and the AEO certificate.

Customs conducted process of the business enterprises activities' assessment has a number of procedural aspects arising from the activity's particularity. The assessment of business enterprises' activities in EU customs is carried out taking into consideration the issuing/non-issuing of the AEO status – when the customs audit assesses the activities of the economic operator and its compliance with the established criteria. In most cases the main problem related to the activities' assessment, lies in the identification of the appropriate activities assessment's indicators. After analysing the models of the business activities' evaluation, it has been found out that the majority of them include the enterprises strategy's aspects. Therefore, in order to carry out the evaluation of the activities, the organization's mission, policies and objectives should be combined [Kaplan, Norton, 2004; Pongatichat, Johnston, 2008]. It has also been found out that today's models of the business activities' assessment are characterised by the fact that the activities' assessment includes not only traditional business activities assessment's indicators but also the assessment of the entire supply network and inter-operational procedures.

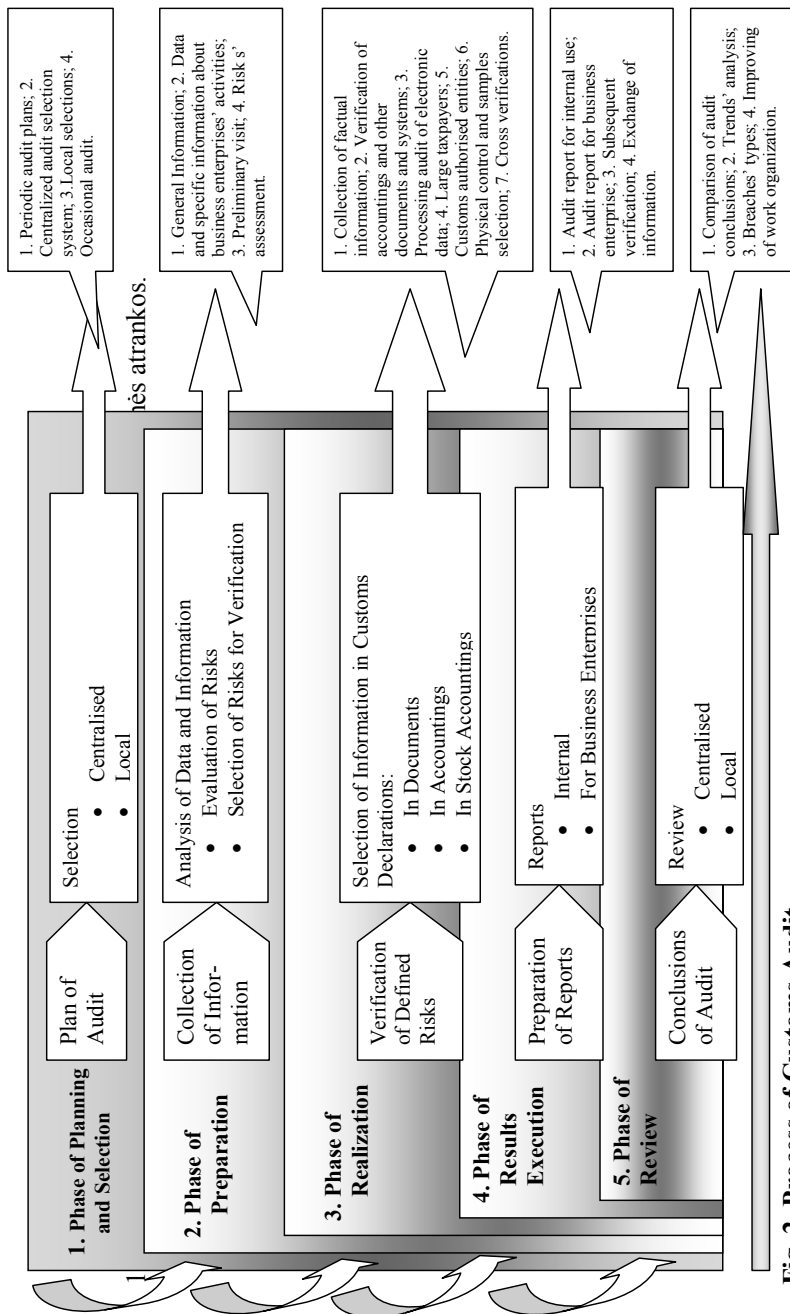


Fig. 2. Process of Customs Audit
Source: compiled by the author

The supply network is influenced by a broad set of environmental factors. That is why, this assessment area is quite tricky and complicated, requiring a broad understanding of the importance of a global context.

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