

**United States Customs Service**

**Audit of U.S. Customs Service's  
Air Automated Manifest System**

**OIG-01-024**

**December 6, 2000**



**Office of Inspector General**

**United States Department of the Treasury**



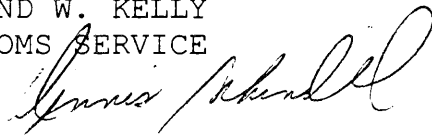
OFFICE OF  
INSPECTOR GENERAL

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

December 6, 2000

MEMORANDUM FOR COMMISSIONER RAYMOND W. KELLY  
UNITED STATES CUSTOMS SERVICE

FROM: Dennis S. Schindel   
Assistant Inspector General for Audit

SUBJECT: Audit of U.S. Customs Service's Air Automated  
Manifest System

This memorandum transmits the subject final report on the Office of Inspector General's (OIG) audit of the Customs Service's Air Automated Manifest System (Air AMS).

In summary, the OIG believes Customs needs to improve its controls over Air AMS to mitigate the risks to the integrity of its cargo processing systems. The Air AMS can be used to circumvent Customs inspection and avoid duties, tariffs, quota and import restrictions on merchandise entering the United States. OIG estimates merchandise manifested on over 3,000 air waybills in Fiscal Year (FY) 1998 was released into commerce without evidence of entry and Customs inspection or release. Customs could have assessed over \$6.5 million in fines and penalties for violations of 19 CFR on those waybills.

Customs recognizes Air AMS is not user friendly and that its utility has been compromised. However, it does not have adequate controls to detect or prevent system misuse, maintain data integrity, or enforce its expectations on system users. A third of the air waybills reviewed in the audit contained incorrect information, far beyond Customs' tolerance levels. OIG estimates over \$184 million in fines and penalties could have been assessed for waybills entered incorrectly into the Air AMS during FY 1998. Because of the risk to Customs' enforcement and revenue collection efforts, the OIG believes that the problems with Air AMS collectively constitute a material weakness in Customs management controls as defined in Office of Management and Budget Circular A-123, *Management Accountability and Control*.

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Customs concurred with all recommendations in this report and has taken or plans to take action that will address the issues surrounding those recommendations. Customs' responses have been incorporated into the report and included in its entirety as Appendix 11.

Please be advised that it is our intent to record potential revenue enhancements of \$136,918 in the Inventory, Tracking and Closure system (ITC) upon issuance of this report relating to fines and penalties Customs assessed as a result of the audit. The related recommendation is identified in Appendix 10 of the report. We will also include the potential revenue enhancement amount in the OIG Semiannual Report to the Congress. Customs management will be responsible for recording the amount of revenue actually collected for these assessments into the ITC.

We appreciate the courtesies and cooperation provided to our staff during the audit. If you wish to discuss this report, you may contact me at (202) 927-5400 or a member of your staff may contact Benny W. Lee, Regional Inspector General for Audit (San Francisco), at (415) 977-8810 extension 222.

Attachment

cc: William Keefer, Assistant Commissioner  
Office of Internal Affairs  
U.S. Customs Service

Brenda Brockman, Office of Planning  
U.S. Customs Service

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# EXECUTIVE DIGEST

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## Overview

The U.S. Customs Service (Customs) needs to improve its controls over the Air Automated Manifest System (Air AMS) to mitigate the risks to the integrity of its cargo processing systems. The Air AMS can be used to circumvent Customs inspection and avoid duties, tariffs, as well as quota and import restrictions on merchandise entering the United States (U.S). Based on a statistical sample of air waybills reviewed, the Office of Inspector General (OIG) estimated merchandise manifested on over 3,000 air waybills in Fiscal Year (FY) 1998 was released into commerce without evidence of entry and Customs inspection or release. Customs could have assessed over \$6.5 million in fines and penalties for violations of 19 CFR on those waybills. The full effect on Customs' enforcement and revenue collection efforts is unknown.

In addition, a third of the air waybills reviewed by the OIG contained incorrect information, far beyond Customs' tolerance levels. Customs recognizes Air AMS is not user friendly and its utility has been compromised, but does not have adequate controls to prevent or detect system misuse, maintain data integrity or enforce its expectations on system users. OIG estimated over \$184 million in fines and penalties could have been assessed for inputting incorrect waybill information into the Air AMS during FY 1998.

Because of the risk to Customs' enforcement and revenue collection efforts, the OIG believes the problems with Air AMS collectively constitute a material weakness in Customs' management controls as defined in the Office of Management and Budget's (OMB) Circular A-123, *Management Accountability and Control*.

## Objective, Scope And Methodology

The audit objectives were to determine: (1) if Air AMS allowed merchandise to enter United States commerce without entry and Customs inspection or release as required by 19 CFR; and (2) if so, the impact on Customs enforcement and revenue collection efforts.

The audit focused on merchandise that arrived in the U.S. in FY 1998 on an AMS-participating air carrier and was transferred to a non-participating Container Freight Station (CFS). The fieldwork was conducted between September 1998 and October 1999 at Customs':

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## EXECUTIVE DIGEST

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(1) Headquarters in Washington, DC; (2) Office of Information and Technology (OIT) in Newington, Virginia; and (3) offices at 6 airports.

The OIG used a computer-assisted auditing tool developed by Customs to identify its audit universe and select a sample of waybills for 7 randomly selected days in FY 1998. Random sampling was based on an expected confidence interval of 95 percent, a precision of  $\pm 5$  percent and a pValue of 50 percent. Based on the sample results, OIG estimated the waybills in the universe lacking evidence of entry, inspection and release as well as the related fines and penalties. Because OIG focused on the system, the sample size was not sufficient to detect patterns or practices of improper or illegal activities by interested parties of the merchandise. (See Page 5)

### Detailed Audit Results

Customs' cargo manifesting and entry processes were paper-driven and labor intensive until international trade exploded and automation became necessary. Customs implemented its Automated Commercial System (ACS) in the mid-1980's and eventually developed sub-systems to automate the manifesting process at airports and seaports. These subsystems are known as Sea and Air Automated Manifest Systems.

Air AMS was to standardize communications between Customs and the trade, streamline the manifesting process and facilitate reconciliation of information in air waybills with that in entry documents. In doing so, Customs hoped to enhance its release of merchandise while meeting its contraband interdiction, trade enforcement and revenue collection responsibilities.

Air AMS allows the trade to electronically notify Customs of an aircraft's pending arrival and transmit air waybill information for the merchandise onboard. Because Air AMS is part of ACS, Customs can "inspect" merchandise by reviewing information in ACS or by physically inspecting the merchandise. Either method meets the regulatory requirement that Customs inspect all merchandise entering commerce.

The ability to electronically inspect merchandise allows Customs opportunity to better use its personnel. In turn, it permits quicker transfer of merchandise off the busy tarmac into a CFS resulting in reduced airport congestion, faster release of merchandise and lower handling costs. (See Page 1)

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## EXECUTIVE DIGEST

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### **Lack Of AMS Participation Presents Risks**

Although Customs expected to fully automate its manifesting process by 1996, Air AMS participation as of September 30, 1998, consisted of only 56 carriers and 127 CFS' operating at 29 airports in the U.S. Only about 13 percent of the CFS' participated in Air AMS. (See Page 2)

The Air AMS system works best in a total electronic environment; i.e., when carriers and CFS' participate in Air AMS and when importers and brokers participate in Automated Broker Interface (ABI) in ACS. In such an environment, waybill and entry information is in the system when carriers electronically request transfer of merchandise to a CFS. ACS will match waybill information in AMS to entry information in ACS and approve the transfer without further Customs involvement.

However, when CFS' do not participate in Air AMS, the process becomes paper-driven and labor intensive. This is especially so if brokers or importers do not electronically submit entry documents. In such an environment, entry information is not always available when carriers request transfer of the merchandise because entry documents are generally filed after merchandise has been transferred.

In order for the system to approve the transfer, Customs must "trick" the system into thinking waybill and entry information have been matched or reconciled. Customs does this through a special automatic release feature. Once the transfer is approved, Air AMS will show the waybill and entry information was reconciled and the merchandise has been transferred and released.

The merchandise is to remain at the CFS until the trade submits paper entry documents and Customs inspects the merchandise. Once inspected, Customs must manually record the correct entry information on the waybill records in Air AMS.

ACS can not detect when entry documents have not been filed on merchandise manifested on a waybill in Air AMS. If entry documents are not filed, the waybill records in Air AMS are the only information available to Customs. However, because of the special automatic release feature, those records show waybill and entry information was matched and the merchandise transferred to a CFS and released into commerce.

Thus, the special automatic release feature provides opportunity for merchandise to enter commerce without proper entry and Customs

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## EXECUTIVE DIGEST

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inspection or release and can be used to circumvent Customs' contraband interdiction, trade enforcement and revenue collection efforts.

Customs is most vulnerable when importers, brokers and CFS operators have close business relationships. This is especially so where importers or brokers are co-located in a CFS and have access to merchandise. The greater threat is when the CFS operator is also an importer or broker, thereby providing total control and unfettered access to merchandise. (See Page 3)

**Merchandise Is  
Entering Commerce  
Without Customs  
Inspection**      The OIG estimated that merchandise manifested on 3,053 waybills in FY 1998 entered commerce without evidence of entry by the trade or inspection and release by Customs. (See Page 9)

Because the merchandise is gone, it is difficult to quantify the consequences of merchandise entering commerce without proper entry, inspection or release. The waybill record in Air AMS provides only generic information on the merchandise. Thus, it is difficult, if not impossible, to reconstruct events and determine the nature and quantity of the merchandise, existence of contraband, the applicable trade laws and revenue due to the Government. As such, OIG can only provide indicators of diminished enforcement effectiveness and lost revenues. (See Page 10)

Some merchandise manifested on the 3,053 waybills could pose a risk to Customs' enforcement efforts. The decision to physically examine the merchandise is often based on entry information and, in those instances, there was none. The type, configuration, size and weight of some merchandise could have provided opportunity to conceal and smuggle drugs and other contraband through some of the busiest highest risk airports in the U.S.

It is also difficult to quantify lost revenues. The OIG estimates Customs could have assessed over \$6.5 million in fines and penalties on the 3,053 waybills lacking evidence of entry and inspection. (See Page 11)

However, fines and penalties understate the Government's true revenue losses because they do not compensate for lost revenue from duties and tariffs that should have been collected. Nor do they compensate for the hidden costs of violating quotas, trademark and patent laws, or other trade requirements. (See Page 12)

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## EXECUTIVE DIGEST

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### **Better Controls Needed To Ensure System Integrity**

Although the special automatic release feature in Air AMS poses a unique problem, other system problems compromise the integrity of Air AMS and threaten Customs' cargo processing control.

The Air AMS system is not user-friendly. Although integral to Customs' cargo control, it is difficult to operate and hard to control. Designed as a historical record, it records and retains all information on every air waybill in the system. When trade users do not enter accurate information, the system can not reconcile waybill and entry information. Unable to reconcile, it creates a duplicate and useless record known as a "shell" record that remains in the system's active database indefinitely. Customs recognized the problem and had begun to remove shell records from the system. (See Page 15)

However, other control problems with the Air AMS could compromise Customs' drug interdiction and trade enforcement efforts. Air AMS contains a special feature known as a "permit-to-transfer" authorization. This feature allows the transfer of merchandise to a CFS. Although designed for transferring merchandise to a local CFS, Customs reported the trade at all six airports were using it to move merchandise to other ports of entry in the country. In total, 20 percent (206 of 1,031) of the waybills OIG referred to Customs for evidence of inspection involved a permit-to-transfer to move merchandise to other ports of entry.

Using the local permit-to-transfer feature to move merchandise to other ports of entry compromises Customs' contraband enforcement inspections because those inspections are often targeted through the manifesting process rather than entry process.

Customs was very concerned the local permit-to-transfer feature was being used to move merchandise to other ports. They agreed it would be very difficult and time consuming to determine if the merchandise was inspected prior to its release into commerce. (See Page 16)

### **Trade Compliance Not Enforced**

The OIG recognizes that special programming features are needed. As such, it advocates controlling rather than eliminating them. Customs provides little control over Air AMS system or its users. In effect, it looked to the trade to maintain the integrity of the system and has not required users to meet its expectations over data integrity.

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## EXECUTIVE DIGEST

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Although participation is voluntary and encouraged, Customs expects a 90 percent accuracy rate over the information entered into the system. Yet, Customs has no systematic means to enforce its expectations. (See Page 18)

Customs reported 339 instances of errors in the 1,031 waybills referred to them for evidence of entry, inspection or release. This represents an exception rate of 32.9 percent, far beyond Customs' 10 percent tolerance limit. Yet, Customs inspectors assessed fines and penalties only on the 55 waybills lacking evidence of inspection and not on the other 284 waybills involving errors. One inspector stated it was not worth the effort because fines and penalties are often mitigated down.

Based on the sample results, OIG projected that information on approximately 20,000 waybills was incorrectly entered in the Air AMS during 1998. Had a \$1,000 fine or penalty been assessed for these record keeping violations, over \$20 million in fines and penalties could have been assessed in FY 1998. Based on the higher of the \$1,000 record keeping fine or a fine based on the declared weight on the waybill, OIG estimated \$184.6 million in fines and penalties could have been assessed in FY 1998.

A senior Customs official at the exit conference acknowledged inspectors were reluctant to assess fines and penalties. He stated Customs preferred voluntary compliance to forced compliance through punitive measures. The OIG does not disagree with the preference for voluntary compliance. However, an unwillingness to assess fines and penalties or apply other sanctions when appropriate can encourage further non-compliance. (See Page 21)

**Computer Program Could Be A Useful Tool To Customs** The OIG believes the computer program Customs developed for the audit could be very useful, especially at higher risk ports of entry. It can target any data element in Air AMS and could be used to detect unusual and suspicious activity by members of the trade. As such, it could have application to investigations, management special projects and risk assessments. (See Page 22)

### Recommendations

In this report, OIG recommends Customs: (1) collect the fines and penalties assessed during the audit, (2) establish controls to mitigate the impact of the special programming features on the integrity of its cargo

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## EXECUTIVE DIGEST

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processing, (3) incorporate controls over Air AMS in the development of any new cargo processing system, (4) determine if the problems associated with Air AMS affects other Customs activities, and (5) consider identifying the control deficiencies with Air AMS as a material weakness under the Department of the Treasury Federal Managers' Financial Integrity Act process. Customs concurred and had taken or planned to take actions that would address the issues surrounding the recommendations. (See Pages 13 and 24)

# INTRODUCTION

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## Background

Federal regulation 19 CFR §122 requires all air carriers arriving in the U.S. from a foreign location to obtain permission from Customs to land and to provide Customs certain documents describing the cargo or merchandise onboard. The primary document for notifying Customs of merchandise entering the U.S. is the air carrier's manifest. The manifest is a summary document describing in very general terms the type, weight and quantity of the merchandise onboard the aircraft. With each manifest are individual air waybills providing a more detailed description of the merchandise listed on the manifest. Upon presenting the manifest and air waybills, the merchandise can be transferred to a local CFS where it must remain until inspected and released by Customs.

Federal regulations 19 CFR §141 and 142 require consignees, brokers, importers or other interested parties to present to Customs, within 5 working days, certain documents requesting inspection and clearance of merchandise seeking entry into U.S. commerce. Customs uses the information on these documents and the air waybills to inspect the merchandise and collect revenue due the Government. Once the inspection is completed and the estimated revenue is billed or collected, the merchandise can be released into commerce.

Customs' cargo manifesting and entry processes were paper-driven and labor intensive until international trade exploded and automation became necessary. In 1984, Customs implemented its Automated Commercial System. Eventually, sub-systems were developed in ACS to automate the manifesting process at major airports and seaports. These similar but separate sub-systems are known as the Sea and Air Automated Manifest Systems.

### **Air AMS Developed To Benefit Customs And Trade Community**

Customs' Air AMS became operational in late 1989. Designed as an inventory control, Air AMS was to standardize communications between Customs and the trade, streamline the manifesting process and facilitate reconciliation of air waybills and entry documents. In doing so, Customs hoped to enhance the timeliness of its release of merchandise while meeting its contraband interdiction, trade enforcement and revenue collection responsibilities. Customs expected the manifesting process to be fully automated by 1996.

Air AMS allows the trade to electronically transmit manifest and air waybill information on incoming merchandise to Customs before it

# INTRODUCTION

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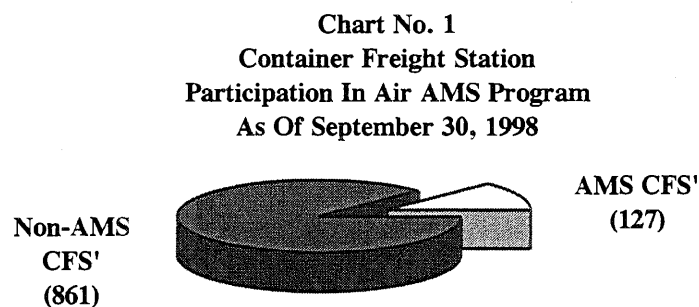
arrives in the U.S. Because AMS is part of ACS, Customs can review the information and decide whether to inspect the merchandise electronically or physically. Either method of inspection meets the requirement that Customs inspect all merchandise entering the U.S. Once inspected, Customs records its results in ACS and communicates its release to interested parties through the ABI in ACS. Once released, the merchandise can enter commerce.

Electronic inspections provide Customs opportunity to better allocate its personnel. In turn, the trade gets faster transfer of merchandise off the busy airport tarmac thereby reducing airport congestion, lowering handling costs and providing quicker release of the merchandise.

## **Air AMS Participation Limited To A Few Carriers At Major Airports**

Participation in Air AMS program is voluntary. Primary participants include air and express carriers, port authorities and CFS operators, including de-consolidators and freight forwarders. Participants invest in Air AMS-related computer hardware and software and are expected to use it on at least 90 percent of their merchandise and to maintain a 90 percent accuracy rate over information they enter into the system.

Although Customs expected full automation by 1996, participation in Air AMS as of September 30, 1998, was limited to 56 carriers and 127 CFS' operating at 29 U.S. airports. According to Customs, system usage averaged nearly 3,000 flights and 168,000 waybills per week in August of 1998. As indicated in Chart No. 1, the CFS' participating in AMS in FY 1998 represented about 13 percent of all CFS' at the 29 airports.



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**Source: U.S. Customs Service**

# INTRODUCTION

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Detailed information on system participation is presented in Appendix 2.

## **Lack Of CFS Participation Can Present Risks**

The Air AMS system works best when carriers and CFS' participate in Air AMS and when importers and brokers participate in ABI. However, when CFS' do not participate in Air AMS, the process goes from an electronic medium at the carrier to a paper medium at the CFS. This deprives Customs and the trade of the system's full benefits and presents opportunity for merchandise to enter U.S. commerce without inspection.

To illustrate the problem when merchandise processing moves from an electronic medium to a paper medium, assume a U.S. importer orders 10 widgets from a foreign manufacturer. The 10 widgets are brought into the U.S. by an air carrier, manifested on a single waybill and transferred to a CFS.

In a **total electronic environment**, an AMS air carrier electronically transmits waybill information and requests permission to transfer the widgets to an AMS CFS before arriving. In doing so, the waybill number and 10 widgets are inventoried in Air AMS. The importer electronically transmits the entry documents to Customs through ABI. As a result, the entry and waybill information is in the system. The Air AMS is programmed to match or "reconcile" the entry and waybill information before approving transfer of the merchandise to the CFS.

Because the information is in the system, Customs can electronically inspect the widgets by reviewing the waybill information in the AMS and the entry information in the ACS. If acceptable and not selected for physical examination, Customs will electronically inspect the merchandise, record the release in ACS and electronically notify the importer and CFS operator. The Air AMS record is now complete or "reconciled" and will show the 10 widgets were inspected and released.

The process is not so streamlined under a **partial or non-electronic environment**. Assume the air carrier participates in AMS but the CFS does not nor does the importer participate in the ABI. The AMS carrier electronically transmits waybill information on the 10 widgets and requests transfer to a non-AMS CFS. Because the importer does not participate in ABI, entry information is not available at the time of carrier's request. Lacking the entry information, the system is unable to match or "reconcile" the waybill and entry information in order to approve the transfer of the merchandise.

# INTRODUCTION

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As a result, Customs must “trick” the system into thinking the widget waybills have been reconciled or matched to entry information. It does so with special programming in AMS known as the “automatic release” feature. Upon the carrier’s transfer request, the system recognizes the CFS does not participate in Air AMS. This activates the automatic release feature and tricks the system into thinking the waybills have been matched to an entry number. Once tricked, the transfer to the CFS is approved. At this time, the Air AMS record will show the 10 widgets were inspected and released by Customs even though they have not.

Once transferred to the CFS, the process becomes labor-intensive and paper driven. The non-ABI importer hand carries the paper entry documents to Customs to obtain inspection and release of the widgets from the CFS. Once the inspection is completed, Customs will manually record the ACS entry information into the Air AMS waybill record. This effectively reverses the effect of the automatic release feature that allowed the widgets to be transferred to the CFS without proper reconciliation. The AMS and ACS records then show 10 widgets were inspected and released by Customs. The importer can present the completed entry documents and retrieve the merchandise from the CFS.

However, the system assumes that entry documents will be filed on all merchandise. It can not detect when an importer fails to file entry documents or when a CFS releases merchandise without Customs inspection and release. If entry documents are not filed, the only information available is the waybill record in Air AMS. However, because of the automatic release feature that record shows Customs inspected and released the 10 widgets into commerce.

Lacking a systematic means to detect the importer’s failure to file entry documents or the improper release of merchandise, Customs can not ensure the merchandise is inspected as required by 19 CFR §142. The merchandise is no longer at the CFS. The only information available to Customs is the air waybill and it does not adequately describe the merchandise. Thus, it is difficult, if not impossible, for Customs to detect the violation or reconstruct events. As such, Customs’ inspection and any duties, tariffs, fines and penalties and import restrictions can be circumvented or avoided.

Given the vast amount of merchandise imported into the U.S. and the lack of a systematic computerized control, Customs is vulnerable to this smuggling threat that can affect contraband interdiction, trade enforcement and revenue collection. It is most vulnerable when importers, brokers and CFS operators have close business relationships.

# INTRODUCTION

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This is especially so when importers or brokers occupy space in a CFS and have access to the merchandise. However, the greater threat is where a CFS operator is also an importer or broker, providing total control over and unfettered access to the merchandise.

## Objective, Scope And Methodology

The audit objective was to determine if Customs' controls over the automatic release feature in Air AMS were adequate to ensure all merchandise entered into commerce was subject to Customs inspection as required by 19 CFR §142. And if not, to determine the impact on Customs' enforcement and revenue collection efforts.

The audit focused on merchandise transferred from an Air AMS carrier to a non-AMS CFS for which no evidence of entry existed in the ACS. The OIG focused on these movements because about 90 percent of the warehouses at the AMS airports were not participating in Air AMS and, as a result, vulnerable to misuse of the automatic release feature.

Fieldwork was conducted between September 1998 and October 1999 at Customs': (1) Headquarters in Washington, DC; (2) Office of Information and Technology (OIT) in Newington, Virginia; and (3) airport offices in Los Angeles and San Francisco, California; Chicago, Illinois; New York City, New York; Atlanta, Georgia; and Miami, Florida.

The OIG used a computer-assisted auditing tool developed by Customs OIT to identify and extract information on air waybills entered into the Air AMS on 7 days randomly selected days in FY 1998 at 6 major AMS airports. After eliminating certain waybills, the OIG referred the remaining waybills to Customs for evidence of entry or inspection of the merchandise. Using an expected confidence interval of 95 percent, a precision of  $\pm 5$  percent and a pValue of 50 percent, the OIG statistically estimated waybills in the universe that lacked evidence of entry or release and the related fines and penalties.

Because the audit focused on the system, the sample size was not sufficient for the OIG to detect possible pattern and practice of improper or illegal activity by individual carriers, CFS operators, brokers, importers or other interested parties involved in importing merchandise.

The audit was conducted in accordance with the *Government Auditing Standards* issued by the Comptroller General of the United States and included such tests that were deemed necessary.

# INTRODUCTION

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A detailed description of the audit objective, scope and methodology is presented in Appendix 1.

# AUDIT RESULTS

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Better controls are needed to mitigate the risk Air AMS presents to Customs' enforcement and revenue collection efforts. The trade can use the automatic release feature in Air AMS to circumvent Customs inspection and avoid duties, tariffs, quotas and other import restrictions on merchandise entering commerce. OIG estimates merchandise manifested on over 3,000 waybills was released into commerce in FY 1998 without evidence of inspection and over \$6.5 million in fines and penalties could have been assessed on those waybills. The full effect on Customs' enforcement or revenue collection efforts is unknown.

Better controls are also needed to ensure the integrity of Customs' cargo control processes. Although Customs recognizes the system is not user friendly and its utility has been compromised, it has done little to police the system or its users. As a result, the system is being misused without action or sanction by Customs. A third of the waybills OIG referred for Customs review contained errors or evidence of misuse, far exceeding Customs' tolerance levels. OIG estimated over \$184.6 million in fines and penalties could have been assessed for system misuse in FY 1998.

Management controls are the organization, policies and procedures used by agencies to reasonably ensure that, among other things (1) programs achieve their intended results, (2) programs and resources are protected from waste, fraud and mismanagement, (3) laws and regulations are followed and (4) reliable and timely information is obtained, maintained, reported and used for decision making. Because of the risk to Customs' enforcement and revenue collection efforts, the OIG believes the problems with Air AMS described in the following findings collectively constitute a material weakness in Customs' management controls as defined in OMB's Circular A-123, *Management Accountability and Control*.

## **Finding 1: Merchandise Is Entering Commerce Without Evidence Of Customs Inspection And Release**

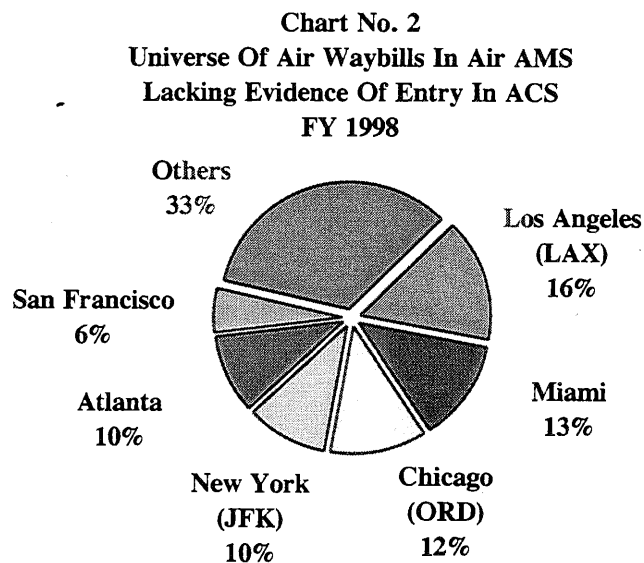
Using the computer-assisted auditing tool to identify and extract information on air waybills, the OIG statistically estimated that merchandise manifested on 3,053 air waybills in FY 1998 entered commerce without evidence of entry or Customs inspection and release. Besides the possible undetected contraband and undeclared merchandise entering the U.S., OIG estimated over \$6.5 million in fines and penalties could have been assessed on the waybills.

# AUDIT RESULTS

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## Customs Does Not Monitor The Use Of Automatic Release Feature

Until the OIG audit, Customs did not have a systematic means of detecting or measuring the use of the automatic release feature in Air AMS. At the OIG's request, Customs OIT developed a computer-assisted auditing tool that identified and extracted information on over 146,000 air waybills entered into Air AMS in FY 1998 that lacked evidence of entry and Customs inspection or release in ACS. As indicated in Chart No. 2, two-thirds of those waybills were at 6 airports.



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**Source: U.S. Customs Service**

The number of air waybills lacking evidence of entry at AMS airports in FY 1998 is presented in Appendix 3.

Using the computer program, Customs OIT identified 2,068 waybills at the above 6 airports for 7 randomly selected days in FY 1998 for audit testing purpose. The OIG reviewed manifest and entry information in ACS and eliminated 1,037 waybills where evidence of entry was found or where the waybills did not meet OIG selection criteria. The OIG also judgmentally eliminated low risk shipments such as informal entries, paper, documents and medical samples. The remaining 1,031 waybills were referred to Customs for evidence of entry, inspection and release.

Detailed information on the OIG sampling techniques, results and precision is presented in Appendices 1, 4 and 5.

# AUDIT RESULTS

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## **Merchandise Is Being Released Without Evidence Of Customs Inspection**

Neither Customs nor the trade could provide evidence of entry, inspection and release on merchandise manifested on 55 waybills. Thirteen waybills were found in developing the audit methodology and the other 42 waybills were found in the random sample.

The 42 waybills in the random sample that lacked evidence of entry or inspection represented 2 percent of the total sample of 2,068 waybills and 4.1 percent of 1,031 waybills referred to Customs. Projecting these results to the universe, the OIG estimated with 95 percent confidence that merchandise manifested on 3,053 air waybills in FY 1998 entered U.S. commerce without evidence of entry, inspection and release.

Because of limitations in the computer program described below, the estimated number of waybills is understated and not a true indicator of the merchandise entering commerce without proper entry, inspection or release.

Specifically, the computer program queried the Air AMS database by waybill number. However, there are actually three types of waybills: master, house and simple.

A "master" waybill is a summary document identifying the amount and identification number of underlying "house" waybills. A master waybill must have at least one house waybill but there is no limit to the number of house waybills that can be on a master waybill. The house waybill identifies the carrier, shipper, country of origin, type, weight, quantity and other general information on the merchandise. If an importer is importing 10 widgets going to 10 different consignees, the master waybill may have as many as 10 underlying house waybills.

A "simple" waybill is similar to a house waybill. It is listed separately on the air carrier's manifest and provides information similar to that on a house waybill. Often, merchandise on a simple waybill is destined to a single consignee. If the 10 widgets were going to a single consignee they would probably be manifested on a simple waybill.

The computer program could not differentiate between the type of waybill. It could only recognize where an air waybill did not match or reconcile to an entry. It could not identify whether those waybills were correctly entered into the system as a master or simple waybill.

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For example, if a master waybill with 100 underlying house waybills was correctly entered into Air AMS and the computer program found no evidence of entry, the program would report the underlying house waybills as 100 audit exceptions. But if entered as a simple waybill, the program would report only 1 audit exception.

The OIG was able to determine the correct type of waybill in the sample through an exhaustive and time-consuming review of ACS information and Customs documents. However, there was no practicable means to estimate which of the 3,053 waybills projected as lacking evidence of entry, inspection and release were simple or master waybills.

As a result, the estimated 3,053 waybills are only an indicator of the problem but not a true measure of the amount of merchandise that entered into commerce without evidence of entry, inspection and release. However, the OIG believes the amount of merchandise that entered commerce could be substantial, especially if the waybills were masters.

Detailed information on the projected number of air waybills lacking evidence of entry, inspection and release is presented in Appendix 6.

## **Substantial Risks From Use Of Automatic Release Feature**

Quantifying the consequences of merchandise entering commerce without entry or inspection was also difficult. The merchandise was not available nor was the information in Air AMS sufficient to determine the nature and value of the merchandise, applicable trade laws or amounts due the Government. Thus, the OIG can only provide indicators of the risk of diminished enforcement efforts and lost revenues.

The OIG could find no meaningful measure of the potential impact on Customs' trade enforcement and contraband interdiction efforts. However, the special automatic release feature presents opportunity to smuggle merchandise into the U.S. and the OIG believes the opportunity poses a meaningful threat to Customs' enforcement efforts.

The waybill record in Air AMS does not adequately describe the merchandise or its value. However, the type, configuration, size and weight of some merchandise manifested on the 42 waybills lacking entry, inspection and release could provide opportunity to conceal and smuggle drugs and contraband through Los Angeles (LAX), John F. Kennedy (JFK) and Miami International Airports; three high risk airports.

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- At JFK, Customs issued a penalty notice on a waybill describing the merchandise only as 196 cartons of “footwear” weighing 7,185 kilograms (15,807 pounds).
- At LAX, Customs issued penalty notices on two air waybills describing the merchandise only as 448 kilograms (985 pounds) of “flowers.” These shipments present a risk because flowers have been used to smuggle drugs into the U.S.
- At JFK, Customs issued a penalty notice on an air waybill describing the merchandise only as 113 cartons of “miscellaneous freight” weighing 2,105 kilograms (4,631 pounds). In another instance at JFK, Customs issued a penalty on a master waybill with 3 house waybills describing the merchandise only as 188 cartons of “Parts.”
- At Miami International, Customs issued a penalty notice on a waybill describing the merchandise only as 194 kilograms (426 pounds) of “documentos.”

The merchandise relating to the 3,053 waybills may not have been selected for physical inspection because Customs often bases that decision on the entry information in the ACS, which in the case of those waybills, there would be none.

Aside from the potential lost revenues from duties and tariffs, Customs issued 44 penalty notices amounting to \$136,918 against the interested parties of the 55 waybills lacking evidence of entry, inspection and release. Over \$47,600 resulted from the methodology phase of the audit. The other \$89,278 resulted from the random sample.

Projecting the random sample results to the universe, OIG estimates with 95 percent confidence that Customs could have assessed over \$6.5 million in fines and penalties on those 3,053 waybills lacking evidence of entry, inspection and release.

Summary and detailed information on the fines and penalties resulting from the audit is presented in Appendix 6, 7 and 8.

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## **The Government's Risk Of Lost Revenue Is Understated**

Customs' fines and penalties are only tangential indicators of the consequences of misusing the AMS and understate the Government's true losses. Fines and penalties are punitive measures and do not compensate the Government for lost revenue from duties and tariffs that could have been collected at the time of entry. Nor do they compensate the Government for the hidden costs of quota violations, trademark infringements and other import restrictions and prohibitions.

However, the merchandise relating to those 55 waybills that lacked entry and inspection had been released into commerce. Information in Customs' systems was not sufficient to determine the nature and value of the merchandise or to reconstruct the events surrounding the movement and release of the merchandise. Thus, it was not possible to retroactively determine the applicable duties, tariffs, quotas and other import restrictions. As such, fines and penalties were the usual sanctions for violating regulations.

Federal regulation 19 CFR §171 provides Customs discretion in assessing fines and penalties. For the 55 waybills found in the audit, Customs inspectors could choose to assess or not assess fines or penalties. If they chose to assess, they could choose to assess based on failure to properly manifest or present merchandise for inspection or for failure to meet regulatory record keeping requirements. The fine or penalty for not properly manifesting or presenting merchandise for inspection is based on the manifested weight of the merchandise; \$10 per pound or \$20 per kilogram. The fine or penalty for not keeping proper records is \$1,000 per violation. If Customs finds a pattern, practice or history of non-compliance or regulatory violations, the fine or penalty can be substantially increased.

Because the computer program could not detect incorrect information in the system or differentiate between types of waybills (master, house, or simple), the estimated number of waybills lacking evidence of entry was understated. This, in turn, understated the estimated fines and penalties that could have been assessed.

There are other reasons within Customs' control why the fines and penalties assessed during the audit are understated. The decision to assess fines and penalties as well as the amount assessed was left to the discretion of the local Customs inspector. In 27 of 44 penalty notices issued on the 55 waybills lacking evidence of entry or release, the

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inspectors assessed the \$1,000 fine or penalty rather than the potentially more substantial fine or penalty based on the manifested weight. In addition, they were not always consistent in the fines and penalties assessed and some were reluctant to assess fines and penalties, as discussed further in Finding 2.

Customs officials at the exit conference accepted the audit methodology and the fines and penalties assessed in the audit. They agreed the fines and penalties assessed during the audit understated the Government's losses because the waybill information in the Air AMS was not sufficient to determine the true amount of duties, tariffs and other revenues due on the merchandise imported.

In its response to the OIG report, Customs stated it did not agree with the characterization of the local permit-to-transfer as a "trick" of the ACS System and provided supplemental information describing the programming and controls over the transfer feature. To clarify, the OIG does not consider the permits-to-transfer authorization a "trick" nor does it contest the need for such transfers. Instead, the "trick" referred to in this report relates to internal programming within AMS that allows cargo to be transferred to a non-AMS warehouse without reconciling waybill and entry information. Also, Customs' controls were mostly dependent on ineffective post audit procedures that, as discussed in Finding 2, were not in place or working as intended in those locations the OIG visited.

## **Recommendation 1-1:**

The Commissioner of Customs should ensure the fines and penalties assessed as a result of the OIG audit were appropriate and the interested parties were not attempting to circumvent inspection of the merchandise as required by 19 CFR.

### Management Response and OIG Comment

Customs concurred with and had taken or planned to take action the OIG believes will address the recommendation. In March 1999, Customs enacted Treasury Decision 99-29 setting higher fines and penalties against the trade for cargo misdeliveries as well as new mitigation guidelines emphasizing the collection of duties, taxes and fees.

Customs is also exploring the creation of a national post audit database to aid in spotting suspicious trends, inconsistencies or possible noncompliance by the trade and to share this information among ports.

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Because of the system programming and testing required, Customs expects to complete this action by October 2002.

## **Recommendation 1-2:**

The Commissioner of Customs should ensure the prompt collection of the \$136,918 of fines and penalties assessed in the OIG audit.

### Management Response and OIG Comment

Customs concurred with and was taking action the OIG believes will address the recommendation. In its response, Customs stated the fines and penalties assessed in the audit have been or were in the process of being collected.

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## **Finding 2: Better Controls Needed To Ensure System Integrity**

Customs needs to establish better controls over Air AMS to ensure the integrity of its cargo processing systems. The primary audit focus was on the special automatic release feature but the OIG found other problems that could also threaten Customs' cargo control processes. Although Customs recognizes the system is not user friendly and its utility has been compromised, it has done little to police the system or its users. As a result, the system is being misused, Customs enforcement efforts are being compromised and the Government is at risk of losing revenue. A third of the waybills reviewed by OIG contained errors or evidence of misuse, far exceeding Customs' tolerance levels. OIG estimated over \$184.6 million in fines and penalties could have been assessed for system misuse in FY 1998.

### **Air AMS Is Not User Friendly**

Customs officials acknowledged Air AMS is not a user-friendly system. It was designed to be a historical record of all activity relating to air waybills in the system. The information is entered into the system by the trade, not Customs, and organized by a unique waybill number assigned by the trade. This information remains in active status for cargo processing control purposes for about 6 months after which it is transferred to an archive file.

However, system problems make it difficult for Customs to use it for inspection purposes. The system can not detect the entry of erroneous waybill information and, thus, is unable to reconcile it to entry information. Unable to do so, it creates a "shell" record.

A shell record is a temporary record that shows the system could not match entry and air waybill information. However, the system will provide conditional release of the merchandise with the expectation the record will be corrected so it can match the entry and waybill information and eventually transfer the record to archives. If not corrected, shell records remain in the active database indefinitely.

According to Customs, the trade often does not provide accurate information or correct entry errors and mistakes and there is no check in Air AMS to ensure the trade does so. Customs found 78 of the 1,031 waybills referred to Customs involved erroneous information that would result in a shell record. In 48 of those instances, a master waybill with

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underlying house waybills was entered as a simple bill. In the other 30, the waybill number or CFS code was entered incorrectly.

The shell records and other system problems hampered the development of the computer-assisted auditing tool, a process that took 6 months. For example, Air AMS has a special code to identify when merchandise is transferred to a non-AMS CFS. This special code was crucial to identifying the audit universe and selecting the sample. However, it was known only to a few in Customs.

Failure to enter accurate and complete waybill information makes the system difficult to operate and control. It also compromises Customs' contraband interdiction efforts because those inspections are often based on manifest information, not entry information. Without accurate and complete waybill information, Customs contraband enforcement teams may not have the information to identify merchandise for inspection.

Customs officials at the exit conference acknowledged that shell records were a problem in Air AMS and stated Customs had begun to clean them out of the system. This may prove difficult because neither the trade nor Customs may have the information needed to match incorrect and correct waybill records. Thus, it may have to eliminate the records using an arbitrary basis, such as record age.

Furthermore, purging the existing shell records from the system does not address the root cause of the shell record problem; i.e., the trade is not properly using the system.

## **The Trade Community Is Not Properly Entering Import Transactions In Air AMS**

Unintended errors, mistakes and carelessness may explain some of the above problems. However, the lack of adequate controls in the Air AMS could compromise Customs' drug interdiction and trade enforcement efforts.

Customs can authorize imported merchandise arriving by air to be either: (1) moved to another location within the port of entry, such as to a CFS (referred to as a local "permit-to-transfer" shipment), (2) moved "in-

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bond" to another port of entry (referred to as an "in-bond" shipment<sup>1</sup>); or (3) remain on the aircraft for a later flight to another port of entry (referred to as a "permit-to-proceed" shipment). The Air AMS has unique programming codes that are to be used by the trade to identify the type of movement authorized by Customs (permit-to-transfer, in-bond or permit-to-proceed).

Customs reported the trade at all 6 airports audited were incorrectly coding merchandise moved to other ports of entry, including in-bond shipments, as permit-to-transfer shipments in the Air AMS. In total, 206 (20 percent) of the 1,031 air waybills the OIG referred to Customs involved in-bond shipments to other ports that were recorded as permit-to-transfer shipments.

The trade was also using the permit-to-transfer code for permit-to-proceed shipments. As presented in Appendix 3, the special program identified over 35,000 waybills where merchandise arrived in Anchorage in FY 1998 that lacked evidence of entry or Customs inspection and release in the ACS. However, Customs believed the merchandise on those 35,000 waybills should have been recorded as permit-to-proceed shipments instead of permit-to-transfer shipments. A Customs inspector in San Francisco told OIG it was common trade practice to use the permit-to-transfer code for permit-to-proceed shipments.

Customs' tracking of the location and movement of merchandise becomes difficult when the local permit-to-transfer code is used to move merchandise to another port of entry. Customs has unique codes in ACS to identify ports of entry and CFS facilities in order to track the movement and location of merchandise. The code for LAX is 2720 and each CFS in the Los Angeles area has its own unique four-digit code.

For example, assume the local permit-to-transfer code is used to move merchandise from LAX to JFK in New York where it will be transferred to a non-AMS CFS. Because the permit-to-transfer is a local transfer option, the waybill record in Air AMS will show the merchandise was unloaded at LAX and transferred to a CFS in the Los Angeles area. However, the system does not match or reconcile the CFS code to the port code and will not recognize the CFS is in New York. Consequently, if Customs at LAX selects the merchandise for inspection, it would find

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<sup>1</sup> An in-bond shipment involves merchandise that arrives at an interim port of entry (e.g., LAX) but whose final destination is another port of entry (e.g., JFK). The merchandise can be unloaded in Los Angeles and held for transportation to New York. However, the merchandise remains under a performance bond until it arrives in New York, entry documents are filed and the merchandise is inspected and released by Customs. Hence, the name in-bond shipment.

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after extensive effort that it was in, or on its way to, New York. Conversely, it is unlikely Customs at JFK would detect if entry documents were not filed because the only information in the system is in the air waybill record. Because of the special automatic release feature in Air AMS, the waybill record would show the merchandise was unloaded in LAX, the waybills were matched or reconciled and the merchandise was released to a local CFS. Thus, it would be very difficult and time consuming for Customs at JFK to locate the merchandise or proof of entry; thereby providing opportunity to circumvent Customs enforcement targeting and inspection in both ports and avoid duties, tariffs, quotas or other import restrictions.

Customs officials at the exit conference were very concerned the local permit-to-transfer code was being used to move merchandise to other ports of entry. They agreed that it would be very time consuming and difficult to track shipments for entry and inspection purposes if the trade improperly uses the local permit-to-transfer code because they “fall off Customs’ radar screen.”

The OIG agrees with Customs. Because of the time and effort involved in tracking in-bond shipments, the OIG was forced to accept paper evidence that the trade filed an in-bond transfer authorization form for those 206 air waybills involving the use of the permit-to-transfer feature. However, Customs at the 6 ports could not provide any evidence to assure the OIG that the merchandise manifested on those 206 air waybills had been inspected by Customs prior to release at the final destination.

## **Trade Compliance Not Enforced**

The OIG recognizes the special programming features in Air AMS are needed to quickly transfer merchandise off the busy airport tarmac. As such, OIG believes Customs needs to better monitor and control their use rather than eliminate them.

Participation in the system is voluntary and encouraged. Customs expects the trade to use the system properly and maintain the integrity of the information entered into it. But Customs does not have adequate controls to prevent or detect the incorrect recording of merchandise movements in the system, maintain data integrity or enforce its expectations on the users.

Federal regulation 19 CFR §4.7a states Customs personnel will not perform any reconciliation of Air AMS records, except in the post audit process. The regulation states it shall be the responsibility of the trade to

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correct and reconcile records. Customs expects users to use the system for at least 90 percent of their activity and maintain an accuracy rate of at least 90 percent for information entered into AMS.

Yet Customs has no systematic means to monitor and enforce compliance with those expectations. The OIG found 339 instances of errors or misuse in the 1,031 waybills referred to Customs, an error rate of 32.9 percent, far beyond Customs' 10 percent tolerance limit and demonstrating the extent of the problems in the system.

Without a computerized means, monitoring was on a waybill by waybill basis. The only maintenance Customs performed was eliminating shell records when transferring records to archive files.

Instead, Customs relied on its carrier post audit function to ensure trade compliance with 19 CFR §4.7a and its cargo processing controls. The carrier post audit group generally measures compliance by reviewing selected manifests, waybills and entry documents. Customs had a carrier post audit group at each airport visited by OIG.

The carrier post audit function was not an effective control over the system or indicator of trade compliance. The staffing of the groups visited by OIG was minimal. In one case, the group consisted of 1 full-time and 1 part-time inspector. In another case, no staff was assigned to the group for about six months in FY 1998.

Given the level of staffing, the effort was minimal. In one case, the group had not performed any testing for 18 months. When testing was performed, it usually did not address the possibility that entry documents were not submitted on manifested merchandise. At the airports visited, the carrier post audit group was only verifying that information on selected entry documents matched information on the waybill. This ensures the merchandise described on the entry document was accurately manifested on the waybill. It does not ensure that entry documents were submitted on all merchandise on the waybill. To provide that assurance, one would start with the waybill and verify it to the entry information, which OIG did in its audit.

Customs officials at the exit conference were concerned carrier post audit groups were not verifying that merchandise manifested on the waybills was presented to Customs for entry and release. They stated Customs instructions require such testing. They also stated a new directive would be issued requiring waybill information be verified to entry information in ACS.

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The OIG also found indications that entry information was not always entered into ACS. Because the merchandise for the 1,031 waybills referred to Customs was processed at a non-AMS CFS through paper entry documents, Customs inspectors were to manually enter information on those paper documents into the ACS. This evidences the merchandise was inspected and released by Customs. Yet, about 95 percent (976) of the 1,031 waybills referred were resolved through paper evidence of proper entry and release even though there was no electronic evidence in ACS. One explanation is that the information was not entered into ACS.

Not entering entry information into ACS can impact Customs' enforcement efforts because physical inspections of merchandise are targeted through the ACS selectivity module. If the entry information on the 976 waybills was not in ACS, it is unlikely the merchandise would be selected for physical inspection under selectivity; thereby circumventing or compromising Customs' enforcement efforts.

## **Forgone Fines And Penalties Indicate Magnitude Of Problems**

The magnitude of Air AMS and Customs' enforcement problems can be demonstrated by the fines and penalties that Customs did not assess. Customs reported that 284 (27.5 percent) of the 1,031 waybills referred involved the trade incorrectly entering information or using the system. Adding the 55 waybills lacking evidence of entry or release increases the number of waybills to 339 or 32.9 percent.

However, Customs assessed fines and penalties only on the 55 waybills where the trade could not provide evidence of entry, inspection and release. It did not assess fines and penalties on the other 284 waybills. As discussed in Finding 1, Customs inspectors can assess fines and penalties based on record keeping violations or on the declared weight of the merchandise manifested.

Based on the sample results, the OIG estimates, with 95 percent confidence, that the trade incorrectly entered information on approximately 20,000 waybills in the Air AMS during FY 1998. Had the \$1,000 fine and penalty been assessed on this projected number of waybills for record keeping violations, over \$20.2 million in fines and penalties, could have been assessed in FY 1998.

Had fines and penalties been assessed based on the higher of \$1,000 or declared weight of the merchandise, the OIG estimates over \$184.6

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million in fines and penalties could have been assessed during that period.

The \$6.5 million of projected fines and penalties on waybills lacking evidence of entry, inspection and release by Customs are not included in the above estimates.

Detailed information on the OIG estimates of fines and penalties that could have been assessed in FY 1998 is presented in Appendix 9.

## **Customs Is Reluctant To Assess Fines And Penalties**

Customs inspectors did not always assess fines and penalties for violations in a consistent manner. One inspector stated the fines and penalties assessed for lack of evidence of entry or release would not have been assessed if the OIG had not been involved. Another told the OIG that it was not worth the effort because the fines and penalties are often mitigated down or dismissed altogether.

In addition to often assessing the lesser fine or penalty, Customs inspectors were not always consistent in their assessments.

- Inspectors in one airport chose to assess a fine or penalty for a violation while inspectors at another airport chose not to assess a fine or penalty for the same violation.
- When dealing with multiple violations by the same party, some inspectors chose to assess \$1,000 for each violation. In some cases, they assessed as much as \$10,000. However, other inspectors chose to combine multiple violations into a single violation and assess only a \$1,000 fine or penalty.
- Customs inspectors at one airport choose not to assess fines or penalties until they accumulated 100 violations by a party; at which time they assessed only \$1,000.

The senior Customs official at the exit conference acknowledged the discretion exercised by Customs inspectors in assessing fines and penalties. He commented Customs prefers to promote voluntary trade compliance rather than forced compliance through punitive measures.

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The OIG does not disagree with the desire to promote voluntary compliance. However, an unwillingness to apply fines, penalties or other sanctions may promote and encourage further non-compliance.

## **System Users Need Training**

Customs officials at the exit conference believed system users needed more training in Air AMS and the OIG agreed. Some Customs inspectors told the OIG they had only limited knowledge in the system and its functions. The number of exceptions found by the OIG supports the need for more and better training for all users, including Customs.

## **System Problems May Extend To Other Cargo Movements**

Many problems found by the OIG were systemic to Air AMS but not necessarily unique to the environment audited. Because of the limited audit scope, OIG can not provide Customs any assurances that similar problems are not occurring in other cargo processing environments.

The OIG audit focused on merchandise transferred from an AMS air carrier to a non-AMS CFS because it was considered the most vulnerable to misuse of the special programming features in Air AMS. However, this was only one of the four types of transfers. The other three were transfers between: (1) an AMS carrier and an AMS CFS (a total electronic environment), (2) a non-AMS carrier to an AMS CFS (a paper to electronic environment), and (3) a non-AMS carrier to a non-AMS CFS (a total paper environment).

Customs officials at the exit conference generally agreed that there was reason for concern over the OIG findings. One official commented that Customs was supposed to have fixed similar problems the last time it reviewed AMS. They also agreed with the need for better controls to ensure the integrity of the system. They were especially receptive to providing more training to system users and enforcing Customs' expectations over its users. However, they questioned the need for Customs to determine if the problems extended to other types of environments. They believed Customs should be able to rely on the OIG results rather than perform their own risk assessment.

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## **Computer Program Could Be A Useful Tool To Customs**

The computer program developed by OIT for the OIG could be very useful to Customs especially at higher risk ports of entry. It is very flexible and can target and extract any data element in the AMS including date of arrival, type and quantity of merchandise, port of entry, carrier, CFS, importer and country of origin. As such, it could be extremely useful for discerning unusual and suspicious activities as well as special management projects, such as risk assessments.

Customs officials at some airports were interested in the program. One official stated Customs could use it periodically as an indicator of trade compliance or to determine the need for further research or investigation of an individual or company suspected of violating Customs regulations.

The program also may have investigative applications. The OIG used it to audit the AMS system. However, the OIT representatives at the exit conference explained that the program can target individual carriers, CFS operators, brokers, importers or other interested parties for suspicious or illegal activities.

Customs officials at the exit conference expressed interest in the computer program. The OIT representatives at the exit conference explained it was available to anyone in Customs.

The OIG recognizes Customs may not have the resources to apply the program in all ports or to follow up on exceptions, as the OIG did in its audit. However, the OIG believes it could provide port directors at the higher risk airports a useful tool if modified to target local concerns and applied judiciously and periodically. It could also be used in Customs special projects such as the "Tin Man" project to measure the compliance with in-bond shipment requirements.

While Customs officials at the exit conference were in general agreement with the OIG findings and the need for better control, they commented that addressing the problems becomes an issue of resource allocation; i.e., where does Customs place its scarce resources?

The OIG appreciates Customs' staffing situation. The OIG recognizes ACS is nearing its capacity and design limits and that Customs is seeking funding for a new automated system. However, the OIG believes the special program could provide an interim control over Air AMS, especially at higher risk ports of entry, until the new system is

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developed. The OIG also believes Customs will need to incorporate controls over the Air AMS special programming features into its new automated cargo processing system. The Customs officials agreed.

## Recommendation 2-1:

The Commissioner of Customs should establish controls to measure trade community compliance with Air AMS requirements, especially over the use of special programming features for automatic release and local permits-to-transfer to ensure all merchandise is inspected prior to release into the commerce.

### Management Response and OIG Comment

Customs concurred with and planned to take action the OIG believes will address the recommendation. In the near-term, Customs will monitor all system transmissions for correct use of the special programming features during the first 45 days of a carrier's Air AMS participation. Any deficiencies will be referred to the Customs Client Representative for corrective action. After the initial 45 days, Customs inspectors will perform cursory audits of the carriers' use of the special programming features including a mandatory post audit of a new Air AMS participant activities in the first six months. Subsequent audits will be performed based on Customs' results. Customs expects to implement these controls by March 2001.

Customs also plans to introduce a post audit compliance review process employing scientifically based random sampling of qualifying air waybills to promote better control and compliance from the trade. This would be similar to the automated random sampling used for in-bond movements. Because of the system programming and testing required, Customs expects to complete this action in October 2002.

## Recommendation 2-2:

The Commissioner of Customs should provide all system users, including Customs inspectors, more and better training over the use of Air AMS to improve the quality and usefulness of system information.

### Management Response and OIG Comment

Customs concurred with and was taking action the OIG believes will address the recommendation. Customs has completed a user guide for the Air AMS and developed training for its personnel. Three training

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sessions have been conducted since August 2000 and additional sessions will be scheduled in the upcoming year. Customs also provided training to its Client Representatives who will assist carriers, de-consolidators and freight forwarders on Air AMS issues.

## Recommendation 2-3:

The Commissioner of Customs should monitor the trade's use of the Air AMS and take appropriate action, including fines, penalties, and other sanction as necessary, to enforce trade compliance with Customs' quality expectations.

### Management Response and OIG Comment

Customs concurred with and has taken or plans to take action the OIG ~~believes will address the recommendation.~~ As discussed in Recommendation 2-1, Customs plans to monitor Air AMS participants' activities, initially through periodic reviews and post audits and eventually through statistical sampling methods similar to that used for in-bond movements. As discussed in Recommendation 1-1, Customs enacted Treasury Decision 99-29 in March 1999 which provide new guidelines for assessing higher amounts of fines, penalties and liquidating damages as well as new mitigation procedures emphasizing the collection of duties, taxes and fees. Customs believes these actions will result in vigorous enforcement of trade compliance. Customs expects these controls to be implemented by October 2001.

## Recommendation 2-4:

The Commissioner of Customs should determine the extent to which the control problems associated with the local permit-to-transfer programming feature in Air AMS affects other Customs programs, reporting, and special projects—such as the Tin Man Project—and take corrective action.

### Management Response and OIG Comment

Customs concurred with and plans to take action the OIG believes will address the recommendation. In the short term, Customs plans to audit as many permits-to-transfer as its staffing will allow. Systemic problems noted will be referred to the Customs Client Representative for ~~corrective action.~~ Problems that are criminal in nature will be referred to enforcement personnel. Other audits will be performed based on the results of these initial audits. This special audit effort along with

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increased uniform post audits will be addressed in a Customs expects to publish in March 2001. new directive that

Customs also intends to make programming changes to Air AMS. In the mid-term, it intends to develop an edit check that will prevent the use of a local permit-to-transfer authorization when a CFS code does not match the local port of entry code. Because of the programming and testing required, Customs expects this control to be implemented by January 2002. In the longer term, Customs is considering adding a new status code in Air AMS for air waybills being transferred to non-AMS de-consolidators. These waybills would be kept in this new status code until waybill is matched to an entry and "reconciled" in ACS. Because of the major programming considerations and certain complications cited in ACS, Customs expects to implement this programming change by January 2002.

## Recommendation 2-5:

The Commissioner of Customs should perform a risk assessment to determine the extent to which the problems identified in this report are occurring in the other types of merchandise movements within Air AMS and take action to address those problems.

### Management Response and OIG Comment

Customs concurred with and was taking or planned to take action the OIG believes will address the recommendation. In its response, Customs stated it had identified the permits-to-transfer and in-bond movements as areas where corrective action was required. Customs' OIT was performing an analysis of those areas. Because of the system programming and testing required, Customs expected the analysis to be completed in January 2002.

## Recommendation 2-6:

The Commissioner of Customs should ensure adequate controls over the manifesting and merchandise entry processes are incorporated in the design and development of any new automated cargo processing system.

### Management Response and OIG Comment

Customs concurred with and planned to take action that the OIG believes will address the recommendation. In its response to the OIG, Customs stated it would consider the Air AMS issues reported by the OIG and

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corrective actions taken in its planning of a new automated cargo processing system.

## **Recommendation 2-7:**

The Commissioner of Customs should consider identifying the control deficiencies with Air AMS as a material weakness under the Department of the Treasury Federal Managers' Financial Integrity Act process.

### Management Response and OIG Comment

Customs concurred with the OIG recommendation and stated in its response that it was performing an analysis regarding the control deficiencies reported by the OIG. Customs expected to complete the analysis in October 2000.

# GLOSSARY

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<b>Air Waybill</b>	<b>Air carrier document that describes specific cargo arriving on an aircraft and other pertinent information.</b>
<b>Automated Broker Interface (ABI)</b>	<b>A module within ACS that allows brokers and importers to electronically communicate with Customs, including filing entry documents and obtaining inspection results.</b>
<b>Cargo Manifest</b>	<b>Air carrier summary document consisting of all individual air waybills for cargo onboard an aircraft. Required of air carrier on or before an aircraft's arrival into the U.S.</b>
<b>Confidence Interval</b>	<b>The probability an estimate lies within a specified range given desired precision. Generally stated in conjunction with precision; e.g. 95% confidence plus or minus 5%.</b>
<b>Expected Error</b>	<b>The amount of error that will be tolerated in sampling estimates. Commonly referred to as precision. Can be calculated in absolute (numbers) or relative (percentages) terms depending on how results are used. Expected error should fall within actual lower and higher error level.</b>
<b>In-Bond Shipment</b>	<b>Movement of cargo from the first port of arrival to the final destination port. Entry or export documents are required at destination port.</b>
<b>Informal Entry</b>	<b>Incoming cargo with declared value of not more than \$2,000. No entry documents required by Customs. Cargo can be released through Section 1321 of 19 USC.</b>
<b>Lower Error Level (LEL)</b>	<b>The lower amount of error that will be tolerated in a sampling estimate.</b>
<b>Permit-to-proceed</b>	<b>Authorization to move cargo from first port of arrival to destination port. Permitted only where cargo does not leave the aircraft.</b>
<b>Permit-to-transfer</b>	<b>Authorization to move cargo under bond from a carrier to a CFS within the same port.</b>
<b>p Value</b>	<b>The variation in or proportion of qualitative characteristics of a population or universe. Used to determine sample size for attribute sampling. Generally, 50% is a conservative p Value if population variation is not well known.</b>
<b>Upper Error Level (UEL)</b>	<b>The higher amount of error that will be tolerated in a sampling estimate.</b>

# OBJECTIVE, SCOPE AND METHODOLOGY

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Appendix 1  
Page 1 of 3

The audit objective was to determine if Customs controls were adequate to ensure inspection of all arriving air cargo prior to its release into commerce as required by 19 CFR. The OIG focused on arriving air cargo reported (manifested) on Customs Air AMS and transferred to a non-AMS CFS for which there was no evidence of entry or clearance in ACS; i.e., an electronic manifest to a paper entry document. The OIG then focused on the potential impact on Customs' revenue collections, trade compliance and contraband enforcement efforts of the electronically manifested air cargo not being properly inspected or released by Customs.

The audit was conducted in accordance with the *Government Auditing Standards* issued by the Comptroller General of the United States and included such tests that were deemed necessary.

The OIG fieldwork was conducted between September 1998 and October 1999 at Customs': (1) Headquarters in Washington, DC; (2) Office of Information And Technology (OIT) in Newington, Virginia; and (3) offices at airports in Los Angeles and San Francisco, California; Miami, Florida; Chicago, Illinois; New York City, New York; and Atlanta, Georgia.

At Customs Headquarters and OIT, the OIG obtained, reviewed and discussed with program officials background information on the Air AMS program. The OIG obtained information on the level of AMS program participation by air carriers and CFSs at 27 of the 29 AMS airports as well as the processes, procedures, programming codes and controls over manifesting, transferring and releasing of cargo within the Air AMS and ACS. The OIG did not include in its audit 2 AMS courier hubs in Ontario, California, and Charlotte, North Carolina, because those hubs were mostly engaged in electronic manifesting and entry.

At the OIG's request, the Customs OIT programming group in Newington, Virginia, developed a program that could match the AMS manifest information to the cargo entry information in the ACS. With this special program, Customs was able to identify and extract information on air waybills at the 27 AMS airports for merchandise manifested on the AMS in FY 1998 and transferred to a non-AMS warehouse for which there was no evidence of entry or release in the ACS. Customs provided the OIG access to ACS. With the aid of Customs staff at LAX, OIG performed parallel testing to ensure the validity of the program and audit methodology. However, the OIG was not able to check the completeness of the data provided by OIT. Program and methodology development required 6 months.

The OIG selected 6 AMS airports for audit testing purposes. The period for audit testing purposes was FY 1998. The 6 airports selected represented about two-thirds of the FY 1998 Air AMS waybills identified by the Customs program as having no evidence of entry or release. The OIG did not select the Anchorage airport even though it was first on the list because most cargo arriving at that airport was reportedly moving to other airports in the lower 48 states under permit to proceed authorizations.

# OBJECTIVE, SCOPE AND METHODOLOGY

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Appendix 1  
Page 2 of 3

Using the services of a statistician, the OIG employed attribute sampling techniques to determine the number and related fines and penalties on those air waybills for which proper entry or release was not found and to compare the results achieved at one AMS airport to another AMS airport. The OIG randomly selected 7 days from a Julian calendar to determine the sample for audit testing purposes. The OIG set a conservative pValue of 50 percent to achieve a much larger than needed sample.

The OIG used a 95 percent confidence interval to determine the level of precision expected from the sampled data. The audit methodology used a single decision (a yes or no condition) to determine an exception to Customs' business processes and inspections. Audit control limits were set at 1.96 standard deviations above and below the mean which means 95 percent of the sample was expected to fall within those limits. Overall precision achieved for all 6 AMS airports was a LEL of 1 percent and an UEL of 3 percent, within expectations and suitable for projection purposes.

Customs OIT group provided detailed information on 2,068 air waybills for the 7 days at the 6 airports where the special program found cargo was transferred to a non AMS warehouse but for which no evidence of entry or clearance was found in the ACS. The OIG reviewed the information in the ACS on all 2,068 waybills in the sample and eliminated those where an entry was found and those that were in-bond movements, duplicate records, deleted records, shell records and low risk cargo, such as paper, documents and medical materials. After this elimination, 1,031 waybills required proof of entry and/or release.

The OIG provided the Customs directors at the 6 selected airports detailed information on the remaining 1,031 waybills and requested them to provide proof of entry and inspection or release by Customs. The directors reported their results to the OIG and provided all documentation relating to those air waybills where proof of entry or release was not found and fines and penalties were assessed. The OIG visited or telephoned Customs at the 6 airports to review and discuss the fines and penalties assessed and to verify at least 10 percent of those waybills where Customs reported finding evidence of entry or release.

The OIG used the random sample results at the 6 airports for two projections. The first projection estimated the number of waybills in the 1998 universe that lacked evidence of proper entry or release at those 6 airports and the related total fines or penalties. The number of waybills lacking evidence of entry or release and the related fines and penalties at the other 21 AMS airports were estimated based on the combined results of the 6 selected airports.

The second projection estimated the magnitude of the misuse of the Air AMS in FY 1998 and quantified the monetary impact in terms of potential fines and penalties. The OIG identified

# **OBJECTIVE, SCOPE AND METHODOLOGY**

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**Appendix 1**  
**Page 3 of 3**

the waybills in the sample containing errors or evidence of misuse and calculated an error or exception rate for the random sample. This exception rate was used to estimate the number of waybills with evidence of errors or misuse of the system in FY 1998. The OIG used those results to determine a range of fines and penalties Customs could have but elected not to assess the trade for misusing AMS. The lower range or estimate was based on a \$1,000 fine and penalty for failing to maintain proper records. The higher range was based on a fine and penalty calculated as the greater of the \$1,000 record keeping fine or the fine based on the declared weight of the manifested merchandise.

Because the cargo had been released into commerce and information in the Air AMS was inadequate, the OIG was not able to determine lost revenues from duties and tariffs, violations of trade laws or instances of contraband smuggling.

Because the audit focused on the system, the size of the audit sample was not sufficient for the OIG to detect possible pattern and practice of improper or illegal activity by individual carriers, CFS operators, brokers, importers or other interested parties involved in the importation of merchandise.

# CUSTOMS AIR AMS PROGRAM PARTICIPATION

Appendix 2

U.S. Customs Service  
Air AMS Program Participation  
As Of September 30, 1998

Port Code	Airport Location	Air Carriers (1)	Number of Warehouses		
			AMS	Non-AMS	Total
3126	Anchorage, AK	7	2	2	4
2720	Los Angeles, CA (LAX)	20	14	16	30
5206	Miami, FL	31	10	178	188
3901	Chicago, IL (O'Hare)	10	6	92	98
4701	New York City, NY (JFK)	29	51	69	120
1704	Atlanta, GA	3	3	58	61
2801	San Francisco, CA	11	8	11	19
3801	Detroit, MI	1	1	31	32
3205	Honolulu, HI	4	1	10	11
0417	Boston, MA	7	4	19	23
4601	Newark, NJ	8	7	98	105
5401	Washington, DC (Dulles)	6	1	2	3
3029	Seattle, WA	6	4	72	76
2006	Memphis, TN	2	2	11	13
4102	Cincinnati, OH	2	2	8	10
5501	Dallas-Fort Worth, TX	2	1	23	24
3501	Minneapolis-Saint Paul, MN	1	0	6	6
2910	Portland, OR	1	0	3	3
4503	Saint Louis, MO	1	0	9	9
2811	Oakland, CA	1	1	28	29
1808	Orlando, FL	2	1	9	10
4913	San Juan, PR	3	1	8	9
2722	Las Vegas, NV	1	0	0	0
5309	Houston, TX	2	1	20	21
4103	Columbus, OH	2	0	28	28
1108	Philadelphia, PA	5	4	29	33
1801	Tampa, FL	2	0	16	16
1512	Charlotte, NC	1	1	5	6
2721	Ontario, CA	1	1	0	1
Total - 29 Airports			<u>127</u>	<u>861</u>	<u>988</u>

- (1) In total, 56 air carriers participated in the Air AMS program. Many of the carriers participated at more than one airport.

Source: U.S. Customs Service

# **AIR AMS WAYBILLS WITHOUT ENTRY – FY 1998**

Appendix 3

U.S. Customs Service  
Universe Of Waybills In Air AMS  
With No Evidence Of Entry Or Release In ACS  
Fiscal Year 1998

<u>Port Code</u>	<u>Airport Location</u>	<u>Waybills</u>	<u>Percent</u>
3126	Anchorage, AK	35,581	24.3
2720	Los Angeles, CA (LAX)	22,727	15.5
5206	Miami, FL	18,525	12.7
3901	Chicago, IL (O'Hare)	17,878	12.2
4701	New York City, NY (JFK)	14,986	10.2
1704	Atlanta, GA	14,650	10.0
2801	San Francisco, CA	8,236	5.6
3801	Detroit, MI	3,911	2.7
3205	Honolulu, HI	2,901	2.0
0401	Boston, MA	2,762	1.9
4601	Newark, NJ	1,115	.8
5401	Washington, DC (Dulles)	599	.4
3029	Seattle, WA	552	.4
2006	Memphis, TN	436	.3
4102	Cincinnati, OH	365	.2
5501	Dallas-Fort Worth, TX	349	.2
3501	Minneapolis-Saint Paul, MN	322	.2
2910	Portland, OR	179	.1
4503	Saint Louis, MO	100	.1
2811	Oakland, CA	84	.1
1808	Orlando, FL	66	.1
4913	San Juan, PR	5	0
2722	Las Vegas, NV	3	0
5309	Houston, TX	3	0
4103	Columbus, OH	2	0
1108	Philadelphia, PA	0	0
1801	Tampa, FL	0	0
Total - 27 Airports (1)		<u>146,337</u>	<u>100.0</u>

(1) Appendix excludes AMS courier hubs at airports in Ontario, CA, and Charlotte, NC.

Source: Office Of Information And Technology  
U.S. Customs Service

# OIG RANDOM SAMPLE OF AIR AMS WAYBILLS

Appendix 4

U.S. Customs Service  
OIG Random Sample Of AMS Air Waybills  
Needing Evidence Of Entry Or Release  
Fiscal Year 1998

	<u>LAX</u>	<u>MIA</u>	<u>ORD</u>	<u>JFK</u>	<u>ATL</u>	<u>SFO</u>	<u>Totals</u>	<u>Percent</u>
TOTAL SAMPLE	479	421	404	304	293	167	2,068	100.0%
<u>OIG ELIMINATIONS:</u>								
Entries Found	(55)	(3)	(46)	(16)	(8)	(39)	(167)	( 8.0%)
Low Risk Shipments	(122)	(242)	(78)	(178)	(17)	(96)	(733)	(35.4%)
Others	(0)	(4)	(56)	(9)	(63)	(5)	(137)	( 6.6%)
WAYBILLS NEEDING EVIDENCE OF ENTRY	<u>302</u>	<u>172</u>	<u>224</u>	<u>101</u>	<u>205</u>	<u>27</u>	<u>1,031</u>	<u>50.0%</u>

Legend:

LAX Los Angeles International Airport  
MIA Miami International Airport  
ORD O'Hare International Airport (Chicago)  
JFK John F. Kennedy International Airport (New York City)  
ATL Hartsfield International Airport (Atlanta)  
SFO San Francisco International Airport

Sampling Methodology:

The OIG randomly selected 7 days in FY 1998 for audit testing purposes at the above six AMS airports. For each of those airports, Customs identified those waybills manifested in AMS that had been transferred to a non-AMS warehouse but for which there was no evidence in the ACS of entry or release. The OIG reviewed ACS for those 2,068 waybills and eliminated those waybills associated with informal entries, in-bond shipments, duplicate records, deleted records, shell records and low risk cargo such as documents, medical material, paper, etc. The OIG then requested each airport director to provide evidence of proper release or entry for the remaining 1,031 waybills.

Source: Office Of The Inspector General

# OIG RANDOM SAMPLING PRECISION

Appendix 5

## U. S. Customs Service OIG Random Sampling Precision Fiscal Year 1998

<u>Airport (1)</u>	<u>Universe</u>	<u>Percent</u>	<u>Sample</u>	<u>Precision (2)</u>		
				<u>Actual LEL</u>	<u>Expected EL</u>	<u>Actual UEL</u>
LAX	22,727	15.5	479	3.45	4.43	5.41
MIA	18,525	12.7	421	3.74	4.72	5.70
ORD	17,878	12.2	404	3.84	4.82	5.80
JFK	14,986	10.2	304	4.58	5.56	6.54
ATL	14,650	10.0	293	4.69	5.67	6.65
SFO	<u>8,236</u>	<u>5.6</u>	<u>167</u>	<u>6.53</u>	<u>7.51</u>	<u>8.49</u>
Subtotal	97,002	66.3	2,068	1.15	2.13	3.11
Others (21)	<u>49,335</u>	<u>33.7</u>	<u>0</u>			
Totals	<u>146,337</u>	<u>100.0</u>	<u>2,068</u>			

(1) See Appendix 4 for Airport Legend.

(2) See Glossary for Definitions.

### Explanation of Sampling Precision:

OIG sampling was based on 95% confidence level  $\pm 5\%$  and a 50% pValue. Based on size of the individual airport and total sample, the OIG calculated the expected error level (EL) and compared it to the actual lower (LEL) and upper (UEL) error levels achieved. In every instance, the expected error level was between the actual lower and upper error levels, indicating the sampling results could be used to statistically project and forecast to the universe for FY 1998. As a result, the OIG is 95 percent confident its projected results for FY 1998 are within 5% ( $\pm$ ) of the actual amounts.

Source: Office Of The Inspector General

# ACTUAL AND PROJECTED FINES & PENALTIES

Appendix 6

U.S. Customs Service  
Projected Fines And Penalties On Universe Of  
AMS Air Waybills Lacking Evidence Of Entry Or Release  
Fiscal Year 1998

<u>Airport (1)</u>	<u>Sample Results</u>		<u>Projected Results</u>	
	<u>Number of Waybills</u>	<u>Amount of Fines &amp; Penalties</u>	<u>Number of Waybills</u>	<u>Amount of Fines &amp; Penalties</u>
LAX (2)	18	\$ 67,304	237	\$ 979,761
MIA	2	4,880	88	214,720
ORD	0	0	0	0
JFK	34	63,257	1,676	3,119,036
ATL	1	1,477	50	73,850
SFO	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Subtotal	55	\$136,918	2,051	\$4,387,367
Others (3)	<u>0</u>	<u>0</u>	<u>1,002</u>	<u>2,130,252</u>
Totals	<u>55</u>	<u>\$136,918</u>	<u>3,053</u>	<u>\$6,517,619</u>

(1) See Appendix 4 for Airport Legend.

(2) LAX random sample fines and penalties include \$47,640 of fines and penalties that were assessed during methodology testing but not used to project to LAX universe.

(3) The 21 airports exclude AMS airports (courier hubs) at Ontario, CA and Charlotte, NC.

Source: Office Of The Inspector General

# RANDOM SAMPLE FINES & PENALTIES

Appendix 7

U.S. Customs Service  
Fines And Penalties Assessed By Customs  
On Randomly Sampled AMS Air Waybills  
Fiscal Year 1998

<u>Airport (1)</u>	<u>Arrival Date</u>	<u>Customs Case Number</u>	<u>Fines &amp; Penalties (2)</u>
LAX	02/15/98	1999272030016101	\$ 3,552
	02/15/98	1999272030016201	7,200
	09/09/98	1999272030016301	6,912
	12/17/97	1999272020203501	1,000
	12/17/97	1999272020203401	1,000
		Port Total	\$19,644
MIA	09/09/98	2000520630000401	\$ 1,000
	12/17/97	2000520630000501	3,880
		Port Total	\$ 4,880
JFK	10/09/97	1999470130042301	\$ 320
	10/09/97	1999470120377901	1,000
	12/17/97	1999470120378101	1,000
	04/16/98	1999470120378001	1,000
	10/09/97	1999470130042401	5,000
	12/17/97	1999470130042701	10,000
	12/17/97	1999470130042901	10,000
	12/17/97	1999470130042801	10,000
	12/17/97	1999470130042201	2,937
	08/07/98	1999470130042501	5,000
	10/09/97	1999470120379701	1,000
	12/17/97	1999470130042601	5,000
	02/15/98	1999470120378301	1,000
	04/16/98	1999470120379501	1,000
	02/15/98	1999470120378201	1,000
	10/09/97	1999470120379601	1,000
	12/17/97	1999470120378401	1,000
	02/15/98	1999470120379401	1,000
	04/16/98	1999470120378501	1,000
	08/07/98	1999470120379001	1,000
	08/07/98	1999470120379101	1,000
	09/09/98	1999470120379301	1,000
	09/09/98	1999470120379201	1,000
		Port Total	\$ 63,257
ATL	02/15/98	1999170420043401	1,477
		Grand Total	\$ 89,278

(1) See Appendix 4 for Airport Legend.

(2) Fines and penalties assessed for violating 19 CFR, including failure to report arrival, hold merchandise, file accurate manifest and keep records. No penalties were assessed by Customs at ORD or SFO.

Source: U.S. Customs Service

# METHODOLOGY TESTING FINES & PENALTIES

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Appendix 8

U.S. Customs Service  
Fines And Penalties Assessed By Customs  
During OIG Methodology Testing  
Fiscal Year 1998

<u>Airport (1)</u>	<u>Arrival Date</u>	<u>Customs Case Number</u>	<u>Fines &amp; Penalties (2)</u>
LAX	03/24/98	1999272030002901	\$ 5,000
	03/24/98	1999272030002801	1,000
	03/24/98	1999272030002501	1,000
	03/24/98	1999272030002601	1,000
	03/24/98	1999272030002701	1,000
	03/25/98	1999272030001901	5,000
	03/25/98	1999272030002001	1,000
	03/25/98	1999272030002101	1,000
	03/25/98	1999272030002201	1,000
	03/25/98	1999272030002301	1,000
	03/25/98	1999272030002401	1,000
	07/07/98	1999272030005401	26,300
	07/06/98	1999272030005501	<u>2,340</u>
		Grand Total	\$ <u>47,640</u>

- (1) See Appendix 4 for Airport Legend.
- (2) Fines and penalties assessed for violating 19 CFR, including failure to report arrival, hold merchandise, file accurate manifest and keep records. Fines and penalties assessed in methodology testing were not used to project sampling results to LAX universe.

Source: U.S. Customs Service

# PROJECTED FORGONE FINES & PENALTIES FOR AMS MISUSE

Appendix 9

## U.S. Customs Service Projected Forgone Fines And Penalties For AMS Misuse Fiscal Year 1998

Airport (4)	Number Of Waybills		OIG Projected Fines And Penalties (1)	
	OIG Sample	OIG Projected	Lower Range (2)	Upper Range (3)
LAX	75	3,559	\$ 3,559,000	\$ 16,545,791
MIA	12	528	528,000	10,502,448
ORD	69	3,053	3,053,000	47,565,740
JFK	43	2,120	2,120,000	15,997,520
ATL	68	3,400	3,400,000	23,541,600
SFO	17	838	838,000	8,085,024
Subtotal	284	13,498	\$13,498,000	\$122,238,123
Others (5)		6,759	6,759,000	62,392,329
Grand Totals	284	20,257	\$20,257,000	\$184,630,452

- (1) Forgone fines and penalties are based on instances where Customs could have but choose not to assess fines and penalties for violations of 19 CFR on waybills in the random sample where carriers misused or abused the AMS system.
- (2) OIG lower range of forgone fines and penalties calculated on minimum \$1,000 fine or penalty.
- (3) OIG upper range of forgone fines and penalties calculated on the greater of the \$1,000 minimum fine or the \$10/kilo or \$20/lb fine or penalty based on cargo weight per carrier manifest.
- (4) See Appendix 4 for Airport Legend. Excludes AMS airports (courier hubs) at Ontario, CA, and Charlotte, NC.
- (5) The waybills and fines and penalties at other 21 AMS airports forecasted on results of random sample at 6 AMS airports.

Source: Office of The Inspector General

# POTENTIAL REVENUE ENHANCEMENTS

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## Appendix 10

A revenue enhancement is an action recommended in an OIG audit report which would, if implemented, enhance the General Fund receipts of the Federal Government, usually without having any budgetary impact on any of the Department of the Treasury's appropriations. The following potential revenue enhancement will be recorded in the Inventory, Tracking and Closure system (ITC) upon issuance of our final report. The potential revenue enhancement will also be included in the OIG Semiannual Report to the Congress.

<u>Recommendation Number</u>	<u>Potential Revenue Enhancement</u>
Finding 1 - Recommendation 2	\$136,918

The above recommendation relates to fine and penalties that were assessed by Customs as a result of this audit. It is Customs management's responsibility to record the actual revenue enhancements realized in the ITC for the collection of these fine and penalty assessments.

# U.S. CUSTOMS MANAGEMENT RESPONSE

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Page 1 of 8



**U.S. Customs Service**

*Memorandum*

DATE: **September 29, 2000**

FILE: AUD-1-OP MD

MEMORANDUM FOR DENNIS SCHINDEL  
ASSISTANT INSPECTOR GENERAL

FROM: Director,  
Office of Planning

SUBJECT: Draft Audit Report on the United States Customs  
Service's Air Automated Manifest Program

Thank you for providing us with a copy of your draft report entitled "U. S. Customs Service's Air Automated Manifest System " (Air AMS) and the opportunity to discuss the issues in this report.

Customs concurs that the substance of the OIG review is accurate and does not disagree with its general or technical content, except for treatment of local transfers being described as a "trick" of the ACS system. Customs has taken a number of steps to address the issues identified during your review. These steps, and additional on-going actions, are outlined in the attached document, as are Customs comments on this draft report. Additionally, a supplemental page outlining information about local transfer authorizations is included as a separate attachment.

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

If you have any questions regarding the attached comments, please have a member of your staff contact Ms. Brenda Brockman at (202)927-1507.

A handwritten signature in black ink, appearing to read "William F. Riley".  
William F. Riley

TRANSMISSION

★

Attachments

SERVICE

★

HONOR

## U.S. Customs Service

### Comments on OIG Draft Report "U.S. Customs Service's Air Automated Manifest System"

#### Recommendation 1-1

The Commissioner of Customs should ensure the fines and penalties assessed as a result of the OIG audit were appropriate and the interested parties were not attempting to circumvent inspection of the merchandise as required by 19 CFR.

#### Comment:

Customs concurs with this recommendation and does not dispute the statistics collected during the OIG audit. Customs emphasizes to the field the importance of assessing fines and penalties correctly and without prejudice. Since the OIG audit, Customs has enacted new regulations, with Treasury Decision 99-29, that outline the execution of fines and penalties, as well as new mitigation guidelines that emphasize collection of duties, taxes and fees.

In determining circumvention by another party to avoid Customs fines and penalties, Customs is exploring creation of a national post audit database and associated reports or query capabilities. This would aid in spotting suspicious trends or inconsistencies from the trade that would signify the possibility of noncompliance. The information gathered from these reports could be shared within the port and between ports as part of a national database.

The creation of such a database will require programming within the ACS system. Expected date of completion will be October 2002. The target date is based on programming and testing that would be required before actual implementation.

#### Recommendation 1-2

The Commissioner of Customs should ensure the prompt collection of the \$136.918 of fines and penalties assessed in the OIG audit.

# U.S. CUSTOMS MANAGEMENT RESPONSE

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Appendix 11

Page 3 of 8

## Comment:

Customs concurs with this recommendation and does not dispute the amount assessed during the OIG audit. Customs has verified that the fines and penalties amounts listed in the report have either been collected or are in the process of being collected. Customs emphasizes to the field the importance of recognizing violations and assessing penalties.

To ensure that post audit procedures are being adhered to, Headquarters is updating a Post Audit Directive, emphasizing proper post audit guidelines to give field personnel consistent instruction during an audit inquiry. Customs is also planning to include in the directive that any penalties uncovered during a post audit should not be discretionary and should be pursued.

To aid in the collection of assessed penalties and claims for liquidated damages, Customs recently promulgated surety sanction procedures. These procedures give early notice of claims to sureties who assist in the encouragement of case resolution with their bond principals. As a result, many cases have been settled.

The items addressed in this recommendation are presently being implemented. Expected date of completion will be March 2001.

## Recommendation 2-1

The Commissioner of Customs should establish controls to measure trade community compliance with Air AMS requirements, especially over the use of special programming features for automatic release and local permits-to-transfer to ensure all merchandise is inspected prior to release into the commerce.

## Comment:

Customs concurs with this recommendation and will implement the following short-term deliverable controls: (1) Customs can closely monitor all carrier transmissions for correct use of the permit-to-transfer, in-bond, and permit to proceed functions during the first 45 days of AAMS participation. If deficiencies are found, referrals to the appropriate Client Representatives can be made for immediate corrective action; (2) AAMS inspectors can perform cursory audits on AAMS carriers targeting the three movements described above; and (3) Mandatory post audits can be performed within the first 6 months of new carrier AAMS participation to ensure continued compliance. Subsequent audits should be performed according to results of the initial audit.

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The short-term deliverable controls will be implemented by March 2001 with the issuance of the new Post audit Directive.

Mid to long-term deliverable controls should include (1) introduction of a statistical sampling methodology, similar to the automated random sampling for post audit compliance reviews of in-bond movements. Scientifically based random sampling of qualifying AAMS air waybills would promote internal controls and enhance trade community compliance with the operational requirements of AAMS and the air commerce portion of 19 CFR 122.

The target date for the mid to long term controls is October 2002. The target date is based on programming and testing that would be required before actual implementation.

## **Recommendation 2-2**

The Commissioner of Customs should provide all system users, including Customs Inspectors, more and better training over the use of Air AMS to improve the quality and usefulness of system information.

### **Comment:**

Customs concurs with the recommendation. Customs has recently completed an Air Automated Manifest System user Guide and developed classroom training on AAMS for Customs personnel. A team of national trainers has been created to conduct this training. Three classes have been conducted since inception in August 2000. The first class was a "train the trainer" class for instructors. The second two classes provided training for field Inspectors. Additional classes will be scheduled in this and coming fiscal years.

The Client Representative Branch of Customs has also received training in Air AMS in September 2000. The Client Representatives have recently been assigned to assist the Trade with AAMS issues. Each carrier, deconsolidator, and freight forwarder has an assigned Client Representative to assist them with AAMS issues.

The items addressed in this recommendation are presently being implemented. Expected date of completion is October 2001.

## **Recommendation 2-3**

The Commissioner of Customs should monitor the trade's use of the Air AMS and take appropriate action, including fines, penalties, and other sanctions as necessary, to enforce trade compliance with Customs' quality expectations.

### **Comment:**

Customs concurs with the recommendation. In the last year, Customs enacted Treasury Decision 99-29, (March 2000) which outlines new guidelines for the assessment of fines and penalties, liquidated damages for cargo misdeliveries and general order merchandise. These guidelines also allow for the execution of higher fine amounts and authorize field personnel to assess penalties on violations newly provided for by regulation. The directive also outlines new mitigation procedures that emphasize the collection of duties, taxes and fees. By utilizing these guidelines, this signifies that Customs is making a vigorous effort in the enforcement of trade compliance.

The items addressed in this recommendation are presently being implemented. Expected date of completion is October 2001.

## **Recommendation 2-4**

The Commissioner of Customs should determine the extent to which the control problems associated with the local permit-to-transfer programming feature in Air AMS affects other Customs programs, reporting, and special projects-such as the Tin Man Project-and take corrective action.

### **Comment:**

Customs concurs with the recommendation. A short-term deliverable control would be to conduct as many post audits of local transfers to non-automated deconsolidators as allowed by staffing. Any identified problems relating to the local transfer function should be referred to the carrier or deconsolidator's respective Client Representative for corrective action if systemic in nature or to enforcement personnel if criminal in nature. Future audits would be dependent on results of the initial audits. This item will be addressed along with the increase of uniform post audits along with the publication of the Post audit Directive in March 2001.

AAMS currently does not have an edit that will reject the local transfer if the FIRMS code is not within the transfer port. A mid-term deliverable control to prevent erroneous permit-to-transfer authorizations when the

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FIRMS code does not match the entry port is to create an edit that will check the FIRMS code against the port code. This edit will be included in future programming.

The target date for this item is January 2002. The target date is based on programming and testing that would be required before actual implementation.

A long-term consideration would be to add a new status for air waybills being transferred to non-automated deconsolidators (Status = Transferred?). These bills would be kept in this new status until entry information is matched with the transferred bills to effect a reconciled status. Major programming considerations must be taken into account before such a change can be implemented. It is further complicated by the fact that not all air waybills are updated by cargo selectivity processing, but require manual posting by inspectors. FTZ admissions and personal shipments are examples of this. The requirement to post manually would currently mean many ports would spend time attempting to post against air waybills that are not in AAMS, since the system currently encompasses less than 50% of all inbound airfreight.

The target date for this item is January 2002. The target date is based on programming and testing that would be required before actual implementation.

## Recommendation 2-5

The Commissioner of Customs should perform a risk assessment to determine the extent to which the problems identified in this report are occurring in the other types of merchandise movements within Air AMS and take action to address those problems.

## Comment:

Customs concurs with this recommendation. The three categories of controlled movements identified by the OIG (permits-to-transfer, permits-to-proceed, and in-bond movements) are the only controlled cargo movements in Air AMS. In the permit-to-proceed area, no substantial problems or complaints have reached HQ. Permits-to-transfer and in-bond movements have been identified as areas where corrective action is required. OIT has identified and is currently performing analysis on the identified areas above.

The items addressed in this recommendation are either in compliance or under research by the Office of Information and Technology. Expected date of completion is January 2002.

## **Recommendation 2-6**

The Commissioner of Customs should ensure adequate controls over the manifesting and merchandise entry processes are incorporated in the design and development of any new automated cargo processing system.

### **Comments:**

Customs concurs with this recommendation and will consider the issues and subsequent corrective actions in its planning for a new automated cargo processing system.

A target date concerning this issue is not applicable at this time.

## **Recommendation 2-7**

The Commissioner of Customs should consider identifying the control deficiencies with Air AMS as a material weakness under the Department of the Treasury Federal Managers' Financial Integrity Act process.

### **Comment:**

Customs concurs with this recommendation and is currently performing an analysis regarding this issue. The analysis is scheduled for completion by October 30, 2000.

## **SUPPLEMENTAL PAGE REGARDING LOCAL TRANSFER AUTHORIZATIONS**

### **Response to OIG Audit**

The Air Automated Manifest System (AAMS) includes a feature that is unique to this manifest system. When freight is authorized to be transferred locally (permit to transfer) from an automated carrier to a non-automated deconsolidator (CFS), AAMS will "reconcile" the bill. This does not release the freight into the commerce of the U.S., but allows for the transfer of the freight from the carrier's premises to the deconsolidator's premises. The intent of the reconciling of the air waybill was to indicate to the inspector that the bills being transferred to a non-automated facility could not be reviewed electronically for entry information.

Permit-to-transfer authorization is granted with a "1-F local transfer authorized" message that is sent to the carrier. It is not a "1-C General Exam" message that is an authorization for release into the commerce of the U.S. The deconsolidator will maintain a paper trail of the freight, requiring an entry or entries before release is authorized into the commerce of the U.S. Post Audit Teams are to visit these non-automated sites to ensure compliance with the entry and release of merchandise.

A feature of Selectivity processing allowed for the writing of an entry record in air manifest when the entry matched an air waybill in AAMS. This occurs even if the air waybill is already marked as "reconciled"; the matching of the entry, however, does not cause a change in the air waybill record. Due to this being an "undocumented feature" of AAMS, it has not always been utilized in the post audit of the non-automated deconsolidators. Post Audits of this kind were always expected to focus on review of the paper documents (transfers, entries, general orders, etc.) at the deconsolidator's premises.

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**Appendix 12**

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Appendix 13

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