



Analysis: In-bond shipments, the Trojan Horse

Journal of Commerce

Wednesday, March 19, 2008

By: James Giermanski / The JOURNAL of COMMERCE ONLINE

In-bond shipments have long been an essential part of trade in the United States, but the system overseen by Customs and Border Protection may be out of step with the increasing demands of national security.

In-bond shipments to and within the United States are shipments not intended to enter U.S. commerce and therefore do not bear the requirement of payment of the appropriate import duties and taxes required under the law. To ensure that the U.S. collects its duties in case an in-bond shipment does enter U.S. commerce, Customs and Border Protection requires the posting of an import bond as security to guarantee payment.

Bonded cargo is carried in sealed containers or trailers. Ordinarily, these conveyances with their cargo have a final destination outside the U.S., but can transit through the country to a border port of export or to a U.S. seaport for export. In-bonds also could have a temporary destination in the U.S., including foreign trade zones and bonded warehouses, that are not technically in U.S. Customs territory.

For merchandise eventually entered into U.S. commerce, an importer may have a "single transaction bond," for a single customs transaction, or a continuous bond for successive transactions used for bonded refining warehouses, like smelting warehouses. In-bonds classified as T&E (transportation and exportation), are bonded goods that must transit from one port of entry to a port of export. In-transit bonds can be used for the movement of bonded cargo to internal ports of entry such as Dallas, St. Louis or Charlotte where they are cleared and any obligated duties and fees are paid. Even the container's transport and handling must be done by a bonded carrier.

All these bonds are surety or indemnity bonds that ensure Customs the payment of the scheduled duty listed in the Harmonized Tariff Schedule should the goods be lost, misdirected or fail to arrive at the port of export, bonded warehouse, or foreign trade zone or illegally entered into U.S. commerce. The port director can set the amount of bond for a single transaction or entry, or for continuous transactions.

Carrier bonds are also required. The minimal carrier bond for all modes of carriage is \$50,000, but a port director can increase that amount. The Trade Act of 2002 demands the identification of cargo at the six-digit harmonized tariff description or better, to identify the cargo accurately so that the proper duty can be assessed. Thus, Customs focuses on identifying contents with respect to their value in the case of an "ad valorem" assessment of duty, or their weight or size if it is a "specific" tariff.

In effect, Customs is fundamentally concerned with tax collection, and thwarting the escape and evasion of taxes through smuggling operations. This was evidenced by Customs' announcement this month that it seized more than \$67 million worth of clothing brought illegally to the U.S. via the in-bond system. The shipment was supposed to transit through the U.S. Southwest to a Mexican destination. "This is a significant example of yet another attempt to evade the U.S. textile trade laws," said Kevin Weeks, Customs' director of field operations in Los Angeles.

Unfortunately, Customs' emphasis seems to be more on revenue collection than on security. Today, thousands of sealed containers from foreign shippers in other countries move on our highways or sit at foreign trade zones, bonded warehouses and in motor carriers' bonded distribution sites in population centers. Regrettably, we don't really know what these conveyances contain! We only know what they are said to contain. We also don't know where they have been or what could have been placed in them at foreign origin or while in transit within the U.S. Let's look at an in-bond from Mexico, for example. Who is the shipper? How do we know if it is a shipment of merchandise or a dirty bomb? Who is the Mexican long-haul carrier, and does it go directly to the border? Even if it does, the carrier typically drops the container in a drop lot where it waits, at some Mexican border ports, for up to 10 days or more. Who tracks this and how? Who has access to the container during that time? What Mexican transfer trucking company actually carries the in-bond into the U.S.? Does that carrier go directly into the U.S. after picking up the container?

These are all questions that can be asked of a normal shipment imported from Mexico. However, unlike the normal entry, the in-bond typically goes through U.S. Customs without a physical inspection unless there is cause for one. Further, because there is a high-priced bond on the contents, and because Customs is focused on revenue collection, there is less of an incentive to inspect, especially if the contents are not supposed to enter U.S. commerce and could be just transiting the U.S. to Canada or to some U.S. seaport for export.

Although Customs does not require an inspection, it encourages one if smuggling is suspected. Customs stated in a directive for preparing the in-bond Customs Form 7512: "Examination of in-bond shipments in addition to mandated 'Tin Man' (paper) examinations is encouraged to prevent smuggling." In 1998, Customs initiated in the Automated Commercial System a tracking and audit system known as "Tin Man." It was designed to provide real-time tracking of in-bond shipments from origin to destination, including entry and exportation. The "real-time" tracking reference, however, consists merely of the entry of departure and arrival times into the ACS system.

Now, Customs requires in-bond requests through its Automated Broker Interface message simply known as QP. As of Feb. 2, 2008, that QP message automatically updates the Automated Commercial Environment e-manifest. All of these messages and interfaces do nothing to confirm what is really in the container entering the U.S. It amounts to simply electronic tracking as opposed to paper tracking.

The Government Accountability Office investigated the in-bond cargo system. In a report issued last May, the GAO found that Customs frequently does not follow up on shipments processed through the in-bond system. This costs the U.S. hundreds of millions of dollars in

revenue, and raises the possibility that contraband could move on to other U.S. destinations.

The conclusion is obvious: The U.S. has and perpetuates an in-bond system that focuses on tax collection and not on security. The GAO stated that the limited information available on in-bond cargo also impedes Customs' efforts to manage security risks and ensure proper targeting of inspections.

Even Mexico has an in-bond program that focuses on more than just tax collection. Its new, yet-to-be-implemented program calls for satellite control and monitoring of in-bond shipments transiting Mexico or entering recinto fiscalizados, Mexico's version of U.S. foreign trade zone.

Finally, one large and respected U.S. customs broker on the U.S.-Mexican border reviewed this manuscript and stated the following: "Customs does not consider any in-bond 'Customs business' and over the years has not had the necessary controls built into its ACS and ACE system. Any carrier, broker, or even a 3PL can issue in-bonds if they have some basic knowledge of the forms and some computer skills."

So why doesn't Customs fix the system? The problem, as I see it, is Customs' lack of knowledge about available systems that can be employed or even mandated for in-bond shipments traveling throughout the U.S. The solution to the in-bond problem is the smart container. Smart containers already exist, Customs just doesn't know that. The agency still talks about creating a smart container as demonstrated by its December, 2007, Request for Information. That RFI was even protested in February by some in the smart container industry. The industry protest informed Customs that the private sector is already well-advanced and past the level of information and sophistication sought by Customs.

Smart containers have already been demonstrated to work. Their use between a foreign origin and a U.S. destination was demonstrated in 2006 between Germany and the U.S. In addition, the cost to the shipper is minimal, hardly more than electronic locks and seals. These smart containers can do what the current U.S. in-bond system cannot. Smart containers can carry and transmit electronically both logistics and sensory data. While there is no single definition of a smart container, it should be defined generally as a conveyance that meets World Customs Organization standards and complies with U.S. law, like the SAFE Port Act, and U.S. programs like C-TPAT by carrying and transmitting electronically, data and security intelligence from origin through destination to Customs when needed and on demand. Smart containers, as they exist today, perform at least seven clearly defined operations:

1. Functioning as a part of a system approach necessary to coordinate all facets of the supply-chain process to ensure visibility and security, beginning at origin;
2. Capturing and transmitting electronically certain trade data that will link to other supply-chain documentation. Examples would be the container number, or booking number;
3. Complying with the WCO, C-TPAT and the European Union's Authorized Economic Operator requirements to maintain the integrity of the entire container, by detecting a breach anywhere into its body;

4. Reporting in real time or as close to real time, any breach;
5. Providing worldwide geographic positioning throughout the supply chain when queried, and when programmed, automatically report its position if it is off its designated course of travel;
6. Recognizing and recording the identity of the authorized person opening the container at destination;
7. The container should be adaptable to different sensors and be able to communicate with or be adapted to divergent software packages used by shippers and carriers within the supply chain.

Smart containers like these will be used in the EU's Seventh Framework program. They also will be able to accommodate the EU's more robust AEO program, a counterpart to C-TPAT. The obvious question is why hasn't Customs fixed the in-bond system by simply requiring in-bonds to utilize smart containers? Not only would these smart containers correct the security weaknesses of our in-bond program, but they also could solve other Customs problems, including the textile transshipment violations caused by fraudulent document manipulations.

James **Giermanski** is chairman of Powers International Inc. and director of the Center for Global Commerce at Belmont Abbey College. He can be contacted at (704) 825-4741, or at powersintlinc@bellsouth.net.