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AUDITS ROUNDTABLE
AAEI Annual Conference
June 7, 2016
Confidential and Anonymous

On June 7, 2016, BPE Global facilitated a roundtable discussion on Audits at the AAEI Annual Conference. We are sharing a consolidated version of the notes taken during each session with all of the roundtable discussion participants to provide insight into the valuable discussions, ideas and strategies.

During our first roundtable session, all the participants were focused on import audits. The subsequent sessions were a mixture of import and export. Additionally, participants stated that both compliance and freight audits are performed. We limited our discussion to only compliance-related audit tasks and topics.

1) How do you pick what to audit?

A significant percentage of the discussion participants stated that they decide what to audit based on risk. All regions are audited, but it was disclosed that some regions have more transparency with data than others. Areas of higher risk would be audited annually, with some regions audited only once every few years. Companies stated that they do a cursory review of every element on a percentage basis, depending on risk.

Trade compliance areas that the participants deemed higher risk included:

Import	Export
• Preferential/free trade agreements	• Classification
• First sale	• Licensing and license management
• Focused Assessment	• License authorizations
• Free Trade Zone	• Electronic Export Information (EEI) filings
• C-TPAT	• Recordkeeping
• Classification	• Jurisdiction
• Valuation	• End-use / End users
• Entry declarations	• Freight forwarders
• Post Entry Amendments (PEAs)	• Valuation
• Recordkeeping	• Domestic/foreign designation on EEI filings
• Other Government Agency (OGA) and Partner Government Agency (PGA) declarations	• Port codes
• Country of Origin	• Powers of Attorney (POA)
• Suppliers	
• Brokers	

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One company develops a risk profile for each country. This would include the types of transactions conducted in the country and the level of risk that the transactions pose. Based on the risk assessment, the auditors decide whether to do a transactional audit versus a focused assessment.

One e-commerce company performs high risk targeting on key issues such as duty free treatment, license / permits, and value, while another audits just the programs that yield the highest duty savings.

Participants mentioned that they develop regional targets and business targets. Targeted audits can identify where processes and policies have gaps.

We mentioned that BPE Global recommends targeted audits to reduce the effort of the audit. If you focus on high volumes, high values, irregular classifications, irregular countries of origin and destination it's practically guaranteed that errors will be discovered.

Another common theme among participants was the requirement for every trade compliance site to perform a quarterly self-audit. In this example, they also a minimum random audit and a focused assessment type audit.

One company specifically indicated that they execute targeted audits based on number of brokers and specific brokers (e.g. couriers). This company samples 10 percent of their entries, which is a pretty high number. This company also requires their brokers to do a 100 percent post-entry audit and the company audits the broker audits.

Several participants mentioned partnering with the corporate Internal Audit function in their compliance audits. This can increase audit resources and frequency. It is an effective tool so long as trade compliance works with Internal Audit to help this function understand the concepts that they are auditing.

Moving away from how audits are structured to specific audit points, we found that the participants agreed that auditing transactions are key. Transactions point to bona fide errors that must be corrected. It was emphasized that businesses must be audited against transactional processes (such as, was the Country of Origin correct, was there a certificate of origin required and subsequently generated?) and the compliance process (such as, does the procedure state which team is responsible for determining or obtaining the Country of Origin?).

Some key sources of data points to audit include reconciliation flags, related parties and incoterms. The topic of Incoterms elicited an animated discussion. Incoterms are not necessarily generated by the trade team; instead they are generated by another team that usually has no training on incoterms and trade compliance. It is clear that incoterms create major issues for trade compliance teams and participants agreed that they should be audited.

Reviews of overages, shortages or other discrepancies were included whenever audits were conducted on-site. One best practice was cited as scheduling time with every person who participates in

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import/export transactions when visiting a site. This allows the auditor to get a sense of the compliance culture at the site and potentially uncover unknown issues.

Exports appear to be mostly audited based on declarations, utilizing EEI filing reports as a source on which to audit. BPE Global noted several gaps in the approach related to auditing EEI filings. First noted was the potential gap in the cases when shipments have been exported from the facility but haven't been declared. Another gap identified was from participants reporting that they are not looking at their export activity to determine if an EEI should have been filed for a single transaction (e.g. transaction greater than $2500 that didn't get filed). Finally, we heard several companies report that they audit transactions only where the company is the USPPI but not the filer.

Special note: Two companies mentioned AES penalty notices for incorrect Port Codes (the company used the airport code instead of the seaport code). They filed on day one and were audited by CBP the next day. The shipment had not even left. It appears that CBP is validating port codes for EEI filings.

We mentioned that all companies that we've worked with have some degree of risk with their recordkeeping. Companies are either relying on their service providers to retain their records or the records the companies claim to retain are difficult to retrieve. We observed that some companies are fluent in recordkeeping, however, most are not. Therefore recordkeeping is a key element of any audit. One participant touted their retention program, featuring a central location for entry record storage.

Some other interesting points that were raised, but we were unable to elaborate on with each team are the following:

- Participants agreed that any type of Trusted Trader program would drive increased auditing.
- Participants agreed that it's important to audit powers of attorney as a data point.
- One participant recommended engaging mailroom personnel as they are looking at exactly what is shipping.
- Other participants mentioned that regional teams can also contribute to risk assessments and they can run mock government audits. The purpose of the mock audits is a preventative measure to ensure that they're ready for a government audit.
- Some companies treat couriers differently than brokers and audit them separately. This appears to be because the brokers and couriers are managed by different teams.

One participant mentioned that their corporate culture is more laid-back than most and most of their factories are based in the western hemisphere. The company stages mock audits at these factories. The purpose of the mock audits is a preventative measure to ensure that they're ready for a government audit.

One last thought related to auditing specific compliance controls is with assists. Assists were reported as a gap that needs to be audited, yet none of the participants offered insight into their assist audit concept or program.

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2) How often do you audit?

Program, complexity, and risk is a driver for the frequency of audits. Usage of specific compliance processes, potential penalty amount and past audit history is part of the risk profile. Depending on culture of company, audits may be more frequent.

Participants tied their classification and valuation audit schedule to calendars (e.g. bi-annually) or the Quarterly Design or Business Review schedule. In many cases, C-TPAT was audited annually. One participant mentioned that they sample transactions once per month for classification and value. Other companies cited that they did 100 percent post entry reviews.

One company has established a 95 percent compliance threshold. Everything over 95 percent compliance accuracy is an acceptable risk to the compliance team.

Participants cited program maturity level as a driver for how often audits happen. Is the program a new program that needs to be monitored to ensure that it is being correctly administered? Is it a new supplier or service provider? These are some of the questions the trade audit team considers.

It is possible that specific audit types or locations can go years without being audited because they are low risk. The converse is also true, items with large duty savings, under OGA scrutiny, etc. may be audited constantly.

3) How do you determine how many transactions to audit?

In many cases participants stated that they would determine how many transactions to audit based on the risk profile of what they are auditing. Participants stated that they might do random, targeted, statistical or 100 percent audits based on the risk profile of a company. One company cited that they have developed a program that generates random samples.

Conversely, several companies appear to have determined that 10 percent of transactions is the correct number of transactions to audit. This audit includes all data elements, including a review of classification performed by a 3rd party. Participants recommended that not only is the classification reviewed, but also the quality of the description and information about items that are to be classified. All too often, the internal or external team responsible for classification receives incomplete or insufficient information to perform classification. This results in incorrect classification determinations and potential exposure for the company.

A recurring theme was to require brokerage companies to audit 100 percent of a company's entries on special programs, anti-dumping/countervailing and other high risk items. One small company that does quarterly audits has a broker performing audits on 100 percent of the transactions.

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In general, participants agreed that the audit itself is very low sample and targeted in order to gain insight into the effectiveness of the company's policies and processes. The biggest issue is not identifying the problem, its agreeing how big that problem is and how to solve it.

With C-TPAT, many participants cited sending C-TPAT questionnaires to all supply chain partners. This was interesting because C-TPAT did not appear to be as risk-based as other compliance program audits. One company mentioned an effort to align AEO and C-TPAT requirements to standardize audits and program management.

In many cases, auditors are not looking if a compliance activity was correctly done (e.g. classification). Instead, they are looking at whether or not the broker did what they were told (e.g. do the SLI and EEI match?). While this doesn't necessarily get you to the right answer, it is a process review.

4) How do you report out/up the results of your audit?

There was a lively discussion regarding reporting audit findings. Some participants explained that they do not put audit reports in writing. Other companies work under the direction of counsel to do their audit work so their reports are privileged and confidential. Another participant provides internal staff with the audit reports. All participants report red flags in their audit reports and that there are different requirements between reporting on an internal audit versus reporting on a government audit or an audit by a service provider.

Some methods of reporting included reporting on quantity (e.g. this many sites, this many issues) rather than exactly what the issues are. Other methods focus on severity, reporting where the issues are and how severe they may be. For example, FCPA issues are immediately escalated, other issues may not be so quickly escalated. Discrepancy reports were also popular, with some companies generating quarterly discrepancy reports while others do this monthly. Discrepancy reports appeared to be less formal, as they are more of an indication for a company to check data elements such as classification, value, and overages or shortages. Reporting is also useful for the compliance department as participants indicated they determine if they are going to follow up with further audits or additional tasks when they compile the audit report.

BPE Global recommended separating material versus immaterial errors in the audit report. This provides a good perspective on risk to non-compliance executives. It was stressed that reporting to the C-level should be in general terms, with a positive spin explaining where the company is compliant and where they are working on issues. Another suggestion we provided for audit reports was to use a "heat map" to track compliance levels. Red may be used for violations and government audits, yellow for potential issues and green for compliant operations. Black can be used for "unknown" trade compliance levels for locations that have not yet been audited.

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5) How is changed effected?

BPE Global stressed that action plans and recommendations should be provided to the business operations with follow-up on any actionable items. In addition, root cause analysis, gap analysis, and a compliance score are useful tools to audited entities.

We mentioned that the internal audit teams must collaborate with the audited business during the audit process. The audited entity should have a chance to review the report before it is finalized and presented to management so they are familiar with the issues and agree with the report.

One participant suggested that corrective actions are tied to performance reviews for businesses. This is sometimes effective, but they have also seen that sometimes nobody reacts.

A key to effecting change is the reporting structure of the compliance team. Some company's compliance teams report to Finance, so that if there is a money issue then Finance is hot on this.

6) Post Script

If you are hitting 99 percent compliance level, what's the incentive to do 100 percent auditing? What some companies do is increase the sample size. If the quality decreases, then the auditing becomes more intense and detailed.

A strong recommendation from participants is that good compliance programs should be integrated into the supply chain rather than be a gatekeeper to supply chain.