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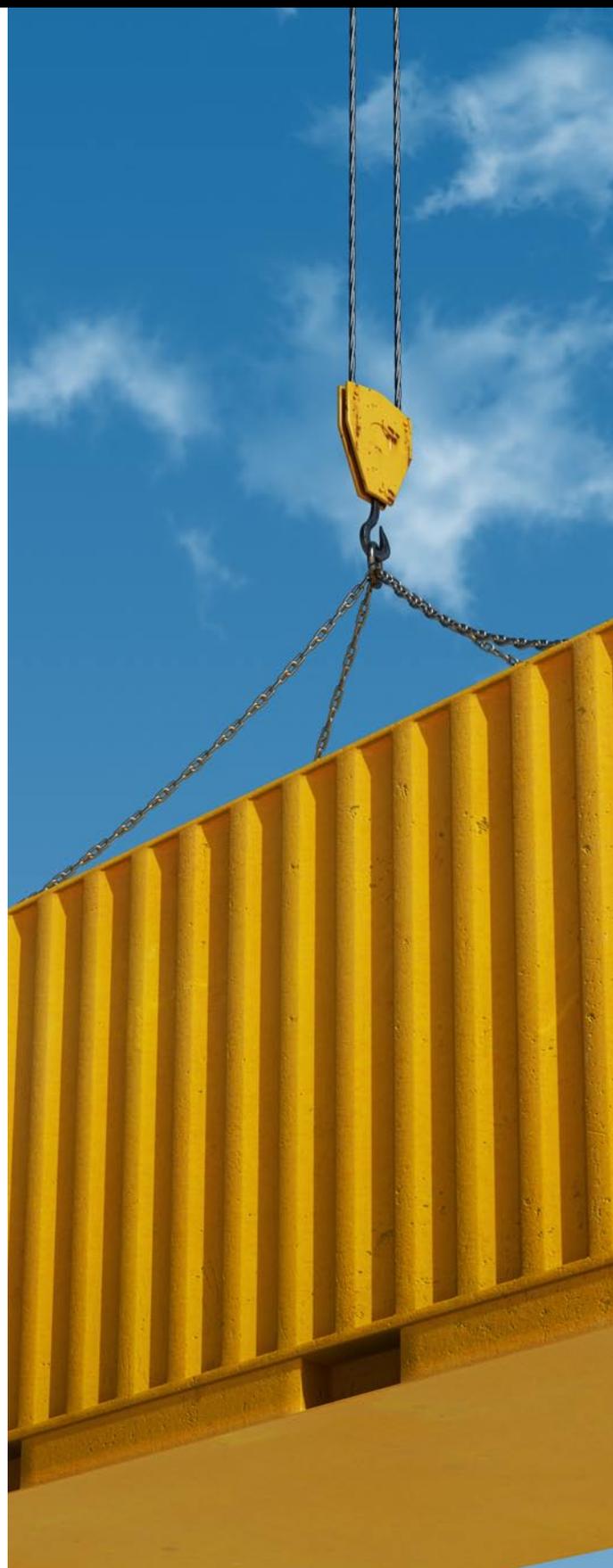
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Trade & Customs

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Financier Worldwide canvasses the opinions of leading professionals around the world on the latest trends in trade & customs.

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The background image shows the interior of a large cargo aircraft. The ceiling is white with several rectangular light fixtures. The walls are also white and feature various panels and labels, including '131' on the right side and 'KL JL' near the bottom. The floor is filled with rows of metal shelving units, each equipped with red-handled locking mechanisms. The perspective is from the front of the aircraft looking down the length of the cargo hold.

INTRODUCTION

As the world becomes smaller and global trade more commonplace, governments internationally are more focused on the need for robust and comprehensive trade and customs monitoring and enforcement activities.

Technological advancements have made a significant impact on customs enforcement across a number of different jurisdictions. In the US, for example, the federal government has made considerable investments in high-tech trade enforcement tools in recent years. The US' new enforcement program can detect a potential enforcement opportunity when a shipment of goods arrives in a US port, and will provide an electronic red flag to Customs and Border Protection officers in every other US port where that importer has entered goods.

Elsewhere, legislative developments have also sought to modernise customs systems, increasing efficiency and compliance wherever possible. Both domestic and foreign companies active in China today face significant pressure from the General Administration of Customs as it attempts to raise customs revenue collections. Similarly, in Germany and across the EU, compliance has been the watchword of late. As member states look to protect the continent's wider economic interests, the EU has modernised its approach to customs. Monitoring activity has been augmented and authorities have introduced increasingly contemporary enforcement activities.

Although enforcement and compliance are issues for government agencies, the emphasis on compliance lies with companies themselves. Firms must take care to ensure that their own customs planning is in place. Staff should be engaged in regular education and training exercises. Legislation has helped to shift this emphasis; as such, internal controls are vital in today's trade climate.



UNITED STATES

MICHAEL T. CONE
FISHERBROYLES, LLP

Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN THE US? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

CONE: Companies engaged in 21st century international trade must understand the state's electronic monitoring and enforcement capabilities. The federal government has invested significantly in high-tech trade enforcement tools. This includes cross-agency communication platforms because US Customs and Border Protection (CBP) enforces the laws of more than 40 different federal agencies at the border. Today, a revenue or enforcement 'opportunity' with a shipment arriving in one US port will generate an electronic red flag to CBP in every other US port where that importer has entered goods. It's increasingly difficult to hide, or to contain the damage once it is done.

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Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

CONE: Broad risks include institutional complacency, internal overconfidence and undue reliance on customs brokers. Trade compliance can be an enormously complicated exercise, but even simple mistakes can wipe out profits – or worse, result in significant penalties. Specific narrow risks include unknowingly sourcing goods subject to antidumping duty liability, or attempting to take advantage of privileges contained in free trade agreements without establishing proper controls or recordkeeping procedures. And then there is the opportunity cost of paying more customs duties than are properly owed. Transfer pricing is also a sensitive area. Periodic check-ups with customs attorneys are always in order.

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Q IN WHAT WAYS CAN COMPANIES MANAGE COMPLIANCE COSTS AND INCREASE THE OPERATIONAL EFFECTIVENESS OF THEIR END-TO-END SUPPLY CHAIN?

CONE: Companies suffer excessive compliance costs when they find themselves responding to agency enforcement actions. Most often those major costs could have been avoided through minor investment in front-end compliance controls. Supply chain efficiencies flow directly from participation in the Customs - Trade Partnership Against Terrorism, or C-TPAT. This voluntary program requires an importer and its foreign suppliers and logistics providers to follow basic security measures such as having fences around their operations and properly sealing and tracking shipments. When it comes time to release merchandise from the US container terminal, shipments imported by C-TPAT participants go to the front of the line.

Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST? HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

CONE: The US is rolling out staged revisions to complicated export control rules. Different regulatory regimes apply to two separate categories of goods and technology: those that 'go boom', which are covered by the International Traffic in Arms Regulations (ITAR), and those that don't, which are covered by the Export Administration Regulations (EAR). ITAR involves munitions and EAR covers 'dual use' items that bad guys might divert to violent ends. Purely domestic activity does not create a safe harbour – conveyance to foreign nationals located anywhere is deemed conveyance to the foreign country. Severe penalties for violations including the failure to obtain required licences are commonplace.



“To implement best practices, assign customs compliance responsibility to a trained individual within your organisation, have a written compliance manual in place, and run internal checks and reviews at least twice a year.”

Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN THE US?

CONE: They often underestimate the risks. The Tariff Act of 1789 imposing customs duties was the first major legislation signed into law by President George Washington. Today customs duties generate \$20bn in annual revenue, and they remain hallowed ground for CBP and the US Department of Justice (DOJ). Nor is there a free ride for duty free goods. CBP enforces all US laws at the border, and a failure to comply with any agency laws can result in detentions, seizures, fines and other mischief. Imported food products need to comply with FDA rules, bicycles with CPSC rules, vehicles with EPA rules, and so on.

Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

CONE: One hotbed of activity is penalty actions commenced by CBP and DOJ against importers – and individuals and companies working in them or in consort with them. Specialised US customs courts appear to be expanding the scope of defendants liable for penalties when mistakes are made. The customs penalty statute presumes negligence whenever a ‘material false statement or omission’ is made – for example, in misdeclaring the country of origin of a good, or improperly classifying the good under the tariff schedule. Another active area of litigation involves lawsuits seeking the embargo of imported goods allegedly infringing intellectual property rights.

Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

CONE: Take it seriously and maintain currency within your organisation. The Customs Modernization Act of 1993 ushered in a brave new world of 'informed compliance' and 'shared responsibility'. Stated another way, CBP now thinks you're on the hook to get everything right. And the government continues to promulgate thick reams of new laws and regulations that impact imported merchandise. To implement best practices, assign customs compliance responsibility to a trained individual within your organisation, have a written compliance manual in place, and run internal checks and reviews at least twice a year. Prepare for the day when CBP might come knocking.



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Michael T. Cone, Esq., practices administrative, customs and international trade law. He counsels clients from all over the world on a wide array of US regulatory compliance issues, and represents their interests before US agencies. His expertise includes matters falling under the jurisdiction of US Customs and Border Protection and the panoply of other administrative bodies that regulate the importation, marketing and sale of merchandise. He represents clients in litigation before federal and state courts including the US Court of International Trade, and has been featured in media including the *New York Times*, the *International Herald Tribune*, and National Public Radio.



ARGENTINA

PABLO GAYOL
MARVAL O'FARRELL & MAIRAL



Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN ARGENTINA? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

GAYOL: In 2012, the Argentine government introduced an Import Prior Sworn Statement – referred to as 'DJAls' by their acronym in Spanish – requirement applicable to almost all imports of goods. An Argentine company cannot place an import purchase order until the Import Prior Sworn Statement is approved by the authorities for each of its import transactions. The approval rate of the Import Prior Sworn Statements varies over time, but it has been increasingly difficult for companies to obtain them. As a result of the Import Prior Sworn Statement system, the foreign trade strategy has been at the top of the agenda for most Argentine companies and, in many cases, senior management has been involved in obtaining the approval of such Import Prior Sworn Statement. This has been particularly the case because government policy in trade matters has been somewhat erratic and dependent on balance of payment concerns.

Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

GAYOL: Under the exchange control regulations in force, exporters must repatriate and liquidate in the exchange market the proceeds of exports of goods and services within timeframes established by the regulations. The major risks are related to the failure of certain exporters to repatriate to Argentina the proceeds of the export of goods and services in the required time and manner. The term for the repatriation of proceeds arising from services is 15 days from collection. In the case of exporting goods, the timeframe depends on the type of goods exported and the counterparty to whom they are sold. The regulations on repatriation are cumbersome and complex. The risk is higher when the counterparty failed to pay for the goods in a timely fashion or if there is a shortage in the payment, since in these cases specific foreign exchange rules apply, with which some exporters are not familiar. In particular, should the importer fail to pay altogether, the exporter should take measures to prove that it has pursued collection in order



to justify the delay in repatriation before the Central Bank. The key is to have a strong trade compliance department that keeps a close track of all exports and the terms for repatriating the funds.

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Q IN WHAT WAYS CAN COMPANIES MANAGE COMPLIANCE COSTS AND INCREASE THE OPERATIONAL EFFECTIVENESS OF THEIR END-TO-END SUPPLY CHAIN?

GAYOL: The ability of companies to manage cost and increase their effectiveness is severely constrained by restrictions on the import of goods and the unpredictability of the approval process for DJAs and the terms applicable to the repatriation of proceeds from exports. Most companies' priority is to be able to import the goods needed for their business, and efficiency and reduction of cost is subordinated to these concerns. Many importers are willing to increase their logistics cost and financial cost, to be able to import. Also, the foreign exchange regulations impose the maximum terms for the collection of exports after clearing customs, and therefore pose a significant constraint on the efficiency of the supply chain.

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Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST? HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

GAYOL: The regulation of export goods with a national security interest poses a low risk in Argentina.

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Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN ARGENTINA?

GAYOL: The compliance and monitoring of imports and exports by Argentine firms has been one of their top priorities as a result of the restrictions on the import of goods, which in practice result in the need to obtain government authorisation for each import, and the strict monitoring of the foreign exchange regulations applicable to the repatriation of proceeds resulting from the export of goods. The senior management of many Argentine companies, especially those that resell imported goods, have been involved in negotiating with the government the necessary authorisations for the import of goods. The seniority of the resources and time devoted by Argentine companies to dealing with the authorisations necessary to import goods has affected the day to day operations of many companies and entailed increased costs.

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Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

GAYOL: In recent years there has been an increase in customs disputes relating to the ability to import goods, as well as in relation to compliance with repatriation of funds regulations. Disputes related to the ability to import goods have been carried out by importers before the courts in order to be able to import goods prior to obtaining the import licences – for example, import certificates or an Import Prior Sworn Statement – which are a condition to the import of almost any good. In most cases, the importers claim that the governmental authorities unduly delayed or denied such licences. In general, importers have been successful in obtaining from courts orders which allowed them to import the goods without such licences, when the delays or denials by the authority are unjustified.

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“In recent years there has been an increase in customs disputes relating to the ability to import goods, as well as in relation to compliance with repatriation of funds regulations.”

Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

GAYOL: Customs compliance management has been at the top of the agenda for most companies. It is important that the customs department closely monitors the status of exports and their collection, since such exports are subject to repatriation obligations. Also, the ability of the logistics and foreign trade department to keep the flow of government authorisation for imports in place can provide a key competitive advantage. Most Argentine companies are fully aware of the importance of customs compliance management.



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Pablo Gayol is a partner at Marval, O'Farrell & Mairal in 1997. He focuses on international trade and financial regulation. He graduated as a lawyer cum laudae from the Universidad Católica Argentina in 1996 and obtained a Masters in Laws from the University of Chicago Law School in 1997 and a Master in Finance from Universidad del CEMA in 2002. He is also a CFA Charterholder. Mr Gayol is Professor of Antidumping and Quantitative Restrictions at Universidad de San Andrés and Professor of Derivatives Law at Universidad Torcuato di Tella and Universidad del CEMA.

**MARVAL
 O'FARRELL
 MAIRAL**



GERMANY

KAY MASORSKY

KPMG



Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN GERMANY? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

MASORSKY: The interpretation and application of the EU customs rules – above all, Customs Code and Implementation Regulation for the Customs Code – in many respects vary significantly among the EU Member States. Over the last 20 years, as a customs consultant I have time and again seen that German customs officers apply the rules in a very strict way. The monitoring activities are definitely increasing as are enforcement activities in Germany – namely, offence proceedings. A general observation therefore is that, in line with so many other areas, compliance is the leading topic in customs matters, as can clearly be seen in connection with the Authorised Economic Operator (AEO).

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Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

MASORSKY: Major risk exposures with respect to trade compliance must be differentiated between import and export trade. For import, a decisive question is whether customs duties have been assessed correctly. The decisive parameters for the assessment are the classification of the imported good and the correct customs value. As customs declarations are nowadays submitted electronically, a major risk exposure is data quality. Mitigation begins with qualified people. Equally important are good processes that ensure that those employees who have responsibility for customs issues are well informed on changes that influence customs issues.

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Q IN WHAT WAYS CAN COMPANIES MANAGE COMPLIANCE COSTS AND INCREASE THE OPERATIONAL EFFECTIVENESS OF THEIR END-TO-END SUPPLY CHAIN?

MASORSKY: It can be observed that many decision making managers still regard customs matters as a mere clearance activity that can be handled by employees on top of their normal business, which in most cases means logistics. This will often automatically mean that these employees will not get the chance to receive training in customs matters. The money that is saved is then often spent later on corrective measures after customs audits reveal findings and – this is especially true for Germany – lead to proceedings against the management, blaming them for a lack of organisation and control. A compliance check of import and export activities, combined with effectiveness testing, will in many cases cost money upfront, but save far more in the long run.

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Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST? HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

MASORSKY: The key topic here is export control. This is an issue of steadily increasing importance – and, at the same time, risk. Export control is not only about the movement of goods, it is also about knowing your customer, knowing the country of ultimate destination and knowing the end-use. It is also about transferring information abroad and making that information accessible or available abroad. Infringements of export control rules will often lead to criminal offence proceedings. Since in the EU no export duties exist, this a mere compliance issue – but one that must definitely be addressed.

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“Customs matters are not a mere clearance activity but a major part of all supply chain activities. It can – and should – be used strategically.”

Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN GERMANY?

MASORSKY: The importance of trade and customs matters to companies is steadily increasing, but I would, as a general observation, say that there is still plenty of room for improvement. For many companies that import or export on a large scale, customs matters remain either outbound to a logistics provider without controlling their work, or handled by employees who are not given the appropriate training and are not included in strategic decisions like contracting new suppliers, changing the technical parameters of goods, or supplying markets in different regions. Thus, risks arise, but at the same time, saving opportunities are not utilised.

Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

MASORSKY: Within Germany, the number of disputes has actually decreased. One area that reflects this trend is disputes arising from appeals against tax assessments. Of course, there are still disputes against BTIs, for instance, and also against tax assessments. But my feeling is that companies are less interested in ‘fighting’. There are two reasons for this. First, they fear the influence of an appeal on their daily work with their locally responsible office and wish to maintain a ‘good relationship’. Second, in the majority of cases the appeal will ultimately result in a court case that – in Germany – will take three or four years to reach a resolution.

Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

MASORSKY: Internal compliance checks and regular reviews are expected by customs. If you look at the AEO criteria, the questionnaire, you will find that customs authorities more than ever expect that things will not be handled correctly just by coincidence, but as a result of a sound process, well-trained people and an effective organisation. At first sight, it might seem that a customs compliance management strategy will only cost money. But taking a closer look reveals that it will save money. Customs matters are not a mere clearance activity but a major part of all supply chain activities. It can – and should – be used strategically.



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Heading KPMG's Global Trade and Customs Practice in Germany, Kay Masorsky has been responsible for various project teams serving clients globally. With more than 20 years of professional experience, he has dealt with customs issues of all kinds. In addition to his legal work on matters such as classification, valuation and origin of goods, a major part of his work includes assisting clients in optimising and implementing customs processes, and in planning and reorganising business structures and supply chains.





ITALY

MASSIMO FABIO
KSTUDIO ASSOCIATO (KPMG)



Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN ITALY? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

FABIO: In the past, Italian companies mainly resorted to forwarding agents for customs advice, especially about compliance. In the last couple of decades, the increasing impact of trade and customs issues on the business of companies with foreign interests, small family companies and large multinational companies, has also led to the formation of specialised centres of excellence within various Italian legal practices. Like the Big Four, more traditional practices have recently started to specialise in customs issues, a complex and constantly evolving field. The greater interest shown by the private sector has been triggered by the evolution of EU customs law, which began in 2006 and which has changed not only the provisions and regulations, but also the duties and functions of EU customs authorities. All the authorities of the Member States have modernised their approach with a view to offering users an all-electronic platform, thereby facilitating lawful exchanges and combating potential fraud detrimental to the EU's interests.

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Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

FABIO: During the last few years, because of this evolution, customs authorities have been paying closer attention to how the normal import/export operations of companies are described. And more often than in the past, the Italian authorities have been focusing on compliance with the rules on origin and value. With regard to origin, there have been increasingly strict controls and inspections to verify compliance with the rules on the use of the term 'made in Italy', denoting typical Italian products, in all sectors from fashion to food. With regard to customs value, the main risk is the incorrect valuation of transactions, when royalties or assists – such as artwork, design, moulds, and so on – are involved, or transfer pricing policies. These components, mentioned in EU customs law, must be added to the invoiced price and included in the taxable base for customs purposes. Companies may mitigate the



risk by using the instruments provided by EU customs regulations.

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Q IN WHAT WAYS CAN COMPANIES MANAGE COMPLIANCE COSTS AND INCREASE THE OPERATIONAL EFFECTIVENESS OF THEIR END-TO-END SUPPLY CHAIN?

FABIO: The best way to achieve international efficiency is to use the local customs clearance system, also through one's own agents, to handle customs matters at one's own premises through a single customs office for the whole EU. In 2014, however, most companies are still operating through multiple customs offices, thereby increasing the risk of different interpretations of the rules, with clear repercussions on the speed of shipment and delivery, and the customer's perception of a firm's competitiveness. Through local customs clearance, as shown by the experience of companies which have already adopted this system, it is possible to reduce the cost of customs formalities considerably, and consequently optimise the import and export supply chain, and reduce the possibility of risks related to irregularities or litigation.

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Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST? HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

FABIO: In Italy, particular attention is paid to typical 'made in Italy' products, expressing world-famous Italian creativity. Examples are the fashion industry, the textile and leather industries, the automotive industry, with its famous sports cars, and the food industry, with a wide range of unique products appreciated all over the world, ranging from wine to cheese, and from cold cuts to mineral waters. In order to produce and trade products which incorporate Italian style and know-how, companies must undergo checks by the authorities, to verify that they have correctly applied the rules on origin. As this is a very sensitive area, each company must control its own production processes in order to avoid any damage to reputation, while there are now general security measures for each type of product. The broader controls introduced



“Among Italian companies, the management of trade and customs has always been underestimated and delegated mainly to forwarding agents, outside the company.”

from 2006 have led the EU to introduce a compliance formula granting AEO status to reliable operators. This is the AEO (Authorised Economic Operator) certification procedure, whereby the applicant discloses the procedures adopted in its foreign affairs.

Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN ITALY?

FABIO: Not as much as in other EU countries. Among Italian companies, the management of trade and customs has always been underestimated and delegated mainly to forwarding agents, outside the company. It is only in the last few years that the cultural approach has changed and that companies have begun to manage their international businesses in a more aware and informed manner. Customs formalities have always been perceived as restrictive and constraining. Now, in tune with the times, they are beginning to be considered as an opportunity to manage customs tax in the best way possible, and, with the harmonised instruments described by the GATT/WTO, to be more fair, effective and secure.

Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

FABIO: Litigation is rising sharply. The wider technical knowledge required by the customs offices, and the higher attention paid to the aspects described above, have recently led to numerous disputes. With particular reference to customs value, there has been litigation about the potential application of customs duties to royalties and the reconciliation of fluctuations in transfer prices. In the past, it was common practice not to properly acknowledge the fees paid for intangibles as necessary elements of the taxable base for customs purposes. Only in the last two years has the trading community acknowledged – due to increased inspections by national customs offices – the need to examine licence agreements, in order to understand whether or not customs duties have to be charged. The same attention must be paid to transfer pricing adjustments, for which a special analysis is now required, in order to evaluate their effect on customs tax.

Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

FABIO: Firstly, Italian companies operating abroad certainly have to overcome a persistent cultural prejudice towards customs law and procedures. Customs law is not an ancillary discipline related only to logistics, but is a priority area of international taxation, knowledge of which is a necessary pre-condition for entering any new market, in order to identify fresh opportunities and potential risks. Therefore, every modern company must regularly train its staff on the constantly evolving regulations, and check that they follow the prescribed procedures. Furthermore, abandoning the traditional approach, which was to address customs issues only in critical situations, each company should do its own customs planning. By considering the different factors involved in the core business – type of product, manufacturing, origin and countries of destination, agreements between the parties, and so on – planning should anticipate any possible issue and provide all the necessary instruments to achieve the best possible scenario, speeding up delivery, decreasing the overall customs burden and preventing any risks or irregularities, thus making the company highly competitive throughout the global market.



Massimo Fabio

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Massimo Fabio is a tax lawyer dealing with international trade and customs planning for multinational companies. Appointed 'Academic of the ICLA' (International Customs Law Academy) in September 2013 at the WCO Headquarters, he is lecturer at the annual LLM in international taxation, in the faculty of Law of the Leiden University (NL), a leading customs litigator and author of many publications in international tax and trade issues, amongst which is the 'Customs Law of the European Union' (Wolters Kluwer, Law & Business, IV ed. 2012). He also implemented innovative customs solutions from virtual warehousing to the Free Trade Area in Italy.



TURKEY

MURAT PALAOGLU
KPMG TURKEY



Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN TURKEY? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

PALAOGLU: As an emerging market and a member of the Customs Union within the EU, Turkey has been attractive to investors both with regard to the growing local market and also its hinterland, which includes MENA countries. This attraction creates a boost in Turkey's foreign trade. The country is becoming a centre for both production and trade as a hub for the MENA market. Transit trading, importation, using bounded facilities, Free Trade Zones and customs regimes might be considered as trade options. Given that different products are being traded across Turkey between various countries, the government has increased related rules and created new tools to prevent illegal trade while at the same time promoting legal trade. Thus, the government is focused on being efficient in both monitoring and enforcement activities via new methods and tools, such as post control audits, risk analysis and e-customs applications. Using the right tool in the correct way is essential for companies in order to benefit from cost reduction as well as to comply with regulations.

Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

PALAOGLU: The nature of gift and the complex structure of import taxation creates an exposure, especially where importers outsource their importation processes. The calculation of base for import duties varies depending on the type of duty and also the product itself. Thus, an error when calculating the tax base or in determining the HS Code of the product may result in penalty exposure. On the other hand, trade policy measures and non-tariff barriers such as standardisation, surveillance and anti-dumping applications should be taken into account. Also, for multinational companies, other tools such as transfer pricing applications and royalty and licence payments should be evaluated from a customs perspective. Since different company departments engage in international trade, each department focuses on its priority;



this should also be improved, with all procedures, from accounting to import declaration, being observed from a compliance perspective. Establishing internal compliance audit units and obtaining customs compliance audit services can help companies to mitigate risks.

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Q IN WHAT WAYS CAN COMPANIES MANAGE COMPLIANCE COSTS AND INCREASE THE OPERATIONAL EFFECTIVENESS OF THEIR END-TO-END SUPPLY CHAIN?

PALAOGLU: I believe that the highest level of cost occurs when companies do not meet compliance requirements. On the other hand, employing experts for compliance purposes sometimes may not be efficient and may also be costly. Outsourcing compliance review and audits, which would include review of end-to-end supply chain processes, is the most efficient way to manage compliance costs. Understanding the needs of the local market and meeting the requirements of local authorities, based on the expertise of an experienced service provider, is a method used frequently in the Turkish market.

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Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST? HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

PALAOGLU: The nature and definition of a traded product should be considered by companies from different perspectives. On one hand, since Turkey's location and neighbours make it strategically sensitive, companies are expected to be aware of the risks arising from the product itself as well as from the foreign party importer or exporter. On the other hand, the determination of goods that are subject to dual use and export controls is essential, especially for companies trading with MENA countries. It is very important for companies to have sufficient information about their foreign partners if they are located in strategic and risky markets.

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“Companies are more aware of the importance of understanding trade and customs regulations in order to mitigate any risk and also to discover opportunities.”

Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN TURKEY?

PALAOGLU: I believe that the importance and potential implications of trade and customs regulations are not fully understood by companies. Regarding current changes in the authority’s approach to foreign trade applications, companies are expected to be ready to deal with a process or potential customs audit at any time. Every year around 500 companies are audited by the customs authority. Meanwhile, the latest legislative changes, such as market and quality controls, Authorized Economic Operator (AEO) and so on, affect daily applications. Based on these facts, each and every day companies are more aware of the importance of understanding trade and customs regulations in order to mitigate any risk and also to discover opportunities.

Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

PALAOGLU: Against the backdrop of increasing customs audits and the continuously changing legislation, we are seeing more trade and customs disputes. Over the last decade, Turkey’s foreign trade has radically increased, which forced companies to deal with customs. Considering the new regulations, the customs regime requirements and also the frequent customs audits, the increase in customs disputes has been observed across the market. Customs value related disputes, such as royalty and transfer pricing oriented applications, and also Resource Utilisation Support Fund oriented disputes, are among the most common. Also, origin rules and preferential tariff applications can be named as other important areas of disputes. Following the procedural law requirements, Customs Code requirements and also preparation of a strong petition are the most important steps to follow in case of a dispute.

Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

PALAOGLU: I would suggest that customs compliance strategy should be approved and determined by top management and followed by each relevant department within the company. Since the outcome of a potential exposure might have a critical financial and reputational effect on a company, the strategy should be established with the involvement of management. Appointing a unit or employee specifically to deal with customs compliance would be prudent, but still not sufficient. A fresh pair of eyes is always best when it comes to identifying hidden risks and opportunities. The compliance status of the company, any potential risks caused by partners or third parties, and developments in the related industry can be evaluated via a review and compliance audit. Since each customs declaration legally binds the company, recurring errors create more risk exposure. Thus, in order to prevent recurring errors and identify opportunities, compliance checks and regular reviews are the most effective tools.



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ICELAND

HELGI MÁR JÓSEPSSON
KPMG EHF



Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN ICELAND? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

JÓSEPSSON: Recently there seems to have been an increased awareness in Iceland about the importance of correct customs classification of goods. This is especially true in relation to changes in technology, related to hardware and equipment. The level of complexity when it comes to import duties, such as customs and excise duties, value added tax and various other costs which may be added upon the import of goods, make correct customs classification extremely important. The Icelandic government's agenda is to simplify excise duties levied on imports. The professed object of excise duties is to protect domestic production, when in fact such levies have been levied on imported goods that are not competing with Icelandic production – that is, similar goods are not produced or manufactured in Iceland. This could lead to fundamental changes in import duties, thus placing even more importance on the correct customs classifications of goods to be cleared through customs in Iceland. Further, there is a bill before the parliament which would abolish most part of the commodity tax in Iceland but the bill has not been approved yet.

Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

JÓSEPSSON: When it comes to trade compliance, the greatest risk exposure would be that the customs classification of imported goods is deemed incorrect. This is especially important as, under the Icelandic customs law, the director of customs is authorised to reassess import charges during the last six years, provided certain conditions are fulfilled. Thus companies, if the customs classification of purchased goods is performed by parties outside the company, should always review customs classification of goods to be imported to Iceland. Incorrect classification may lead to higher import duties. Also, if the import duties could later be deemed to be too low due to an incorrect customs classification, this may expose companies to the risk of penalties and



interest. In addition, importers may need to obtain an import licence, or possibly fulfil other conditions before importing certain goods to Iceland.

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Q IN WHAT WAYS CAN COMPANIES MANAGE COMPLIANCE COSTS AND INCREASE THE OPERATIONAL EFFECTIVENESS OF THEIR END-TO-END SUPPLY CHAIN?

JÓSEPPSON: Companies should set up and maintain a certain structure in order to ensure that from their end of the supply chain, goods to be imported are customs classified as correctly as possible, thus minimising the need for costly corrections later on. A regular review may also prevent costly and time consuming corrections – but authorities can go up to six years back in time with their inspections. Assistance from professionals is always recommended as the complexity of classifications can result in higher duties, penalties, interest, and so on.

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Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST? HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

JÓSEPPSON: Companies need to consider possible licences or special permits when handling products and property with a national security risk, to limit the risk of exposure to potential penalties. They also need to take into consideration whether there might be a reputational risk involved in trading such products or property incorrectly. It is always important for parties to be aware of export issues when moving sensitive information or goods to foreign partners or third parties.

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Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN ICELAND?

JÓSEPPSON: My experience is that companies could place more importance on understanding trade and customs regulation. Due to the specialised knowledge required to understand these sometimes complex rules, companies may not possess the knowledge required to tackle uncertainties relating to trade and customs. With the level of complexity when it comes to various excise duties and other import duties, it is important to have access to domestic parties that understand the local rules and are able to communicate with the Directorate of Customs on equal terms.

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Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

JÓSEPPSON: For the past few years there does seem to be an increase in trade and customs disputes as the customs authorities have performed more customs audits and companies have been more aware of hidden costs related to incorrect customs classifications. Therefore, there seems to be a slow trend towards disputing the customs classification, such as of equipment based on new technology, as well as excise duties on vehicles.

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Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

JÓSEPPSON: It is important to seek advice from the beginning, and become familiar with the current rules and regulations. It is also important to consider the current business environment and be aware of upcoming changes. As with all aspects of business, it is important to carry out regular internal compliance checks and reviews, in order to minimise the risk of being exposed to penalties and interest later on. The Director of Customs carries out audits of, for example, import charges, and is authorised to go back six years in a possible reassessment.

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“Due to the specialised knowledge required to understand these sometimes complex rules, companies may not possess the knowledge required to tackle uncertainties relating to trade and customs.”

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SOUTH AFRICA

MELULEKI NZIMANDE

WEBBER WENTZEL



Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN SOUTH AFRICA? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

NZIMANDE: In terms of trade, on 15 July 2014 the negotiations on the Economic Partnership Agreement (EPA) between the European Union and its Member States, and the SADC EPA States were successfully concluded. The agreement regulates trade between these territories and the private sector will benefit from certainty and the preferential market access regime created by this agreement. In terms of customs, South Africa has published new Customs and Excise legislation with the purpose of bringing customs control in line with the recommendations of the World Customs Organisation as per the Kyoto Convention. The new legislation seeks to modernise customs systems to make them more efficient and to enable implementation of self-compliance. This should make the collection of duties more effective as well as combating cross-border crime.

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Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

NZIMANDE: One of the major risk exposures in trade compliance is ignorance regarding changes to customs requirements which the South African Revenue Service (SARS) and other revenue authorities in the Southern African Customs Union (SACU) introduce from time to time. MFN Duties applied to goods traded between SACU Member States are particularly problematic because ordinarily trade between SACU Member States is free. A recent example is the imposition of duties on all cement imports into Namibia under the infant industry protection clause of the SACU Agreement: South African cement trucks had to be recalled from the border as import costs 'unexpectedly' increased by the amount of the duty. Traders should track customs arrangements applicable to their products.

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Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST?

NZIMANDE: Failure to register with and obtain permits from relevant regulatory authorities is a major risk when dealing with goods with a national security risk. The risk is pronounced in respect of 'dual use goods' as these are civilian goods with a potential military application or controlled chemicals which are inputs in civilian manufacturing operations and civilian users of such goods are not alive to the national security implications. Importation of goods without the requisite registration or permit attracts criminal sanction including imprisonment and fines.

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Q HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

NZIMANDE: Moving sensitive information is a common practice by multinational companies which have operations in multiple jurisdictions. Such companies should be aware of municipal legislation protecting information, particularly third party information. In South Africa, dealings in personal information will soon be subject to the Protection of Personal Information Act, 4 of 2013, which will take effect on a date to be proclaimed by the President. A company that is moving sensitive goods from one country to another must be aware of the applicable legislation from the country of export as well as the legislation in the importing country in respect of the specific goods. A typical example is national, provincial and local government legislation and regulations which would apply to movement explosives or components thereof used in mining operations. Such goods are strictly regulated due to the risk to human life associated with such goods.

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“Some trade issues are regulated by institutions other than customs authorities and companies bear the legal duty to comply.”

Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN SOUTH AFRICA?

NZIMANDE: Generally, firms rely on clearing agents to do most of the compliance work in relation to trade and customs regulation. This is not always sufficient, particularly because liability for non-compliance remains with the company. Companies would benefit from knowing the trade and customs regulations relevant to their products. Some trade issues are regulated by institutions other than customs authorities and companies bear the legal duty to comply. It is therefore advisable for companies to conduct a general scan of the regulatory environment and for their compliance officers to proactively manage the risk of non-compliance.

Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

NZIMANDE: South Africa has experienced an increase in applications for an increase in MFN duties – and other duties such as trade remedy duties – across a number of different products. An increasingly contentious issue in such matters is access to the confidential information which parties furnish to South Africa’s International Trade Administration Commission. Several court applications have recently been instituted where parties are not satisfied with non-confidential summaries of such information and are demanding protected, limited disclosure of such information. South Africa is also starting to impose export controls – for example, scrap metal controls – to promote industrialisation. This has generated fierce opposition from exporters, and there are some pending court cases on this issue.

Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

NZIMANDE: At the base of any customs compliance management strategy is a comprehensive list of traded product and countries in which the goods are sourced or sold. Once such list is in place, an audit of what trade or customs laws and regulations apply should be developed. This will lead to an understanding of what registrations and permits are required and which regulatory authorities are involved. Where a breach is identified, consideration should be given to regularising the conduct and legal advice sought on how to deal with past non-compliant conduct. Internal compliance checks are critical as they enable companies to proactively manage the risk of non-compliance.

WEBBER WENTZEL

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JAPAN

TADAKATSU SANO
JONES DAY



Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN JAPAN? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

SANO: The most significant development is in the field of security products export control regulations. The Japanese government had changed the export control policy of security products based on the policy of the 'right of collective self-defence' and the US-Japan security alliance. There are some disputes regarding the actual application of tariff line.

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Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

SANO: Besides the security products export regulations, other major risk exposures include safety issues in connection with food and products in general. Recently, chicken nuggets manufactured by the Chinese subsidiary of the US-based OSI group threatened the safety of food consumption in Japan. Both McDonald's and Family Mart became exposed to significant reputation risks, which forced them to conduct a much more rigorous safety check by dispatching their own staff to the manufacturing sites or retaining the assistance of third-party verification services. At the same time, major companies are strengthening their compliance program with third-party verification services. Law firms can contribute by assisting the companies to establish compliance programs. In addition, the Japanese government continues its enforcement to prevent counterfeit products.

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Q IN WHAT WAYS CAN COMPANIES MANAGE COMPLIANCE COSTS AND INCREASE THE OPERATIONAL EFFECTIVENESS OF THEIR END-TO-END SUPPLY CHAIN?

SANO: Companies are seeking good third-party verification services even if they are not mandatory as a matter of law. With regard to the export of security products, in April 2010, the Ministry of Economy, Trade and Industry (METI) of Japan issued guidelines on compliance programs (CP) in relation to security products export control that companies engaging in such export ought to establish in-house. Such guidelines ought to be observed according to the Act on Foreign Exchange and Trade. Companies should establish an in-house office to implement compliance programs using the self-check-list issued by METI. METI holds lectures and seminars to promulgate the guidelines by encouraging companies to establish an independent in-house office for its export control practice. With respect to public campaigns to stop counterfeit products, Japan's customs authority has strengthened its checkpoints at the border for illegally imported products.

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Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST? HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

SANO: It is very important for private companies to comply with the security policies of countries in which they engage in business, particularly those with sensitive national security policy points. Law firms are always monitoring the national security regulations of major countries to provide the latest insights, in particular BIS and OFAC, in light of the numerous security concerns in today's world.

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Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN JAPAN?

SANO: Yes, I do. Many law firms provide information on their websites as well as seminars regarding regulatory regimes of interest.

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Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

SANO: Disputes are increasing. Intellectual property related trade issues are increasing. In relation to litigation involving intellectual property, trade remedies are substantial elements in the disputes – in particular, with respect to the ITC process of the United States. We have also seen an increase in antidumping cases as well as countervailing duty cases against developing countries.

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Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

SANO: We advise on regulatory frameworks and rules of major trading countries. As certain regulatory authorities provide detailed guidelines on compliance management programs, we are able to help companies establish their internal programs. Even if no compliance program is strictly required or if no detailed guidelines are provided, when a company establishes its own compliance program and exercise it with periodic training programs with instructions of the relevant authorities, it may be considered as a good citizen and generally so treated in due course. We advise companies to keep good contact with regulatory authorities. When a company is newly established in Japan – for example, a foreign subsidiary which has no experience with Japanese regulations and is unfamiliar with the relevant guidelines – we educate the client and help it carry out its compliance obligations.

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“In relation to litigation involving intellectual property, trade remedies are substantial elements in the disputes – in particular, with respect to the ITC process of the United States.”



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CHINA & HONG KONG

STEPHEN PENG
JT&N



Q WHAT RECENT DEVELOPMENTS HAVE YOU SEEN IN TRADE AND CUSTOMS PRACTICES IN CHINA & HONG KONG? HOW WOULD YOU DESCRIBE GOVERNMENT MONITORING AND ENFORCEMENT ACTIVITIES?

PENG: For a long time, the General Administration of Customs (GAC) has made a concerted effort to increase customs revenue collection and to strengthen its regulation. Over the last 12 months, this effort followed an ongoing active pattern of customs audit and inspection across all major customs issues, including valuation, classification and processing trade compliance. Companies, both domestic and foreign, are facing increasing pressure on customs compliance, with failures on this front resulting in payment of deficient duties and taxes, fines or even penalties.

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Q IN YOUR EXPERIENCE, WHAT ARE SOME OF THE MAJOR RISK EXPOSURES WHEN IT COMES TO TRADE COMPLIANCE, AND WHAT STEPS CAN FIRMS TAKE TO MITIGATE THEM?

PENG: In our experience, risks are most commonly seen in customs valuation and processing trade. Related-party sales prices are scrutinised by the GAC. The GAC keeps a database of average benchmark prices which are used to test related-party prices. If importers cannot provide a reasonable explanation for related-party prices, it is not uncommon for the GAC to use its benchmark prices as transaction prices for calculating higher customs duties and import VAT. The GAC is paying more and more attention to non-trade payments, such as royalties, in determining dutiable transaction prices. According to the WTO valuation rules, the royalties that the buyer pays, directly or indirectly, to the seller or relevant party should be included in dutiable transaction prices unless the royalties are irrelevant to the imported goods or the payment of royalties does not constitute the conditions for the imported goods to be sold within China. In other words, the importer will have to prove to the GAC that either of the conditions are met, or royalties will be dutiable.

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Q IN WHAT WAYS CAN COMPANIES MANAGE COMPLIANCE COSTS AND INCREASE THE OPERATIONAL EFFECTIVENESS OF THEIR END-TO-END SUPPLY CHAIN?

PENG: It is more advisable and more cost-effective for companies to take a pre-emptive approach to ensure compliance rather than take a troubleshooting approach that deals with compliance problems when they arise. The pre-emptive system includes establishing an internal control system. Actually, the GAC is also shifting its focus from auditing and inspecting non-compliance to requiring companies to set up internal control systems that prevent non-compliance. For example, the GAC requires that processing trade companies physically separate their bonded and non-bonded materials and that their inventory and logistics management module for ERP systems is evaluated to ensure the required physical separation. The pre-emptive approach also includes seeking assistances from outside professionals such as lawyers and accountants. They will be able to help companies to plan and establish their internal control system, to audit their actual compliance and to provide legal opinions or improvement suggestions on customs compliance issues.

Q WHAT SPECIFIC RISKS MIGHT ARISE FROM PRODUCTS AND PROPERTY WITH A NATIONAL SECURITY INTEREST? HOW IMPORTANT IS IT FOR FIRMS TO BE AWARE OF EXPORT ISSUES WHEN MOVING SENSITIVE INFORMATION OR GOODS TO FOREIGN PARTNERS OR THIRD PARTIES?

PENG: Exporting goods or technology in the following circumstances is restricted or even prohibited: for the purpose of maintaining state security, social welfare or public morality; for the purpose of protecting human health or security, the life or health of any animal or plant, or the environment; for the purpose of governing the import or export of gold or silver; to conserve any exhaustible natural resources that are in short supply or subject to effective protection; due to the limited market capacity of the destination country or region; due to the serious disorder of export management; and in any other circumstance as provided for in those international treaties or agreements to which China has acceded. China applies a quota and licensing system to goods and technologies subject to export restrictions. Export quotas for



each year are promulgated by the Ministry of Commerce (MOFCOM) and licences are usually issued on the basis of applications for quota. Exporting goods and technologies subject to a licence must strictly follow the specific rules of the licence during its period of validity. China imposes quotas, licensing and duties restraints on exporting certain strategic raw materials, ostensibly for the purposes of environmental protection. The following products are subject to special export control: military exports; guided missiles and related items and technologies; dual-use nuclear equipment and related technologies; dual-use biological products and related equipment and technologies; and chemical products and related equipment and technologies.

Q DO YOU BELIEVE THAT FIRMS PLACE ENOUGH IMPORTANCE ON UNDERSTANDING TRADE AND CUSTOMS REGULATIONS IN CHINA & HONG KONG?

PENG: The answer here is probably 'no'. Companies are often unaware or do not address trade and customs compliance issues until they are approached by customs officials. By this time, a company may already be under investigation and its imports subject to close scrutiny. What makes things worse is that they often do not have an appropriate internal system that keeps track of decisions made in connection with customs issues. Delays and increased costs emerge as a result. It is not uncommon for companies to blame China's customs system and they feel that they have little recourse to defend their position or control customs costs. In fact, companies with customs compliance systems and with knowledge and professional assistance to help them communicate and interact with customs officials can take proactive steps to reduce compliance risks, delays and control costs.

Q HAVE YOU SEEN AN INCREASE IN TRADE AND CUSTOMS DISPUTES? ARE THERE ANY COMMON ISSUES THAT SEEM TO SURFACE FREQUENTLY?

PENG: Trade and customs disputes are increasing. We see more disputes related to customs valuation – especially those related to transaction values between related parties and to dutiable non-trade payments as royalties – and processing trade.

“Companies are often unaware or do not address trade and customs compliance issues until they are approached by customs officials.”

Q WHAT ADVICE WOULD YOU GIVE TO COMPANIES ON DEVELOPING A CUSTOMS COMPLIANCE MANAGEMENT STRATEGY? HOW IMPORTANT IS IT TO CARRY OUT INTERNAL COMPLIANCE CHECKS AND REGULAR REVIEWS?

PENG: It is important for companies to pay attention to pre-emptive approaches, to establish an internal control system that monitors their customs practices, and to conduct an internal or third party audit of customs practices to determine whether their practices are inconsistent with current requirements. This pre-emptive approach will be more cost-effective than a troubleshooting approach that deals with compliance problems when they arise, because a pre-emptive approach will reduce delays in responding to challenges by the GAC and help to encourage the confidence of customs officials.



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Stephen Peng specialises in cross-border investment and international trade. Mr Peng is among the few Chinese lawyers that are qualified to represent the PRC government and the Ministry of Commerce (MOFCOM) in WTO dispute settlement and bilateral investment treaty negotiations. Mr Peng has an extensive practice advising clients on customs compliance. He has advised investors on foreign direct investment and overseas direct investment projects in China for over 15 years. Mr Peng also has an extensive practice advising clients on venture capital and private equity fund investment transactions both on-shore and off-shore, as well as M&A transactions and IPOs.



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