

US Customs: The New 10 + 2 Rules

Roberto Bergami*

The paper discusses the introduction of new US Customs regulations that are likely to impose additional financial burdens on exporters and importers wanting to trade with the USA. The new data element requirements from the US Customs will place pressure on supply lines, interfere with just-in-time management systems, add costs to the international transport of goods and make it more difficult altogether for some type of businesses, such as trading houses, to maintain confidentiality and protect their businesses interests. It appears that insufficient consultation has taken place with key stakeholders and the paper concludes that traders will need to review their sales agreements and other contracts to ensure that everyone involved in trading with the USA remains compliant with the new regulations.

Field of Research: International Trade, Customs Regulations, Cargo Security

1. Background and Introduction

This paper considers new US Customs rules that are being introduced in 2008 that will result in increased costs to trade with the USA, and force changes to current practices that are likely to hamper, rather than enhance, trade facilitation. The discussion in this paper is important because of the influence the US still carries in world trade. The introduction of new measures requiring difficult to obtain data, appear to be a *de facto* imposition of local regulations, with subsequent increased costs to business. The tension between security and international trade facilitation should become evident in reading this paper. "The events of 9/11 have changed the future forever", someone said, and how true this has been for the movement of cargo around the world. The terrorist acts that led to the regrettable events of 9/11 have indeed contributed to a changed environment for the physical movement of goods across international borders.

Previous decades had witnessed advances in trade facilitation through diminished reporting requirements and a general relaxation of government requirements for imports and exports. Coincidentally, this was taking place with the simultaneous globalization phenomena. The WTO was 'born' in 1995 and that was the catalyst for the liberalisation and opening up of many markets under the mantra of 'free trade'.

*Roberto Bergami, CDGS, Senior Lecturer, School of Economics and Finance, Centre for International Corporate Governance Research, Victoria University, P.O. Box 14428 MCMC, Victoria 8001 Australia, email: Roberto.Bergami@vu.edu.au

Then 9/11. This even had a major impact on governmental border control security issues, especially the USA. Ships, once treated as mere transport vehicles, were suddenly regarded as potential weapons of mass destruction, with a commensurate increase in cargo scrutiny. Within the World Customs Organisation (WCO), the securing the supply chain, including the requirement for more information and detailed knowledge about individual consignments and their movements became an area of focus and renewed interest. Advanced cargo reporting was one measure introduced to enhance the control over cargo movements by customs authorities around the world.

The new customs control measures that had been developed, aligned to the principles of the Kyoto Convention (World Customs Organization 1999) that focus on electronic risk management systems as an efficient means of discharging border security functions. Yet, risk controls measures urgently implemented to theoretically prevent another 9/11 like attack, mean operating under increasing compliance mechanisms with rigorous standards that are unwelcoming of mistakes, and cause concerns over contractual obligations among the parties involved in a transaction.

Following a literature review, the paper considers the latest requirements to be introduced by the US Bureau of Customs and Border Protection (CBP), commonly referred to as the “10 + 2” rule (that follows from the “24 hour” rule), in the contexts of:

- *de facto* extraterritorial border control applications,
- origin and classification of commercially traded goods for customs purposes,
- contractual confidentiality considerations, and
- terms of delivery (Incoterms 2000) obligations.

2. Literature Review

As the implementation of the 10+2 rule is currently taking effect, the amount of available literature in the public domain at the time of writing this paper is very limited, despite extensive database searches. There is some analysis by the OECD of the likely impact on business following the container security initiative and related international trade transport risks by Crist (2003), and this is referred to in the next section. Most of the other available literature on this topic appears to be in industry based publications (Feldman 2009; Gersper 2008; Plume 2008; Reynolds 2009), largely comprising of articles of two pages or less, providing a commentary on some aspects of the 10+2 rule requirements, with no further analysis of the logistical implications abroad. A 2008 submission to the US Bureau of Customs (The National Industrial Transportation League 2008) highlights foreseeable compliance problems with the introduction of the 10+2 rule, particularly in relation to the terms of delivery obligations and the provision of timely information, sentiments echoed by others (Edmondson 2008; Goodrich 2007; Kohn Ross 2008). There appears to be a gap in currently existing literature and this paper aims to provide greater understanding of the international practices surrounding the 10+2 rule implementation in the discussion that follows.

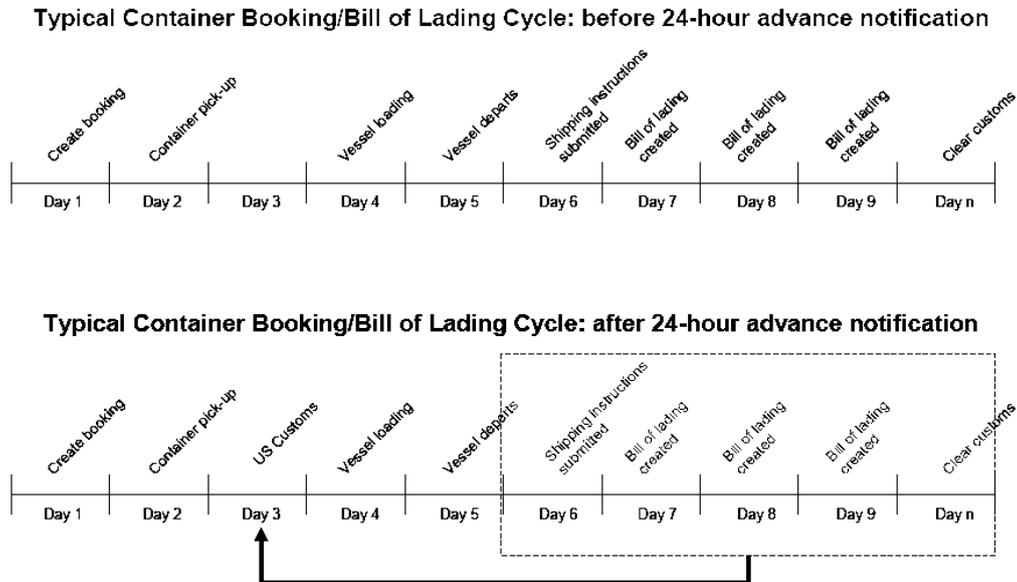
3. Extraterritorial Application Of US Domestic Regulations

It is commonly accepted that international statutory export and import requirements mirror each other. This means that, for example, where an exported good requires an entry permit in the destination country, there will usually be a requirement for an exit permit from the origin country. Thus, the certification provided by the exporting country (administered under its local laws and regulations) serves to simultaneously satisfy the import requirements of the destination country. However, for US imports the CBP requirements appear to be enjoying extraterritorial privileges. In 2004, the CBP mandated a “24 hour rule” whereby vessel manifest information for containerised cargo had to be submitted by the incoming carrier to the CBP “by the Vessel Automated System no later than 24 hours prior to loading at the foreign port” (Chalos 2004, p. 1). Until then the onus for notification of impending cargo arrivals was at some time prior to the vessel entering territorial waters, and not ahead of its loading at a foreign port. This change impacted greatly on shipping operations as

it must be emphasized that Customs, having analysed the cargo information, do not send "permission to load" messages to carriers to authorize them to proceed with loading. Therefore, in order to avoid risking a penalty, carriers need to delay loading operations for 24 hours after the submission of the manifest to U.S. Customs to be sure that there is no problem with any particular container. Of course, this is, unless a "do not load" message has been sent by U.S. Customs (United Nations Conference on Trade And Development 2004, p. 13).

Thus, if “a carrier loads a “do not load” container, the vessel will not be allowed to discharge at an American port” (Crist 2003, p. 49). Other breaches of the 24 hour rule may attract fines, product seizure, or withholding permission to unload all or part of the vessel’s cargo. The main concern with the 24 hour rule, is the issue of timing, as shown in Figure 1 (Crist 2003, p. 50).

Figure 1: The timing effect of the 24 hour rule data requirements



Compliance with this timing issue has forced operational changes for exporters, logistics providers and carriers alike. For example, it is no longer possible to lodge “late” containers – up to 12 hours prior to departure. Because exporters must provide data earlier, they are tending to deliver containers early, adding pressure on temporary storage facilities. Carriers need extra staff to provide around the clock service seven days a week, and as data is handled more times now, container progress through the port is comparatively slower. It is conservatively estimated that the “potential burden imposed on carriers by the rule [is] approximately USD 281.7 million” per annum (Crist 2003, p. 50). Of course these costs are passed on to exporters, with the ultimate consequence being increased costs to the importing customer. As an example, industry sources in Australia reveal that an additional fee of AUD 25.00 per bill of lading (sea transport document) has been imposed to exporters as a result of the CBP requirements. Industry sources estimate that approximately 100,000 containers were destined to the USA in 2007, and therefore the added cost to the export industry in Australia is estimated to be at least at AUD 2.5 million per annum. This cost does not include any added inventory costs resulting from pipeline holdings due to the earlier reporting requirements. A day’s extra inventory cost alone, at an interest rate of 5% per annum has been estimated to cost the Australian export industry approximately AUD 1.4 million, based on export volumes for the year 2007-08.

The profitability of firms that work to ‘just-in-time’ principles to reduce inventory and holding costs have been negatively impacted by the 24-hour rule, yet this is proceeding – why? This is largely attributed to the economic strength and political influence that can be exerted in global circles, coupled with desire by the US

government to avoid another 9/11 episode. The CBP is one of the agencies charged with this responsibility as the

role of customs has now expanded to include national security, in particular the security and facilitation of legitimate trade from the threats imposed by terrorism, trans-national organised crime commercial fraud, counterfeiting and piracy (World Customs Organization 2006, p. 3).

It should also be remembered that in container traffic, “inspections are extremely difficult to carry out on board a modern container vessel where the majority of the containers may be inaccessible below deck” (Crist 2003, p. 48). Therefore, to exercise container movement security control more effectively it is better to intervene at the beginning of the process.

The ‘Proposed Rule Making on Importer Security Filing and Additional Carrier Requirements’, was published on 2 January 2008, and this is commonly referred to as the ‘10+2 rule’. Essentially, the 10+2 rule is an extension of the 24 hour rule, requiring importers to declare ten additional data fields, and carriers, an additional two data fields. Carriers would need to electronically lodge data on: i) vessel stow plans and ii) container status messages (CSM). The demand for stow plans does not seem onerous, but the same cannot be said for CSM. Mandatory filing of a CSM is triggered by events such as confirmation of a booking, container terminal gate inspection, loading or unloading of a container, gate-in or gate-out movements, container stuffing or unstuffing, and intra-terminal movements. Given the majority of these events are routine with containerised traffic, as the consignment travels from origin to destination, it is no surprise that carriers/logistics providers are concerned with the “over-reporting” required by the CBP, as this increases operating costs.

The data required from importers are (US Customs and Border Protection 2008):

- a) Manufacturer (or supplier) name and address,
- b) Seller (or owner) name and address,
- c) Buyer (or owner) name and address,
- d) Ship-to name and address,
- e) Container stuffing location,
- f) Consolidator (stuffer) name and address,
- g) Importer of record number/foreign trade zone applicant identification number,
- h) Consignee number(s),
- i) Country of origin, and
- j) Commodity Harmonised Tariff Schedule number.

As “10+2 is an extension of Custom’s strategy to use data in advance to identify high-risk shipments before they reach the United States” (CFBCA 2008), the data elements are additional to the 24 hour rule’s requirement and precede the creation of a customs import entry. This rule has certainly sparked much debate within the trade and logistics communities worldwide, but why is it so contentious? The supply of certain data elements poses difficulties for US importers, yet they are the

party, under the US regulations, that are responsible for ensuring correct information is electronically filed with the CBP. Some of the difficulties relate to the timely availability of the data, whereas others relate to contractual arrangements and interpretation of customs matters, as discussed below.

4. Manufacture, Origin and Classification

Firstly, the identity of a manufacturer may be more difficult to obtain than initially appears. Where the supplier is a trading company (Goodrich 2007), there will be an understandable reluctance to divulge the identity of the manufacturer, for fear that they may be by-passed by the importer dealing directly with the manufacturer, with resultant loss of income for the trading company. Being unable to identify the manufacturer may not be problematic, as seemingly, the US importer is permitted to report only the supplier details where due diligence fails to establish the identity of the manufacturer, but because due diligence is not defined problems may arise with consignments originating from high security risk areas, from the CPB's perspective.

Secondly, origin is a lot more complex.

A definitive position in relation to the country of origin ... is difficult, if not at all times impossible to determine ... the origin of the goods in the time available to make the definitive decision required. In many cases definitive information in relation to the country of origin (or manufacturer) may take time to determine and only then by way of tracking processes. On balance the country of origin is perceived by many to be the country of manufacture of the goods subject to the contract of sale. This in many cases is not correct. It is therefore suggested that most sellers, manufacturers, exporters, consignees, buyers, importers or consignors do not fully appreciate the intricacies of the country of origin requirements (Morris 2008).

Thirdly, the determination of origin, classification and valuation for customs purposes are most argued topics in the context of customs clearance declarations. For example, there is no standard treatment for determination of origin among bilateral agreements, making it difficult for the importer to declare the correct information with certainty, particularly as the rules for origin are complex and subject to varying interpretations across the globe. Matters of customs classification require specialist skills, as the classification system is a legal instrument, requiring interpretation, an understanding of the classification principles and legal precedents, because

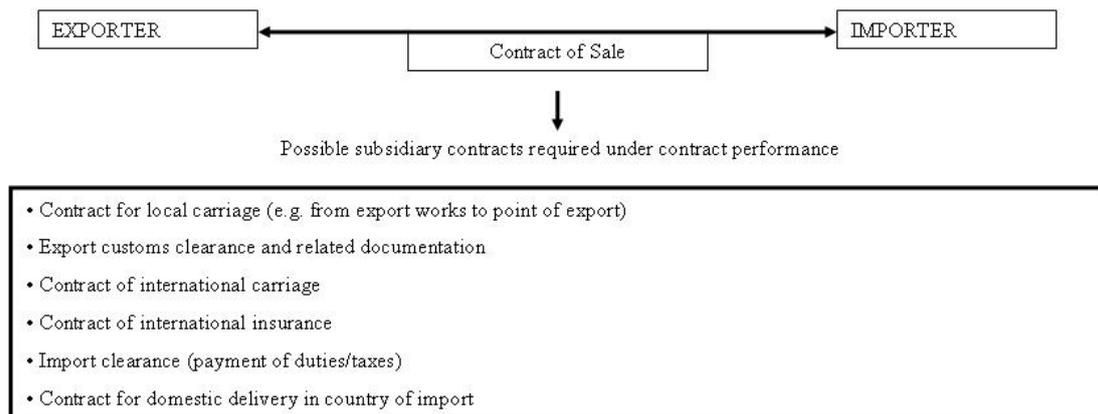
disputes arise regularly ... as to the correct tariff classification of goods at the time of importation. These disputes are either satisfied by way of ... Customs internal review, or ... referenced to the Administrative Appeals Tribunal or the Federal Court for legal determination (Morris 2008).

Customs authorities decide on the classification to be applied where there is a difference of opinions, and subsequently if the importer may need to seek relief through legal means. Because classification is so complex, a degree of flexibility is required to ensure the 'wheels of commerce keep turning'..

5. Terms Of Delivery Data

The Incoterms 2000 (International Chamber of Commerce 1999) are the standard terms of delivery for international trade contracts.. These terms apportion specific obligations arising from the sales contract, in accordance with which one of the thirteen Incoterms 2000 is chosen. It then becomes the responsibility of the exporter, or the importer, to enter into separate subsidiary contracts, as shown in Figure 2 (Bergami 2004, p. 136). Under Incoterms 2000, the exporter is responsible to contract for carriage under the following terms: Cost and Freight (CFR), Cost Insurance and Freight (CIF), Carriage Paid to (CPT), Carriage and Insurance Paid to (CIP), Delivered at Frontier (DAF), Delivered Ex-Ship (DES), Delivered Ex Quay (DEQ), Delivered Duty Unpaid (DDU) and Delivered Duty Paid (DDP). With all other terms, viz, EX Woks (EXW), Free Alongside Ship (FAS), Free Carrier (FCA) and Free on Board (FOB), the importer is responsible to contract for carriage, and therefore the US importer could demand data availability directly from their contracted logistics provider/carrier as required.

Figure 2: Possible subsidiary contracts (for the movement of goods) arising from the sales contract



Depending on the term chosen, the seller, or buyer, will be responsible for all, or only some of the above

Where the importers 'purchase goods under 'C' or 'D' Incoterms ... [they] may be unable to obtain the required data elements" (The National Industrial Transportation League 2008, p. 12), such as container stuffing details. To ensure compliance, the US importer may wish to incorporate the provisions of the 10+2

data requirements in the sales contract via a specific clause, however the exporter may not be so willing to be bound by such a requirement, because the data elements are generated by third parties (carrier/logistics providers), and clearly the release of such data is beyond the exporter's control. To ensure data elements were provided in time, the carrier/logistics provider's contract would need to be amended accordingly. It is unlikely that these parties would agree to being held liable for the delay in transmission of information. What if the delay in information resulted in a "do not load" notification, and the intended sailing date was missed? Who would make good the loss under such an event? What if this resulted in the consignment becoming obsolete because of its seasonality, or perishability, e.g. Christmas decorations, or a product with a limited use-by date? What would the value of this merchandise be then and who would assess this value? These would be difficult issues to solve indeed. These examples highlight the importance of developing and implementing a strategic approach to appropriate risk management systems. Exporters should incorporate rigorous force majeure clauses in all their contracts, seeking exemption, or relief, where third parties cause delays in data availability.

The comments above are unlikely to apply to either EXW or DDP Incoterms 2000 sales contracts. Under EXW terms, the importer is completely responsible for all actions (including export clearance) from the collection (origin) point in the country of export (typically the exporter's premises). Therefore the importer may demand timely data to satisfy the 10+2 rule directly from their carrier/logistics providers. Under DDP terms, the import clearance functions are the responsibility of the exporter, who is deemed as the importer of record in the destination country, for customs purposes. Under these contractual arrangements, the provision of timely data to the importing country authorities (in this case the CBP), is of no concern to the US importer. Because the exporter must comply with the CBP requirements in a DDP transaction, appropriate risk management strategies, resulting in minimum disruption to business flows, should be implemented. Because the 10+2 rule emphasises the timely submission of data, it may be beneficial to consider re-engineering business flows to allow more time for the processing of consignments, both in-house and externally, so as to capture and submit relevant data, setting up timely automatic notification of data elements from service providers, and ensuring that access to the CBP electronic gateway is obtained in advance, to ensure that electronic data submission can be lodged as required.

6. CONCLUSION

The Revised Kyoto Convention laid a framework for customs authorities around the world to utilise electronic systems as an added tool in the discharge of border control obligations. There is no argument that customs authorities are the best agencies equipped to deal with the control of cross border traffic, the issue is how these obligations are discharged, because that is what makes a difference to the global trading communities.

Customs operations worldwide are currently being heavily influenced by security concerns and this is where much of the focus in risk assessment of consignments is directed. IT systems are increasingly being utilised and incorporated in customs

operations to make more informed, and better judgements about import and export consignments. Of course, IT systems need data input at the onset, before they can be employed to interrogate the available information. The timing of the data capture surrounding the 24 hour rule and the 10+2 rule is, for traders and service providers, one of the more problematic issues, as compliance with these rules demands major changes in business processes and cargo flows, with increased costs to commercial transactions.

The global trading community understands well the role of customs authorities and appreciates their key roles of 'border policeman', but in some cases, the data demanded is difficult to obtain, and has potential contractual ramifications for exporters, importers and their service providers. Perhaps further consultation and a phased implementation may be required to ensure a smooth transition towards meeting the compliance obligations of the 10+2 rule. No, this rule does not only affect US importers – international trade transactions do not work in a vacuum and, therefore, parties outside the US will also be impacted upon. Exporters may also need to rethink which delivery terms may prove to be too risky to use as a consequence of the additional data burdens imposed by the 10+2 rule.

Carriers/logistics providers will feel the compliance pressures arising from their cargo reporting obligations, particularly in relation to CSM. Changes in business practices will not happen overnight, nor will they be cheap. The increase in electronic traffic may need to be met with more elaborate and expensive IT solutions, that will result in increased operational costs for this industry sector, as indicated by the previously mentioned projected figures. The type and timing of data requirements may necessitate changes in contractual clauses to ensure compliance. Exporters will need to be vigilant and ensure that sales and other contracts incorporate clauses that adequately address the issues raised in this paper.

References

- Bergami, R 2004, *International Trade: A Practical Introduction*, 2 edn, Eruditions Publishing, Melbourne, Victoria, Australia.
- CFBCA 2008, 'United States Customs and Border Protection', *CBFCA Web Communicator*, vol. 2008, no. 9, viewed 8 May 2008 <<http://www.cbfca.com.au/BulletinArticle.aspx?EntityId=538511> >.
- Chalos, M, Cummins, C. 2004, 'U.S. Bureau of Customs and Border Protection Regulations Concerning Automatic Manifest Filing'.
- Crist, P 2003, *Security in Maritime Transport: Risk Factors and Economic Impact*, Maritime Transport Committee OECD, Paris, France.
- Edmondson, RG 2008, 'Importers urge Customs to revise the 10+2 rules - incomplete or late filings could prove costly', *Shipping Digest*, vol. 85, no. 4442, pp. 10-1.
- Feldman, L 2009, 'The 10+2 Importer Security Filing: Ready? Set? Load!' *Florida Shipper*, vol. 34, no. 2, p. 2 & 61.
- Gersper, M 2008, 'the 10+2 opportunity', *Journal of Commerce*, vol. 9, no. 31, p. 36.

BERGAMI

- Goodrich, J 2007, "'10+2" does not always equal 12', *International Business Training*, no. 30 July, viewed 10 May 2008, <http://www.i-b-t.net/absnet/templates/trade_article.aspx?articleid=28&zoneid=2>.
- International Chamber of Commerce 1999, *Incoterms 2000*, ICC Publishing, Paris, France.
- Kohn Ross, S 2008, 'Customs Update: 10+2 = Part Deux', *The Journal of Commerce Online*, no. 23 January, viewed 10 May 2008, <<http://www.joc.com/articles/news.asp?section=spec3&sid=44193>>.
- Morris, S 2008, 'CBFCA Submission to CBP', viewed 8 May 2008, <<http://www.cbfca.com.au/BulletinArticle.aspx?EntityId=533035>>.
- Plume, J 2008, 'Doing the import math', *Shipping Digest*, vol. 84, no. 4444, p. 4.
- Reynolds, F 2009, '10+2, Lacey Act and more', *Journal of Commerce*, vol. Supplement 12 January, pp. 64-6.
- The National Industrial Transportation League 2008, 'Importer security filing and additional carrier requirements', no. USCBP-2007-0077 RIN 1651-AA70, 18 March.
- United Nations Conference on Trade And Development 2004, *Container Security: Major Initiatives and related International Developments, Report by the UNCTAD Secretariat, Document UNCTAD/SDTE/TLB/2004/1, 26 February*.
- US Customs and Border Protection 2008, 'CBP Issues Proposed Rule Requiring Additional Cargo Information', viewed 16 January 2008, <http://cbp.gov/xp/cgov/newsroom/news_releases/01022008.xml>.
- World Customs Organization 1999, 'International Convention on the simplification and harmonization of Customs procedures (Kyoto Convention) Revised version, June 1999', viewed 10 May 2008, <<http://www.wcoomd.org/kybodycontent.htm>>.
- 2006, *Revised Kyoto Convention: Let's talk ... your questions answered (Document D/2006/0448/8)*, World Customs Organization, Brussels, Belgium.