



Implementation of risk management for customs modernization in Sri Lanka

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Abstract

The Customs Department is one of the most important departments for the Sri Lankan Government. From the last three decades the customs workload has increased rapidly, at the same time, their number of staff and resources in same. So, Customs is seriously challenged by the gap between the increase volume of trade and the shortage of the resources. On the other hand, along with the economic globalization, the government, traders and passengers expect that the customs operations could be more efficient, the procedures more simplified and the cost reduced further. Risk Management should provide us with an opportunity to solve the efficient control, simplified procedures and facilitated international trade. Risk management is a logical and systematic method of identifying, analyzing and managing risk. The aim of this paper is to sophisticate the functions of the Customs Departments by recommending the proper application of risk management in Sri Lanka. The paper mainly deals with evolution and definition of risk management, the importance and implementation of risk management to the Long Room in Sri Lanka Customs, tools & model for risk management, which could be used in the Long Room, experience from Japanese Customs and the recommendation for risk management in Sri Lanka Customs.

Introduction

The Customs department was established in 1806. Though its activities have over a period of time been diversified, its primary role still continues to be the collection of revenue and the enforcement of the laws related to facilitate the trade. The Customs Department collects nearly 50% of Government tax revenue. In addition to the Customs Duty, it also has the responsibility to collect the Value Added tax, Excise Duty, Surcharge and Cess at the point of import.

The Department's mission is "to enforce the Customs law and related revenue and social protection laws, while facilitating the trade, travel and industry, with the objective of contributing to the national policy is also a vital of its mission".

The Long Room in Sri Lanka Customs

The Long Room, being the Import Goods Declaration Processing Center for sea cargo that are subject to Customs duty and other levies, is the highest revenue collecting point (almost 80% of total customs revenue) in the Customs. From the inception of the Department, the entire

import documents processing exercise has been carried on here. With the expansion of import trade over the years, the import document process was computerized and ASYCUDA system was implemented in January 1994 to minimize delays, errors and irregularities and provide efficient and effective service to the trading community.

Responsibilities and objectives of the Long Room

- Collect correct Customs Duties and other levies such as Goods and Services Tax, National Security Levy, Excise Duty etc on importation
- Ascertain whether commodities are correctly classified and valued for collection of correct Customs duty and other levies for statistical purposes
- Enforce Customs law and other related laws in the country
- Facilitate trade by providing effective and efficient service
- Take suitable actions against the violators of the Customs Law and other related laws

Evolution of risk management

A common characteristic of customs work is the high volume of transactions and the impractical of checking all of them. Customs administrations therefore face the challenge of facilitating the movement of legitimate passengers and cargo while applying controls to detect customs fraud and other offences. Customs services find themselves increasingly under pressure from the national government and the international organizations to facilitate the clearance of legitimate passengers and cargo while concurrently responding to increase in international crime. These competing interests mean that it is necessary to find a balance between trade facilitation and law enforcement.

The purpose of all customs controls is to ensure that the movement of vessels, vehicles, aircraft, goods and persons across international borders occurs within the framework of laws, regulations and procedures that comprise the customs clearance process. Against this backdrop, the solution to passenger and cargo examination is best found in the development of customs controls that are based on risk assessment, profiling and selectivity.

In the importing environment, the three levels of customs controls are pre-clearance, clearance and post-clearance audit. These controls are intelligence-led and focused on the identification of high-risk commercial activity. Risk identification is crucial to the process and this is achieved by identifying risks that are a serious threat to customs enforcement activities and the consideration of existing customs controls and determining why weaknesses exist and establishing risk indicators which may increase or decrease the degree of risk. Risk indicators may relate to a particular commodity code, country of origin, value¹ of goods, etc.

¹ For the purpose of Customs Valuation Control the WCO has produced a Handbook which might be of value to Members to obtain further and detailed information on this matter. "Kyoto Convention-General Annex- Chapter 6, Guidelines on Customs Control", WCO publication, page-19.

The WCO defines Risk Management² "as the systematic application of management procedures and practices providing customs with the necessary information to address movements or consignments which present a risk".

The benefits of this concept have been widely recognized in other relevant international organizations. For example, the following excerpt from the WCO Guidelines on the Revised Kyoto Convention could be a useful reference in understanding the concept of risk management.

Advantages of Risk Management

- Increase in Government revenue
- Trade facilitation
- Encourages the Foreign Direct Investment
- Reduction in informal trade
- Better human resource allocation
- Reduced cargo release time
- Lower transaction cost
- Improved compliance with laws and regulations

The importance of the risk management for Sri Lanka Customs

Especially in the recent decades, Sri Lanka has witnessed rapid development of foreign trade. Sri Lanka Customs totally supervise and examine import and export of goods, transits cargo, sea and air passengers. From the last three decades the customs workload has increased rapidly, while the central government is required to relocate the available resources well to provide a better service, modernize customs internal structures, minimize the staff scale and improve efficiency. It is realized that increase the Customs staff can never catch up with the increasing workload. Now, with in 2,500 working staff, Customs is seriously challenged by the gap between the increase volume of trade and the shortage of the resources.

On the other hand, along with the economic globalization, the government, traders and

² World Customs Organization (June 2003), "Risk management Guide", WCO publication, page-8.

passengers expect that the customs operations could be more efficient, the procedures more simplified and the cost reduced further. Sri Lanka customs, as the Customs of various countries in the world, is confronted with the challenges, careful control, better service, strict execution of the law, while conducting highly efficient operation.

Risk Management should provide us with an opportunity to solve the efficient control, simplified procedures and facilitated international trade. Risk management has turned to be the common choice of Customs in the world for facing conflicts of interests among these kinds of challenges.

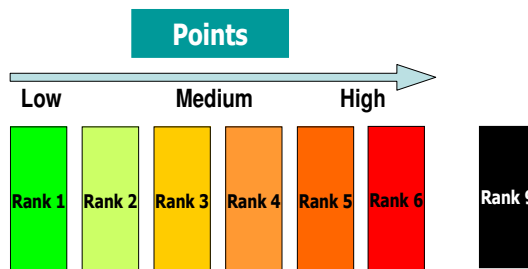
Tools and a model to be used in application of Risk Management in to the Long Room

There are three main tools for Risk Management;

I. Ranking of importers

At present huge number of importers have been registered with the Customs, but, limited number of importers are currently working with the Customs. Customs has to review all of the importers. For this purpose, Customs has to review history of all importers, background of all importers, to see whether they have violated any customs rules or procedures, if so, in accordance with the seriousness of their violations, they have been penalized by the Customs or other government department and etc. Customs can get information and data about the importers from various investigation units in the Customs. Presently, Customs has several kinds of investigation and examinations divisions and units, such as, Preventive division, Narcotic division, Central Cargo Surveillance Unit, Central Intelligence Unit. Considering the above facts, Customs can give points for each importer. And, after that, Customs can rank all importers by using the points system.

Basement of these points system, basically all of these importers can be categorized in to Low risk, Medium risk and High risk.



Source: Customs and Tariff Bureau, Ministry of Finance, Japan

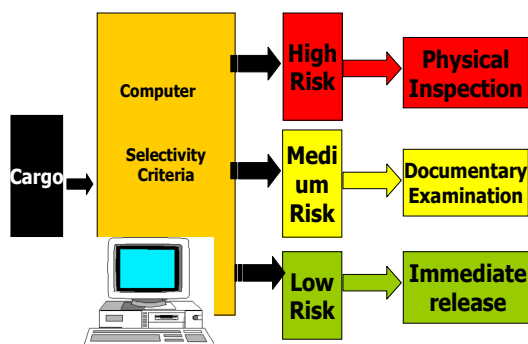
II. Rating of importers

Rating of Importers (Credibility)		
Rating of importers	Rank1	Good importer
	Rank2	Semi-good importer
	Rank3	Standard importer
	Rank4	Semi-Risky importer
	Rank5	Risky importer
	Rank6	Targeted importer with intelligence
	Rank9	Unknown importer

Source: Customs and Tariff Bureau, Ministry of Finance, Japan

After ranking the importers, Customs has to do “Rating of Importers”. This stage, Customs categorizes ranks all importers in-to nine ranks (Rank 1- 9) by using point system. Rank 1 is good importers and the Rank 9 is a unknown importer. Risk factor is the base for the ranking and rating of importers.

III. Criteria for risk assessment



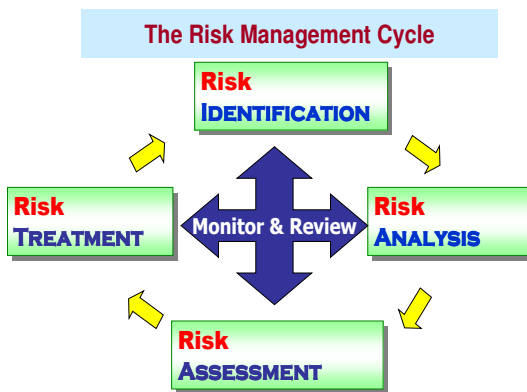
Source: Customs and Tariff Bureau, Ministry of Finance, Japan

When implementing Risk Management, Risk Assessment Criteria as shown in the above diagram is the most important and necessary tool for implementing of risk management. Once the ratings are finalized, customs will have all data about importers in the computer system. Then, Customs should input tax rates for each commodity, import regulations and other relevant details for import goods. According to the above data, the computer system categorized all imported cargoes as High risk, Medium risk and Low risk. This is called the “Criteria for risk assessment”.

As explained in the above paragraphs, Customs can identify risky importers (or cargo) and un risky importers, by ranking imported cargoes either as Non/Low risk, Medium risk, High risk with the use of the “Computerized selectivity criteria”. Along with these tools, Customs has to implement “Risk Management Cycle”, which is a model of risk management process.

The risk management cycle³

The Risk Management Cycle comprises risk identification, risk analysis, risk assessment, treatments the risks and monitors and reviews the process.



Source: Kyoto Convention-General Annex-Chapter 6-Guidline on Customs Control and Risk Management Guide-World Customs Organization

As is evident from the above diagram, the risk management cycle is a continuous process. If Customs identify new risk, this cycle has to be activated until the final solution is obtained. This cycle should activate time-to-time, then, Risk Management Process always remains in good condition.

The recommendations of implementation of risk management

The implementation of risk management for the Long Room in Sri Lanka Customs is a totally new process. So, this will be new experience to all of the staff as well as to the Department. So, implementation process has to be launched carefully, accurately and on a step-by-step basis.

- It is vital to change the mentality of staff and management, so that everybody recognized that value and effectiveness of risk management.
- A risk management policy and a strategic management plan must be drawn up to highlight the objectives and priorities in introducing new system.

- Establishment of risk management committee

The risk management committee, representative from various levels/grades of customs officials, such as Director General of Customs, higher management and Staff officers should be established. The objective of this Committee is to discuss and agree on new risk criteria and new risk policies.

- A risk management unit
A separate risk management unit must also be established and it should become responsible for the maintenance and operation of the system. This unit must gather intelligence data, chart and analyze intelligence data on importers and carriers from several sources, including from traders and agents, business organizations, WCO database, national seizure reports, and other administration acting under the Nairobi Convention or bilateral agreements. This unit will consist of around 25 to 30 staff and headed by the Deputy Director of Customs, and directly

³ Risk Management Guide (June 2003), “World Customs Organization”. And, Kyoto Convention-General Annex-Chapter 6-Guideline on Customs Control. Page 10.

responsible for the Director General of Customs. And, this staff will ensure ongoing monitoring of the risk criteria, i.e. development of new criteria when needed- and abolishment of those criteria that are no longer valid.

- Establishment of customs intelligence database system (centralized intelligence system) and introduce an electronic manifest

This is a system of information technology, which is an effective tool for risk management. It enables a more rapid analysis of selectivity criteria than would be made possible manually. This system allows Customs administrations to establish a national database of information on all transactions and movements, which could be updated and used for rapid information sharing and identification of changed risk areas. It can also provide a database to all risk profiles, which could be used as a basis for a selectivity module within an automated clearance system. An automated system allows Customs administrations to do a subject declaration to a series of selectivity filters to determine which declarations may require further examinations. And, the electronic manifest, which is aligned to international standards, should provide for advanced identification of high-risk shipments.

- Review of the post-clearance audit division

At the moment, the Customs Department has a Post Clearance Audit (PCA) division. When implementing risk management system, Customs Administration should review the function of the PCA division. It is an effective tool for Customs control because it provides a clear and comprehensive picture of the transactions, because it is identified in the books of Customs and international traders.

- Training and awareness programmes and capacity building

An awareness of risk management techniques among staff and higher management skills should be created through training programmes. Through training programmes overall thinking pattern of the staff can be changed and also by this we can make them understand value and effectiveness of risk management. Awareness courses must be

organized for the entire organization to bring about a common understanding of the new procedures and policies. A special Information Technology courses (local and abroad) must be arranged to staff who are directly involved in the implementation and operation of the new procedures.

- Review of organization structure and customs laws and regulations
Customs laws, regulations and the organization structure must be reviewed to ensure use of risk management instead of traditional examination of goods.

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