
***A look at the present
and future of customs
and trade***

To stay competitive in a global trade environment increasingly dominated by preferential trade, electronic customs clearance and export regulations, companies need a smart strategy integrating the entire range of customs and trade activities in their value chain – particularly on the IT side.

Market access negotiations were the cornerstone of the foundation of the World Trade Organisation (WTO) in 1996. But since then it has not been possible to reach any significant global deal on trade in goods at a multilateral level. On the other hand, between 2000 and 2015 the number of bilateral or regional free-trade agreements (FTAs) almost doubled worldwide. The tremendous increase in bilateral arrangements between interested parties is a clear consequence of the standstill in WTO negotiations. Global trade liberalisation at a bilateral level is accelerating, and is not likely to stop.

By the end of the 1990s, only a handful of customs administrations had electronic customs clearance systems in place. Barely 20 years later, technology breakthroughs and post-9/11 security requirements have made it inconceivable not to use electronic clearance to deal with cross-border formalities and procedures. In the next few decades, a paperless trade environment will be the norm.

While trade is growing and technology is developing, the risks are as well. Export-related controls and regulations constitute one of the major – if not the biggest – stumbling blocks faced by economic operators today. These requirements arguably serve admissible purposes – safeguarding health, the environment or national security, for example – and ultimately they simply have to be dealt with. With global trade having reached such levels of intensity, this has become the favourite instrument of governments for imposing political sanctions and combating weapons proliferation. Companies are consequently being forced to respect an increasing number of embargoes, international sanctions and dual-use goods regulations to ensure compliance and avoid sharp penalties.

These three prominent trends – preferential trade, electronic customs clearance and export regulations – will continue to shape global trade



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and the way companies approach trading activities in the years ahead.

How to make it through the global trade jungle

It's important to remember that in the great global trade jungle there are as many opportunities to seize as there are risks to deal with. Let's look at a few facts and examples.

Leveraging free trade agreements

The EU, Switzerland's main economic partner, applies customs duties of between 5% and 10% on the import of most chemical products. Customs duties levied on electrical equipment in the EU are generally between 5% and 15%. In China, customs duties charged on machinery are as high as 15%, or even 20% in some cases. With chemicals, electrical equipment and machinery among Switzerland's top exports, it's easy to see the economic benefits of FTAs (for more detailed information see box).

But to make the most of such treaties, companies need to do a great deal of organisational planning, and may also have to make significant investments. Issuing false origin certificates, or not being able to authenticate the Swiss origin of goods once they have been declared, can lead to severe penalties. Swiss law (the Ordinance on the Issuing of Proofs of Origin, SR 946.32) stipulates fines of up to CHF 40,000 for failures to respect the relevant legal framework. Not only that, but economic operators can potentially have their preferential status (e.g. authorised exporter) revoked.

Preferential origin is a strategic issue and should be dealt with at management level

In most countries, customs duties are levied on the importation of goods. These duties are in most cases calculated as a percentage of the value of the imported goods. For instance, if a company imports goods for a total amount of EUR 1,000,000 and the customs duties applied to such goods are 10%, EUR 100,000 must be paid to the local customs administration. To give their economic operators a competitive advantage, some governments refrain from levying such duties within the framework of bilateral or regional FTAs.

But what does it take for a company to benefit from an FTA? To

avoid trade circumvention, the governments negotiating an FTA agree on so-called rules of origin. These determine what kind of processing products must undergo to acquire preferential origin status and be granted tariff exemptions when crossing the border. For example, the FTA recently concluded between Switzerland and China states that to benefit from preferential origin, machinery built in one of the signatory countries must contain at least 50% Swiss or Chinese components. Along the same lines, the FTA Switzerland and the EU signed in 1972 states that Swiss cheese can only be granted tariff preferences when exported to the EU if the milk used in its processing originates in Switzerland.

Such rules are negotiated and thus vary from one FTA to the other and from product to product. Given that Switzerland has negotiated 30 FTAs (in force) to date with around 40 countries and partners, economic operators face a huge challenge when it comes to dealing with origins. It's not unusual for one product to bear several 'preferential origins' at the same time depending on the FTA and the price it is exported at. This situation has led to the so-called spaghetti bowl effect, a metaphor used to describe the entanglement of rules of origin.

What does all this mean in concrete terms for companies exporting and importing goods? Firstly, sales, production and purchasing departments need to communicate closely with each other. Otherwise how can firms certify the origin of their exports when they're not aware of their content and the origin of their components? This means that companies need to track the origins of most of their purchases and be able to authenticate and document them.

Secondly, legal departments need to be aware of the relevant legislation and the consequences of breaches. Penalties for a false declaration of origin are severe. Thirdly, companies have to realise that smooth handling of preferences is not possible if corners are cut in terms of solid integration with IT systems. This entails investment, training and maintenance. On the other hand, it also brings more transparency and ensures auditability in case of customs audits. Finally, for such a complex plan to actually work, the company's organisation has to be horizontally integrated. Roles and responsibilities should be clearly defined (establishment of a policy) and accountability needs to be ensured at management level.

Streamlining e-customs clearance

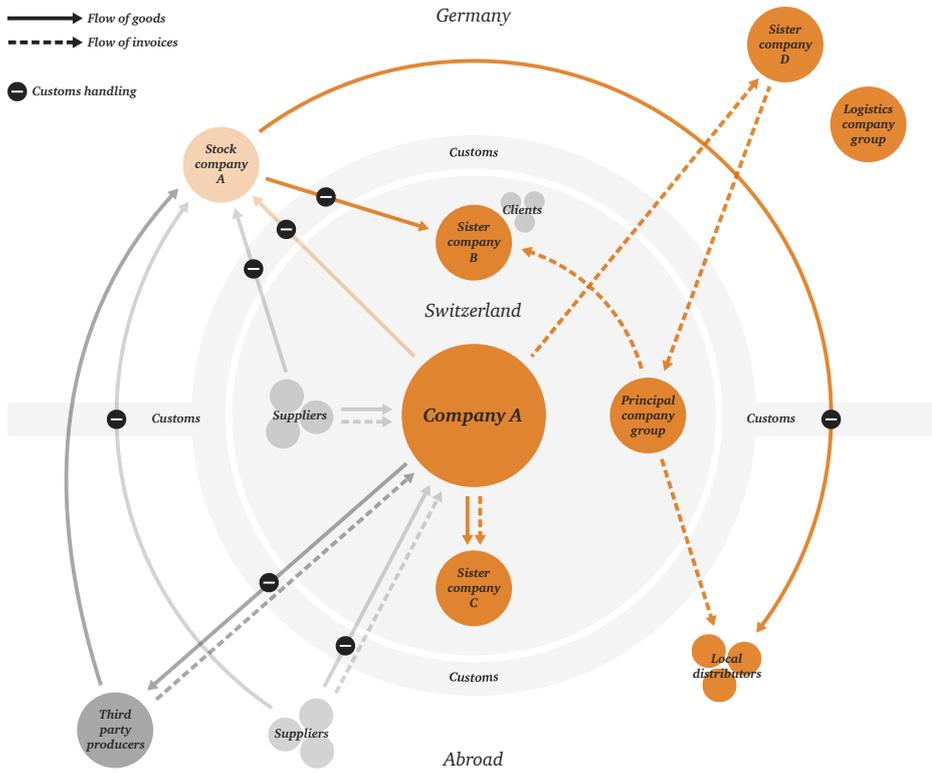
Why do people pay accountants to do their tax returns? Because it's a complex and tedious task, and they're likely to save some money in the end. Why do companies outsource customs formalities to customs brokers? Probably for the same reasons. But does this really make sense in the age of e-customs? In Switzerland you pay a customs broker between CHF 50 and CHF 150 to fill out and execute a single import declaration. Add up the monthly shipments of a major company and you'll have a pretty good idea of how much money can be saved by insourcing customs clearance. Insourcing can also give you better control over your flows of goods and enable you to monitor them and enhance their auditability and traceability. And don't forget that eventually it's the importer who is accountable for the goods declared, not the customs broker. The Swiss Law on Customs (SR 631.0) is especially severe when it comes to false declarations leading to non-payment or underpayment of customs duties: fines amounting to five times the unpaid duties, with the possibility of imprisonment too.

These days electronic customs clearance offers multiple opportunities to firms willing to take back control of their flows of goods. At the same time it allows them to save money and strengthen compliance and transparency. It goes without saying that investments on the IT side are needed. But we would argue that this is a valuable way of capitalising on systems already in place: since the 1990s companies have gone to a great deal of effort in supply chains and logistics. We see no reason not to close the loop by integrating customs formalities into supply chain procedures.

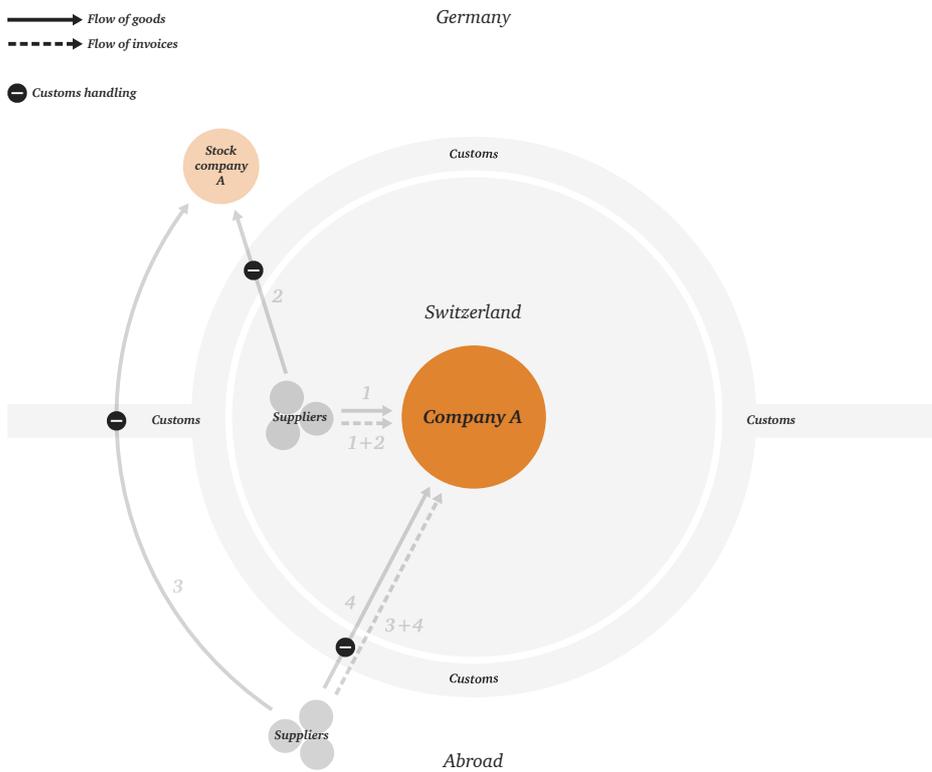
Figure 1: An example along the supply chain

———— Supply/purchase ———— External production ———— Export/import ———— Sales

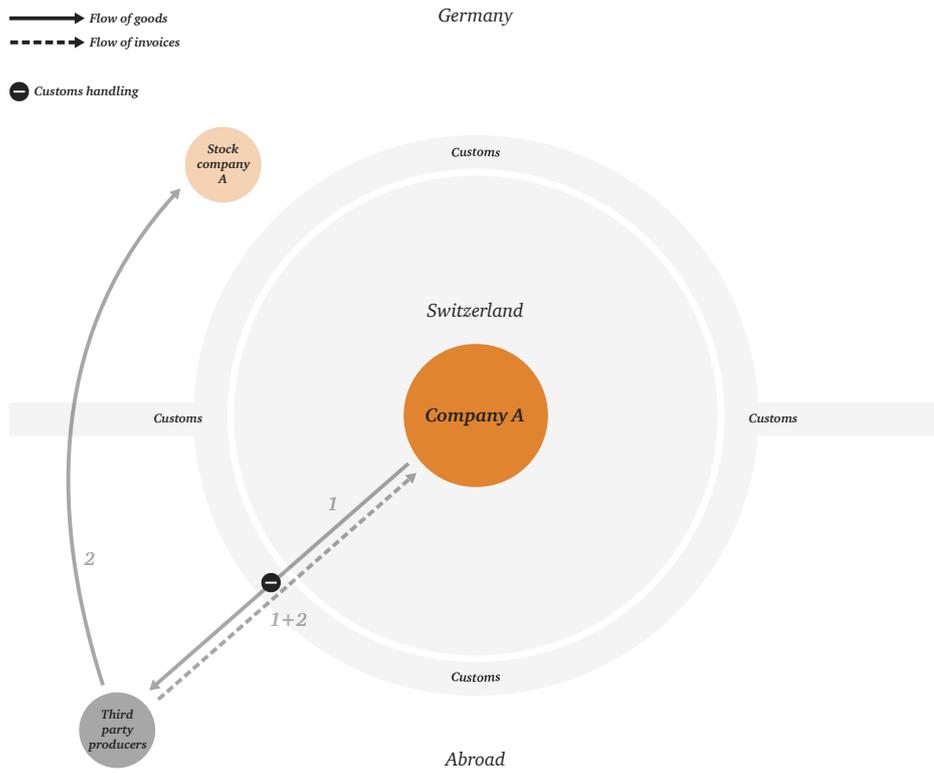
Overview



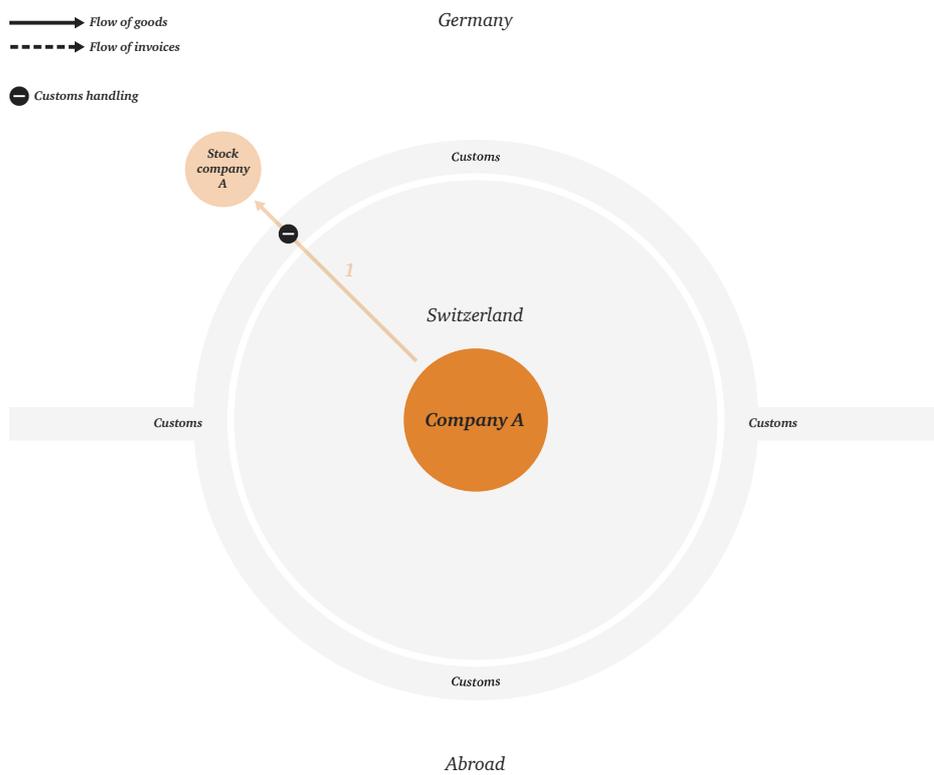
Supply/purchase



External production



Export/import



Sales

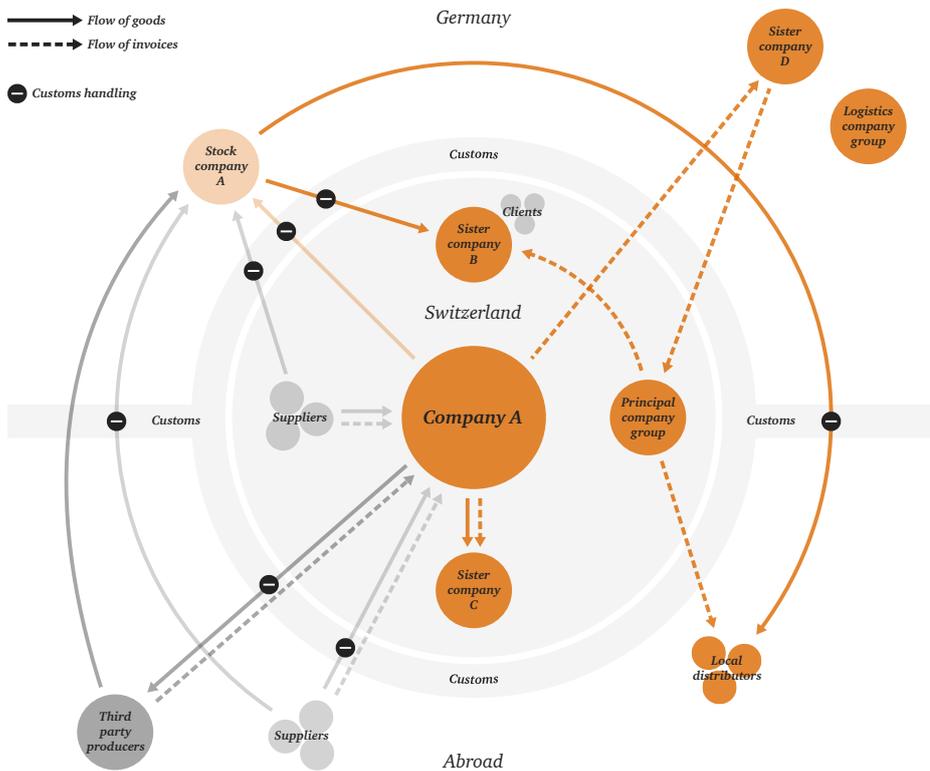


Figure 2: Points to consider in a complex international supply chain/delivery structure

- Importer of record/exporter of record in different countries
- Customs valuation
- Product classification
- Corporate/direct tax implications (principal structure)
- Transfer pricing issues (intercompany transactions)
- Incoterms
- Origin calculation
- Certificates of (preferential/non-preferential) origin
- Potential VAT liabilities in different countries
- Tax and duty overview
- Responsibilities
- Documentation
- Filing and archiving
- Collaboration with service providers (customs brokers, freight forwarders)
- Etc.

Complying with export control regulations

Most companies enjoy being in the headlines for good financial results or corporate responsibility practices. But it's a whole different story when it comes to supplying weapons to dictatorships or trading dual-use goods with sanctioned members of Al-Qaeda. Breaches of the Federal Act on the Implementation of International Sanctions

(SR 946.231) are no trifling matter. The legislation foresees up to five years of imprisonment and fines of CHF 1 million with regard to sanctions and embargoes and up to ten years of imprisonment and fines of CHF 5 million in relation to regulations on dual use and munitions. In this respect, US regulations are among the most stringent in the world, with companies facing the risk of being blacklisted (trade ban) if they fail to comply, rendering them unable to fulfil their orders and deliveries. However, according to many companies, the worst damage is to reputation with the public, business partners and the authorities. On the other hand, those that comply strictly with export regulations can also benefit from simplified arrangements such as general export licences.

Knowing the regulations is not enough, though. How can a major company importing and exporting tonnes of goods every day to all corners of the globe handle the screening of dozens of lists of sanctioned parties? How can they assert that a certain type of product is not considered as a dual-use good when shipped to a specific destination? How can they provide all the relevant licences and certificates along the supply chain when just-in-time business has become a standard staple of global trade? Added to this, in terms of export controls customs brokers and middlemen are of no help; only the company itself can be held accountable for an infraction and is therefore responsible for compliance. We would argue that only solid IT integration – including the screening of goods, business partners, destinations, etc. – and a bullet-proof organisation can give companies maximum safety and enable them to comply with the relevant regulations.

To plan is to anticipate: best practices and lessons learned

Our experience with clients has shown us that while companies derive value from global trade activities, they lack a coordinated strategy. They address preferences management, customs clearance and export controls in a disjointed manner. What is the reason for this? Customs formalities and trade operations affect several different departments, including purchasing, sales, IT, legal, production and logistics. Too often, the right hand doesn't know what the left hand is doing. For this reason we recommend a holistic approach and a single strategy defined at management level. What measures can be taken?

- Establish responsibilities and lay down a policy for trade and customs.
- Invest in training and disseminating know-how inside the company.
- Define organisational procedures and implement them in the IT

***We're at your
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infrastructure.

- Have accurate documentation, manuals, etc., at hand, and archived in accordance with the relevant legal requirements.

Summary

Global trade is a constantly-evolving landscape, with new regulations, technologies, risks and opportunities cropping up all the time. To be able to anticipate these, companies should define tools and solutions in line with technology developments and design an organisation that brings all customs and trade activities under the same roof. Investing in logistics optimisation is certainly the right thing to do, but the journey doesn't end there. To enable our clients to remain competitive in an ever-changing environment, we advise them to proactively address the issues resulting from the three megatrends we have described. Act now!