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Testimony

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INTERNATIONAL TRADE

**Observations on U.S.
Government Efforts to
Address Textile
Transshipment**

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GAO

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Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to appear today to provide our perspective on the issues associated with textile transshipment. I have had the opportunity to testify on a number of occasions before the Committee on Small Business, and learned more in each of those hearings about the importance of trade to the small business community. It is particularly important in the current economic environment that the United States does everything it can to ensure that U.S. laws regarding the entry of illegal goods are fully enforced at the U.S. borders. Effective monitoring of textile and apparel imports are also important because duties on textile and apparel products account for a significant share of U.S. duty collections. However, this enforcement takes place in the challenging and busy environment of U.S. ports of entry - - in fiscal year 2008, there were nearly 29 million trade entries processed at more than 300 ports of entry throughout the United States.

In my statement today, after providing some background on the role of Customs and Border Protection (CBP) with regard to textile imports and other goods, I will summarize key findings from our prior reports on (1) U.S. government efforts to enforce laws related to imports of textiles and other goods, including transshipment, and (2) the revenue implications of these efforts, as well as discuss the recommendations we made to improve those efforts.

GAO's last report on the subject of textile transshipment was published in 2004 and there have been many changes in world trade and in customs enforcement since that time. However, we have consulted with CBP since that report was issued on the status of their response to the GAO recommendations to improve that system. In addition, we have completed additional studies on customs enforcement issues, which provide important insights into the challenges CBP faces as it addresses textile transshipment. One of those reports covered the in-bond system, which was a key subject in the 2004 report on textiles, and a second is on CBP's ability to maintain an emphasis on revenue such as duties collected from textile and apparel imports. In addition, we have also completed numerous studies on intellectual property enforcement by CBP and other U.S. agencies, and there is considerable overlap between those efforts and textile enforcement efforts. We conducted our work in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained

provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

CBP is the agency primarily responsible for border enforcement, given its authority to detain and examine shipments and seize goods that violate U.S. law. These illegal goods could include textiles and apparel that are illegally entering the U.S., but could also include goods that violate U.S. laws related to intellectual property, illegal drugs, or product safety. CBP's priority mission is keeping terrorists and their weapons out of the U.S. CBP is also responsible for enforcing immigration and other border related laws and regulations. Two CBP offices are central to carrying out policies and procedures related to enforcement efforts at the U.S. border:¹

- Office of Field Operations – This office houses CBP's border operations and is comprised of 20 field offices under which are CBP's more than 300 ports of entry. With more than 20,000 CBP officers, the office is responsible for carrying out CBP's cargo and passenger-processing activities related to security, trade, immigration, and agricultural inspection. Daily management of port operations is highly decentralized, with field offices overseeing but not directly managing port operations. CBP's port operations oversee an array of cargo- and passenger-processing environments, and port management structures are not uniform. For example, some ports' management oversees a single port of entry while others oversee multiple ports of entry (e.g., a seaport and nearby airport).
- Office of International Trade – Established in October 2006, this office consolidates the trade policy, program development, and compliance measurement functions of CBP into one office. It is responsible for providing uniformity and clarity for the development of CBP's national strategy to facilitate legitimate trade and managing the design and implementation of strategic initiatives related to trade compliance and enforcement. CBP has identified seven customs issues considered to be its priority trade issues, one of which is textiles.

Although all goods imported into the United States are subject to examination, CBP examines only a small portion of them. The total number of exams conducted each year increased dramatically after

¹GAO, *Intellectual Property: Better Data Analysis and Integration Could Help U.S. Customs and Border Protection Improve Border Enforcement Efforts*, [GAO-07-735](#), (Washington, D.C.: April 26, 2007).

September 2001, but most exams conducted between 2001 and 2005 were for security rather than trade reasons; the percent of exams conducted for trade purposes decreased during that time period. When CBP detects imported goods that violate U.S. law, additional law enforcement agencies such as the Department of Homeland Security's (DHS) Immigration and Customs Enforcement (ICE) and the Department of Justice may become involved to further investigate and/or prosecute violators.²

CBP Attempts to Address Textile Transshipment, but Significant Challenges Remain

GAO's prior work has shown that CBP targets potential textile transshipment on several levels. However, we have found that CBP's efforts continue to face challenges which inhibit its ability to fully address the risk of textile transshipment.

To identify potential illegal textile transshipments to the United States, CBP targets countries, manufacturers, shipments, and importers that it determines to be at a higher risk for textile transshipment. CBP uses a targeting process that relies heavily on analyzing available trade data and other information to focus limited review and enforcement resources on the most suspect activity.

First, CBP identifies the countries in which trade flows and other information indicate a large potential for transshipment. Second, it focuses on selected manufacturers in those high-risk countries for overseas factory visits, by what are known as Textile Production Verification Teams. The teams attempt to verify that factories are able to produce the shipments they have claimed or to discover evidence of transshipment, such as counterfeit documents. If evidence of transshipment is found, CBP uses this information to target shipments to the United States for review and potential exclusions, seizures, or penalties. CBP also targets importers based on high-risk activity, and conducts internal control audits that include verifying whether the importers have controls against transshipment. However, resource constraints limit the number of foreign factories and shipments that CBP can target and review annually to a small share of textile and apparel trade.

²GAO, *Intellectual Property: Federal Enforcement Has Generally Increased, but Assessing Performance Could Strengthen Law Enforcement Efforts*, [GAO-08-157](#), (Washington, D.C.: March 11, 2008).

CBP's textile review process for preventing illegal textile transshipment has adapted to the changing security environment, but our past work found that CBP faces challenges in its monitoring and enforcement activities. The textile review process includes analysis of entry documents, inspection of shipments, and verification of foreign production. We found that CBP ports increasingly depend on information received from targeting the most high-risk shipments, the results of CBP's Textile Production Verification Team foreign factory visits, and other intelligence.

Our prior reports identified three key challenges to effectively addressing textile transshipment. First, in 2004 we found that CBP's Textile Production Verification Team reports were not always finalized and provided to CBP ports, other agencies, or foreign governments for follow-up in a timely manner.³ CBP adopted our recommendation to improve the timeliness of this follow-up. We also found that information from overseas Customs Attaché offices and cooperative efforts by foreign governments can provide important information for port inspections. Since the time of our report, CBP has increased the number of attaches in foreign ports to 20 in 2009. In addition, ICE has also increased its overseas personnel to over 50 in 2009.⁴

Second, the in-bond program creates the risk that importers can circumvent trade rules, including those applying to textile imports. To facilitate trade, the U.S. customs system allows imported cargo intended for either U.S. or foreign markets to move from one U.S. port to another without being assessed duties or quotas and without officially entering U.S. commerce. This cargo—referred to as an in-bond shipment, requires a responsible party to be covered by a CBP-approved bond and to agree to comply with applicable regulations. Some CBP port officials have estimated that in-bond shipments represent from 30 percent to 60 percent of goods received at their ports.

In our original report on textile transshipment and in a later review, we found that CBP's ability to assess and manage the risks of the in-bond cargo system was impaired by both (1) the limited information it collected on in-bond cargo and (2) the limited analysis it performed on available

³GAO, *International Trade: U.S. Customs and Border Protection Faces Challenges in Addressing Illegal Textile Transshipment*, [GAO-04-345](#), (Washington, D.C.: Jan. 23, 2004).

⁴GAO, *Overseas U.S. Government Personnel Involved in Efforts to Protect and Enforce Intellectual Property Rights*, [GAO-09-402R](#), (Washington, D.C.: Feb. 26, 2009).

information.⁵ Evidence indicates that the in-bond system has been used at times for moving unauthorized goods through the country. For example, in 2007, we reported that about one-third of the value of goods that CBP seized for intellectual property violations in 2004 and 2006 were moving through the in-bond system. With the tremendous volume of trade coming through U.S. ports, CBP needs detailed information and accurate monitoring systems to set priorities for targeting and tracking cargo shipments that pose security or revenue risks. However, we found that CBP did not collect detailed information on the value or type of in-bond cargo being transported through U.S. ports; the in-bond form asks only for a general description. As a result, CBP did not have the information needed to set priorities for targeting and tracking cargo moving within the in-bond program, so as to concentrate on cargo of highest security, law enforcement, or revenue impact.

To address these weaknesses, GAO recommended in 2004 and again in 2007 that CBP increase targeting and inspection of in-bond shipments and collect more detailed information about such shipments. In response, CBP issued new in-bond inspection and data collection guidance to its ports, as well as updated guidance on in-bond processing requirements. In 2008, CBP issued guidance to advise ports on using automated targeting systems to identify at-risk in-bond shipments. CBP has also been working under the SAFE Port Act of 2006 to establish new information requirements for all maritime cargo destined to the United States, through its Secure Freight Initiative.

Third, in reviewing the in-bond system, we also found that CBP had failed to perform basic analyses of available information. CBP was not able to tell us, for example, the extent of the system's use, what products are shipped in-bond, or what shipments are expected for entry (and thus expected revenue collection from applicable trade duties) at inland ports. Despite prior audit recommendations, important management weaknesses persisted in CBP's tracking of in-bond cargo, with the result that CBP still does not know whether in-bond cargo shipments of greatest security or revenue interest are in fact entered into U.S. commerce or exported as required. In particular, CBP continued to have high numbers of open in-bond transactions with uncertain disposition. As a result, GAO made a

⁵GAO, *International Trade: Persistent Weaknesses in the In-Bond Cargo System Impede Customs and Border Protection's Ability to Address Revenue, Trade, and Security Concerns*, [GAO-07-561](#), (Washington, D.C.: April 17, 2007).

series of recommendations to improve the oversight and monitoring of cargo moving within the in-bond system.

In response to those recommendations, CBP has taken steps to improve monitoring and oversight of in-bond shipments. For example, it increased data collection requirements on in-bond shipments and updated its Automated Commercial System (ACS) to better track, link, and report on such shipments. These steps have reduced the number of open in-bond transactions. CBP also modified the development plans for its Automated Commercial Environment System (ACE) to ensure that ACE provides adequate in-bond tracking and reporting capabilities. CBP also developed proposed regulatory changes that are expected to address certain weaknesses with in-bond regulation, by shortening the time period during which in-bond shipments can transit the country and requiring importers to notify CBP if their shipment plans change. As of August 2008, these proposed changes were being reviewed within CBP. To the extent that these changes address problems with the in-bond system, they will also address one of the ways in which textiles and other goods might illegally enter the United States or enter without paying the appropriate duties.

CBP Needs to Renew Its Focus on Revenue Functions

In addition to needed improvements on specific programs, we also found that CBP had to find a way to better balance security and important trade functions such as revenue collection. Although CBP's priority mission relates to homeland security, it collected more than \$34 billion in fiscal year 2008, making it the second largest revenue generator for the federal government. Because of the high concentration of duties collected on textiles and apparel—four percent of U.S. imports generate approximately 40 percent of U.S. duties collected—any efforts to focus on revenue functions would likely generate improved oversight of textile and apparel imports. When the Customs Service was created in 1789 under the Department of the Treasury, its mission was almost entirely focused on revenue collection. Over time, the agency was presented with new missions and challenges, including drug interdiction, immigration enforcement, and airport passenger processing. But customs revenue functions, such as assessing and collecting duties, excise taxes, and fees and penalties, were always central to the Customs Service's mission because they produced substantial revenue.

To preserve a high level of customs revenue collections, Congress required in Section 412(b) of the Homeland Security Act that CBP, at a minimum, maintain certain revenue function positions and the level of staff resources that were present in the U.S. Customs Service when it became part of DHS

in March 2003. The nine specific revenue function positions Congress required CBP to maintain were Import Specialists; Entry Specialists; Drawback Specialists; National Import Specialists; Fines, Penalties, and Forfeiture Specialists; attorneys of the Office of Regulations and Rulings; Customs Auditors; International Trade Specialists; and Financial Systems Specialists. The act also mandated that CBP maintain, at a minimum, the levels of support staff associated with customs revenue positions. Associated support staff provide a variety of management, technical, and administrative support functions. Some staff considered associated support staff includes Liquidators, Seized Property Custodians, Customs Technicians, as well as, Assistant Port Directors, Account Managers, and Economists. In 2007 we reported that CBP had not maintained the minimum number of staff in each position.⁶ In addition, other positions that were not specified in the act (e.g., CBP Officers) that previously performed primarily customs enforcement functions, were spending much of their time performing homeland security functions.

Our previous findings suggest that Congress' concerns about the potential effects of moving customs revenue functions into DHS, whose priority mission is homeland security, were warranted. We found that this shift in mission contributed to reduced focus and resources devoted to customs revenue functions. Specifically, the number of staff in most customs revenue positions declined since the creation of DHS, despite a legislative mandate that they should not. In addition, the number of Auditors in the Office of Inspector General dedicated to customs issues has declined as the office's resources were focused in other areas. As a result the DHS Office of Inspector General conducted no performance audits related to customs revenue functions until 2007.

As a result of these findings, GAO recommended that CBP perform workforce planning to ensure that they had the necessary expertise to perform the various functions related to collection of duties and penalties. In addition, we also recommended that the DHS Office of Inspector General should identify whether areas of high risk related to customs revenue functions exist and consider initiating performance audits to explore and mitigate those risks.

⁶GAO, *Customs Revenue: Customs and Border Protection Needs to Improve Workforce Planning and Accountability*, [GAO-07-529](#), (Washington, D.C.: April 12, 2007).

In response the DHS Office of Inspector General initiated a broad survey of customs revenue functions to determine whether areas of high risk related to customs revenue functions exist and initiated additional work. For example, in February 2009, the DHS Office of Inspector General reported on CBP's management of revenue analysis functions.⁷ In addition, in preparing its fiscal year 2010 budget request, CBP employed a resource allocation model to determine the resources necessary to perform trade functions. As a result, it requested funding for 103 positions related to import safety and trade enforcement.

Conclusion

Mr. Chairman, we appreciate the opportunity to summarize our work related to CBP's efforts to enforce U.S. laws regarding illegal shipments of textiles and other products. As I have noted in my statement, we have performed a number of studies for the U.S. Congress both on textile issues specifically as well as on a number of closely related issues such as the in-bond program, revenue collection, and intellectual property enforcement at the U.S. border. Over time, we have found that CBP has made improvements in its efforts to enforce trade laws, including those related to textiles, but trade enforcement issues continue to present long-term challenges with significant revenue implications for the U.S. government. This concludes my statement, but I welcome the opportunity to answer any additional questions from you or other members of the Subcommittee.

⁷Department of Homeland Security Office of Inspector General, *Management of CBP Revenue Analysis Functions*, OIG-09-29 (Washington, D.C.: Feb. 12, 2009).

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