

Supply Chain Security

Opportunity or threat?

The impact of 9/11 has hit the EU shores and from January 2008 businesses that want their goods to continue to move freely into and out of the EU should consider applying for a new accreditation from HMRC to become an Authorised Economic Operator (AEO). It is likely to become a 'kitemark' for trusted business partners.

Who is affected?

All businesses that own or move goods through the international supply chain are affected, irrespective of size or trade sector, including:

- manufacturers,
- importers,
- exporters,
- freight forwarders,
- agents,
- warehousekeepers and
- logistics service providers.

Kim Hutchinson, Director of specialist tax consultancy SKS (GB) Ltd, looks at the pros and cons of becoming an Authorised Economic Operator

'The AEO could therefore be chosen as a business partner, instead of a non-AEO ...'

Are there benefits to becoming an AEO?

Currently most of the benefits are commercial, one of the main ones being the fast-tracking of consignments through customs controls. Many large businesses are now asking those involved in their supply chains if they are applying for AEO or equivalent. Although AEO is EU-based, similar initiatives are developing worldwide and many companies are

of global trade; of these 149 have so far expressed their intention to implement the SAFE framework. The SAFE framework introduced the concept of AEO. An AEO is seen as a member of the international supply chain whose compliance with WCO supply chain security standards (or equivalent) has been approved by (or on behalf of) the customs authorities.

The Customs Security Programme (CSP) is an EU-wide initiative to tackle terrorism, counterfeiting and fraud. By introducing enhanced security controls the programme aims to ensure that the EU internal market is protected and, through co-operation with major world trading partners, secure the international supply chain.

The EU's supply chain security regime adopts the principles introduced by the WCO's SAFE framework. The EU AEO regime is one part of the CSP and introduces an accreditation scheme for reliable businesses that can show themselves to be trusted and compliant members of the international supply chain and are therefore entitled to certain benefits. AEO status will take effect from 1 January 2008.

Similar measures are in place in the United States, New Zealand, South Africa, Canada and Vietnam.

Within the EU AEO status will be granted to businesses meeting the criteria for one of three possible certificates:

- customs simplifications;
- security and safety; and
- a combined certificate.

How to apply

Applications for AEO are voluntary and in the UK HMRC is responsible

The AEO guidelines published by the European Commission explain that: 'An AEO who meets the security and safety criteria is considered to be a safe and secure partner in the supply chain'

What is its purpose?

HMRC states:

'The aim is to provide business with an internationally recognised quality mark which will indicate that their role in the international supply chain is secure and their customs controls and procedures are efficient and compliant.'

The AEO guidelines published by the European Commission explain that:

'An AEO who meets the security and safety criteria is considered to be a safe and secure partner in the supply chain. This means that the AEO does everything in his power to reduce threats in the supply chain where he is involved. The AEO status enhances his reputation.

applying simply because they do not want to be left behind.

Background

Following the 9/11 terrorist attacks on the United States, securing the global supply chain became a priority for governments and business alike. The recent failed attacks in the UK have once again brought the question of security to the top of the agenda.

The World Customs Organisation (WCO) is encouraging all its members to adopt supply chain security measures as outlined in its 'Framework of Standards to Secure and Facilitate Global Trade', known as the 'SAFE framework'. Countries which are members of the WCO account for approximately 99%

for approving applicants. In the future it is likely that HMRC will be working closely with the new UK Border Agency in relation to supply chain security and the AEO regime.

HMRC has been accepting applications for AEO status since 1 July 2007.

Depending on the type of certification sought, the applicant is required to prove to HMRC that its business meets certain criteria in terms of its financial solvency, customs compliance, record-keeping and safety and security procedures. The criteria cover many areas of business operations beyond just safety, security and customs matters and include IT security, employment policies, training and contracts with employment agencies, transport and cleaning companies.

The processes and systems in place will be subject to scrutiny by HMRC prior to granting the approval. HMRC will take into account existing international accreditations, such as ISO standards, to the extent that the criteria correspond to or are identical to the AEO criteria.

What are the benefits?

The benefits an AEO receives will depend upon the type of certificate held, but may include:

- fewer physical or documentary examinations due to a lower risk score;
- fast-tracking of consignments through customs controls and if selected for examination the AEO's goods will take priority over those not similarly accredited;
- the AEO can also request, subject to agreement by HMRC, for controls to be carried out in a different location to minimise cost – for example, due to demurrage charges and delays;
- quicker authorisation for customs simplified procedures, as requirements already complied with as part of the AEO application process will not need to be re-examined;
- access to simplifications such as guarantee waivers, centralised clearance and single community authorisations when the modernised Customs Code is agreed;
- easier access to simplifications in other Member States due to the recognition of AEO status across the EU; and
- AEO is seen as a 'kitemark' for businesses involved in international trade.

The benefits apply only to the AEO; they do not, for example in the case of a freight forwarder, apply to its clients.

Based upon initiatives elsewhere in the world participants in such programmes may experience further indirect benefits from investing in supply chain security.

What benefits have participants in supply chain security programmes in other countries enjoyed?

The US launched the Customs-Trade Partnership Against Terrorism programme, known as C-TPAT, in November 2001 with seven major importing companies. There are currently about 6,000 C-TPAT certified companies. In addition to a decrease in the number of inspections

Will AEO status be recognised by the authorities in other countries?

One of the aims of the WCO SAFE framework is an international system of mutual recognition of supply chain security measures between WCO member states, which should result in more predictability in international trade for those that attain AEO status or equivalent.

The EU is currently in talks with a number of trading partners, including the US, regarding mutual accreditation of supply chain security regimes.

On 29 June 2007 the US and New Zealand signed a 'Mutual Recognition Arrangement' which provides for

HMRC will take into account existing international accreditations, such as ISO standards, to the extent that the criteria correspond to or are identical to the AEO criteria

carried out by US Customs and Border Protection and a reduction in the time taken to clear goods, C-TPAT participants have also reported certain indirect benefits of improved supply chain security:

- reduction in losses due to theft or damage;
- improvement in on-time deliveries and reduction in shipping delays and costs, resulting in enhanced customer relationships, fewer cancelled orders and increased customer confidence;

closer co-ordination and co-operation between New Zealand's 'Secure Export Scheme' and the US's C-TPAT scheme. Ultimately the two countries are expected to treat members of the other country's supply chain security programme in the same manner as members of their own programme. In addition to working towards mutual recognition of the EU AEO regime, the US is also expected to sign agreements with Japan and Jordan in the near future.

The US President recently approved a Security Bill which will require, within five years, the scanning of 100% of cargo containers destined for the United States before they leave a foreign port

- improvements in inventory management and reduction in stock levels;
- improvements in supply chain visibility in relation to the location and condition of goods;
- improved process compliance which led to improved performance in other areas of the businesses such as quality and health and safety;
- increased security awareness throughout the business resulting in an improvement in the time taken to identify and resolve problems, potentially reducing their impact; and
- reduced insurance premiums due to security procedures having been vetted by the customs authorities.

The ultimate aim is a global green channel for legitimate trade.

Recent steps taken by the US authorities

The US President recently approved a Security Bill which will require, within five years, the scanning of 100% of cargo containers destined for the United States before they leave a foreign port. Approval was granted despite the fact that the current pilot on the technical feasibility of 100% scanning has not yet been completed, nor has it been established.

Many millions of containers enter the United States by sea every year, some 11 to 12 million from European ports alone:

forcing all to undergo scanning and radiation detection monitoring before leaving a foreign port will undoubtedly result in delays and increased costs.

Whether these will be borne by the exporter or the US importer remains to be seen. However, it is feared that the burden of protecting the US will fall on her international trading partners.

Could supply chain security become a future barrier to trade?

Opposition to the unilateral imposition of these cargo security measures is being voiced by business groups and politicians, both within the US and around the world.

The WCO's SAFE framework, referred to earlier, states that:

'... at the reasonable request of the receiving nation, based upon a comparable risk-targeting methodology, the sending nation's customs administration will perform an outbound inspection of high-risk containers and cargo, preferably using non-intrusive detection equipment such as large-scale X-ray machines and radiation detectors.'

100% scanning does not seem to sit comfortably with this targeted, risk-based approach or to comply with the spirit of the framework, particularly with regard to the aim of facilitating trade. Indeed the US move could ultimately unravel the framework and lead to disruption in trade.

An obvious risk is that the US's international trading partners may demand reciprocal screening of outbound cargo from the US. Doubts have been voiced in the US as to whether its ports have the technology or manpower to meet the very requirements it is seeking to impose on its trading partners. The EU has indicated that it is not currently interested in retaliating by imposing additional barriers to trade. However, if these measures result in EU traders suffering a disadvantage when compared to their US competitors, this could lead to a complaint by the EU to the World Trade Organisation. No doubt other trading nations would take a similar stance.

Eventually companies involved in international trade which do not hold AEO status (or equivalent) may find themselves operating in a much more difficult trading environment.

Will those businesses without AEO status be at a commercial disadvantage?

Many businesses that have begun to seek AEO authorisation have done so for commercial rather than tax reasons. The likelihood is that most large businesses will seek accreditation and may only wish to deal with suppliers and service providers that are similarly accredited or can demonstrate safety and security standards which meet or exceed those required for AEO accreditation. The presence of a non-authorised business in the supply chain may result in a higher risk rating, greater scrutiny by HMRC, potential delays in the movement of goods and increased costs.

What next?

HMRC has published the application documents on its website and businesses intending to apply should begin the process by downloading this information.

Kim Hutchinson is a director of specialist tax consultancy SKS (GB) Ltd (www.sks.gb.com) and can be contacted by phone: 07766 726 750 or by e-mail at: kimhutchinson@sks.gb.com.