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BEFORE THE

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UNITED STATES SENATE

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FIRST SESSION

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CONTENTS

THURSDAY, MAY 13, 1999

(MEETING THE CHALLENGE OF GLOBAL COMMERCE)

OPENING STATEMENTS

CUSTOMS SERVICE WITNESSES

DEPARTMENT OF THE TREASURY WITNESSES

CONGRESSIONAL WITNESSES

PUBLIC WITNESSES

TUESDAY, MAY 18, 1999

(MEASURING EFFECTIVENESS IN ENFORCEMENT OPERATIONS)

OPENING STATEMENTS

CONGRESSIONAL WITNESSES

TUESDAY, MAY 25, 1999

(ENSURING EFFECTIVENESS, INTEGRITY, AND ACCOUNTABILITY IN CUSTOMS OPERATIONS)

COMMUNICATIONS

U.S. CUSTOMS SERVICE: MEETING THE CHALLENGE OF GLOBAL COMMERCE

THURSDAY, MAY 13, 1999

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 10:15 a.m., in room SD–215, Dirksen Senate Office Building, Hon. William V. Roth, Jr., (chairman of the committee) presiding.

Also present: Senators Grassley, Gramm, Moynihan, Baucus, Graham, and Kerrey.

OPENING STATEMENT OF HON. WILLIAM V. ROTH, JR., A U.S. SENATOR FROM DELAWARE, CHAIRMAN, COMMITTEE ON FINANCE

The CHAIRMAN. The committee will please be in order.

This is the first of three oversight hearings the committee plans to hold on the performance of the U.S. Customs Service. The hearings parallel and reinforce a broader oversight process that I initiated this past year when the committee considered authorizing additional appropriations for Customs.

At that time, I highlighted the need to assess Customs' performance of its twin missions of facilitation of international commerce on which our economy increasingly depends, and the effective enforcement of the Custom laws of the U.S. Today, I would like to add the need to assess whether Customs has been effective in the management of its own internal affairs.

Five years have passed since the committee and the Congress ordered improvements in Customs Service operations, with the passage of the Customs Modernization Act. In these 5 years, the volume of trade crossing our borders and the challenges facing the Customs Service has at least doubled.

Implementation of the NAFTA and the Uruguay Round agreements and the prolonged expansion of the U.S. economy has dramatically increased the traffic, both inbound and outbound at our ports and along our northern and southern land borders.

That trade, which Customs is responsible for facilitating, has contributed significantly to our national well-being. While Customs' responsibilities were growing, however, the agency's resources declined in real terms.

Reports of brown-out in the Customs' computer system and lengthy delays reported at U.S. ports and border crossings suggest that Customs may be headed for a serious breakdown, either in en-

forcement or in its commercial operations, and will have a profound impact on the flow of legitimate commerce that benefits our Nation.

Left unattended, the festering problem could have serious consequences, where our economy and our trade policy in an economy that depends on just-in-time inventory can mean slow-downs on the production line, higher costs, and lost sales.

I can give you a real-life example from my home State of Delaware. The workers in the Chrysler facility in Newark, Delaware produce one of the hottest selling vehicles in America, the Dodge Durango. Every week, 50 shipments must clear Customs at the Canadian border in order to keep the production line running.

If the current Custom transaction processing system goes down, it would bring production to a halt and idle the entire plant and its work force. That is why I believe the question before the committee, Pat, and Customs, in these hearings is whether the agency is, in fact, prepared to meet the challenge of global commerce.

I would now be happy to call upon Senator Moynihan.

OPENING STATEMENT OF HON. DANIEL PATRICK MOYNIHAN, A U.S. SENATOR FROM NEW YORK

Senator MOYNIHAN. A brief word, Mr. Chairman, once again, to thank you for pursuing this matter. I know how strongly Commissioner Kelly feels about this. You will remember, we met a month or so ago and he was very much in favor of what we are doing here, as is Undersecretary Johnson and Ms. Killefer.

I have one matter that has just been on my mind. I know it has been on Mr. Kelly's the same way. That is, the complexity of our tariff schedule. The American tariffs are still the Smoot-Hawley tariffs of 1930. We have 10,308 categories. After 60 years of cleaning up all this and getting rid of most of it, it is still in print and it needs to be attended to. I expect Mr. Kelly will tell us about his plans.

You could not be more right about those Durangos. Up on the Canadian border, we are very much aware of this in New York. Since the Free Trade Agreement with Canada, our trade with Canada has reached $1 billion a day. The facilities are not there for that. I mean, they were built for an earlier age in Buffalo, Champlain, and Alexandria Bay. We are going to have to do better.

So, Mr. Chairman, brace yourself: there is going to be a matter of appropriations coming along soon. [Laughter.] Thank you again, sir.

The CHAIRMAN. Thank you.

I would ask the other members of the panel to put any opening remarks in the record, as we have three groups of witnesses today. So, time is running late.

It is my pleasure to welcome, of course, the Honorable Raymond Kelly, the Commissioner of Customs, as well as Hon. James Johnson, who, of course, is Undersecretary of the Treasury for Enforcement. We are also very pleased to have Nancy Killefer, the Assistant Secretary of the Treasury for Management, who is accompanying Undersecretary Johnson.

Commissioner Kelly, would you please proceed? Your full statement, of course, will be included as if read.

STATEMENT OF HON. RAYMOND W. KELLY, COMMISSIONER, U.S. CUSTOMS SERVICE, WASHINGTON, DC

Commissioner KELLY. Thank you very much, Mr. Chairman, Senator Moynihan, members of the committee. Thank you for giving me this opportunity to testify today.

Before I came to Washington, I had a better-than-average understanding of the workings of the U.S. Customs Service from my tenure in the New York City Police Department.

Our paths crossed on everything from narcotics arrest and money laundering investigations to the smashing of an international auto theft ring that specialized in stealing luxury sedans off the streets of Manhattan for resale abroad.

But it was not until I came to the Department of Treasury as Undersecretary for Enforcement that I fully appreciated the vast and complex responsibilities of the Customs Service, as well as the difficulties and the very real dangers faced by our employees.

The men and women of the Customs Service continue to process trade and passengers in record numbers. In 1998, we processed 19.7 million trade entries. To give you some perspective, in 1994 we processed 12.3 million entries. That is an average annual growth rate of about 12.5 percent. Four hundred and sixty million passengers moved through our inspection areas last year; 13 million more than 1997.

The statement of processing trade and passengers in record numbers, however, does not quite capture just how hard that work can be. Many of you know what I am talking about through your visits to our border areas. You have seen what it is like for inspectors to work border crossings in searing heat, doing painstaking, difficult, and dangerous searches. Our agents, marine officers, and pilots also constantly put themselves in harm's way in pursuit of our mission.

The price for our successes in 1998 was the lives of two agents and one pilot. The families of these fallen officers are here in Washington this week to attend the memorial service at the Treasury Department as part of National Police Week.

As difficult as it was for Customs to lose these brave men, our grief is nothing compared to the hardship borne by the spouses, children, and friends of these officers. Their sacrifices were not in vain.

Combined, our agents and inspectors seized a record 1.35 million pounds of illegal narcotics in 1998. That is over 1 million pounds of drugs that will not find its way into American schools, streets, and communities.

Our people are not only stopping drugs, we are protecting our Nation's children with our expertise in areas such as child exploitation on the Internet. Recently, an alert Customs agent assigned to stop this crime saved a 12-year-old girl from a cyber pedophile. The suspect had lured the child into a possible face-to-face meeting through e-mail conversations in a chat room. These are real, modern-day threats our front-line people must contend with.

Along with our dedicated corps of import specialists, technical personnel, and intelligence analysts, they make a formidable defense against trade fraud, drug smuggling, terrorist activity, and Internet crime.

People who work this hard and take such risk on behalf of the American public deserve to be supported by the most ably-managed agency possible. So, of course, to the American people.

It was clear to me when I arrived that too much was at stake in the Customs Service to let problems fester, problems that threaten to compromise the mission of a great agency at a time when the country could least afford it.

Instead of informed, consistent, and service-wide policy making emanating from Washington headquarters, I found that inconsistent, often uninformed, decisions were being made out of hundreds of ports across the country.

Decision making on hiring, promotion, and disciplinary issues differed from one region to the next, without headquarters' oversight. All of this conspired to fuel fear among the rank and file that favoritism, real or perceived, dictated who was promoted, or worse, who was protected from disciplinary action.

Instead of a robust Office of Internal Affairs to combat corruption, a poorly-led shell of a function existed that was further emasculated by a lack of resources and authority.

On top of all of this, the frailty of our automated system to handle imports threatened to reduce our processing power dramatically. In its candid and thoughtful assessment, the GAO said the system could be fixed, but the Customs Service was not up to the task. Clearly, actions had to be taken.

One of my first undertakings upon being confirmed as Commissioner was to develop a priority list of these problem areas. We used this list to develop a document we referred to as Action Plan 1999.

The plan covers all of the major areas that we have to be concerned about, from both a law enforcement perspective and a trade perspective. These include integrity, accountability, discipline, training, automation, and passenger services, to name a few.

These reforms are explained in greater detail in my submitted statement. I would like to briefly summarize them here. Reinforcing integrity at U.S. Customs has been, and continues to be, our top priority. Any organization with powers like those granted to Customs must uphold the highest standards of ethics and integrity.

Our Internal Affairs Office, the focus of our integrity efforts, has been thoroughly reformed. It has received, and continues to receive, the resources, the support the personnel and the priority it must have to make our corruption-fighting capacity second to none.

To underpin our efforts in Internal Affairs, we replaced a weak, fractured, and inconsistent employee allegation and disciplinary process with a new, integrated system. It includes a computer tracking program that is designed to stop integrity and disciplinary problems from falling through the cracks.

New, agency-wide accountability standards will help to solidify these reforms. A new inspection regime has our field operations reporting directly to headquarters with greater frequency as opposed to the dislocated process of the past. Management roles have been clearly defined, to leave no confusion about who is responsible for getting the job done.

However, integrity cannot be reinforced through discipline and accountability alone. It must be strengthened through training. We

have established a New Office of Training, led by an assistant commissioner, to bolster training in all respects, both in-service and for new employees. This person has been selected and should be on board soon.

I would like to say a few words about our passenger services. It has been disturbing, to say the least, for the Customs Service to be confronted with charges of racism in the conduct of what is, admittedly, a demeaning process in even the most impartial of circumstances, namely the personal search for illegal drugs.

As long as the national appetite for illegal drugs is such that traffickers will hide drugs on, or even in, the persons they recruit to smuggle contraband into America, some form of invasive search as a last resort will be required to stop them.

Last year, we seized over 2.5 tons of illegal narcotics from air passengers. The lengths that they will go to are astonishing. In fact, Mr. Chairman, I have here examples of the pellets drug couriers swallow, which they often make from the fingers of rubber gloves.

These two pellets weigh about 18 grams each. The average smuggler would swallow about 60 of these pellets. That is roughly one kilogram, or 2.2 pounds. Each of these would be filled with heroin, worth about $1,800 on the streets. The whole kilogram would be worth about a quarter of a million dollars, retail. Now you have a sense of why these people are willing to try anything to get their drugs through.

Drug dealers will exploit anyone they can, children, even infants. Stopping this threat is not easy work, but it is something we have to do. I much prefer using the advanced technology available, like body scanners, to move away from personal searches. We have already installed some of this equipment at our busiest airports. We need to install more.

We have also changed our procedures to make certain that the supervisor is engaged in each decision whether or not to proceed with a personal search when alternatives are not available.

Most importantly, we establish an independent commission to examine the Custom Service's record of personal searches to determine whether racial bias, conscious or otherwise, has been a factor in these searches. We will not tolerate racial bias, not in the name of the war on drugs, not for any reason.

Still, the cartels and others should not mistake our color-blind commitment to the rights of individuals as a flagging in our determination to deny traffickers and their mules entry into the United States. They will be stopped and brought to justice.

From an operational standpoint, there is no issue more critical to Customs' future than automation. It is the heart and soul of our commercial operations and the key to our relationship with the all-important trade community.

We are at a crucial junction in our efforts to meet the mandates established by the Customs Modernization Act of 1993. Before trade automation, all entries looked like this. This particular entry covers one container of goods destined for a department store. It covers several commodities: sweaters, handbags, and glassware.

Now, this is paperwork for one container. Before automation, Customs officers had to pore over these documents line by line to

ensure that the proper amount of duty was paid and that these goods were not in violation of trade agreements.

In this case, that is 624 pages. Today, less than one percent of entries are received this way. For the most part, we receive them electronically. We can pull up the needed data immediately, meaning less delay.

Without automation, we are back to this pile of paper. If our current overburdened system breaks down, this is what we have to work with. You can imagine the difficulties we would face. The flow of trade across our borders would be slowed significantly, if not brought to a halt, in many places. Customs cannot afford to do this, and neither can American business.

We need a long-term answer to this problem. We need the Automated Commercial Environment, or ACE. We have taken steps to ensure that our systems modernization plans are competent, well-managed, and up to date.

We have worked closely with the private sector on both the design and the technical specifications for the new automated system. We have restructured our Office of Information and Technology, appointed capable and experienced leaders for this project, and reviewed our cost and accounting methods with an independent consultant.

We have also run a series of prototypes for a new automated system that has met with great praise from the private sector. We are adopting all of the recommendations put forward by GAO.

Today's hearing offers Customs the chance to provide the Congress with perhaps the most comprehensive assessment of our trade modernization efforts to date. We look forward to working with the Congress and this committee on clearing the substantial hurdles that remain.

Mr. Chairman, members of the committee, many have questioned our ability to institute reforms at an agency that has repeatedly shaken off criticism in the past and settled back to its old ways.

Oversight hearings by the House Ways and Means Committee several years ago precipitated a number of reforms in the Customs Service. Over time, many of these reforms were dismantled. Since being sworn in just over 9 months ago, I instituted many of these and added more. I believe these changes cut much deeper than before into Custom's management culture.

Our new disciplinary system, our new inspection regime, our centralized reporting lines, these are real initiatives that will become institutionalized, resulting not just in a temporary fix, but in lasting changes in how Customs employees view their roles and responsibilities. These reforms, with the help of Congress, must be allowed to permeate the organization and take hold.

Somebody said that I would occupy the hot seat today. But, in truth, I would not trade places with anyone. As Commissioner, I accept the accountability that comes with this job and I welcome the oversight. This is good government.

I am confident that your examination of the Service will, in the end, make for a stronger agency, better equipped to do the job and better understood by this committee, by the Congress, and by the American people. Ultimately, that is a prescription for success that I believe all of us are searching for.

In closing, I want to thank all the members here for supporting the Customs Service over the past year. Thank you, Mr. Chairman.

[The prepared statement of Commissioner Kelly appears in the appendix.]

The CHAIRMAN. Thank you, Commissioner Kelly. Just let me say, I think you have one of the most challenging jobs in government. But it is also an opportunity.

Once again, Pat, we are talking about changing the culture of an organization, which is not easy.

We look forward to working with you on this critical, pressing problem.

Now we would be very happy to hear from Secretary Johnson.

STATEMENT OF HON. JAMES E. JOHNSON, UNDERSECRETARY OF TREASURY FOR ENFORCEMENT, DEPARTMENT OF THE TREASURY, WASHINGTON, DC

Secretary JOHNSON. Thank you, Mr. Chairman, Senator Moynihan, and members of the committee. Good morning. It is an honor for me to be here today in support of the U.S. Customs Service and the Customs Service's efforts to carry out its intricate dual responsibilities of facilitating international trade and pursuing aggressive law enforcement.

You have clearly heard very strongly from the Commissioner. Many of the issues that he raised, I will not rehearse for you in my testimony. I would ask instead that, with the committee's consent, my written testimony be submitted for the record. I would summarize, and then make myself available to answer any questions the committee would have for me.

The CHAIRMAN. So ordered.

[The prepared statement of Undersecretary Johnson appears in the appendix.]

Secretary JOHNSON. My written testimony focuses and sums up the department's role, particularly that of the Office of Enforcement, in providing support to the Customs Service and Commissioner Kelly as they pursue the action plan and perform Customs' mission in an environment of constrained budgets and increasing demand for services.

This morning I would like to take the opportunity to highlight some of the major themes of my statement. As each year passes, the world becomes a much more complex and a much more dangerous place.

The danger to law enforcement personnel was brought home to all of us this week as we mark Police Week and honor those who have sacrificed their lives in service to our Nation, including two of our Customs agents and the pilot that Commissioner Kelly referred to just a while ago.

Customs' vital place within this law enforcement community and in the service it provides to the country makes this a crucially important hearing. We thank the committee for its continuing interest in, and support of, the U.S. Customs Service.

This is a unique moment in Customs' long and proud history. The Service faces daunting challenges based upon a mission that, on the one hand, requires the facilitation of legitimate commerce and travel, while on the other requires the greatest vigilance in

countering attempts to smuggle narcotics and other contraband into our country, those attempts that were just so vividly illustrated in the Commissioner's testimony.

Customs is meeting the trade and enforcement challenges before it, in large part, through the dedication and professionalism of its people. It also, however, is moving into a better position to respond to challenges because of its willingness to adopt changes that will make an already strong agency that much stronger.

One of its most powerful agents of change is Commissioner Kelly. Through his entire professional career, and most notably for purposes of this hearing, first, as Undersecretary for Enforcement, and now as Commissioner of Customs, Ray Kelly has had a unique capability of evaluating an organization, reinforcing those elements proven to be constructive, and overhauling those in need of repair.

His ability to make change work for an organization has always led to a more productive work force, and we expect it to lead to more accountable management and better service to the public.

In the case of Customs, the Commissioner is pursuing his agenda, our overall agenda, for change through development of a detailed action plan, which he has often referred to as a living document.

The action plan includes tangible goals for improvements in the organization structure, management, and operations. Some of the issues that were raised in the testimony are obviously key: the integrity of the Customs Service, the way that we handle and treat passengers.

We all know that very often the first face that our citizens see when they come into the United States or visitors see when they come into the United States is the official face of government in the form of the Customs inspector.

We all know that everyone coming to these shores, whether citizen or no, expects to be treated fairly, and should be treated fairly. We uphold that ideal and we applaud Commissioner Kelly's efforts to make sure that that ideal is enforced.

For its part, the Office of Enforcement supports Customs and its mission in a variety of forms, two of which are policy guidance and operational oversight. By enhancing both, we hope to ensure that Customs performs its mission as safely, professionally, and effectively as possible. I would refer the committee to my written statement for more detail of the functions of the Office of Enforcement.

One thing I would like to focus on, in part, is the Office of Professional Responsibility, which is a recent addition to the Office of Enforcement. Shortly after Commissioner Kelly was confirmed as Undersecretary, through the work of the appropriators and also his work with the Congress, the Office of Professional Responsibility was formed within the Office of Enforcement.

This office has many functions, one of which it was tasked to do was to oversee and take a top-to-bottom look at the integrity functions within the Customs Service.

OPR undertook this review at the direction of then-Undersecretary Kelly, and completed that work after he left office, but continued to benefit from his continued guidance and influence on this process.

Many of the changes that were recommended in the final report were changes that actually Undersecretary Kelly, then Commissioner of Customs, started because he knew the issues, he had spotted them before, and he set them in motion. But it is through this mechanism within the Office of Enforcement that we seek to support and work with our bureaus.

One issue that I know that this committee is very much interested in is Customs' performance overall. It has been noted very often that Customs has a decidedly complex mission, that it is being asked to do more and more over time to deal with a larger, increasing volume of trade with resources that are tight.

One of the tools that has been used and has been employed at the Treasury Department overall is a strategic management process to assist our bureaus—all of our bureaus—in becoming as effective as possible.

In the formulation of the Treasury Department's strategic plan, the Secretary, the Deputy Secretary, and the Under Secretary of Enforcement, as well as the Office of Management were personally involved in the development of Treasury's fiscal year 1997 through 2002 strategic plan.

Working closely with the Office of Management and Treasury's law enforcement bureaus, the Office of Enforcement evaluated the missions and unique characteristics of our bureaus and formulated broad policy goals for the department's law enforcement mission.

Based on the Secretary's guidance in June of 1997, Enforcement, working together with Customs and Management, established priorities for Customs to prevent drugs from entering the country and ensure the highest percentage of compliance with tariff and trade laws.

Customs, as well as the other bureaus, then developed strategic plans which were reviewed, refined, and approved by the department. This was a collaborative effort, and it continues today.

The strategic plans provide direction for the budget formulation process and lay the foundation for performance plan. Beginning in fiscal year 1997, Treasury defined performance goals for each budget activity and integrated into our budget justification the proposed performance plan for the budget year, and a final performance plan for the current year.

Thus, budget justification documents request resources under each budget activity and are linked to their respective performance goals and supporting performance measures.

In addition to this process, Enforcement is working to coordinate law enforcement measures with other agencies. During 1998, the Offices of Enforcement and Management jointly created the Law Enforcement Performance Measures Working Group to formalize the intra-agency coordination of law enforcement measures.

While there is much to be done in this area, particularly in the area of law enforcement performance measures, there have been successes. Customs worked with the Department of Agriculture and the Immigration and Naturalization Service to develop the inter-agency goal of clearing international air passengers in 30 minutes or less, while improving enforcement and regulatory processing. This is an ongoing and evolving process.

As the committee is aware, the performance measurement process throughout the entire government, not just the Treasury, is evolving. We are making a concerted effort to measure and assess bureau performance in a proactive manner that is linked to resource allocation.

Equally important, we are striving to assure that presentation of key measures that will reflect performance results rather than the traditional output-oriented or workload measures are put in place. We share the committee's goal of ensuring that we have the right measures and that we incorporate them into the budget process.

As the performance measurement system evolves, we continue to assess how accurately the measures in question reflect organizational effectiveness. Currently, many of the measures judge success only as meeting a precise numeric goal, without reference to how close a bureau comes to actually achieving that goal.

Thus, in fiscal year 1998, Treasury law enforcement bureaus achieved approximately 63 percent of their 115 total performance targets. For its part, the Customs Service met approximately 46 percent of its 48 performance targets for fiscal year 1998.

But if one includes those measures where the Treasury law enforcement bureaus' performance was at least 90 percent, 83 percent of the measures were met. For Customs, in particular, their performance was at 79 percent. I would submit that that is a more appropriate lens through which to examine Customs' performance.

We are reviewing these results to determine how we can work with Customs, and work with all of our bureaus, to enhance overall performance, but make sure as well that we determine that the measures that have been set are appropriate and they accurately reflect program results.

To this end, enforcement has worked with management and Customs to refine targets for fiscal year 2000. As this process continues, we expect to make further improvements in future presentations, but we hope to benefit tremendously from the insights of this committee as we go through this very complicated and, in certain respects unprecedented, process, particularly in the law enforcement area.

As the amount and quality of performance data grows more robust, we will continue to formulate budget proposals to Treasury based on concerns about gaps in performance. In many cases, demand-driven work load may be challenging our capacity to achieve acceptable results.

Despite a tremendous increase in its responsibilities, Customs is making, in my view, the best possible effort to achieve its goal. Automation is critical—critical—to Customs' ability to enhance its efficiency and continue to meet the standards that it sets for itself. That is the principal reason why the ACE initiative is so vital.

There may be other cases that also may justify resource enhancements as we develop future budgets for sensible investments in technology that improve productivity while also improving quality. We are, of course, committed to working closely with this committee as we make these assessments.

In summary, Mr. Chairman, the Treasury Department is proud, and I am personally proud, of the contributions that the men and

women of the U.S. Customs Service have made in the past, and continue to make each and every day to this Nation.

Treasury and Customs have defined goals and objectives to ensure excellence in protecting our borders, in defeating financial crimes, and facilitating international commerce and passenger service.

Increasingly realistic strategies and goals, effective law enforcement and compliance, and a commitment to work in partnership with the regulated commercial community toward modernization will enable Customs to make great strides in meeting current challenges and to begin preparations for the daunting challenges facing all of us in the 21st century.

Thank you, Mr. Chairman. I would be pleased to answer any questions that the committee has.

[The prepared statement of Secretary Johnson appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Secretary.

Mr. Commissioner, as I mentioned in my opening remarks, we are very concerned about the recent failures in the system that processed imports. I recognize that part of the problem is the significant growth of trade and what that means to your agency.

I would be interested in knowing what specific steps you are taking to maintain so that trade is not disrupted further. If I might just follow through, because I assume that growth and complexity of trade is going to continue in the years ahead. So if you look down the road in the next 5, 10 years, what are we doing to be able to address those problems then? You have got a tough job, Mr. Kelly.

Commissioner KELLY. Mr. Chairman, you are absolutely right. We are projecting that the value of imports will essentially double by the year 2005 and reach $1.8 trillion. So, we do have a daunting task.

What we are doing now is focusing on our automated commercial system, our current system, to keep it going. Life support, we call it. We have $32 million in recurring funds. We are requesting, through the President's budget, another $35 million. We believe we need some more and we are looking at alternatives to that.

But, clearly, that is our number-one objective now, is to keep the ACS system up and running. I think we have some talented people. We have a first-rate chief information officer, who came aboard a little over a year ago and has the respect of his community, certainly, and my respect. But we see that as the primary mission.

Even so, we clearly need a new system. This system, the ACS system, has been in existence for 16 years. It uses software that was designed in 1978. It speaks an archaic computer language, COBOL, and it does not enable us to do business the way the trade is doing business.

You mentioned in your opening comments just-in-time inventory. We want to be flexible, we want to be compatible, with America's business so we can continue to enjoy this tremendous boon of prosperity in imports. We need the Automated Commerce Environment, we are convinced, to carry forward.

You mentioned the Mod Act. The Mod Act was passed in 1993. We have moved forward as best we can with the roughly 32 rec-

ommendations that were encompassed in the Mod Act. However, there are seven of them that rely on technology that we simply do not have, and will not have unless we get the ACE system up and running.

We have prototypes addressing some of the issues such as reconciliation and such as remote location filing, but they are really significantly constrained. We will not be able to carry out the spirit and the direction of the Mod Act until we move to the new system.

The CHAIRMAN. I cannot emphasize how important I think not only catching up for what the challenges of today are, but I really think this whole situation is going to become increasingly complex and difficult. Hopefully, trade is going to expand significantly.

This raises a question of revenue. In fiscal year 2000, funding for 28 percent of Customs' position and the development of the automation upgrade is dependent on revenues from proposed user taxes.

Do you have any contingencies in the likely event that these tax proposals are not enacted? You may want Ms. Killefer to help out on this, but I would be interested in your comments.

Commissioner KELLY. Well, that amount of money, $312 million, translates into a little less than 5,000 FTE for the Customs Service. So it would impact drastically on our operations. We would have to look at a reduction in force. It would mean closing of ports, or certainly limiting times that ports are open. So it would be a very traumatic blow to the service that we are currently providing.

The CHAIRMAN. Do you have any comment, Ms. Killefer?

Ms. KILLEFER. No. I would only echo Mr. Kelly, that we believe that the current program levels that are in the President's budget are absolutely necessary for Customs to continue to provide both its trade facilitation as well as its enforcement role.

We recognize that the fees are problematic. We have been talking to the Appropriations Committee to look for ways, indeed, to fund the program levels that we have submitted to Congress.

The CHAIRMAN. I am concerned because, in a sense, the answer sounds like we either raise taxes or close down.

Ms. KILLEFER. I think you recognize, as I think everyone does, that dealing under the current budget caps is very difficult for all agencies. I think, in particular, Treasury, that performs very basic functions throughout all of its bureaus, be it Customs at the borders, IRS in collecting revenue, FMS in printing the checks that deliver Social Security, we are finding it very difficult under a constrained environment to actually deliver the level of service that we think the American public deserves.

The CHAIRMAN. Well, I would just urge, Commissioner Kelly and Mr. Secretary, that consideration be given to how we can address this problem. I would not necessarily count on a tax increase.

Customs' budget has lagged, not only those of justice and law enforcement units, but also those of other Treasury units in terms of real, and even nominal, growth.

What explains this situation and what does the Treasury propose to do to ensure that Customs receives the resources it needs to carry out its admittedly very complex mission? Why has it been short while others have gotten more?

Ms. KILLEFER. I cannot comment on a 5-year period. I can comment on most recent history, where we have looked carefully at each bureau's requirements with the intention and the hope of funding each one of them.

I do not believe they actually have been unfairly disadvantaged. We have a couple of situations, if you go through the budget in detail, where we have requirements, for instance, in the case of the Secret Service budget in 2000, there is a bump-up in funding for the 2000 candidate nominee program. It is a blip in funding that happens every 4 years for them.

In the case of a bureau like IRS, which you as a committee are very familiar with, their funding is essentially flat for 2000. When you include in the year 2000, they stay absolutely flat. We are now taking the funds required for year 2000 funding into their base budget, where last year the appropriators took it out of emergency funds.

So we faced an enormously constrained environment. I do not believe that Customs was disadvantaged relative to other bureaus at Treasury. I would add that, if we had more funding available to us, we could certainly use it. There is absolutely no question that we would like to enhance both our staffing at border crossings, our investment in the facilities, as well as our investments in technology for Customs.

The CHAIRMAN. I will ask one more question, then I will turn to you, Pat.

Commissioner Kelly, Customs has faced continued problems with documented personnel incompetence, misconduct, and corruption, but apparently has had very difficult problems solving this.

Could you tell me what you propose, or are doing, to solve these problems and what additional tools, if any, you need to help you solve them?

Commissioner KELLY. We did an organizational assessment survey last year. Basically, it showed that Customs employees are happy working for Customs, but they had a sense that the agency was unfair: unfair in promotions, unfair in hires as far as local hires are concerned, unfair in discipline.

We have set about to correct, in some cases the reality, and the perception of that problem. We have put in place, for instance, an agency-wide discipline review board to make discipline more consistent throughout the agency. You could commit an offense on the west coast and get no penalty at all, and commit the same offense on the east coast and receive a relatively harsh penalty.

There was no agency-wide record keeping of a lot of the disciplinary actions that were taken. Many of them were insufficient, but even those that were taken were not recorded. So, there was no vetting of individuals who were being promoted or being transferred.

We have pulled up the authority to the Assistant Commissioners as far as hirings and promotions are concerned because there were numerous allegations of unfairness, as I say, in this area.

As I mentioned in my opening remarks, the Internal Affairs operation was greatly wanting. It was not well led, not well organized. There was internal friction with other parts of the organization.

We brought in a top-flight leader for that organization, Mr. William Keefer, former U.S. Attorney, Acting U.S. Attorney for the Southern District of Florida, and 10 years in the Public Integrity Section of the Justice Department.

We have begun to rotate internal investigators from our Office of Internal Affairs to Office of Investigation. A total of 80 transfers are being effected.

We have put in a new system to collect allegations and to follow up on allegations. What was happening in the past, is that an allegation of wrongdoing would come in, it would be referred to management, and there would be no record of it so it just literally fell through the cracks. We cannot find dispositions on some of these cases.

We put in a whistle-blower unit that reports directly to me in my office to let employees know that they can come forward and can be protected and will not be the subject of retaliation.

We have put in much clearer lines of accountability and responsibility, clearly delineating to managers what they are responsible for. At one time, there were 301 ports of entry reporting to one position in headquarters. Now, that is just an unacceptable span of control.

It makes it extremely difficult for whoever the Commissioner is to put policy in place, have policy go down through the organization, and get reasonable feedback as to what is going on. We have now strengthened and clearly delineated, as I say, the next line of management's responsibilities.

All in all, I think we have come a long way in putting the organization on track. A lot more work needs to be done. I think the responsibility and accountability should be, and I accept that it should be, at the commissioner's level. That is the person ultimately held accountable.

At some time in the near future if I am deemed not to be doing an appropriate job, then fine, a new commissioner should come in. But I think attempts in the past to flatten the organization have left the lines of authority murky, and people were not aware sufficiently as to what their responsibilities are.

Now, they are, or should be, clearly aware of what they are responsible for and what they are going to be held accountable for.

The CHAIRMAN. Senator Moynihan?

Senator MOYNIHAN. Thank you, Mr. Chairman. If you will not mind, I am going to suggest a slightly different tack here. Undersecretary Johnson, you referred to the law enforcement mission of the Customs Service. Well, yes, there is that. But, basically, you raise revenue for the Federal Government.

Commissioner Kelly, as former commissioner of the New York City Police Department, and you, Under Secretary Johnson, were Deputy Assistant U.S. Attorney in the Criminal Division in the Southern District of New York, I am not worried about your keeping a clean outfit. That is what you are good at, what you are renowned for. It is the trade that matters.

I mean, up until the early part of this century, the majority of the revenue of the Federal Government came from Customs, most of it collected at the Port of New York. You are a very old institution. Alexander Hamilton commissioned those revenue cutters, I

think, in 1794 to get money. You have had some very distinguished employees. That is not necessarily widely known. Herman Melville was a Customs clerk for years and years in Manhattan.

You are bringing in revenues of $22 billion a year. We no longer look to you for revenue, we look to you for facilitating trade. So, you have had a shift in a two-century institutional culture. We want trade to move quickly.

If you have COBOL systems, they are very much in demand around the world. The Russians could use those fellows a lot. Their missiles are on COBOL and there is nobody around who knows COBOL anymore.

But did I not hear you, Commissioner, say that you were going to need some revenue to put in place the recommendations that you have developed on your own, and those from GAO, and we are going to have to find it for you?

I hate to put it to you this way, Mr. Chairman, but I think we ought to hear what the Commissioner says, or thinks. And you, Mr. Secretary, and Secretary Killefer.

Commissioner KELLY. Well, clearly, we need money, a lot of money, to put in the Automated Commercial system. That will go a long way to facilitating the great growth of trade that we anticipate. The money that has been estimated we need is $1.4 billion. That is a rough estimate. Our method of arriving at that number has been determined to be reasonable by an outside consultant, Peat, Marwick.

Senator MOYNIHAN. Well, that is not a lot of money in the world trading system that we know. You are putting in a 10-year system, as it were. It will last about 10 years?

Commissioner KELLY. We would like to put it in in a 4-year time frame.

Senator MOYNIHAN. And have it last another 10, or so.

Commissioner KELLY. Right.

Senator MOYNIHAN. Which is about what banks and Chrysler and other commercial activities do. They roll this over. You need it now. Do not hesitate to say it. You are not going to have another opportunity to come over here and be asked if you need a tax increase.

Commissioner KELLY. We clearly need it as soon as possible. There is, at this juncture, no money in the 2000 budget. There is a proposal for an access fee that would be made available in fiscal year 2001.

Senator MOYNIHAN. So you are not in the 2000 budget. Then we are going to be holding a hearing in 2003 asking why you have not done this and that. I do not think it is fair. I mean, you are a recognizable organization that has needs that turn over very quickly in response to product.

To spend all of your time on body searches—if you would like to know, if I can just say a memorial to the effectiveness of closing your borders to undesirable products, there is the Seagram's building on Park Avenue. It is about as large and elegant a structure as you will find. It all came from whiskey smuggled across Lake Ontario. [Laughter.] Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Senator Grassley?

Senator GRASSLEY. What I am going to say, first of all, to each of you at the table, when we talk about spending more money on upgrading computer systems, just make sure that you do not do it the way IRS did earlier this decade, when we gave them $4 billion to upgrade their computer system, and 90 percent of it was wasted.

So, whatever you need to do, and if you get the money, do not make that mistake. Look to them for an example of how not to do it.

I would like to bring closure to the issue that Senator Roth brought up, continued by Senator Moynihan. That is about the money that is needed, and asked for. And this is not to denigrate anything you folks said, but I think, to lay out on the table that there is a problem here that has not been created by any of you, yet somehow we are dancing around the bigger problem at the highest levels of this administration when it comes to playing games with the budget.

That is that there were $300 million asked for in the Customs' budget, and OMB and the White House forced Customs to take the $300 million out and use it elsewhere. I think we ought to find out where that $300 million is used elsewhere, but then come back with $300 million of a new user's fee to have this money in the budget. So the game that is being played here is, this administration decided way last fall that they could not break the budget caps. But there is a way around the budget caps, and that is, raise taxes. That is what has been done here.

think the more candid way for the administration to do it, is if they needed to spend more money than what the budget caps had allowed spending, then to just come forth and do it instead of playing this game of taking $300 million away from what Mr. Kelly feels he needed and spend it someplace else, and where we do not know, and then raise the user's fees or raise taxes by $300 million to accomplish the same thing and to get around the budget caps.

My first question is unrelated to my first two comments, but directly to the work that you have to do, Mr. Kelly. It involves my being worried about how effectively the government is able to track and monitor end-use verification of sensitive dual-use technology that we ship to China. I know that the Department of Commerce has jurisdiction over export controls, but Customs has a lot of expertise in this area.

How good is our inter-agency coordination in the vital area that clearly affects our National security?

Commissioner KELLY. We are involved in some investigations now with other agencies. I think cooperation is all right. It probably could be better.It is always an issue in the Federal Government when agencies get together.

We are sensitive to the issue. You may have read about a case that broke about 2 months ago in Boston. Customs has a program where our strategic weapons investigators go around to companies that deal in dual-use or deal in defense-type items, and tell them that we are in existence and, if anybody approaches you, to notify us. What happened is, an individual, who is a Chinese American, came forward to a company and tried to purchase fiberoptic gyroscopes.

His request for a license from the State Department was rejected. About a year later, someone else approached the same company. In the interim, we had notified that company that Customs is concerned about this issue.

In fact, he tried to do it in a clandestine way, tried to purchase these items. Customs set up a dummy corporation and arrested this individual for violations of the Weapons Control Act. It is the type of investigation, type of vigilance, that we are involved in. It is difficult to get a handle on just how much of that is ongoing.

Senator GRASSLEY. Can I use your benchmark, where you said that cooperation could maybe be a little better, and measure against that statement the specific question I was asking about China and the sensitive material that we have sent to China? Was the cooperation less in that instance than normally?

Commissioner KELLY. No. We did not send anything in the first approach. That license was rejected. In the second approach made by a different individual, but who had connections with the first, we had cooperation and we ultimately made an arrest.

Senator GRASSLEY. Thank you, Mr. Chairman.

The CHAIRMAN. I would make the observation that, a far as the so-called user fee, I think it is really, technically, a tax.

Senator GRASSLEY. Yes. I agree with you.

Senator GRAMM. It has been proposed many, many times and we rejected it, solidly, on a bipartisan basis over, and over, and over.

Senator GRASSLEY. It is a basis of where the White House can have its cake and eat it, too.

The CHAIRMAN. With that, we will call on Senator Graham.

Senator GRAHAM. Thank you, Mr. Chairman.

I would just like to observe that there are other ways in which one can have their cake and eat it too, and we are about to experience one of those probably in the next few hours, if not days.

That is, by declaring what previously had been thought of as regular appropriations emergencies and financing them without having to have an offset on the spending of the revenue side, and having our grandchildren pay it by reducing the Social Security trust fund.

So we all have our own creative ways to eat our cake and try to have it, too. Unfortunately, that option is not available to our grandchildren, because they will end up paying for it.

Let me go back to the ACE system. I recognize the controversy that has broken out between those proposing the method of funding it and the users who are resisting that proposal.

What would be the enhanced benefits that the ACE program will provide to the importing community? How will things be different for the users with this system than with the status quo? What is the anticipated impact on international trade if ACE is further delayed or if it is not deployed?

Absent the proposed user fees, what alternative funding mechanism will be available to develop and deploy ACE? You indicated that there has been some discussion with the appropriations committees. If we do not act, do we have some expectation that there will be a sustained and adequate funding base to proceed with this initiative?

Commissioner KELLY. Well, the major benefit of ACE is compatibility with how business conducts itself these days. Under the Mod Act of 1993, there is a shared responsibility between Customs and the trade community. A lot more responsibility has been put on the trade, but the obligation on Customs is to have informed compliance. In other words, to give information to the trade as to how they can comply. ACE would allow the trade to have a lot more information and be able to do a lot more things.

One of the issues you mentioned before was remote location filing, where you can file an entry from anywhere in the country. You cannot do that now. We have a stovepipe system, where it is basically a port-by-port system. You cannot get into that system for security reasons.

It will enable reconciliation. You do not know what is in every shipment that comes in. Reconciliation will enable companies at the end of the year, or within 15 months, to be able to reconcile, to pay what is owed, or to get reimbursement.

That is the way the world does business. We do business now transaction by transaction. It will enable account management for us. We will be able to look at business as an entity rather than a series of transactions.

Of course, it gives us more capacity, which is something that is fundamental, but very, very important. It just is, I think, the smart way to do business. We just should not be buying more memory. Everyone I speak to—and certainly, I am a newcomer to this field—in the trade thinks that this is the only way for us to do business.

You mentioned, Senator, the funding. I am not aware of any alternative funding mechanisms that have been proposed for ACE.

Senator GRAHAM. So are you saying that if the Congress, therefore, does not vote for this tax/user fee, that the system will stagnate?

Commissioner KELLY. Well, unless we get funding, if there is some other source. The fee that is proposed would allow for the collection of an access fee to the system during fiscal year 2000, and then that would translate into $150 million in fiscal year 2001. That is the proposal.

If we had our druthers, of course, we would have more money and we would have it right away, roughly, $250 million a year. We believe that ACE should be constructed in a 4-year time frame rather than a 7-year time frame, although it is a little cheaper in the long run to do it in 7 years.

We are concerned about the viability of the ACS system, the current system, over that period of time. Of course, technology changes so much, that if you stretch it out to 7 years, you will be kind of chasing your tail and coming around again with more problems.

Senator GRAHAM. If I could, with just limited seconds left, one alternative proposal has been an increase in the merchandise processing fee which is charged on all imports.

Would that be an acceptable alternative to the fee on electronic communications?

Commissioner KELLY. Well, it is my understanding that the merchandise processing fee has to be related to the level of service that

it buys. I think, of course, we already have a merchandise processing fee now that translates into about $900 million a year. So, I think there may be some issues there if you increase the merchandise processing fee.

Senator GRAHAM. Thank you, Mr. Chairman.

The CHAIRMAN. Next, is Senator Gramm.

Senator GRAMM. Mr. Chairman, thank you. I get plenty of opportunities to talk to Commissioner Kelly. Let me say, we have an excellent working relationship and I appreciate the good job you are doing.

I want to go back to Senator Moynihan's point. I think the incredible thing in this whole debate is, we are probably funding Customs at about a third of the level that we should be funding it, given the fundamental service it provides and given how critical that service is to the general prosperity of the Nation.

We have an exploding level of world trade. We know that our level of exports and imports are going to explode in the next decade, and we are counting on it. Yet, we are operating a computer system that is so bad, so antiquated, that when Congress mandated what seemed to be a reasonable proposal, that we keep up with people who come into and leave the United States, something that would be trivial given the capacity of Mastercard or Visa, we not only were unable to do it, but we were so incapable of doing it that Congress is in the process of delaying it, eliminating it. Yet, we have no funds to replace that computer system.

You just mentioned a user fee where you collect $900 million from that fee. What are Customs' collections now, $23 billion or something?

Commissioner KELLY. $22 billion, I believe.

Senator GRAMM. Yet, we do not have the resources we need to modernize our computer. We passed in this committee last year the Drug-Free Borders Act, which is really an act trying to give you money to promote the flow of legitimate commerce, given the burden on your budget from other sources. That bill passed the House and Senate. We had a problem with a labor issue dispute and it did not become law.

But it is an authorization bill, not appropriation. I would just like to say on this user fee, the bottom line is, whether it is a good idea, whether it is a bad idea—I happen to think it is a bad idea—the administration, from the very beginning, has made this or similar proposals. It is clear that the Congress is not going to adopt this fee. Nobody believes they are going to adopt this fee.

But what this enables the administration to do, is to deny you money without admitting it. It is part of this budget which has reached a new level of phoneyness, in my opinion, to almost across the board. It is shameful.

I would just like to say, Mr. Chairman, it seems to me that something is wrong when we have an agency that is generating billions of dollars of revenue that is absolutely essential to the economic prosperity of the country, and we cannot compete for available funding to fund that agency and give them the people and the technology they need.

There must be 500 programs in the Federal budget that get an increase in funding this year. I would have to believe that at least 450 of them would have less merit, a weaker claim, than Customs.

So I think we need to find a way to claim some of this revenue that Customs is collecting. We need to fund this computer this year, not debate it next year. We should have done this 10 years ago. We could use twice as many Customs agents as we have.

I will just give you a little example of the problem. Twenty years ago, it was not uncommon for people in my State to go to Laredo, spend the night, go over to Nuevo Laredo, eat, shop, come back across the border. The plain truth is, it looks like there is this border along the southern region of the country. You draw a line on it, and there is a little river there.

But the truth is, those cities are pretty integrated economically—or used to be. Now, you go across to Laredo to Nuevo Laredo and you get behind miles of truck traffic, you may never get back. [Laughter.] It is sort of like the old guy from the 1950's song about "waiting to get a pass on the MTA."

So this has had a devastating impact on these communities and it has destroyed commerce on both sides of the border. We are going to reach a point where we are going to begin to affect the prosperity level of this country if we do not deal with this problem. And $1 billion is a lot of money, but the plain truth is, in a budget of $1.7 trillion, we are talking about a relatively small amount of money for a function that no person has ever argued is not a government function.

I mean, this is not like we are debating Americorps, where we are paying people to volunteer, or something like that. If government does not have this function, it has no function.

We just need to find a way to come up with this money. I think it is very important, and we need to take it away from something else. If we have got to take all these entitlements under our jurisdiction and cut one of them to fund this, we ought to do it because we are going to hurt people a lot more by not funding it than we are taking money away from some exploding program to make it happen.

Thank you, Mr. Chairman.

The CHAIRMAN. Next, is Senator Kerrey.

Senator KERREY. Well, first of all, Commissioner Kelly, I appreciate very much your testimony and your service. I do not think there is any disagreement from this committee that you need to be provided the resources to be able to do what you have to do. I agree with what both Senator Moynihan and Senator Gramm have said, that Customs is a vital service.

I pledge to work, although it is not directly impacting upon a State like Nebraska. We do not have any Customs people checking people when they come across Kansas into Nebraska. So, I do not have any clever story to tell like Senator Gramm did. That was Charlie on the MTA, by the way, that could not get his sandwich. [Laughter.]

But, nonetheless, indirectly, it affects us. This is a vital government service. There is debate in lots of other areas. I just pledge myself to work with Senator Moynihan, Senator Graham, and Sen-

ator Gramm, Senator Roth, and others. We need to find a way to fund this, and we are not going to have a tax increase.

The Federal Government currently takes 20.5 percent of total U.S. income. We have not been that high since the Vietnam days or World War II. I mean, there is a limit to what we can take. Although we are not prohibited by it under law, I think the majority of us recognize that there is a limit, and I think we have reached it. So the question is, where do we get it?

I have got to tell you, I think that what we have to face immediately is this growing claim on income that we have from Americans who have served their country and done well who are over the age of 65 and who have a claim on Medicare, Social Security, and long-term care Medicaid.

The budget this year is $700 billion for those three programs alone, growing $40 billion from last year to this, and it is heading to be 100 percent of the budget. That is what is going on. We are turning our entire government into an ATM machine because we are unwilling to go, not just to people over the age of 65, but people under the age of 55 and say, we have got to reduce that claim. The claim is too big.

For another reason we need to do it, because what we are doing is we are saying to Americans, you are going to be more dependent on your government when you hit age 65, and we need to make them less dependent on the government.

So, I put that pitch out, that this problem is connected to the unwillingness of the President to say, I support premium support, or I support some change in the underlying law that will reduce this claim. Until we get that kind of leadership—and I think Congress needs to rally as well to it, everybody is terrified of it, and I understand it, for political reasons.

But that is the problem, the growing share of the budget that is going to a mandated program. So, I just pledge myself to work, Mr. Chairman, with you, Senator Moynihan, and Senators Graham and Gramm. I think we have got to fund this vital service one way or the other this year.

Commissioner Kelly, in the Restructuring and Reform Act of the IRS that we passed in 1998, we had a number of other things in that law that we put that increased the authority of the commissioner. We gave him personnel flexibilities under the law, we set a term and qualifications for the commissioner. At the IRS right now, he is doing a lot of personnel things as well. But people know that he is going to be around for a couple of years after the new administration gets in, so they do not just sit there and say, all we have to do is wait another year and wait him out. We have provisions in there for a more open budget process. We also had provisions in there for a board. As I say, I am not very impressed with the people that have been sent over thus far. I was hoping that we would get some real, strong manager that would be able to establish immediate credibility with the Congress. Now, maybe I do not know the individuals well enough. I just want to put that statement out as well.

But I ask you, are you familiar with these provisions? If you are, do you think this is something, in addition to fighting to try to make certain that we get you the resources necessary to do this

vital service, this is something we ought to also look at to increase the likelihood that you can manage to success?

Commissioner KELLY. I am generally familiar with the provisions. I think some of them are good and would be helpful. I think it would be particularly helpful to bring in people from industry, experienced managers who would stay for a relatively short period of time, three, 4 years, pay them at a rate that is higher than the going government rate, which Commissioner Rossotti is able to do.

At the other end of the spectrum, I would like to have Schedule B hiring authority, similar to what Secret Service has, that provides you with flexibility as to who you can hire as far as skills are concerned. It allows for a 3-year probationary period, and then people move into a civil service track, so people's rights are protected.

I think we need more SES positions in our organization. We have the lowest ratio of SES to workers that I am aware of. We have one SES for 300 employees, versus, for instance, FBI, DEA, and other agencies that have about 1 to 130. That would be helpful right now.

I think the issue of term for commissioner is a good one to discuss. I think there probably are people out there that say, well, people turn over, like temporary help, and somebody else will come along.

I think that is probably something that would be helpful as well. Not necessarily for me, but for future commissioners.

Senator KERREY. Well, I would just say, Mr. Chairman, Senator Moynihan, if you think these kinds of things are worthwhile, I would pledge, in addition, to working with you to try to find the resources so that Customs can do its job. I pledge to work with you on these changes as well if you think these kinds of authority, like with the IRS, would be helpful.

The CHAIRMAN. Thank you, Senator Kerrey.

Last, is Senator Baucus.

Senator BAUCUS. Thank you, Mr. Chairman.

Commissioner, as you know, we had a good, fruitful discussion yesterday and I very much appreciate your taking the time. Along with the drift of the conversation here, I, too, want to help you get what you need to do.

That is, the automation, address the integrity question, and have more authority, Schedule B authority that you mentioned, more SES people, and be able to have high-quality people, where necessary, to run, on a professional basis, a very large, complex organization. I think that will help you to address some of the integrity issues that are recurrent in Customs. So, I think you are going to have the support of this committee, very strong support, in doing all that.

One thing that struck me at a hearing yesterday on the subject of Medicare. One of the witnesses was talking about transferring private enterprise techniques and management techniques—the Druckers of the world, and so forth—to government.

She mentioned what they are trying to do in Rhode Island. It was basically the point that you need goals, defined goals, perhaps quantifiable goals, so everybody knows what the objective is, the mission is, in the organization.

That enables people lower down to be delegated more, trusted more. I am sure they will make a couple of mistakes, but at least they know what the plan is because everyone is working for the same one, two, or three goals rather than the agency working at cross purposes, not really knowing what the goals are. I suspect that when you get the Schedule B and other people that you will be able to do some of that.

In addition, I just want to emphasize the need for personnel along the border, particularly in the high plain States, in Montana and so forth. We have a lot of space out there. There are a lot of crossings, but the personnel are not there. They are closed down a lot. It is very frustrating. Both ways, particularly coming into the United States.

In addition to the border, because Montana is such a big State, lots of towns all around Montana, and general aviation is so important, that there are no Customs officers in a lot of our towns. They are not there full time, either. In fact, the number has been cut back in recent years.

We, as a State, are struggling as a small business State, to look out for the future. It is mid-tech, high-tech, small companies, and so forth. We just desperately need to have people there, officials there, at those airports so that, when a business person comes in, he or she can be able to go through Customs and not have to not go because of knowing there is nobody there, et cetera. I just strongly urge you to look at that. We did discuss this previously.

Commissioner KELLY. Certainly. We will do that.

Senator BAUCUS. You are off doing a great job, and we are here to help you do what you need to do.

Commissioner KELLY. Thank you, sir.

Senator BAUCUS. Thank you, Mr. Chairman.

The CHAIRMAN. Well, thank you for being here today. We look forward to continuing this dialogue and working with you.

It is now my pleasure to welcome our second panel. Kevin Smith is the director of Customs Administration for General Motors Corporation. Representing the Vastera Corporation are George Bardos, the executive vice president, and Ty Bordner, the director of Application Consulting. We also have with us today Randy Hite, the associate director of Governmentwide Defense Information Systems of the GAO.

As I said earlier, the full statements of each witness will be included as if read. We would ask you to keep your comments to 5 minutes.

Mr. Hite, would you please begin?

STATEMENT OF RANDOLPH C. HITE, ASSOCIATE DIRECTOR, GOVERNMENTWIDE AND DEFENSE INFORMATION SYSTEMS, ACCOUNTING AND INFORMATION MANAGEMENT DIVISION, U.S. GENERAL ACCOUNTING OFFICE, WASHINGTON, DC

Mr. HITE. Thank you, Mr. Chairman, for the opportunity to appear before the committee today. As you requested, my testimony will focus on Customs' management of ACE. It is based on our recent report, in which we laid out a series of recommendations to address technical and management weaknesses with that program.

It also includes information on Customs' actions to date to implement our recommendations.

Before summarizing my statement, I would like to make two points. First, the need to leverage information technology to modernize the way that Customs handles its import processing function is undeniable. I have seen firsthand the outdated import processes that Customs currently relies on. It is transaction-based, paper-laden, error-prone, and it is out of step with the just-in-time inventory practices of the trade.

Second, Customs has concurred with our findings concerning ACE and it has moved aggressively to implement our recommendations. We are very encouraged by this. I would like to take the opportunity to compliment Commissioner Kelly and Customs CIO Woody Hall for their efforts to date in this regard.

Having said this, I would add that many of the actions taken to date, while in my view appropriate given the time that has elapsed since we have made these recommendations, are nevertheless first steps and much remains to be accomplished.

It was mentioned earlier that we do not want to repeat the IRS situation. I was involved in our work on the IRS modernization. There were a lot of parallels between where Customs was, and is, on its modernization and the problems we found at IRS.

I will now summarize the three categories of ACE weaknesses that are discussed in my written statement and our position on Customs' efforts to date to address them.

The first weakness: Customs had not been building ACE within the context of a complete enterprise systems architecture. In lay terms, an architecture is a blueprint of an organization's future business and system's environment.

Over the years, our work has shown that, without enterprise architectures, incompatible systems are produced that require additional time and resources to interconnect and maintain, and that an organization's mission performance is suboptimized. In response to recommendations that we made last year on this subject, Customs has made good progress.

Based on a briefing and a demonstration that I received 2 days ago, it appears that Customs has fully implemented our recommendations to complete its architecture, also to put in place the means for effectively maintaining the architecture and for enforcing it on projects like ACE.

The second weakness we reported on, was that Customs did not have a firm basis for knowing whether the ACE system solution that it was pursuing was the most cost-effective alternative.

Now, when investing in systems organizations should: 1) identifying and analyze alternative system solutions; 2) reliably forecast system return on investment, or ROI, and invest in the alternative providing the highest ROI; 3) manage large investments by breaking them into a series of increments and validating these increments one at a time. For ACE, Customs did not satisfy any of these requirements.

In response to our recommendations in this area, Customs reports that it has twice revised its cost estimate and it has redone its analysis of cost effectiveness, that it will perform cost benefit

and post-implementation analyses on system increments and it will have these analyses independently validated.

These initial steps are consistent with our recommendations. However, I cannot offer any opinion on either the revised cost estimates or the revised economic analysis at this time because Customs has told us that they are not ready yet to be shared with us.

The third weakness dealt with Customs' processes for developing and acquiring software. Those processes lacked rigor and discipline. One measure of such rigor and discipline, is the software engineering institutes, or SEIs, software maturity models.

Using GAO staff that had been trained by SEI, we evaluated Customs' software acquisition and development processes and found that they did not satisfy the Level 2 on a 5-scale level of SCI's model. As a result, Customs' processes in the areas of software engineering are, by definition, ineffective, immature, and at times, chaotic.

Senator MOYNIHAN. Mr. Hite, is 5 the highest and 1 the lowest?

Mr. HITE. Yes, sir.

Senator MOYNIHAN. Thank you.

Mr. HITE. In response to our recommendations, Customs has instituted an SCI Level 2 requirement for its software contractors. It has hired an FFRDC contractor to help it to, among other things, develop and implement plans for Customs to achieve SEI Level 2, and then Level 3, capability.

Then also to assist it in awarding and managing an ACE prime integration contractor which is similar to the model that the IRS is following on its modernization now. In my view, these are reasonable first steps to begin addressing our recommendations in this area.

In conclusion, successful systems modernizations is critical to Customs' ability to perform its import function in the 21st century. To be successful, Customs must do the right thing and it must do it the right way.

To be right, Customs must, as we have recommended, invest in and build systems within the context of an enterprise architecture, make informed, data-driven decisions about investment options based on reliable analyses of ROI for system increments, and build the increments using mature software processes.

Our work on other challenge modernization programs. I mentioned IRS. We have also done work at FAA on its air traffic control modernization, and at the National Weather Service on their modernization.

It shows that to do less increases the risk of delivering less-than-expected benefits and failing to meet cost and performance goals.

Now, neither of these things would be in the best interest of the trade or the government. To Customs' credit, it appears to have fully responded to our recommendation on architectural foundation for its modernization and, based on the initial steps——

The CHAIRMAN. The time is growing late, so I would ask you to summarize.

Mr. HITE. Yes, sir. Its initial steps to establish the investment management and software engineering maturity. It is headed down the right path in both of those areas.

This concludes my statement. I would be happy to answer any questions.

[The prepared statement of Mr. Hite appears in the appendix.]

The CHAIRMAN. Thank you.

Next, we will call on Mr. Bardos.

STATEMENT OF GEORGE BARDOS, EXECUTIVE VICE PRESIDENT, VASTERA, DULLES, VA, ACCOMPANIED BY TY BORDNER, DIRECTOR OF APPLICATION CONSULTING, VASTERA, DULLES, VA

Mr. BARDOS. Thank you, sir. I am here to talk about Customs, ACE, and our recommended position.

First of all, I just want to point out that Vastera is a software company and we write software that automates international trade logistics for importers and exporters around the world. We do have over 100 customers in the Fortune 100 category.

The automation of trade is extremely important to them. The software that we do provide is interface to Customs, ABI, ACS. These systems have been in place for a long time. They do work.

We are concerned, however, that the outages and the brown-outs are going to affect trade negatively, that our customers are going to have equipment held up and impacted because of that. I think everybody is aware of it. I think Mr. Kelly articulated that very well.

Our concern, is that 7 years to develop ACE is a long time. We do believe in ACE. We think it is well-designed. We do believe that Customs has done a good job and is capable of its development. We think, as I said, 7 years is too long. Even 4 years is too long. We should have had it in place.

So, we would like to encourage whatever it takes to accelerate that program. We think redesign is what is necessary, and not patching of an old system. There are some technical characteristics that we are here to discuss. Mr. Bordner will get into that. He is our development director. But we do think that the system needs updating, needs replacing, and it needs it as soon as possible.

Now, as far as the maturity model, we do believe in the principles of it, but we question whether, at this point, will it cause further delay if it has to be adopted?

Our recommendations are, because of the problems with ACS, it is going to put the businesses that we serve at risk. International trade is important to them and the borders are important. The facilitation that Customs provides has to continue.

We do think Customs has a good track record. ACE is sound. We do not want to see a lot of multiple releases because the cost every single time of a release puts a burden on us as software developers to implement the new releases, the recertifications that are required for every release, and so on.

But, in general, we do support it, we would like to see it accelerated, and we believe that Congress should fund the Customs' automation as recommended and required by the Customs officials.

Mr. Bordner is here to answer any questions or follow up on any information you like.

[The prepared statement of Mr. Bardos appears in the appendix.]

The CHAIRMAN. Thank you. I will now call on Mr. Smith.

STATEMENT OF KEVIN SMITH, DIRECTOR, CUSTOMS ADMINISTRATION, GENERAL MOTORS CORPORATION, DETROIT, MI

Mr. SMITH. Mr. Chairman, members of the committee, my name is Kevin Smith and I am the director of Customs Administration for General Motors Corporation.

In that capacity, I am responsible for ensuring that GM's import and export operations comply with all relevant Customs requirements in the United States.

I want to thank you for giving me the opportunity to be here today to share with you GM's views on the modernization of U.S. Customs.

Last year alone, GM filed close to 500,000 Customs entries, or about 2.5 percent of the total entries reported to Customs. Of those entries, 450,000 crossed the Canadian and Mexican land borders, with about 90 percent of those carried on trucks.

In the U.S., most of GM's Customs filings are made electronically. However, the current process is still unnecessarily cumbersome and subject to delays that can create unnecessary cost. The Customs entry process now in effect is based on practices established in the 1950's and 1960's, and systems put in place in the early 1980's.

Most U.S. Customs entries require the presentation of paper invoices to obtain the release of goods. These invoices are created from electronic data maintained by importers and shippers purely so that they can be handed to Customs officers and brokers, who then retype that information into other electronic systems. With practices such as this, it is understandable that the private sector would embrace the Customs Modernization Act of 1993.

The Mod Act, as it has become called, established the National Customs Automation Program to modernize U.S. Customs software and implement programs to enhance and streamline Customs' processes. These programs included importer activity summary statements, remote entry filing, and reconciliation of prior entries.

The Mod Act also stipulated that the Customs Service seek the participation of the private sector in the development of these new systems. However, the benefits of the Mod Act have not come without a cost. In return for the promised programs, much of the responsibilities, as well as the cost of Customs' commercial operations, was transferred to the private sector.

Unfortunately, a funding shortage has slowed the development of the promised systems, while the existing systems have become alarmingly unreliable. Last year, the current system, the Automated Commercial System, or ACS, suffered a number of interruptions, creating serious problems in the Nation's ports.

For GM, such delays can be extremely costly because they interrupt the flow of parts required in our just-in-time production systems. These missing parts can cause assembly line shut-downs, costly rework of our vehicles, and idling of our work force.

Although we have been disappointed generally with the pace at which the new Customs automated systems are being developed, we are impressed with the performance of a number of the prototypes that have been introduced to test future systems.

GM, Ford, and Dameler Chrysler are participating in one of these prototypes, a new automated Customs process for entering and releasing goods crossing U.S. land borders.

This new system is based on the use of electronic data used in our normal business processes. Although the prototype has required a considerable investment of us, both in time and money, we think that it has been a great success.

Currently, GM and Customs are processing over 2,000 shipments a week through the ports of Port Huron in Detroit, MI and Laredo, TX. In our opinion, the success of this prototype can be traced to the willingness of Customs to seek out the participation and support of the Customs users in developing these programs and the cooperative spirit that is involved as the project moved ahead.

Throughout the process, the Customs Service has used a disciplined managerial approach and worked closely with all those affected to make sure that the end product worked well, is user-friendly, and efficient to operate.

Our most immediate concern today is keeping the current ACS system running to prevent delays in our U.S. ports of entry. Unless the necessary funding is provided, we are at risk of a serious and prolonged failure of this system that could adversely impact many businesses and jobs.

We ask the support of the committee for the complete development of the next generation of Customs automation programs, including the full implementation of the National Customs Automation program.

In our view, this would require funding, including adequate appropriations in the fiscal year 2000 budget to support the continuation of the current prototypes and to fully implement the new system within 4 years.

General Motors opposes the establishment of new user fees as a source of funding. The private sector has already taken on many costly new responsibilities as a result of the Mod Act.

More importantly, we are already paying for the support of the operations of the U.S. Customs Service through the general taxes we pay, and, more specifically, importers are paying $800 million annually in merchandise processing fees, and over $20 billion in import duties.

Again, I would like to thank the committee for the opportunity of appearing here today, and I would be happy to answer any questions.

[The prepared statement of Mr. Smith appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Smith.

What would be the operational and cost impact on General Motors if Customs' current automated system were to be temporarily interrupted or shut down for long periods of time?

Mr. SMITH. In most of our assembly plants today, we carry less than 1 day's worth of inventory. If those systems were to be shut down for a prolonged period of time, literally within a day our assembly lines would stop, as would our production.

The CHAIRMAN. One day.

Mr. SMITH. Yes, sir.

The CHAIRMAN. Let me ask you, Mr. Hite. What needs to be done to ensure that Customs' response to GAO's concerns are effective and sustained?

Mr. HITE. A couple of thoughts in that regard. Hearings such as this, where the oversight committees exercise the oversight function, are very important. Another very positive step is the leadership of Customs and the role that they have taken in aggressively pursuing improvements in this area is very important.

I have seen cases where attempts to improve modernizations have not occurred because they lacked the executive involvement, executive leadership. That is not the case here in Customs.

Another item, would be a continued oversight role on the part of Treasury and OMB as part of whatever the annual funding mechanism that is set up for, funding the modernization to ensure that the appropriate questions are getting asked as they move through the modernization process.

The CHAIRMAN. Thank you, Mr. Hite.

Let me ask Mr. Bardos and Mr. Bordner. Could you explain the additional costs to members of the trade community to run concurrently two separate systems for up to 7 years?

Mr. BORDNER. Yes. Supporting two systems, I think, has a couple of fundamental costs to it. One, is the people required to support those systems. Salaries today of technical people to support those kinds of systems are very high. Getting the resources to do that is difficult in the software industry. The hardware costs to support multiple systems is also an additional cost. Perhaps the most difficult thing is managing the complexity of two systems at the same time.

Presumably, ACE would be released to add incremental functionality, whereas, some previous functionality would still be part of the ACS system. So, trying to manage both systems at the same time and that complexity is going to be a difficult thing to manage, both for software companies and the trade community as well.

The CHAIRMAN. Senator Moynihan?

Senator MOYNIHAN. I have a question which will appall our panel by its ignorance. At this time I would ask, what is a broker? They are part of this transaction system and I have never quite understood what they do. Mr. Smith, you mentioned them.

Mr. SMITH. Yes. Brokers are licensed by the Department of Treasury and the U.S. Customs Service to act on behalf of importers in transacting business. They clear goods on behalf of importers. They generally have offices in local ports where the importer may not have any staff, and they act as the importer's agents. They will collect duties on behalf of the importers and tender them to the Customs Service. They are a service provider.

Senator MOYNIHAN. They are a service provider. Is it a large community?

Mr. SMITH. There are lots of Customs house brokerage companies throughout the country. Some of them are very large organizations, and some of them operate in one port only.

Senator MOYNIHAN. Well, may I just say, and I hope the Chairman agrees, we have been getting such good reports about how Customs is doing and some urgent arguments about what needs,

still, to be done. I see Mr. Bardos agreeing, and Mr. Hite. It is so clear. Sir, it falls to you. You are Chairman. [Laughter.]

The CHAIRMAN. You have described the situation well. We will leave the record open for some additional questions to be submitted in writing. But, gentlemen, unfortunately, the hour is growing late. We do appreciate you being here.

Senator MOYNIHAN. And we have another panel.

The CHAIRMAN. And we have another panel. That is right. So, thank you very much for your very helpful testimony.

Senator MOYNIHAN. Thank you, indeed.

The CHAIRMAN. I would like to call up the third panel. Morgan Kinghorn is a partner of Price, Waterhouse, Coopers; Malcolm McLouth is the deputy executive director for Business Development at Canaveral Port Authority; James Phillips is the executive director of the Canadian-American Border Trade Alliance; and Sam Vale is the chair of the Border Trade Alliance.

Thank you all for joining us. We would ask that you do limit your testimony to 5 minutes. Your full statement will be included as if read.

We will begin with Mr. Kinghorn.

STATEMENT OF MORGAN KINGHORN, PARTNER, PRICE, WATERHOUSE, COOPERS, L.L.P., FAIRFAX, VA

Mr. KINGHORN. Thank you, Mr. Chairman.

My name is Morgan Kinghorn. I am a partner with Price, Waterhouse, Coopers. I am pleased to have the opportunity to discuss how the U.S. Customs Service is improving the linkage between performance and its resources.

Last year, the U.S. Customs Service partnered with us to develop a resource allocation model that would enable the Customs Service to improve the methods by which it allocates resources.

With the full participation of the Customs Commissioner and his leadership team, we demonstrated that it is possible to develop a model which can assist a large and diverse organization such as Customs in determining its resource requirements by location and by activity, and to do so on the basis of results.

The completion of the model met the objectives of the Commissioner, to establish a stronger strategic framework upon which to make improved resource decisions regarding the Customs Service.

In order to develop the model, the project team, composed of both PWC and Customs staff, met the following objectives: successfully integrated data from eight Customs data sources; we linked Customs' performance measurements to occupations actually performing those specific activities; developed analysis and performance measurement methodologies that can be reapplied in the future and can help the Commissioner and his team identify and avoid significant data issues; and we developed user-friendly what-if capabilities that can be applied to the analysis output.

PWC also worked with Customs personnel to attain corporate agreement on which current performance measures should be linked to each occupation, and the activities they perform. This allowed the team to create a new performance measurement analysis methodology.

This performance map, as we called it, details workload drivers, things that drive work load, workload assumptions, and the time data sources for all of Customs' core functions and core occupations.

It was also designed so that future data efforts can include a link between existing data and results, and potentially total threat data which can also have a significant impact on how Customs may want to apply their resources.

As in most organizations, performance data at Customs is contained in a number of different systems, often not well-integrated, because historically people only want to look at specific data for specific purposes.

PWC, and in particular the Commissioner, wanted the model in the new methodology to be used as a tool to assist in the establishment of corporate staffing information and to determine levels across functions, across occupations, and locations.

We wanted to do so using a consistent set of performance measures. The data for these measures is now integrated from eight different data sources and collect data from over 400 field locations.

The resource allocation model improves Customs' previous methods of allocating and justifying resources in several ways. First, it is a Customs-wide model, covering all of Customs locations and occupations. Second, it is based on an established and agreed upon key performance measurement. The models, therefore, allow for the use of a consistent set of assessments from year to year.

Finally, it was developed using input from both headquarters and field staff. It provides a unique answer to some difficult questions. Basically, how do I objectively justify the need for resources, particularly in a competitive environment? What are my resource needs if I need to increase the inspection times at a particular port, or group of ports, because of increased threat? And what happens to my resource requirements if I can improve my operations in terms of timeliness? What happens if I have increased demand across the board, or at a particular location?

The model still requires the use of professional judgment, the analysis of risk factors, and basic operational common sense. It is not intended as a tool simply to run and take results blindly without discussion and analysis. There are imitations, many of which are now being improved by Customs to be used in the future.

Mr. Chairman, that completes my statement. I would be pleased to answer any questions.

[The prepared statement of Mr. Kinghorn appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Kinghorn.

Next, Mr. Vale.

STATEMENT OF SAM F. VALE, CHAIR, BORDER TRADE ALLIANCE, RIO GRANDE CITY, TX

Mr. VALE. My name is Sam Vale. I am here to testify on behalf of the Border Trade Alliance. We are a grass roots organization that operates along primarily the southwest border, but we do have substantial new interests along the northern border.

We strongly endorse legislation that Senator Gramm has introduced, which is S. 658, which would fully fund Customs with addi-

tional positions to address many of the things that have already been brought up today.

More importantly, we feel that it does have some standards in it that have never been before, of 20-minute wait times, the requirement to make some reports back to the Congress on how they are using the funds and how they are handling themselves, which I think is a new component that has never been in authorization legislation before.

Since April of 1998, with the support of the Customs Service, the BTA and other Federal agencies have been meeting in open session to reach common ground on how we can best solve some of the problems at the border. We are looking at drug enforcement, waiting times, environment policies, infrastructure needs, as well as immigration policies. The types of agencies, to show you how difficult it is and why you need brokers and you need these other people that are involved in these discussions, are the U.S. Customs Service, Immigration and Naturalization Service, the Department of State, the Food and Drug Administration, the General Services Administration, the Drug Enforcement Administration, the Environmental Protection Agency, the Department of Agriculture. We even had the embassies of Mexico and Canada and representatives of four Governors. All of these people play a role in what happens at our borders, so it takes a tremendous amount of coordination.

The bottom line, Mr. Chairman, is the Customs needs a substantial increase in personnel and funding for the technology. Trucks have gone up, and all the statistics will show you, that the biggest bridges on the northern and southern border, the Ambassador Bridge in the North, Laredo in the south, had over 1 million trucks crossing last year. None of them expected those types of increases.

In San Ysidro, California, the largest non-commercial port on the southern border, on January 5, 1999, the average length of the line of vehicles waiting to cross the border was 85, and a wait time of 27 minutes. By the end of that month of January of 1999, you had 180 vehicles average waiting, with a 47-minute wait time. This is getting worse. On weekends, it is 180 and 61 minutes' wait time to cross the border.

That is why people do not want to go back and forth. Mexicans come over here and buy, and we go to Mexico. Canadians come, Americans go to Canada. We need to do something to increase the staffing levels, the way business is done. We need a new atmosphere, we need a new attitude, we need a new mentality.

I am the president of a company that owns and operates an international port of entry, and I am also a businessman, an importer and an exporter. I face, daily, the challenge of movement of legitimate commerce in the United States against an under-funded, under-staffed U.S. Customs Service. They are costing me money; I pay you less taxes as a result. That is what we should be looking at. We all make more profits, we pay more taxes, you have more money to do what you need to do.

Rail traffic is up by 115 percent, truck traffic from Mexico, 50 percent. We have companies in Mexico right now that are now no longer shipping by truck, they are shipping, by sea to the ports, perishables. That cost transportation jobs, that cost hotel jobs, that cost restaurant jobs, that cost mechanics.

These are foreign ships that are taking the stuff around to the east coast. We need to have the Customs Service doing its job so that we can keep the business and the jobs that we have along the southwest and the northern border of the United States.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Vale appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Vale.

Mr. McLouth?

STATEMENT OF MALCOLM E. McLOUTH, DEPUTY EXECUTIVE DIRECTOR FOR BUSINESS DEVELOPMENT, CANAVERAL PORT AUTHORITY, CAPE CANAVERAL, FL

Mr. MCLOUTH. Yes. I am Malcolm McLouth. I am deputy executive director of the Canaveral Port Authority. It is an honor to be here today.

Exceeding the 10 percent growth in international trade in the United States, Florida's cargo trade has already doubled this decade. Between 1990 and 1997, Florida's international trade increased by 110 percent.

Sea ports are responsible for approximately two-thirds of Florida's international trade. Containerized cargo increased 148 percent during this same time period, and we have provided our graphs explaining that.

Florida is also the world's busiest cruise port, along with cargoes expanding rapidly. In fiscal year 1999, U.S. Customs is expected to be available to clear and process approximately 4 million passengers and crew arriving from foreign destinations in Florida ports alone.

Depicted in the attached graph is the expected volume of passengers and crews for clearance that the three largest ports in Florida will be allowed to do. Clearance processing of both cargo and passengers is impacted by the available U.S. Customs staffing and support equipment.

I am most familiar with Port Canaveral and describe it as follows. Currently, U.S. Customs staff in the port consists of about 17 to 18 positions. In comparison, Miami has a staff of about 120 positions, with 75 being assigned to cruise operation. It is only through innovative scheduling and a dedicated Customs staff that Port Canaveral has been able to meet the challenges to date.

Port Authority staff is working closely with U.S. Customs during the design of highly efficient cruise terminals, and we also recognize that we have been required to take on, or Customs, additional responsibilities to meet the drug interdiction goals imposed by Congress.

Understandably, the port's rapid growth of cruise and cargo supporting requirements, being placed on a limited Customs staff, something has had to give, as follows. Due to the lack of personnel to cover both the debarkation of ships, crew, and passengers, Customs had to impose crew or support services windows.

The crew has about 30 minutes, from 7:00 to 8:00. The passengers get off at 8:00 to about 10:30. Then there is continuous monitoring by Customs of the crew until they leave around 5:00 p.m.

The Customs staff, due to its small size, has very limited flexibility to allow changes in these windows once adopted. Typical problems created for a cruise line is, a supplier or ship repair worker, for one reason or another, have been delayed and now they are forced to wait until the passengers are cleared and they may not get their work done.

By design, scheduling priority is given to the passenger over the crew to ensure that they are off in time to make connecting air transportation. But the crew needs also to do their shopping, telephone calls, postal, recreation, and so forth, so they need as much time as possible.

Three. A negative perception exists in the cruise industry that Canaveral Customs staff is tighter, more picky, and inflexible in their enforcement of basic Customs regulations.

Positive, is the fact that enforcement of Customs regulations at Canaveral is one of the reasons that we have done a good job on drug interdiction. Over on the negative side, the lack of operational flexibility with a ship's crew and staff, as compared with other major cruise ports, is entrenched in the minds of the cruise lines.

Four. The lack of staffing by Customs at Canaveral is a public relations disaster waiting to happen. The Customs staff already utilizes allowable time to the maximum when an inspector is ill-trained.

One of the problems that we would have, is Port Canaveral's growth in the past has been significant and can be expected to continue. Driving this expansion is the many new cruise ships under construction that are to be added in the Florida-based cruise ship industry and the maxxing out of the capacity in the two South Florida ports.

Customs' response to this information at Canaveral has been, in the case of Fast Ferries, which is due to start in June of 1999, is we just will not be able to handle it on a continuous basis because we do not have the overtime.

Or, in the case of Disney's second 2,200-passenger cruise ship coming in the next 90 days, the Disney Wonder, if we do not get more staff, we will only be able to handle two cruise ships at one time and the third will have to wait three or four hours. A three- or four-hour wait would be catastrophic for cruise ship operations. At the same time, keeping the crew on the ship would cause serious labor problems.

Customs does not even want to speculate what will happen when RCI Sovereign of the Seas, with its 350,000-a-year passenger and crew clearances arrives about a year from now.

Added to Canaveral's Customs workload is the fact that we recently completed a $9 million container facility to service all of Central Florida. In discussions with Customs, the immediate need for at least six new positions at Canaveral has been suggested.

We have been in close contact with U.S. Customs' management at all levels, and you could not ask for a better Customs staff. But they desperately need more personnel. We have recognized this serious funding problem, and I hear today that money is needed.

U.S. Customs encountered at the national level, due to the elimination of the COBRA funding for cruise ships which is a result of the NAFTA trade agreement, a $5 head tax fee for cruise pas-

sengers which was eliminated some 9 months ago, and we have been trying to get that rectified. After some 6 months of negotiations——

The CHAIRMAN. If you would summarize the rest, please.

Mr. MCLOUTH. I will. We strongly support the $1.75 per passenger user fee which was negotiated, and hope that the U.S. Senate proceeds with that. Thank you.

[The prepared statement of Mr. McLouth appears in the appendix.]

The CHAIRMAN. Thank you.

Mr. Phillips?

Senator MOYNIHAN. Mr. Chairman, may I welcome Mr. Phillips back to the committee. He was here about 6 months ago.

Mr. PHILLIPS. Yes, Senator. Thank you.

The CHAIRMAN. It is a pleasure to have you here.

STATEMENT OF JAMES B. PHILLIPS, EXECUTIVE DIRECTOR, CANADIAN-AMERICAN BORDER TRADE ALLIANCE, LEWISTON, NY

Mr. PHILLIPS. I appreciate having the opportunity to discuss U.S. Customs' northern border resource shortfall and trade facilitation needs. I ask that my full statement be put in the record.

Canada BTA is a binational, transcontinental organization. It represents 22 States and all of the Canadian provinces. Participants have among their individual memberships about 60,000 companies and organizations, and we are on the U.S.-Canada border to focus and to stay.

Workload demands on Customs from the $40 million an hour of binational trade that crosses are increasing substantially. Primary inspection. A head count deployed on the northern border continues at the 1980's level, less than 900 on a 5,500-mile border—the stretched, long, blue line, as I referred to before—compared to about 500 inspectors at JFK airport alone, just to set the perspective.

On the northern border, 65.2 percent of the trucks cross to the United States, 85 percent of the trains. Containers are increasing. Critical issue on enforcement as well. Drug interdiction on containers increased 33 percent in 1998 over 1997, and 44 percent in 1997 over 1996. A critical new need.

Drug seizures are up 19 percent on the northern border, 4,400 pounds, but the Commissioner mentioned something like 1.5 million pounds. So, the increase on the northern border is there. We do not want to be viewed as the weakest link. It is critical to keep our enforcement capabilities on the northern border.

One element is the Canada-U.S. accord on our shared borders, which is an absolutely essential binational initiative. It needs priority, it needs monitoring, to ensure it achieves its results. Bob Trotter has been recently appointed by the Commissioner as the first northern border ombudsman. We welcome that and look forward to a great increase in leadership.

Trade and tourism are critical to the U.S. economy and they are each doubling in double-digit increases annually, while inspection and facilitation resources at the borders are capped, particularly at the northern border, where one-half of the primary lanes at any

given time are closed or unused. Neither of U.S. Customs' dual import missions must be risked.

I came with four specific recommendations, which are in my written testimony, which I will quickly go over. Oversight and needs. It was mentioned earlier that Customs had not been economically disadvantaged. I just want to point out that Customs, for years, in their original budget submissions, have asked for the resources they need and they have not survived elimination.

I would submit to this committee that you ought to receive directly the original budget request so you can take a look and assess over the years what the unfilled needs really are from the line management as opposed to the budget.

Second, is airport pre-clearance. You are about to lose 26 COBRA positions at Canadian airports immediately now due to the removal, under the NAFTA provisions, of the fees. We need legislative enactment such as S. 262 to immediately bring those positions active, or this summer we will have a severe reduction.

In my written testimony, I call your attention to a perspective of funding U.S. Customs. They collect $22.6 billion, industry pays $800 million in merchandise processing fees. I submit to you that you ought to think about paying the costs of collection before we spend the money.

Generally, if we were to fund the entire $1.7 billion budget of Customs for 1999, plus the $300 million needed for Customs modernization and automation, plus $250 million in Senator Gramm's bill, $658 million in Senator Moynihan's bill, S. 219, both critical bills, to increase the technology, the equipment, and the staff, including all those elements, it would be 13 cents on the dollar of duties and fees already collected.

I submit to you that industry is already paying $800 million a year in merchandise processing fees. That money has not been spent for automation, much less for Customs operations. I submit to you that you ought to think seriously about taking the merchandise processing fee and dedicating it, much like the passenger processing fee is at the airports.

Finally, on automation. Essentially, it is a necessity, not an option. It is a disgrace to say that we need to take 7 to 10 years. We need to fund automation modernization now. It needs to be done yesterday, frankly. ACS is a crash already happening, not a threat. It is already being experienced. I again would submit to you, you need about $1.2 billion over 4 years.

Industry has already paid much more than that $1.2 billion, although not dedicated to Customs. A Section 110 is a threat that needs to be amended. Again, I would just submit that Senator Gramm's bill and Senator Moynihan's bill, S. 658 and S. 219, plus Senator Abraham's bill, S. 745, will do more to defend the borders against terrorism and illegal drug interdiction than Section 110 ever will do.

The southern border needs every position it has, and more that it has requested. The northern border's need is even more needed, because for 10 years the northern border has not had any increase in resources.

Again, I urge your serious consideration to passing both Senator Moynihan's and Senator Gramm's bills that have really stated the need.

Thank you very much.

[The prepared statement of Mr. Phillips appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Phillips.

Let me ask each of you, for purposes of the record, to summarize the key Custom-related issues faced by members of your organization. Mr. Kinghorn?

Mr. KINGHORN. I think the key issue in terms of using the model is to begin using it, and Customs is. They have established a group that will take ownership and work with the models development.

Second, I think, is to begin to put it into the model, and they are also considering that, large-scale threats. The model is built to, you may have equal resources going into two different locations, but you may have a bigger threat in one of those locations and that should be considered. But I think they are doing everything right at this point in terms of using this model at the corporate level.

The CHAIRMAN. Mr. McLouth?

Mr. MCLOUTH. Certainly, personnel is the very biggest thing that we need. We are growing so rapidly that Customs is so thin that drug interdiction is suffering. They are not able to pre-examine cruise passengers. It is a very serious situation.

Along with the fact that enforcement at the various ports varies very substantially. I suspect that people look very carefully at those ports they can get in and out of very easily as opposed to those that have enough staffing so it is very difficult to come in and out. But it would be a very serious thing if the cruise industry was essentially shut down.

That is what will happen if we do not pass some of these bills that were mentioned. One, in particular, is the $1.75. If that does not happen, we are going to lose almost half of our people. Miami will lose 26 to 36 people.

We just will not be able to handle those cruise ships at all and the ships will not be able to be processed in time. They will lose days. People will miss their airlines and it will be a public relations disaster.

The CHAIRMAN. Mr. Phillips?

Mr. PHILLIPS. I think very critically, a successful U.S. economy essentially depends on trade, and trade depends on Customs' ability to facilitate and enforce. I would simply say, I think the question is not where we need to go. I think we all know where we need to go. The problem is, how do we get there?

It was stated by Senator Gramm earlier that this committee championed the Drug Protection bill and the Northern Border Trade Facilitation bill together, yet it got hung up because of a question about labor issues. We have not dealt with the reality of funding Customs.

If we do not change the way Customs if viewed in its funding process, both for automation, by the resources it needs, and to get its job done, we are asking it to do something and not giving it the ability to do it. I have got to be very blunt about that. I think it is time we completely changed our view of how we fund Customs.

I submit to you, it ought to come out of their revenue before it is distributed otherwise to other purposes. A very critical issue, because we have not even begun to face the needs of tomorrow as of today. Thank you.

The CHAIRMAN. Mr. Vale?

Mr. VALE. The thing that always amazes me, is that you seem to discuss that there is a dual mission of facilitation and enforcement. That is the same mission. The more you enforce, the more you facilitate. The more people you have inspecting, the quicker people get through.

These are not opposing activities, these are complimentary activities. You cannot do drug enforcement without facilitating, because the more people you examine, the quicker you examine them, the more thoroughly you examine them, they get through. We need to understand that these are not opposing forces. Quite frankly, there is some need to make some changes in the way Customs has been managing.

Commissioner Kelly needs to be given his opportunity to do that. But there is, clearly, a need for that. There is also, clearly, for much more oversight from this committee and from others to see that there is reporting back to you on the results of what you do.

Merchandise processing fees. Where does that money go? How is it spent? We do not know. I do not think they know. It goes into the general fund, as best we know. There are a lot of activities that I think you can do well to stay involved in the process.

The CHAIRMAN. Senator Moynihan?

Senator MOYNIHAN. Thank you, Mr. Chairman. This gives me an opportunity be brief.

First of all, I note that our old friend, Sam Gibbons, is with us today. He has been here all morning.

The CHAIRMAN. Let me join you. It is always a pleasure to see Sam. I'm glad to have him.

Senator MOYNIHAN. Second, to go back to a theme that Mr. Phillips and others mentioned. This was just handed to me by Debbie, that the original Customs budget request for fiscal year 2000 was $1 billion more than the budget included by the President in his submission to Congress. That is a big cut, $1 billion.

Just a speculative thing that just suddenly occurs to me. Mr. Kelly is still in the room, and he may want to make use of it. I was handed a note by Dr. Podoff over here, who will soon be our director of the Minority staff, after Mr. Smith noted that, on average, the inventories available in General Motors factory are for 1 day.

David remarks that, in the 1960's when he was studying economics from Robert Solow at MIT, who has since become a Nobel laureate, they were studying the business cycle.

The issue was mostly devoted to the changes in inventories. This had been one of the discoveries of the early first half of the 20th century, that when inventory built up, demand dropped off. That is one way it cycles. Then when inventory ran down, business started going up again.

If we are in an extraordinary expansion, as we are, and the world has never known anything like it, can it be that just-in-time inventories explains a great deal of it? The Customs Service has an

absolutely singular role in seeing that just-in-time inventories are possible.

The CHAIRMAN. Otherwise it stalls the whole economy.

Senator MOYNIHAN. Yes. Yes. I mean, next to the Council of Economic Advisors and Bob Rubin, that may be the most——[Laughter.] A thought, sir.

Thank you for this hearing. Thank you all.

The CHAIRMAN. I want to thank you gentlemen for being here today. I note that the Commissioner has stayed on to listen to your testimony, so he is well aware of the problems faced by each of you.

I want to say how important I think his action plan is for improvement, which highlights such areas as integrity, accountability. We certainly will be watching with great interest as these policies are implemented. So, again, thank you, Commissioner Kelly, for being here today.

Gentlemen, we appreciate your very helpful testimony. The committee is in recess.

[Whereupon, at 12:31 p.m., the hearing was recessed.]

U.S. CUSTOMS SERVICE: MEASURING EFFECTIVENESS IN ENFORCEMENT OPERATIONS

TUESDAY, MAY 18, 1999

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 10:18 a.m., in room SD–215, Dirksen Senate Office Building, Hon. William V. Roth, Jr. (chairman of the committee) presiding.

Also present: Senators Chafee, Grassley, Graham, and Robb.

OPENING STATEMENT OF HON. WILLIAM V. ROTH, JR., A U.S. SENATOR FROM DELAWARE, CHAIRMAN, COMMITTEE ON FINANCE

The CHAIRMAN. The committee will please be in order. Today, we will turn to the daunting challenge of enforcing the Customs laws in the United States in this new era of global commerce.

A number of recent Customs Service operations have produced dramatic results in terms of arrests and seizures. They include Operation Hardline addressing drug trafficking along the southwest border, Operation Casablanca interdicting the money laundering operations of drug smugglers and their accomplices and of financial institutions in both the U.S. and Mexico, as well as recent exposure of a child pornography ring.

Now, what the success of these operations and the number of arrests and seizures do not tell us is whether Customs is having an impact on the problem overall. And the answer to that question depends to a significant degree on how we should measure success.

And while there are significant arrests and seizures, they alone do not provide an answer because they measure activity and not outcome. Taken out of context, they can be seriously misleading.

For example, to the extent Customs enforcement efforts have been criticized in recent years, that criticism has focused on the fact that seizures in narcotics were down along the U.S.-Mexican border. Now, the fact that seizures went down does nothing to tell you why. Seizures could be drawn down due to a lack of enforcement effort or because the enforcement efforts of programs like Operation Hardline have in fact succeeded.

Now, what that illustrates is that gross figures like the overall number of seizures and arrests, are simply the wrong box score for determining whether Customs is winning in its effort to stem the flow of illegal contraband. Determining the right box score requires an understanding of what counts from the smuggler's perspective

and how Customs can apply its resources to affect the smuggler's calculus of risk and reward.

This hearing will focus on that calculus as a means of measuring Customs performance and for establishing Customs enforcement priorities going forward.

Our first witness offers unique how to measure Customs success or failure from the perspective of a drug smuggler. We will hear how he probed and exploited weak points in Customs enforcement efforts. We will also hear how he bluntly assesses Customs enforcement efforts through their impact on his cost of doing business.

Our second panel of witnesses will expand on this theme, discussing the proper measure of performance and enforcement. We must look at outcomes rather than simple arrest and seizure statistics.

I will without objection put my full statement in as if read.

And now, I am pleased to call on Senator Robb.

OPENING STATEMENT OF HON. CHARLES S. ROBB, A U.S. SENATOR FROM VIRGINIA

Senator ROBB. Thank you, Mr. Chairman, and thank you for holding this hearing. I was not able to attend the first hearing in this series because of a mark-up over in the defense authorization bill, but I look forward to today's hearing.

I think the question frequently, as it does in many other instances, boils down to the question of resources and where those resources are most effectively applied and particularly in the enforcement effort. And I think that your lead-off witness will have, as you suggest, a unique perspective to bring. And I look forward to hearing from this witness. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Robb.

Our first panel consists of a former smuggler who was arrested by Customs. And he will speak about his experiences and observations while he smuggled. The witness has requested that his identity be protected out of concern for his and his family's safety. Please note that when the witness is questioned following his testimony, he may not be able to answer certain questions that may reveal his identity.

I will now ask the witness to please proceed.

STATEMENT OF SENATE PROTECTED WITNESS (FORMER SMUGGLER)

The WITNESS. I have prepared a statement. And I wish to thank you for the opportunity to continue an effort I began several years ago, assisting in the war on drugs in which I was once a participant.

I was a narcotics smuggler for over 20 years. After I was arrested by Customs for smuggling a large amount of cocaine, I agreed to cooperate with the government. This included offering my knowledge to Customs inspectors to assist in targeting shipments for narcotics. It is because of this continued cooperation that I am before you today.

I was educated at an ivy league institution. And soon after, I began employment with a United States intelligence agency in a capacity unrelated to my later smuggling activity. During this Viet-

nam era, while in this employment, I was held as a prisoner of war for two years by the communists.

In the early 1970's, I decided to start a legitimate seafood business. Unfortunately, this business venture did poorly and failed, but it was during this time that I became aware of how little interaction there was with Customs while operating on the high seas. I followed the allure of easy money and decided to enter the narcotics smuggling business.

I offered to solve an essential part of the smuggling puzzle. I provided the "transportation bridge" which closed the gap between the supply and great demand for drugs. I was the middle man who would receive the drugs from the cartels in South and Central America and smuggle them into the United States where I would turn them over to the local distributors in charge of packaging and dealing to the streets.

As with any business, smuggling is driven by profit. And it is determined by subtracting the cost of physically moving the drugs from the amount of money negotiated for the transportation. Smuggling is less expensive when there is little resistance crossing the border.

For example, when the drugs were destined to enter the United States at a border or port that was not heavily policed by Customs, then the smuggling method does not have to be as sophisticated. It is less expensive to smuggle 1,000 pounds of marijuana in an open fishing boat than hidden in an ocean container. These additional costs are absorbed by the smuggler.

The goal of the smuggler is to lower transportation costs and pocket as much money as possible. This forces smugglers to "shop" ports in an effort to find the weak link in Customs armor. This becomes a shell game because as soon as the smugglers find this opening, they exploit it until Customs reacts, forcing the smugglers to find a new entry way. This is apparent in the methods and ports I utilized during my smuggling career.

My first smuggling venture involved over 10,000 pounds of marijuana. Because the Customs present in the Caribbean at the time was scarce, I was able to use a fishing vessel without secret compartments.

After that successful operation, all future undertakings were targets of opportunity, meaning that I would exploit the weakest area in Customs resources at the time, usually in vessels through the Caribbean. From the late 1970's to the early 1980's, I smuggled over 500,000 pounds of marijuana into the United States, valued at approximately $125 million.

During this time period, I experimented with dropping cocaine out of airplanes to waiting boats. After limited success, I had some bad luck and the drugs were dropped to the wrong location and lost.

As the emphasis began to focus on the Caribbean and Customs began making large seizures with a concentrated effort of airplanes and "go fast" boats, I moved operations to New York city where I smuggled over 400,000 pounds of marijuana in just over 3 years. One venture resulted in the off-loading of 100,000 pounds of marijuana across the Hudson River from the World Trade Center.

I also moved to smuggling cocaine hidden in containerized cargo into the New York seaports. Finding logical products and a country of origin that would not raise red flags were important factors in being successful.

I developed a relationship with Italian organized crime in New York city. And I was able to infiltrate a Fortune 500 company who did a great deal of importing. The company did not realize that I was able to import hundreds of kilograms of cocaine valued at $81 million hidden within their shipments.

Before I was arrested, I attempted to smuggle a load of cocaine through this company, but the Customs inspectors noticed a paper work discrepancy and discovered approximately 1,000 kilograms of cocaine, valued at $130 million. I was arrested by Customs special agents during an undercover operation and decided to cooperate and use my knowledge to help further Customs efforts.

I was sentenced for my role in smuggling this load of cocaine and was released from custody 2 years ago. While I was working closely with the Customs agents who arrested me, I promised them that when I was released from jail my cooperation would continue and I would continue to assist in any way possible.

I was asked to make observations on drug-related areas in which I have experience. And there is one in particular regarding Customs mission. Aside from the physical placement of inspectors and agents, an important element in the war is intelligence.

During my smuggling days and time in prison, I met many people who had their drugs seized and were arrested. The common thread to their downfall was almost always prior information by Customs, DEA, or the FBI. Information should be an invaluable element when targeting cargo and people for narcotics. As an alumni of the intelligence community, I fully understand how vital timely information is when targeting and infiltrating organizations at all levels.

In closing, I hope that I have been helpful in describing the smuggler's abilities to exploit openings created by placement of Customs officers and resources. I understand and accept the condemnation that I have brought upon myself through a lifetime of smuggling. However, I would like to make clear that since the day I was arrested I have not looked back in my efforts to assist in the battle against narcotics smuggling.

Thank you for this opportunity. And I hope I can answer any questions that you may have.

[The prepared statement of the Senate Protected Witness appears in the appendix.]

The CHAIRMAN. Let me start out by asking you this: Based on your experience, what would be the most effective deterrents that Customs could use against drug smugglers? And would you set priorities as to what you think are the most important?

The WITNESS. Well, I believe that you can have two things that could work simultaneously. One is like to have equipment to x-ray containers as they come into ports or x-ray ships or yachts or smaller boats. And the other one which is sometimes down played is the need for the prior information so that whatever efforts can be done in gathering intelligence beforehand is very, very helpful, those two things.

The CHAIRMAN. Let me ask you about intelligence; you said you had prior experience as, I take it, an intelligence officer. What kind of information would you try to collect? And how would you go about seeking that information?

The WITNESS. Well, the information would be whenever a contraband is coming in. Now, of course, I had been concentrating on drugs, but there is many other kinds of contraband. And to get your sources of information, motivation is the most difficult thing to discover.

Some people do it for patriotic reasons. Others do it strictly for monetary reasons. Others do it because they are upset or mad at somebody else and they want to get even with them. But the point is that a well managed intelligence department would be a very, very helpful thing in the overall efforts.

The CHAIRMAN. Could you describe in some detail how you selected particular ports or an operational method by which to smuggle drugs?

The WITNESS. Well, first, it is from what experience other smugglers are having. And within the, let us say, fraternity of smugglers, the port that so and so was able to come in through, a port, let us say Norfolk, Virginia or something and that going into Jacksonville, Florida was no good because they had a number of agents there. So then, people would shift to other areas.

And the methods, of course, have varied. Initially, it was all you had to do was to look the part. If you were in a commercial fishing boat, you have to look like a commercial fisherman. And if you are in a luxury yacht, you have to look like a yachtsman. You cannot be looking like a mechanic. So appearance was first the utmost.

Now, when they started looking inside the boats, then it was a matter that secret compartments had to be preferred because that is not a matter that you could just pass because you had a Brooke Brothers suit on. And so throughout the years, different methods have been successful. And it was played by years, so to speak.

The CHAIRMAN. Let me ask you this question, to what extent do you think technical means of securing intelligence is more important than that of having human resources? Do you care to comment on the importance of the two approaches?

The WITNESS. Well, I think that they are both important. But as far as the technical part, it would be basically for surveillance efforts if something is in en route, like to follow a boat or airplane that does not have a flight plan or things of that nature. The human resources are to forewarn you of the intent of someone who is going into a smuggling operation.

The CHAIRMAN. In the context of gathering intelligence, how did you make contact with the individuals or groups who——

The WITNESS. Well, initially, it took almost two years to be properly introduced. You have to be properly introduced. Once you have been introduced, they are responsible. And the word "responsible", all of us think, well, yes, he is a responsible person, he will pay his bills, and so forth. But responsible means if there is any problems that their life, it is they hold it in their hands.

Anyway without getting sidetracked, after I was properly introduced to some marijuana exporters, all they wanted to see is the success of the first shipment. What took 2 years to achieve, then

within two weeks another shipment was ready. And after that, it was a matter of they would give you whatever you could carry because it was they would give it to you on consignment. I am talking about marijuana. And, of course, I am talking about 25 years ago.

The CHAIRMAN. Then, are you saying it really took you 4 years to accomplish your first sale, 2 years to——

The WITNESS. Two years to be introduced.

The CHAIRMAN. Yes.

The WITNESS. To get into the business, in order to be introduced to a Columbian producer.

The CHAIRMAN. And once you were introduced, how long did it take to get involved? Was that immediate?

The WITNESS. That was immediate.

The CHAIRMAN. That was immediate?

The WITNESS. Yes. Once that was rolling, it was 2 years. Then, it was every two weeks. It was a dramatic change.

The CHAIRMAN. When you speak of information and intelligence that would enhance the interdiction of drugs, do you mean specific information from places like Columbia?

The WITNESS. Yes. For instance, let us say that into the port of Newark, someone was shipping some cocaine. You can quote whatever figure you want, whether it is 100 kilos or 1,000 kilos. And it would be a matter of saying that such and such company that manufactures blue jeans is sending a shipment out. And, of course, if they can tell you on such and such a shipment the number of the containers and so forth, then you have everything. But at least otherwise, you would have a general picture.

The CHAIRMAN. Are you personally aware of any instances of corrupt Customs inspectors assisting you or others in the smuggling operations?

The WITNESS. No, I never had that experience, sir. I know I read the newspapers about all these, but I personally have never run into any corrupt employees.

The CHAIRMAN. Or have you had contact with anyone who claimed they have?

The WITNESS. No, because we work pretty much independently.

The CHAIRMAN. Senator Robb?

Senator ROBB. Thank you, Mr. Chairman.

In your testimony, you indicated that you attempted to exploit the weakest link in the Customs chain. Is there a particular link that is more likely to provide that weakest link than others in your experience or in the experience with others with whom you may have had contact from your "former business"?

The WITNESS. Initially, it was just like computers were years ago that they would have the main computer, let us say, at Kennedy airport, but that computer was not available, let us say, in Atlanta or in some other cities. And people would use that opportunity to come in through those kinds of holes in, let us say, the protected area. And now——

Senator ROBB. Let me ask you on that question, right now, it is my understanding that we are doing a much better job of linking our computers and making that data base available regardless of the port of entry.

The WITNESS. Now, the computer is like a huge Chinese wall. There is no problems with the computer. I was just using that as an example of what it used to be like.

Today, it is a matter that sometimes you go to the other extreme. They try to get more and more sophisticated, secret compartments, and so forth. And then, the biggest problem was that somebody would inform that it is coming in on such and such a shipment.

So then, they went to the other extreme where they did an air drop to a small boat. And the small boat would come in. And this was the Customs surveillance of airplanes. And their physical presence is important.

Senator ROBB. Is it fair to say that without the intelligence component that the Customs Service would be virtually blind and unable to do any significant level of interdiction as it is able to do today?

The WITNESS. Well, I would not say that it would be impossible, but I can tell you that 50 years ago just in a chat with the Customs agent not talking about business, when nobody ever heard of drugs at the time, you are talking about diamonds, diamond importing.

It was a big thing in the papers about a man walking in with a briefcase. And the diamonds were inside the handle of the briefcase. And he was arrested at the airport. Here is an executive from a large company, walking through. I said, gee, that is amazing how you guys can swamp the diamonds. He said, well, we had a little prior information.

So this is nothing new. The information is like gold, but you need both because, for instance, if you have the x-rays to check the containers and they know that these are going through, then they are not going to put it in the different areas of a container because those will be checked as the container is going by.

Now, there are things that you cannot stop, every car that goes down on I–95. And you cannot check everything. But to show that they are compatible, let us say, the technical aspect is important. And the information aspect is important.

Senator ROBB. How effective are our computers today if they are available and in good working condition and applied to a particular vessel, vehicle, or any other form of transportation?

Is an x-ray today normally sufficient to detect the presence virtually of any type of contraband? Or are there certain types of contraband that are not able to be picked up on the x-ray?

The WITNESS. Well, sir, I am——

Senator ROBB. I realize this may be beyond your technical capability.

The WITNESS. This is beyond my reach. I am not familiar with the high-tech things today. People think if we go to the airport and they are going to be like walking naked, they are not going to be carrying money on their bodies or drugs because they can find it. And what happens or does not happen, the fact that it could happen, then it eliminates, it starts separating the men from the boys, so to speak. You have to be more and more sophisticated to be able to do smuggling.

Senator ROBB. How effective are dogs in the personal smuggling as opposed to the transshipment of containers and whatever in drugs that are not ingested?

The WITNESS. I know they work. In other words, if somebody sees a dog coming, especially in a car or in a small yacht, that those people—and nearly often the dog does find the product. This is without prior information.

Senator ROBB. That is what I meant. In terms of simply taking random traffickers, whether they be smugglers or just travelers, if you have either x-rays or dogs, and this comes back to resources, your chances of discovering the attempt to smuggle is dramatically increased?

The WITNESS. Well, I would say that again, and forgive me for being redundant on this, but if you have the two things, if you have the manpower and the physical resources together with prior information, you have a combination that could really make a big difference.

Senator ROBB. Thank you very much. My time has expired.

Mr. Chairman, I thank you.

The CHAIRMAN. Thank you, Senator Robb.

Senator Grassley?

Senator GRASSLEY. Have you ever bribed or attempted to bribe a public official, including law enforcement officials in your attempts to get drugs into the country?

The WITNESS. No, sir.

Senator GRASSLEY. How effective would you say that law enforcement efforts are to stop or uncover bribery?

The WITNESS. I would say I have never met anyone who even attempted that. When you go into South America, it is natural. In other words, it is acceptable. Whether it is Mexico or Columbia or Venezuela, it is standard procedure. Up here, it is not, sir, that I know of at least.

Senator GRASSLEY. Following up on what Senator Robb was talking about, x-ray equipment, and you probably have answered this already, but I did not get the point that I wanted. Have you been successful against Customs detection equipment at our borders? And is the increase in x-ray technology at our borders a real threat to the smuggling community?

The WITNESS. I would say that we never had that problem. We had the problem with the paper work. For instance, that is another thing that you do not hear too much about it, but Customs does go over all bills of lading and so forth. If they do not have the proper product accompanying it, that will alert something. In fact, this is how we got into problems.

And what was the last point?

Senator GRASSLEY. In regard to x-rays, do you feel that you ran into the use of x-rays in any way? And is that a real threat to the smuggling community?

The WITNESS. It is a threat, but the results are that then the smuggling becomes much more expensive. And the volume will come down because then only those sophisticated people can accomplish it.

Senator GRASSLEY. Other than x-rays, and following up on what you just said that there is other ways to get around x-rays, as an example, what other technologies or policies would you suggest that would be effective?

The WITNESS. Well, I do not know how much budget you would have to do this, but airplanes, if you check their fuel when they come in. You check and see, just like checking the tanks to see if they have water in them. You can check and see if they have contaminants because you can smuggle things mixed in with the fuel. That is one example. If we had time, we could go into other things.

Senator GRASSLEY. Narcotics traffickers are well aware of our efforts to strengthen law enforcement presence along the southwest border. And as you indicated, smuggling organizations shift their smuggling routes to adjust to the Customs law enforcement efforts.

Today, we are once again seeing a shift by traffickers with the rise in narcotic smuggling activity moving to south Florida and the Caribbean.

What recommendations do you have from the perspective of someone who has actually watched and shifted his smuggling routes around the Customs Service to successfully smuggle drugs in our country?

The WITNESS. Well, what I would focus on is the longest border that is unguarded and because it is a lot cheaper to go into Canada and then come back into the United States. And that is something that is overlooked. You can beef up that, put in a couple extra wires.

Senator GRASSLEY. And from the standpoint of being a person who smuggled yourself, you see drugs coming in from Canada, that to be less of a concern on the part of our officials and consequently a route that is overlooked in law enforcement?

The WITNESS. Well, I do not know I would use the words "less of a concern". They would like to contain it, but it is a scenario like the back door. When people look at the front door, they do not look at the back door.

Senator GRASSLEY. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Grassley.

Senator Chafee?

Senator CHAFEE. Thank you, Mr. Chairman.

You sort of answered this in other questions, but what would you recommend that the Customs Service do that they are not doing now, in other words, what constructive suggestion? I think you indicated you did not have quite enough time with Senator Grassley in answering part of that question. So I have some time here.

The WITNESS. Well, it is an old saying that you win wars with money. And this goes back 200 years ago from Napoleon's days. So the more resources you have, the more likely you are to be successful.

Senator CHAFEE. And by resources, you mean manpower?

The WITNESS. Well, first of all, money which will provide you with manpower and with the technical support you need whether it is x-ray machines or airplanes or boats or whatever.

Senator CHAFEE. It always is remarkable to me that they get the information that they do get. The intelligence that the U.S. Customs Service is able to obtain, do they obtain that through paying money to these people? Or is it rival gangs will sometimes squeal on the others? How does that work?

The WITNESS. Well, as I mentioned, motivation is almost like for a psychiatrist to best answer that. Some people do it, as I said, for

patriotic reasons. Others do it strictly for monetary reasons. And others do it for personal reasons.

But as far as these gains, that is at the sales or street level. The part that I am familiar with is strictly importing. And then, you do not deal with that at all. You just deal with the distributors like you are dealing in any commodity.

Senator CHAFEE. All right. Thank you.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Chafee.

Let me ask you one final question. Then, we may have written questions submitted to you. You mentioned infiltrating a Fortune 500 company. How did you accomplish this infiltration? And how did you accomplish taking advantage of it?

The Witness. Well, it was in the manner that when we were coming in with loads of marijuana, one of the people that was a driver, basically a chauffeur said, well, I have a friend that works at one of these large companies. So without mentioning any name, but let us say, it is a million-dollar company.

And so initially, it was a matter of just storing something over there. And then, that started to open the door for actually putting out a purchase order and having it directly imported by them. And, of course, the company itself, the president, vice president, the upper management did not know about this. It was like the lower management.

The CHAIRMAN. My final question is, why did you want your identity secure?

The WITNESS. Why I want my identity secure?

The CHAIRMAN. Yes. Why do you think it is necessary to testify behind a screen?

The WITNESS. Well, a lot of people do not know that I am testifying here. And I have family that live in South America. And there, it could definitely be hazardous to their health.

The CHAIRMAN. Well, I think that is all the questions we have today. We appreciate you being here. We will ask that you be removed from the room. And I will turn it over to the police for that purpose.

Senator CHAFEE. Mr. Chairman, I would like to join in thanks to our witness. I know there is some risk involved in all this. And the easy thing to do was not do anything on his part, but his willingness to come here, I think it is a great tribute to him. And we are grateful.

The CHAIRMAN. Thank you, Senator Chafee.

We will now proceed to our second panel. Michael Chertoff is a partner with Latham and Watkins, a former U.S. attorney. Norman Rabkin is the Director for Administration of Justice at the GAO office. And Lawrence Sherman is a professor and chairman of the Department of Criminology at the University of Maryland.

Gentlemen, it is a pleasure to welcome you here today. Your full statements will be included as if read.

And we ask to start with Mr. Chertoff.

STATEMENT OF MICHAEL CHERTOFF, PARTNER, LITIGATION DEPARTMENT, LATHAM & WATKINS, NEWARK, NJ

Mr. CHERTOFF. Thank you, Mr. Chairman. It is a pleasure to appear before the committee. As I indicated in my written statement, I bring to this my experience of 11 years as a Federal prosecutor, including four as a United States attorney from 1990 to 1994.

During the time that I was a prosecutor, one thing that I learned was that numbers have a powerful attraction and that law enforcement agencies including Customs have a tendency to want to measure their performance in very numerical terms, whether it be number of arrests, pounds of seizures, numbers of forfeitures.

And with that suggestion that is not useful, one of the things that I observed was too much emphasis on numbers winds up leading to quantities of cases, but not high quality cases. The best example of that I can think of is the example of organized crime.

In the 1960's and 1970's, there were a lot of cases involving individual, organized criminals, driven by the FBI's policy of promoting statistics. But in the 1980's and 1990's, the program was much more successful because there was an emphasis on high quality cases, cases that were focused on the leadership of organized crime, on institutions that were infiltrated by organized crime.

And as a consequence, even though the numbers of arrests and numbers of seizures may have been reduced, the quality and the impact of the program was very much enhanced. And it is my position very briefly that the same principle ought to apply here with respect to Customs or any other kind of enforcement agency.

Customs will always have a reactive element. There will always be a need to patrol the border and police the airport and make sure that we are identifying and arresting the people who are smuggling in contraband and seizing the contraband and the narcotics. But if that is all that drives the program, all that is going to happen is, one, we will replace one set of bad actors with another set of bad actors. And you will never wind up accomplishing anything.

You have to marry that reactive program with a strategic program. And that is a program that takes the intelligence base developed over years and targets organizations and institutions that are persistent violators and persistent importers of contraband.

And to encourage that in budgets and plans for performance in a law enforcement agency, you have to separately budget and plan for those strategic initiatives. You cannot mix apples and oranges. You have to resist the temptation to push the program to those things that are easily measured and away from things that are more long term, more difficult to measure because they are qualitative and more wide ranging.

Therefore, my suggestion is very simply this. In programming and planning for Customs and any other law enforcement agency, you should make a decision upfront about the degree to which you want to commit resources to strategic activities. You then ought to program that separately.

For those kinds of efforts, you have to have intelligence people who can identify your major organizations and your major institutions. And then, you have to put together programs which lead to convictions or dismantling of institutions or organizations or imposition of trusteeships. And then, measure the accomplishment of

those goals not every 6 months or every annual budget cycle, but over a period of two to 3 years.

I think if you have that kind of a mixed program, it is possible to have the kind of success with respect to narcotics trafficker and other smuggling that we have seen the government has had with respect to traditional organized crime. Thank you.

The CHAIRMAN. Thank you.

[The prepared statement of Mr. Chertoff appears in the appendix.]

The CHAIRMAN. Next, I will call Mr. Sherman. It is a pleasure to have you here.

STATEMENT OF LAWRENCE W. SHERMAN, PROFESSOR AND CHAIR DEPARTMENT OF CRIMINOLOGY, UNIVERSITY OF MARYLAND, COLLEGE PARK, MD

Professor SHERMAN. Thank you very much, Mr. Chairman, Senator Chafee, and Senator Grassley. I am delighted to have a chance to comment on this issue of numbers driving the operations of law enforcement agencies.

I have been working for about 30 years with agencies all over the world on the issue of measuring performance. And it is a common complaint that the emphasis on production of outputs, those numbers, the activities of the organization, such as arrests made or seizures of drugs does distort the goals and the accomplishments of the mission of the agency. And the more difficult-to-measure items do get ignored.

I just have a slightly different solution to that problem from Mr. Chertoff. And that is I suggest that you invest in the more difficult-to-measure information which is absolutely critical, as you observed in your opening remarks, Mr. Chairman, to telling whether the decline in drug seizures is a reflection of the decline in drug shipments and a success, or a decline in drug seizures is an indication of less effective detection relative to a base of increasing shipments of drugs.

The only way we can get the equivalent of the homicide rate which provides that kind of denominator to local police for Customs enforcement is to spend the money on doing the kind of measurement that has been done on a test basis already which is essentially a random selection of all units of entry, including persons and cargo.

That would be done for each, at least at the major ports of entry if not all of them, and to do that every year to provide your underlying trend line of how much shipment there is and indeed what percentages of the contraband shipment are coming from well established and recognized historical sources and how much of it might be coming from new sources.

It seems to me that the comments of the preceding witness about intelligence go very much to this point because the traditional way to think about intelligence is informers and spies, but in fact having a good statistical base of what kind of activity is going on and how it is changing is an excellent form of intelligence.

And it is comparable to the National Crime Victimization Survey which the Department of Justice conducts every year to supple-

ment the police-reported statistics on crime simply because we know that people do not report all crimes to the police.

And it provides a very useful check at the national level. It does not do that at the local level. And that is really what I think from a management standpoint could be most helpful to the Customs Service.

The commissioner of Customs could evaluate each of the ports of entry in terms of the ratio of contraband detected to the estimated ratio of contraband that is getting through which would be based on this annual random sample of searching everyone selected purely at random with an equal probability.

That would enable the Customs Service to allocate resources more effectively in terms of where they are needed, not just in terms of absolute numbers of seizures, but the percentage of contraband that gets seized and which you will never know unless you invest in this kind of random sample procedure.

And I suggest in my written testimony that the Census Bureau which in fact conducts the National Crime Victimization Survey for the Justice Department is the kind of organization, certainly not the only organization, but the kind of organization that understands the sampling procedures and the methodology that would produce an independent report on each of those ports of entry, estimating how much is getting through and then allowing Customs to see what percentage of it is getting detected.

A second benefit that this tool produces is in fact to produce a much more accurate profile of the kinds of people who are shipping contraband and would therefore lead to more effective use of resources within each port because they would have a port specific profile of the kinds of people most at risk of getting the contraband through.

Mr. Chairman, I suggest that even though this kind of plan would cost tens of millions of dollars that its value would greatly exceed that and that in the absence of this kind of investment, we will continue to be guessing about the effectiveness of Customs operations. We will not have the critically important intelligence needed to allocate resources in the ways in which they will be useful, both across the ports of entry to where the greatest need is and then within the ports of entry in terms of the high-risk profiles of people shipping contraband.

Thank you for the opportunity to bring this idea to your attention.

The CHAIRMAN. Let me welcome Commissioner Kelly. I believe he is in the audience. It is a pleasure to have him.

You make a very interesting suggestion, but I wonder. I guess I will ask you later how you go about selling the public on that kind of sampling. It could be quite an uproar, but we will give you the chance to comment on that.

Professor SHERMAN. Thank you.

[The prepared statement of Professor Sherman appears in the appendix.]

The CHAIRMAN. Mr. Rabkin?

STATEMENT OF NORMAN J. RABKIN, DIRECTOR, ADMINISTRATION OF JUSTICE ISSUE AREA, GENERAL GOVERNMENT DIVISION, U.S. GENERAL ACCOUNTING OFFICE, WASHINGTON, DC

Mr. RABKIN. Thank you, Mr. Chairman and members of the committee. I am pleased to be here today to discuss the work we have done addressing the Customs Service's efforts to interdict drugs, to allocate its resources, and to measure its performance.

My statement summarizes products GAO has issued on these subjects since 1997. And it also covers our views on the action plan developed by the commissioner earlier this year, as you had requested.

Keeping with the theme of today's hearing, I will focus in my oral comments on the Customs performance measures and how they relate to its enforcement mission. The Customs performance plan is divided into two major components: commercial which deals with the trade side of the house and drugs which deals with the enforcement or the interdiction side of the house.

Customs enforcement goals disrupt the individuals and organizations smuggling drugs through U.S. ports of entry. Customs uses intelligence it gathers and receives about smuggling activities, interdiction efforts at the ports, and follow-up investigations to try to achieve this goal.

For fiscal year 2000, the Customs Service has proposed to use three measures to indicate how well it is achieving that goal. First, Customs is going to try to measure the transportation costs incurred by drug organizations to smuggle cocaine through the ports. Customs believes that the more drugs it seizes, the more expensive it becomes for smugglers to get their product to market.

The logic continues that as these costs increase, so do the costs of the drugs on the streets. And then, either the transportation cost gets so high that the smugglers go out of business or the street price gets so high that the demand drops.

Customs has not publicly described how it will determine what smuggler's transportation costs are or how these costs might have been affected by Customs enforcement activities. Customs says that it has these data, but that they are classified.

Even assuming that Customs has a way to tell how much it costs drug smugglers to move cocaine into the United States, Customs has not set a specific goal that it expects to achieve in fiscal year 2000. This defeats the purpose of the Results Act because it limits the dialogue that Customs and its stakeholders, including this committee can have about whether they are best using available resources to achieve the results.

Customs has also proposed continuing to measure its effectiveness by counting the number of drugs seizures that it makes and the amounts of drugs that it seizes. These traditional measures are indicators of what Customs catches at the ports, but as you have heard tell very little about what Customs misses.

In any event, these performance targets for fiscal year 2000 are very modest, given the increase in resources Customs received for fiscal year 1999. For example, compared to its plan for fiscal year 1999, Customs expects to have only 4 percent more cocaine sei-

zures, but not to seize any more volume of cocaine in the fiscal year 2000.

The only other comment I would like to make on Customs performance measures is that Customs has no formal measures for management issues, such as improving its financial management or internal control systems.

On the one hand, this may not seem like a big issue. As long as Customs achieves its major goals regarding trade and drug enforcement, what difference does it make whether its books are in order or it has conducted the number of port inspections that it had planned?

On the other hand, Customs is a very decentralized organization with a history of management problems. Despite the strong beginning shown by Commissioner Kelly, it may be helpful to have Customs include some key management indicators in its performance plan. This will help you, other Congressional committees, and even GAO keep track of how well Customs is achieving many of the goals it sets for itself in its action plan.

This completes my oral comments. And I would be glad to try to answer your questions.

[The prepared statement of Mr. Rabkin appears in the appendix.]

The CHAIRMAN. Well, let me ask each of you what you think is the single most important criterion that Customs and the committee should rely on in assessing the effectiveness of Customs law enforcement operations.

Now, you talked about sampling. Maybe that will be your answer, but I will call on you first, Mr. Sherman.

Professor SHERMAN. Thank you, Mr. Chairman. I think that your concern about whether the American people will accept this needs to be compared to the concern that the American people have about the effectiveness of interdicting contraband.

Our experience in mounting programs for detecting guns being carried on the streets in Kansas City and Prince George's County and elsewhere is that people are very happy to cooperate with an effort that is politely explained to them. And if the purpose is made known as part of a general improvement safety, people have consented to having their cars searched for guns in Prince George's County. And complaints against the police have actually gone down rather than up.

My experience as a frequent international traveler is that the customs agencies are generally a very polite service and perfectly capable of explaining to people that they have been selected through a computer formula for participation in a test of the shipment of contraband. And this will take perhaps 5 or 10 minutes. Sorry to delay you after your long and exhausting flight and very much sympathize with the imposition that this may require.

The legal basis for this is something that, as I understand it, resides in the authority of the agency. And I think it is like so many things. It is not the question of what we are doing, but how politely it is done, how respectfully it is done.

And I have a lot of confidence that if this has been done already on a test basis without causing disruption that this could be ruled out as a national program perhaps in stages in a way that would

test the waters carefully and try to refine and do mid-course corrections as you go along.

But I would not dismiss it out of hand on the assumption that the public will be adverse to the idea because I do not think that the evidence is there to prove that.

The CHAIRMAN. Mr. Chertoff?

Mr. CHERTOFF. I guess I share a little of your skepticism, Mr. Chairman, about how well received a program of random sampling of that sort would be, but I guess I think it is an interesting issue to explore. So many people would tolerate it. I do not know that it answers the question.

I have a sense that what happens is we wind up gathering a lot of statistics that tell us things that are of anecdotal significance, but do not give us guidance about how to prevent things from occurring in the future.

Again, my experience as a practical matter is that you really have to identify the organizations and the institutions that makes smuggling profitable. I happen to think, for example, focus on money laundering and institutions that allow people to remove money from the country to extract the profit is a very priority way of dealing with this issue because I think that is an area where you do have the ability to affect the profit. And that then drives down the desire to smuggle.

So I think that while statistics are useful, there is no substitute for quality intelligence identifying who are the principal organizations are, looking over time at where the sources of narcotics are, and looking where the profits are being removed and sent overseas and then mounting operations aimed at those institutions and organizations and measuring success through convictions, through institutions that have been cleaned up, and through gross statistical trends over a long period of time.

The CHAIRMAN. As you said, a little bit large and organized crime.

Mr. CHERTOFF. Exactly, exactly.

The CHAIRMAN. Mr. Rabkin.

Mr. RABKIN. I guess the answer to the question, you have to put it in the context of the national drug control strategy. Customs is one of many players at the Federal level that are trying to achieve the ultimate goal of reducing the use of illegal drugs in America. The Customs role is dealing with the supply reduction side. As you know, there is a demand reduction side dealing with prevention and treatment.

But in terms of reducing the supply of drugs, the strategy calls for a focus at both the source that is overseas and some of the domestic sources, the transportation of the drugs, and the distribution on the streets. And Customs role is for the most in that middle area as the drugs are brought into this country.

So I think that if we look at how well Customs is doing in achieving that goal, it has to be in the context of the broader drug control strategy. In that strategy, the measure that OMBCP has proposed is the dismantling and disruption of drug smuggling organizations generally.

I am not prepared to say today and I do not think anybody is whether that is the right strategy to follow to cut the source of drugs because in Columbia where they have been successful in get-

ting rid of a couple of the drug organizations, others have taken their place. And the quantity of drugs coming in from Columbia has nut suffered. So I think whatever the issue is for the Customs Service, it has to be put into that context.

Now, the question about the over sampling of passengers coming in is also applicable to cargo. It is something that the Customs has been doing for a few years. I think Customs recognizes the expense and I think would appreciate the support of this committee and the appropriations committees if it is something that you all want them to do, to be able to, whether it is tens of millions of dollars or whatever the cost.

But it requires them to inspect more people than they normally would have, more cargo than they normally would have to see not only what they are missing, but how well are their other detection techniques, how well is the intelligence working, how well are their inspectors able to use their subjective judgment to focus on behavioral techniques or even paper work that might be a little out of sort on cargo coming in.

So I think all of these are important.

The CHAIRMAN. Now, Customs is not alone in its enforcement efforts. Of course, we have DEA. On alcohol and tobacco imports, we have the ATF. Do we risk having these agencies working at cross purposes if they are not all working under the basic performance measures, Mr. Sherman?

Professor SHERMAN. I do not think they need to have. In fact, it is probably not a good idea to have the same performance measures for different agencies that take different specific missions, even though they are all wrapped around similar general goals.

And I would think that the unique mission of Customs as the lead agency for protecting the borders even to the extent that ATF might be involved in supporting that mission, that the ATF efforts would be measured with respect to that mission with those same indicators.

And I guess that the question would remain. If we do not use indicators that involve the measurement of a base line amount of contraband shipped, we are still not going to know whether that problem is going down or up, whether it is ATF or Customs who is being tasked with that objective.

The CHAIRMAN. Mr. Chertoff.

Mr. CHERTOFF. Mr. Chairman, I think with respect to the reactive mission of Customs, it is always going to be measured a little bit differently than the FBI or the DEA because does have the primary responsibility with respect to imports.

I think with respect to the strategic mission, they have to be coordinated. I have lived through many instances in which you spent more time arbitrating between the FBI and DEA and Customs than you did actually working on the case plan.

In our district, as it happened, the leaders of the various agencies worked well together. And I think when you have a common set of strategic goals and some commonality measurement, you can get that kind of cooperation. If you do not, then you wind up with the all too familiar turf war phenomenon.

The CHAIRMAN. Very good.

Mr. Rabkin?

Mr. RABKIN. I agree. And I think that the national drug strategy is what pulls all these agencies together. I think their performance measures can be uniquely tailored to each agency depending on the mission. And I think in fact that is what is happening.

The CHAIRMAN. Thank you. Can you tell me in practical terms how Customs can best measure the impact of its operation? Now, we have talked about counting the number of arrests and seizures by itself as a useful way of measuring Customs performance. Or would you favor an approach that focuses on raising the cost of smuggled drugs, as proposed by Customs?

Do you want to answer that?

Mr. CHERTOFF. If you could measure the cost of drugs smuggling, I think it is a useful measuring tool. I do not think it is the exclusive tool. I do not know how Customs comes up with its statistical estimate of what the cost is. I think the other thing that is important to measure is not in a snapshot of 3 months or 6 months. You really have to look at the trend over a substantial period of time.

Again, drawing on the analogy with organized crime, I think if you looked at the performance of the effort in battling organized crime in a single year, you might not have seen much impact. If you look over a 10-year period, you see a tremendous impact.

The CHAIRMAN. Professor Sherman?

Professor SHERMAN. I am not sure that the cost is an unambiguous measure of the economics. The price of drugs shows lots of different factors contributing to that.

And it is I think much harder to demonstrate the impact of Customs enforcement activities on that in relation to the ultimate goal of reducing contraband than it would be use the ratio of detection to estimated shipments before and after some change in the strategy at a port of entry.

So if you wanted to take, for example, five ports of entry and beef up the resources, but to have them do different things, you could see by using the sampling method before and after that change where you had the biggest impact in the sample measured of how much contraband got through.

So I think it is one of the many uses to which you can put this kind of tool. And I would have a lot more confidence in measuring the impact, investing in strategies that have proven more effective with this approach than in simply looking at costs of drugs shipped.

The CHAIRMAN. Going back to your sampling, some of the measures taken to investigate are fairly invasive. If a citizen refuses to do it, what would you do under those circumstances?

Professor SHERMAN. I am certainly not here as a legal advisor on that issue, but I can point out that even under conditions in which citizens would be allowed to refuse the full search, merely establishing a random search as opposed to a targeted or probable cause search as a standard procedure could have an enormous deterrent effect, as indeed it has in Australia where random breath testing is the basis for drunk driving enforcement. And they have had a 60-percent reduction in lives lost since they undertook that, at least in New South Wales.

It seems to that merely the prospect that you could be selected at random which is what people essentially understand with re-

spect to their income taxes, although it is a bad subject to bring up I think in this committee, there is pretty good evidence that that creates a deterrent effect.

And I want to stress, the numbers here are very small. To do 2,000 randomly selected searches in one year at JFK in relation to the millions of people who go through there is a tiny drop in the bucket. So it is not as if you would be testing a substantial portion of all people coming in. That would slow up the flow of people in a very busy time.

You only need to do something in the order of 6 or 7 a day out of tens of thousands of people coming through. So I do not think it would be as intrusive necessarily as it might sound at first blush.

The CHAIRMAN. I was speaking of some complaints that we have had already on the part that some of the methods used are intrusive, but I appreciate your suggestion.

Mr. Rabkin?

Mr. RABKIN. I agree that the best measure to determine the Customs impact is to look at what is the percentage of the drugs they get compared to what they are missing, what is actually coming across the borders. And one way to do that is this random checking, this over sampling at both airports and other ports of entry, the seaports and the truck ports as they come in.

And it is being done. I was in Miami a couple of years ago at the airport where they were doing there, something they called compliance examinations or COMPEX where they would over sample and randomly ask people to go for it. And it was not the invasive type of inspection. It was just to have their baggage checked.

The people who were sent did not know that they were being sent either because the computer told them to go or it was the inspector saw something about the way they were behaving or the clothes they were wearing or the itinerary or any other factor. And the methodology the Customs was using there seemed to be sound and allowing them to make the kinds of judgments and reach conclusions that they were doing.

They had planned to do it elsewhere. It was, as I recall, going to require a little additional resources because they were going to have to have additional inspectors to do these additional inspections, especially costly for the cargo ports of entry where it ties up additional trucks and you have problems with space and things like that.

But I think it is also important to measure that while this is important at a strategic level at the operational level for the inspectors or the agents, the number of arrests and seizures that are made are important to them. There are ways to gauge the success of their daily activities. And so I would not discount those kinds of measures. I think they have their place.

The CHAIRMAN. Thank you.

Senator Grassley?

Senator GRASSLEY. Your GAO report talks about Federal interagency, counter drug intelligence coordination. And it seems to point out rightly that the Customs Service is the lead agency for interdicting drugs being smuggled into the United States, other agencies being the Department of Justice, the Treasury, the De-

fense. And these others account for over 90 percent of the money spent for the counter drug intelligence activities.

Could you tell us how good the interagency coordination really is?

Obviously, we in Congress cannot go out on counter drug missions that involve several agencies. We do not sit in on planning sessions and see firsthand results of this interagency efforts. So obviously, we depend upon you to tell us what works and what does not, whether we need more resources and better cooperation.

And I know it is not easy to sit where you are and be critical of one specific or other Federal agencies if that is what needed, but it seems to me that we need to have you be very forthright with us. Where are the gaps? And what has to be done better?

Mr. RABKIN. Senator Grassley, I wish I could answer that question as thoroughly as you have asked it, but unfortunately, we have not done the kind of work to identify specifically on an operational level whether there is adequate cooperation and coordination among all the agencies that are involved.

There is a lot of work that is being done to look at the architecture of the drug intelligence networking community. OMBCP has done some work and is in the process of reporting out on that.

From what I have observed and from what our work has shown at an operational level, the limited work that we have done, there is coordination and cooperation among agents, among inspectors at the border, agents that are stationed around the country and overseas. There is an exchange of information.

Whether it is enough, fast enough or whether it is used appropriately are questions that we have not looked at and I cannot answer at this time.

Senator GRASSLEY. All right. Is it a matter of your not having been asked to look at them or you would not have the resources to do it if you were asked to look at that?

Mr. RABKIN. We have not been asked. I think we would have the resources to do it. But it would be in terms of resources, we have a limited number of people who have the appropriate clearances to get involved in this kind of work. It is getting the agencies to share the intelligence with us and then to follow up and to see how it was used and to make some judgments about how it should have been used. So if asked, I think we could probably do some work in that area.

Senator GRASSLEY. The Customs Service has enforcement authority not only over substances that are brought into this country, but also for things like control technology.

Last week, I asked Commissioner Kelly about interagency enforcement efforts directed at end-use verification, particularly for sensitive, dual-use technology that is shipped to China.

I was specifically interested in the coordination of end-use verification and enforcement efforts between the Customs Service and the Commerce Department's Bureau of Export Administration. Commissioner Kelly told me that interagency coordination, and he said this very candidly, could be better.

I am concerned that in looking at the effectiveness of the Customs Service, it is important to look at more than outcomes, processes, resources, and evaluation methods.

Where there is shared bureaucratic responsibility for a vital important mission like protecting our National security, it is very important to look at how well agencies work together or how well they do not work together.

Has your evaluation looked at the effectiveness of interagency coordination in this critical important area that affects our National security? And if you have not, why not?

Mr. RABKIN. My group has not. We have been focusing on the law enforcement and the drug interdiction efforts. We have other groups that deal with trade issues. And I am just not sure whether they looked at this issue or not. I would certainly check into it and get back to you on that.

Senator GRASSLEY. Would you do that and give us a contact person?

Mr. RABKIN. Certainly.

Senator GRASSLEY. Have you ever been denied information directly or indirectly, such as not complying with document requests or thwarting access to individuals by the government about the effectiveness of interagency coordination or about the effectiveness of any other element of the Federal Government's efforts to monitor and control highly sensitive technology?

Mr. RABKIN. I cannot answer that question about technologies. I can answer about other things we have done with the Customs Service.

Senator GRASSLEY. All right. Then, do two things for me. Answer about what you can talk about and then give us, again, an answer in writing in regard to the dual-use technology and highly sensitive technology.

Mr. RABKIN. We worked with the Customs Service recently on some issues involving the corruption. And we did for the caucus that you chair. And during the course of that work, we had asked the Customs Service to provide us files on the investigations of allegations of corruption that they had received and cases that had been prosecuted.

And while we eventually got that information, it did take a little while. And there were some redactions that the Customs Service had to make of that.

We are also doing some work with the Customs Service now looking at airport inspections. And because of the sensitivity of that work and ongoing litigation, the access to people and documents is slow, but we understand that. And we are working with them on that.

And I will get back to you in writing on any problems with the dual-use technology.

Senator GRASSLEY. You say it is going slow, but are you getting what you call cooperation?

Mr. RABKIN. Yes, we are.

Senator GRASSLEY. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Grassley.

Senator Graham.

Senator GRAHAM. Thank you, Mr. Chairman. The first witness talked about the fact that people in his business would look for where the softest spot was in order to find where they would try to bring drugs into the United States. If the soft spot was the Car-

ibbean, through their own aircraft and boats, they would do that. If the soft spot was commercial traffic through New York, they would do that.

What is your sense of the Customs current ability to allocate its resources so that there is a relatively uniformed level of enforcement at each of the points of entry, i.e. to provide creating these soft areas for exportation?

Professor SHERMAN. Senator Graham, I think that requires a two-part answer. The first part is with respect to ports of entry where I think the answer is that the current information available to the management is very weak, if not nonexistent with respect to this ratio of drugs detected to drugs being shipped through that port.

But with a really modest investment in terms of the overall budget in an annual sample of both cargo units and persons coming in relatively non-intrusive inspections, it is possible to get that estimate and to reallocate resources to try to if not equalize the ratio of detection to shipment, then to try to go where the greatest amounts are coming in and to get the detection ratio in those ports of entry to the point where you are getting maximum prevention of contraband getting into the country.

I think there is a whole different with respect to non-port of entry borders. I know much less about it. I do not travel in and out of the country through those borders the way I do the airports and other controlled ports of entry, but I think that the same principle applies, that is that whatever enforcement is going on there can be the use of random selection methods rather than probable cause in a way that would allow an estimate of what the average annual amount of shipment is, for example, across the Gulf of Mexico or the coast of Florida in whatever enforcement is being done there and perhaps coordinating with the Coast Guard and other agencies that are also engaged in patrolling those borders, border patrol on land and so on in a way that compiles the information and helps to improve the management information available, not only to the Customs Service, but also to this committee in looking at the Results Act in a meaningful way in terms of the results of enforcement for the amount of contraband getting through.

I think that information is missing. And until we have it, it is not going to be possible to meaningfully apply the Results Act to Customs enforcement.

Mr. CHERTOFF. Senator, my sense is that you kind of put your finger on what I think is a traditional problem with the approach to this. And the problem would be too statistically driven. There will never be enough agents and resources to really protect all the areas of the border.

And the people who import drugs are not stupid. They can see where there are shifts of enforcement. And they shift their methods of importation. So what you are measuring is what happened yesterday. You are not preventing what will happen tomorrow.

And I am not saying you should not do some of that, but if that becomes your exclusive way of deciding how you are going to allocate your resources, that is all you are going to do.

My suggestion is that in addition to the process of allocating resources on that method of measuring, we look at trying to be what

they say in the trade as proactive. We try to identify institutions and organizations that are particularly skilled at bringing in narcotics and do have the ability to be flexible. And we try to take down those organizations either by arresting people and incapacitating them or by choking off the methods that they use to reclaim the money and the profits or by addressing the infrastructure that allows them to bring the drugs in.

And I think if you err too much on the side of measuring statistical performance or numbers of arrests, you wind up driving yourself away from that kind of qualitative case building which you need for an effective program.

Senator GRAHAM. Let me ask a follow-up question to the first. And if, Mr. Rabkin, you would like to comment on both questions.

Currently, the Customs has employed a private consultant to evaluate its allocation of resources. What advice would you give to that consultant as to what factors it ought to look at in terms of achieving the goal of maximizing the allocation of resources towards the goal of maximizing the reduction of contraband flowing into the United States.

Mr. CHERTOFF. I guess I would go first. I think I would sit down first and look not only at the strategic plan that Customs has with respect to narcotics enforcement if you are looking at narcotics, but I would look at the entire program across the board because you cannot really evaluate Customs without looking at DEA and even these local task forces that we have.

And what I would try to do is have an qualitative evaluation of how much effort Customs ought to be putting into strategic work as opposed to other agencies. Once I answered that question, I could then—and you would have to discuss it with the people who run the agency. Then, I would sit down and say if we are going to spend X amount of more effort on reactive interdiction, we need to come up with a way of measuring and being very flexible about deploying resources as we detect shifts in patterns of traffic.

And then, to the extent we are going to be strategic, we need to have a pretty rigorous system of evaluating what are the targets we ought to be selecting.

So I would start at the top. And I would try to get a sense of what the policy is. And then, I would work my way down.

Mr. RABKIN. I would like to start by suggesting that I know the Customs Service is a very complex organization, but let us look at it in two parts. One is the inspector that you see at the ports of entry. And the others are the investigators and the special agents that do the investigative work behind the scenes.

And we have reported that the Customs Service needs a better way of allocating the resources around the country to the ports and to the special agent in charge of the SAC offices for the investigators. It needs to be data driven. It needs to be repetitive, etcetera.

And I think that is why they hired the consultant. I think it is easier to move the agents around in response to changes and threat to work with the other agencies.

The investigators are much more flexible, much more mobile. And Customs as an organization can move them around a little easier.

The inspectors, however, I think it is a little more difficult for the Customs Service to move them around. It is much more difficult for the Customs Service to figure out how many they need in each port. That number is driven to a large extent by the volume of traffic that comes through the port, but it is also driven by the threat.

And I think while the Customs is trying to get better data on volume and historical as well as projected volume, being able to quantify threat and then apply that to this model, to be able to predict how many inspectors you need to look at the trucks and look at the containers that come off the ships and look at the passengers that come off the planes is much more difficult.

And I think that is where I would focus as to how they are doing that, now whether they are using some of the samples that Mr. Sherman talked about or some other ways to do it, but there are ought to be some data-driven basis for that.

Professor SHERMAN. And, Senator, I would think that within the confines of the contract depending on resources one thing they could is to try out this method of sampling in, say, 5 major ports of entry where there is high volume already and see indeed how much difference there is across the ports of entry in this ratio of detected to estimated shipped contraband.

And I suspect that if it is done in a way that includes an evaluation of the citizens and foreign visitors, their reaction to this and whether they thought it was handled in a polite way and whether they had constitutional concerns and so forth that we could learn from trying this out in a way that would lead to the decision about whether to go further or whether to abandon the idea.

We could also then in terms of the assignment issue, I think the first time the sampling might be done nationally, you would consider a long-term shift in inspectors. It probably would not have that much of a year-to-year shift barring radical changes in the patterns of shipments from different countries.

But even in terms of Mr. Chertoff's very useful suggestion of identifying major institutions and organization for proactive targeting, I think that again being systematic, creating a list of those having some basis for estimating the volume of contraband associated with them, and setting some priorities in terms of a set of principles, and then tracking year-to-year in reporting back to this committee the success of the agency in taking out those organizations. That all is part of this broader piece of looking at results in as systematic a way that we can independent of simply looking at the outputs of the organization. So I think your consulting firm is just the right thing at this stage of developing the Results Act which I must say is not uniquely Customs. I think it is true throughout the Federal Government that everybody is wrestling with how we meaningfully produce the outcome measures that American citizens want to know.

Senator GRAHAM. Thank you.

The CHAIRMAN. Thank you, gentlemen. This panel has been very helpful. We appreciate you being here today. We will keep the record open for written questions until this evening. But we appreciate your contribution and look forward to working with you.

The committee is in recess.

[Whereupon, at 11:47 a.m., the hearing was recessed.]

THE U.S. CUSTOMS SERVICE: ENSURING EFFECTIVENESS, INTEGRITY, AND ACCOUNTABILITY IN CUSTOMS OPERATIONS

TUESDAY, MAY 25, 1999

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 11:00 a.m., in room SD–215, Dirksen Senate Office Building, Hon. William V. Roth, Jr., (chairman of the committee) presiding.

Also present: Senators Grassley, Moynihan, and Graham.

OPENING STATEMENT OF HON. WILLIAM V. ROTH, JR., A U.S. SENATOR FROM DELAWARE, CHAIRMAN, COMMITTEE ON FINANCE

The CHAIRMAN. The committee will please come to order.

I apologize to our witnesses. In the good old days, we had hearings in the morning and Senate business in the afternoon. But that is no longer true and, consequently, we became unavoidably delayed.

I have a brilliant opening statement, Pat, but I will not read it and just ask that it be included in the record. I would call upon you for any comments you would care to make.

[The prepared statement of Chairman Roth appears in the appendix.]

OPENING STATEMENT OF HON. DANIEL PATRICK MOYNIHAN, A U.S. SENATOR FROM NEW YORK

Senator MOYNIHAN. It is a little early for brilliance. I think you are probably right in that regard. I will be equally restrained in my statement. But, also, Mr. Chairman, the Commissioner of Customs, Mr. Kelly, has asked me to place in the record for him the special report that he has had produced with respect to these matters, and the orders he had issued immediately on learning of the situation in Miami, which we are going to deal with today.

I would appreciate it if those would be placed in the record.

The CHAIRMAN. Without objection.

[The prepared statement of Senator Moynihan and material submitted by Commissioner Kelly appear in the appendix.]

The CHAIRMAN. It is a pleasure to welcome our first panel, which consists of William Keefer, who is the Assistant Commissioner for the Office of Internal Affairs at the Customs Service; Hon. Milton

Mollen, in the firm of Graubard, Mollen, and Miller; Vincent Parolisi, who is the Director of Narcotics and Currency Inspection in the Office of Internal Affairs at the Customs Service; and Michael Tarr, the Acting IG for the Department of Treasury.

Judge Mollen, we would be pleased to start with you.

STATEMENT OF HON. MILTON MOLLEN, OF COUNSEL, GRAUBARD, MOLLEN AND MILLER, NEW YORK, NY

Mr. MOLLEN. Mr. Chairman, Senator Moynihan, I appreciate your invitation to appear before this committee to testify on the issue of Customs management, and more particularly with regard to the specific issue of combatting corruption within the Customs Service.

I believe that we are all aware that corruption is not a recent invention. One might reasonably argue that its history goes back to the Garden of Eden. Corruption, in various forms, has plagued society down through the ages and it is a particular concern when it affects law enforcement agencies.

A major mission of law enforcement agencies is to enforce the law and to inspire public confidence in the integrity of the government to which the public has entrusted its power to govern.

However, while we might hope for better, the fact is that law enforcement agencies mirror and reflect society at large, its strengths and its weaknesses. Most law enforcement personnel are trustworthy, dedicated, and committed to honorably fulfilling their responsibilities.

However, some are weak, vulnerable, and susceptible to the temptation of easy money. Others are just plain venal, who view public service as a means of using their power to illegally enrich themselves.

When we factor into the equation the enormous amounts of money involved in drug trades and money laundering, one can readily understand the concern about maintaining the integrity of the Customs Service and the necessity for constant vigilance, and for the creation and maintenance of internal and external safeguards to protect that integrity.

I would, therefore, humbly offer a few thoughts as to those means which I believe are most likely to achieve the goals of deterring corruption within the Customs Service to the fullest extent possible and to finding it and rooting it out where it exists.

These suggestions are based upon my experience and observations of many years, and in the executive and judicial branches of government, most recently as chairman of the New York City commission to investigate allegations of police corruption and the anticorruption procedures of the police department more commonly known as the Mollen Commission.

I strongly believe that the battle to combat corruption in agencies such as the Customs Service must be comprehensive and multifaceted. It must commence with the recruitment process, by reaching out for and attracting the right kind of candidates, and conducting proper and expeditious investigations prior to appointment.

Thereafter, there should be appropriate training, with emphasis on integrity, in terms of adequate time devoted to such training, and with the effective, substantive material utilizing updated tech-

nology. The training should not be confined to newly appointed agents. There should be refresher courses at appropriate intervals.

After the agents are sent into the field, it is essential that there be effective supervision. I recognize that this is not easily achieved in an agency which is spread out as widely as the Customs Service. However, I believe that with a leadership firmly and totally committed to maintaining the integrity of this service, the goal can, and will, be achieved.

Obviously, the leadership must be given adequate resources in order to accomplish this objective. I am convinced that, with reasonable appropriation of funds and with prudent management, the mission can be accomplished.

I am firmly convinced that, with adequate resources and the implementation of a policy of strict accountability at each level of authority, a leadership fully committed to the maintenance of integrity can succeed in achieving that goal.

At this point, I would like to take note of two actions taken by Commissioner Kelly which I believe are salutary and important in spreading the right message and effecting positive change within the Service.

One, was his altering the chain of command to provide for direct reporting of the Assistant Commissioner for Internal Affairs directly to the Commissioner. This change in process should result in the Commissioner being constantly informed and aware of any integrity or misconduct problems in the Service and enable him to take prompt and effective action.

Second, I have been informed that Commissioner Kelly is instituting a selective form of rotation in and out of Internal Affairs. I believe that this approach will assist in changing the culture within the Service in a positive way.

I have noted that the recent Inspector General's report expresses some concerns regarding rotation. I can understand the concerns, but, on balance, and with judicious implementation, I believe such a program will be salutary.

In order to be truly effective, the effort to combat corruption must alter, in a positive manner, the existing culture within the Service. It has been my observation that, in most law enforcement agencies, there is a strong tendency to resent and hold in contempt the Internal Affairs unit.

A policy of rotating agents into Internal Affairs should ameliorate the customary perception and lead to an effective and more cooperative relationship between Internal Affairs and the other agents.

Lastly, I shall like to address a most important issue, that of sustaining the durability of any program for promoting integrity implemented by Commissioner Kelly. I have known Commissioner Kelly for approximately 10 years, and I have total faith in his integrity and in his ability.

I have enormous respect for him professionally, and high regard for him personally. I have no doubt that he will do his utmost to meet the challenge of improving the system for maintaining the integrity of the Customs Service.

However, I must note that my studies and experiences with struggles to achieve and maintain the integrity of law enforcement

agencies lead clearly and strongly to the conclusion that an essential ingredient in the long-range success in combatting corruption is the existence of some form of effective outside monitoring of the internal efforts in confronting corruption.

Most institutions are reluctant to, as they see it, expose their dirty laundry in public. They find all kinds of rationalizations to buttress their failures to make public what they perceive to be their shortcomings.

Furthermore, I am firmly convinced that if there exists an outside entity to monitor and review their success or failure in combatting corruption, it will result in a more sustained and more effective campaign to deter and root out corruption.

I have been informed that there are two possible instrumentalities for accomplishing this important result. One, is the Inspector General of the Treasury Department, the other, is the Office of Professional Responsibility. It may well be that either, or both, may provide the most successful means to accomplish the desired objective as long as independence and objectivity are the guiding factors.

Of one thing I have no doubt: to achieve the most effective means of establishing a long-range, ongoing, successful method of combatting corruption, it is essential that there exist a permanent monitor to work alongside of, and in cooperation with, the Commissioner in the difficult task of successfully confronting corruption and fulfilling the Customs Service's responsibility to the people of our country.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Mollen appears in the appendix.]

The CHAIRMAN. Thank you, Judge Mollen.

Mr. Parolisi, please.

STATEMENT OF VINCENT J. PAROLISI, FORMER INTERNAL AFFAIRS ADVISOR, OFFICE OF PROFESSIONAL RESPONSIBILITY, U.S. DEPARTMENT OF THE TREASURY; DIRECTOR, NARCOTICS AND CURRENCY INSPECTION, OFFICE OF INTERNAL AFFAIRS, U.S. CUSTOMS SERVICE, WASHINGTON, DC

Mr. PAROLISI. Thank you, Mr. Chairman, Senator Moynihan, and members of the committee for inviting me to testify on the findings and recommendations contained in the Office of Professional Responsibility's report and assessment of vulnerabilities to corruption and effectiveness of the Office of Internal Affairs, U.S. Customs Service.

I completed this review when I was the Internal Affairs Advisor at the Department of Treasury's Office of Professional Responsibility, and was a principal member of the OPR assessment team. I have been an employee of the U.S. Customs Service since May 9, 1999.

The purpose of OPR's review was to conduct a comprehensive review of integrity issues and other matters related to the potential vulnerability of the U.S. Customs Service to corruption, to include an examination of charges of professional misconduct and corruption as well as an analysis of the efficiency of the departmental and bureau internal affairs system pursuant to Congressional directive.

The review began under the direction of Raymond W. Kelly, then Under Secretary for Enforcement at the Department of Treasury.

While Under Secretary, Mr. Kelly recognized many management deficiencies within Customs and took action to improve the level of integrity and professionalism within the organization.

OPR did not uncover any evidence of systemic corruption within Customs. It did conclude, however, that the most formidable corruption threat facing Customs is the illegal drug trade. OPR also found that the Office of Internal Affairs is more reactionary than proactive in detecting and combatting corruption.

OPR identified eight factors which have weakened Customs' ability to confront issues of corruption. The following is a brief overview of those findings and recommendations which are discussed in more detail in my written testimony.

Until recently, the Office of Internal Affairs was on the same organizational level of Customs' other 10 Assistant Commissioners, reporting to the Commissioner through the Deputy Commissioner.

OPR recommended that the Commissioner realign the Office of Internal Affairs to give the Assistant Commissioner of Internal Affairs direct access to the Commissioner. This recommendation has been implemented by Commissioner Kelly.

OPR found that Customs' Office of Internal Affairs required new leadership. The mission of Internal Affairs is complex and demanding and requires aggressive leadership, which we found lacking.

OPR recommended that the Commissioner select a new Assistant Commissioner of Internal Affairs. In December of 1998, Commissioner Kelly selected Mr. William Keefer, who you will hear from shortly, as the new Assistant Commissioner of Internal Affairs.

OPR found that conflicts between the Office of Investigations and the Office of Internal Affairs has significantly interfered with the successful performance of Internal Affairs' operations. OPR recommended that the Commissioner establish conflict resolution strategies to rebuild positive relationships between these offices.

In February of this year, Commissioner Kelly issued a memorandum mandating cooperative measures be instituted between the two offices. OPR found that a uniform nationwide process is needed to ensure consistency in the recruitment and hiring of Customs inspectors. Shortcomings in monitoring practices had resulted in a backlog of approximately 5,600 periodic review investigations of employee background reinvestigations.

OPR recommended that Customs continue its work with the quality recruitment and hiring initiative and take affirmative action to resolve the backlog of periodic reinvestigations.

In response, Customs has appointed a national recruitment manager, and Commissioner Kelly has reprogrammed funds to eliminate the backlog in the period review investigations over a 2-year period.

OPR found that integrity training for Customs employees was inadequate for deterring corruption. OPR recommended that Customs create an Office of Training to coordinate and implement agency-wide training, and that the Assistant Commissioner of Internal Affairs should work cooperatively with this new office to ensure that adequate training becomes a priority for all Customs employees.

Prior to the release of the OPR report, Commissioner Kelly created the Office of Training and Development at the Assistant Com-

missioner level, and will soon be announcing the appointment of a new Assistant Commissioner for Training.

OPR found that Customs' disciplinary system was fragmented, resulting in perceived inequities in the application of discipline. Furthermore, the database used to record and track disciplinary cases did not allow for comparances or analysis of disciplinary matters.

OPR recommended that Customs redesign its disciplinary database system to provide information for evaluation and comparison, and that it establish a uniform internal mechanism for the adjudication of administrative discipline.

Customs is currently developing an integrated computer system which will allow for a single data query for specific allegations received, investigative findings, and the disciplinary results applied. In addition, Service-wide disciplinary review boards have been implemented.

Finally, OPR conducted a quantitative and qualitative assessment of the Office of Internal Affairs and found that Internal Affairs was not focusing sufficient attention on more serious criminal investigations, nor effectively using its investigative resources.

A significant number of recommendations were made to correct these deficiencies, to include centralizing the operation of Internal Affairs' case management system at headquarters.

Recently, Internal Affairs has established an intake review group at headquarters which will have the responsibility to assess and process all allegations in a structured, uniform environment.

Over the past several months, Commissioner Kelly has implemented changes consistent with OPR's recommendations. I appreciate the committee's interest in this very important issue, and believe that this committee's continued oversight of the Customs Service is not only warranted, but an added benefit in the fight against corruption.

This concludes my testimony. I look forward to answering any questions the committee might have. Thank you.

[The prepared statement of Mr. Parolisi appears in the appendix.]

The CHAIRMAN. Thank you.

Now we will hear from Mr. Keefer.

STATEMENT OF WILLIAM A. KEEFER, ASSISTANT COMMISSIONER, OFFICE OF INTERNAL AFFAIRS, U.S. CUSTOMS SERVICE, WASHINGTON, DC

Mr. KEEFER. Chairman Roth, Senator Moynihan, thank you for the opportunity to appear before you today. I am pleased to have the opportunity to discuss Commissioner Kelly's actions to reinforce the organizational integrity of Customs.

You have my written statement, I believe, and I would like to add a few comments this morning.

The CHAIRMAN. The full statements of the panel will be included as if read.

Mr. KEEFER. Thank you, sir.

[The prepared statement of Mr. Keefer appears in the appendix.]

Mr. KEEFER. Before I was appointed Assistant Commissioner for Internal Affairs in February, I was a career Federal prosecutor.

During 23 years with the Department of Justice, I had a number of jobs, including interim United States Attorney, and Deputy Chief of the Public Integrity Section of the Department of Justice.

I have a wealth of experience in the investigation and prosecution of corruption cases around the country. That is a long way of saying that I knew what I was getting into when I took this job. I look forward to the challenges and the opportunities ahead.

As you know, every internal and external review of Customs has concluded that no systemic corruption exists within the agency. While instances of corruption in Customs are few, we have not done a good job in responding to allegations of misconduct.

Under Commissioner Kelly's leadership, we are moving rapidly to fix the problem and to make changes that will remain in place regardless of who heads the agency in the future.

To elevate the issue of integrity at Customs, Commissioner Kelly took several important steps. First, he placed Internal Affairs under his direct supervision. I report to him.

The Commissioner also upgraded several critical positions at Internal Affairs, headquarters, and in the field. He made them SES positions, bringing them into parity, for the first time, with supervisors in the Office of Investigations and with other Federal law enforcement agencies. These new, permanent positions will attract the highest caliber of applicants, and the benefit to Internal Affairs will both be immediate and lasting.

I would like to, briefly, highlight some of the other reforms that the Commissioner is implementing. The old practice of reporting misconduct allegations to Internal Affairs was fractured, and sometimes misused.

To correct the problem, every allegation of misconduct, without exception, is now being reported directly to my office. Every allegation is now being tracked by my office. Every allegation is now being classified by my office.

This new procedure is simple, unambiguous, and ensures accountability. We have a fully-staffed, 24-hour hotline to make sure that misconduct allegations are reported in a timely manner.

The new allegation intake system triggers two important accountability processes. First, a retrievable computer record is created to follow the allegation from receipt to final disposition. Second, specific time limits have been incorporated into the new procedures. We require frequent case reviews by field supervisors, tracked at headquarters.

Final investigative reports are closely reviewed at headquarters, and every final report will include a finding for each allegation investigation by Internal Affairs.

In my view, failure to follow viable leads or to interview knowledgeable witnesses is inexcusable. An untimely report is a useless report. These are failings of supervision, both in the field and at headquarters, and they will not be tolerated.

In its report, the Inspector General stated that Customs has no published directive for conducting management inquiries and that there is no oversight review of them by Internal Affairs. That is not correct.

The Commissioner issued a directive on management inquiries dated April 13, 1999 which, among other things, mandates over-

sight by Internal Affairs. I have that directive available for the committee, if you desire.

An important initiative that we have undertaken is a Special Investigative Unit, which is now being formed at Customs' headquarters, which will handle the most serious and high-level cases. These senior agents, GS-14s, will report directly to me.

They will also quickly and efficiently handle misconduct allegations of SES and GS-15 personnel when the inspector returns those cases to Customs for investigations, which they do in about 90 percent of those cases.

To improve cooperation and effectiveness between the Office of Investigations and Internal Affairs, the Commissioner has instituted a rotation process for senior agents at all levels between the offices.

We think rotation is appropriate, and respectfully disagree with the Inspector General's report regarding rotation. Most of our investigations do not involve the Office of Investigations. For those few that do, impartiality can be ensured through a clear recusal policy and effective supervision.

Retaliation and the fear of retaliation have been persistent issues at Customs. We are addressing this problem through better training of our Internal Affairs personnel and by specifically informing managers who are interviewed in retaliation investigations about the rules against retaliation.

Those being considered for promotion now undergo a vetting process in which their disciplinary history is scrutinized before any action is taken, and Assistant Commissioners are held accountable for that process.

Nothing is more important to law enforcement than integrity. Commissioner Kelly is committed to doing whatever it takes to make Internal Affairs succeed in this critical mission.

Thank you very much for your time and attention. I am prepared to answer your questions.

The CHAIRMAN. Thank you.

Now it is my pleasure to call upon Michael C. Tarr, who is the Acting Assistant Inspector General for Investigations. Mr. Tarr?

STATEMENT OF MICHAEL C. TARR, ACTING ASSISTANT INSPECTOR GENERAL, U.S. DEPARTMENT OF THE TREASURY, WASHINGTON, DC

Mr. TARR. Chairman Roth, members of the committee, I appreciate the opportunity to discuss with you today the results of our investigation at the U.S. Customs Service.

On Sunday, December 13, 1998, the Miami Herald published a special report entitled, "U.S. Customs: A Culture of Favoritism." On December 17, 1998, Senator Roth requested that our office conduct an independent review of the allegations outlined in the Miami Herald article concerning the Customs Service's "ability to effectively assess allegations of mismanagement within the agency and impose appropriate discipline where warranted."

Since this request related directly to the allegations of agency mismanagement and inappropriate disciplinary practices dating back to 1986, the Office of the Inspector General concentrated its

initial phase of the review on files relevant to allegations in the article.

The purpose of the review was to determine the effectiveness of investigations conducted by the U.S. Customs' Office of Internal Affairs, review the basis for the claims of management failure, and assess the application of penalties based upon established policies within the Customs Service.

In further discussions with this committee, it was requested that we expand the scope of our review to include additional Internal Affairs investigations and address additional concerns regarding employee perceptions of Customs' Internal Affairs.

We visited Internal Affairs offices in 13 cities and reviewed 395 closed investigations for fiscal years 1997 and 1998. These reviews were conducted to determine if similar deficiencies as those addressed in the Miami Herald were also present in other offices.

We conducted over 500 interviews of Customs employees concerning the role of Internal Affairs, the application of discipline within Customs, and the fear, if any, of retaliation from management for reporting wrongdoing.

During our review of 50 Internal Affairs files relating to individuals named in the Miami Herald article, we found evidence that Customs' Internal Affairs investigators did not exhaust all relevant leads or interview all knowledgeable witnesses that may have substantiated or refuted an allegation.

The inadequacies identified during our review suggest that the lack of supervisory review, both at the field office and headquarters level, contributed to an inferior quality of investigation.

We found a number of instances in which Internal Affairs investigations failed to comply with proper reporting requirements stated in the Customs' Internal Affairs handbook.

We identified serious misconduct allegations that were initially referred to Internal Affairs for investigation that were subsequently referred to Customs' management for inquiry.

We found there are no published directives for conducting management inquiries with the Customs Service, and there is no oversight review by Internal Affairs to ensure thoroughness.

We also found the use of management inquiries exposed the sources of the allegations, which may tend to erode employee confidence in Internal Affairs. We determined that disciplinary penalties were inconsistently applied.

Customs' inability to equity administer discipline fosters the perception of favoritism. We found that awards and promotions were issued to employees who were the subject of Internal Affairs investigations. That is a direct violation of Customs' policy.

In expanding the scope of our review, we requested that Internal Affairs provide a comprehensive and complete report from their automated case management system, listing all closed internal investigations for fiscal years 1997 and 1998.

We determined that the case management system report did not conform with field office files and, in many cases, was inaccurate and incomplete. We reviewed 395 closed internal affairs files and found many of the same problems that we identified in the Miami Herald review. Investigations failed to comply with proper report-

ing requirements, lacked thoroughness, timeliness, and did not receive quality management review.

During our interviews with over 500 Customs employees, many expressed their lack of confidence in the Internal Affairs program. Concerns were raised regarding impartiality, confidentiality, and investigative quality. Some employees were fearful of retaliation from management for reported alleged wrongdoing to Internal Affairs, and were concerned that Internal Affairs forwarded too many allegations to management for inquiry.

Our review disclosed that there was no standard policy on the issue of special agent rotation between the Office of Investigation and the Office of Internal Affairs. However, Customs is currently proposing rotating special agents between Investigations and Internal Affairs by reassigning the agents within the same geographic area.

The Office of Inspector General believes that this proposal may call into question the objectivity of Internal Affairs agents. In addition, it may give the impression of agents investigating themselves. Objectivity is critical to overall employee confidence in the Customs' integrity program.

The problems we found in our review of Customs are issues which the Office of Inspector General should have identified over the years. Had a thorough oversight process occurred, some of the problems would have been identified sooner, and others less likely to have occurred as a result.

We have made some organization and staffing changes during the past year and we are undertaking other initiatives to reestablish a firm understanding of the oversight role of the Office of Inspector General with Customs.

The Office of Inspector General believes that the challenge of any substantial and long-lasting change in Customs must be management led and policy driven. We look forward to assisting Customs and sharing the responsibility to bring about the changes necessary.

Mr. Chairman and members of the committee, this concludes my testimony and I will be pleased to answer your questions at this time.

[The prepared statement of Mr. Tarr appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Tarr.

Let me ask you this. To what extent do your findings relating to the Miami Herald allegations indicate a more widespread problem of mismanagement, misconduct and corruption within Customs than generally thought?

Mr. TARR. As I indicated in my statement, we found, on a parallel track with the Miami Herald allegations, instances where investigations conducted by Internal Affairs had occasions where interviews were not conducted of all potential witnesses that should have been done; there were issues of timeliness as well in those reports. So I would say that they ran on a parallel track with some of the Customs allegations. We did not uncover any allegations or substantiate any issues of corruption.

The CHAIRMAN. I would like to ask the panel this question. Three recent reports have identified structural, operational, and management problems that have hampered Customs' ability to identify, in-

vestigate, and punish misconduct and corruption. Such problems have been apparently identified in the past and, despite proposed solutions, persist today.

Would each of you please comment on what you think needs to change, internally and externally, to ensure that Customs responds decisively and effectively to the misconduct and corruption charges. Do you want to start, Mr. Parolisi?

Mr. PAROLISI. Yes, Mr. Chairman. Quite frankly, I think the change has already happened. That change is the new leadership within the Customs Service, particularly with the appointment of Commissioner Kelly as the head of the agency and the appointment of Mr. Keefer as the new leader of the Internal Affairs Division.

I think that is the most significant thing that could happen at Customs, is a new leadership team to take Customs in a new direction. I believe that that is the most important step, and it has already been taken.

The CHAIRMAN. Mr. Mollen, please.

Mr. MOLLEN. Mr. Chairman, I believe that there has to be strong, effective leadership from the top. I think it is now being supplied by Commissioner Kelly, with the assistance of Mr. Keefer.

I think the message has to go out that there will be zero tolerance for corruption or incompetence. I think that, in order to implement that, there must be a strong sense of accountability. That message must go throughout the Service, that each and every official at every level of performance will be held accountable for proper performance.

I think it is absolutely essential to get that message across. At the same time, I think that there must be a sensitivity to an awareness effort to modify the culture within the Service, the prevalent thought processes that go on day in and day out among the members of the Service.

They must understand that there will be this zero tolerance for corruption, that there will be this drive for competence in dealing with the complaints and problems and just ordinary management and structural issues.

If that is done, and I believe it is in the process of being done, I agree with Mr. Parolisi, I think with that kind of leadership and that kind of effort, that the problem can be, at the very least, contained to a minimal degree, if not totally dealt with effectively.

The CHAIRMAN. When you say zero tolerance, could you define what you mean by that?

Mr. MOLLEN. I mean that any form of corruption or venality should, at the very least, result in the immediate dismissal from the Service and, where facts lend themselves, to prosecution through the criminal justice system. If that message goes out, I think that this will have some tendency to curb people.

We have found in our experience that there are all types of people who do engage in various degrees of corruption. There are some who are just plain, corrupt people, venal people. They obviously must be driven out wherever they are found.

But, in addition to that, there are people who are weak and who have a tendency to ride with the wave, so to speak. If they know and they understand that there will be no tolerance for any misconduct, I think that they will be saved from themselves and some

of their weaker instincts to start, sometimes, with petty corruption, and then it develops into major corruption.

So, if they understand that the governing pathology of the department, of the Service here, the Customs Service, is that it will not tolerate corruption or misconduct, I think this will have a very salutary impact on the Service as a whole.

The CHAIRMAN. Let me ask you one further question. You talk about cultural change. How long is that going to take to come about, and how do we ensure that that continues?

Mr. MOLLEN. In terms of totality, it will take a long time. But it is done incrementally. Change takes place and is a constant progress. If the message goes out loud and clear from the Commissioner and his supervisors, it will get across to the bulk of the members of the Service. I am convinced that this will occur.

Now, one of the aspects of it, and that is why I happen to agree with the Commissioner and somewhat disagree with the Inspector General's report, is, in my experience, the other members of a law enforcement agency, whichever agency it is, almost invariably I found they have total contempt for the internal affairs mechanisms.

They think that they are incompetent and they do not trust them. To use the common expression, they think their function is to "rat out" their fellow colleagues. They think that people go that route because it enables them to get a quick promotion, and that they are basically not competent.

If, instead, you do have a rotation system, as is apparently being implemented by Commissioner Kelly, that becomes part of a regular procedure within the department and it is no longer seen as a deterrence to advancement within the Customs Service, if it is seen as a form of service that every agent will have an opportunity to do, it will stop this "us against them" culture which exists throughout many law enforcement agencies where they perceive the internal affairs unit to be the enemy, and to be an incompetent, weak enemy for whom they have contempt and which imposes no sense of fear in the individual agents that, we must be honest, otherwise Internal Affairs might get us. They feel Internal Affairs is incompetent and they just have no respect for them.

If you break that down, that culture, that is one aspect of the cultural problem, I think it will be a very important factor in improving the integrity of the system.

The CHAIRMAN. Thank you.

Mr. Keefer?

Mr. KEEFER. I would respectfully suggest that the breadth and the scope of the changes that Commissioner Kelly has undertaken here is really unprecedented, that it is not comparable to previous responses that Customs has done.

To the extent that structural problems have been identified, they have been addressed. To the extent that other problems have been identified, I think those revolve around issues of supervision and resources. Those are things that good leadership can fix.

So, I think all we need now are the resources and the time to watch these changes that the Commissioner has instituted take effect.

The CHAIRMAN. Mr. Tarr?

Mr. TARR. A couple of points. I indicated earlier that long-lasting change is management-led and policy-driven. Mr. Keefer has referred to some of those policy changes. But the key, it seems to me, is the unwavering commitment at all levels within Customs and holding Customs' managers accountable. Not Internal Affairs' managers, I believe managers throughout the entire Customs Service, irrespective of the location, whether it is investigations, administrative, or another discipline.

Externally, I would say, certainly, the Treasury Inspector General has a role to play. It is time to reassert the oversight role that this office should have been playing for the last few years. So, with respect to the external impact on this program, there is a role for the IG to play.

The CHAIRMAN. Now I will call on Senator Moynihan.

Senator MOYNIHAN. Thank you. Mr. Chairman, it is an honor for this committee to have before it such a distinguished man as Judge Mollen, known throughout the world, certainly throughout New York, for his perceptions in these regards.

I would say, and I do not want to ask you to say more than you wish, but would you not be much encouraged by what you have heard this morning, your Honor?

Mr. MOLLEN. Yes, I certainly am. When I read the Inspector General's report and the OPR report, I was somewhat discouraged. But I have heard the steps that have been taken by Commissioner Kelly to address the issues presented in those reports and, in listening today to my colleagues here on the panel, I am encouraged. You are absolutely correct, Senator. Thank you for your gracious comment.

Senator MOYNIHAN. Thank you for what you have said. It is not too much to note that the person you are talking about is sitting behind you. He slipped in. Commissioner, welcome.

Mr. Tarr, you said you did not find any systemic corruption in your inquiry in the Miami situation.

Mr. TARR. That is correct, Senator.

Senator MOYNIHAN. Yes. I mean, all life goes on. There are going to be incidents. But, as much as you can think your way through a problem like this, it seems to me you have done. I was very much impressed by your comment, Judge Mollen, on the idea of rotation in Internal Affairs and not set that job apart, those are they, we are here, and they are trying to get something on us. That is an important idea, is it not?

Mr. MOLLEN. I think so. I know that Commissioner Kelly instituted, or commenced the institution, of that reform within the New York City Police Department before he left that department. I think it was a most salutary policy and act.

I noticed, during the 2 years of our investigation, we spoke to many members of the department of all ranks. There was one uniform view of Internal Affairs, and that was total contempt. That was expressed at all levels of authority. There was very much this "us against them" attitude.

I think that, when Commissioner Kelly instituted that in the department, it was very beneficial to the department and it changed what was considered to be a career deterrent into a career en-

hancement program, among other results. So, I look with great favor upon it.

I understand the concerns expressed by Mr. Tarr and by the Inspector General's report, but I think they can be dealt with. There are very few cures for any disease that do not have some side effects that have to be addressed. I have faith in Commissioner Kelly and Mr. Keefer and their ability to address those potential side effects. I think they can be kept in check. The major result will be a very salutary one.

Senator MOYNIHAN. Well, more, I could not hope to hear. We were quite prepared to hear the opposite, if that was your judgment, if those were your findings. But I find myself very much encouraged and wish we could see the same elsewhere. But, thank you, your Honor. It is, again, a great privilege for this committee to have you come down for this purpose, and we are most appreciative. Thank you all.

The CHAIRMAN. Senator Graham?

Senator GRAHAM. Thank you, Mr. Chairman. Thank you for holding this, and the series of hearings that have given us the opportunity to focus on the operations of a very important and often under-appreciated U.S. agency, the Customs Service.

On the issue of integrity and accountability, the Customs operates typically in facilities that are not under Federal Government control. They are typically a local seaport or a local airport which is managed by a governmental body elected or appointed from the community that it serves.

To what degree does that relationship create problems for the Customs in terms of security and integrity? Unfortunately, the series of articles that Mr. Tarr discussed in the Miami Herald have had as one of their major themes the issue of corruption at the local level within the ports that then the Customs are given the responsibility of enforcing, tax collection and the proper movement of passengers and cargo.

Mr. TARR. Senator, I would respond that the focus of our inquiry, again, was on the issues raised in the Miami Herald article. I indicated to Senator Moynihan that there were no basic issues or systemic kinds of corruption issues.

With respect to the facilities that Customs must utilize in the course of their duties, frankly, I do not think that was much of a focus for us. I think, perhaps, Mr. Keefer may be more qualified than I to respond to that issue.

Mr. KEEFER. Senator, as I am sure you are aware, there have been a number of investigations by Customs and other agencies in Miami involving criminal conspiracies between Customs employees and sometimes State and local police officers or security guards, and those kinds of things. Those are continuing issues. We have a number of initiatives right now in that area. It is a continuing problem not only in Miami, but elsewhere.

Senator GRAHAM. Because of the history of the two, there tends to have been a greater degree of Federal regulation and control over airports than over seaports. As an example, in the South Florida area it has been common for 15 or 20 years for personnel, whoever their employer happens to be, to be subject to security checks

if they work at the airport. But that is not the case of persons who hold similar positions at the seaport.

Do you have any recommendations as to what Federal policy should be relative to non-Federal personnel who are working in environments that are then subject to supervision, enforcement, and tax collection measures by the U.S. Customs?

Mr. KEEFER. I would have to get back to you on that, Senator. I know that we have looked recently at the civilian personnel who were involved in our burn facilities where narcotics are destroyed. As you know, there was an incident in Tucson not too long ago in which that became a serious problem.

Senator GRAHAM. Other agencies, particularly in the intelligence community, have had a tradition of using techniques such as polygraphs and financial records as a means of initial employment screening and ongoing observation after employment. To what degree do you believe those kinds of things would be an appropriate addition to the Customs Service?

Mr. KEEFER. We very much support those initiatives. I believe we are poised to receive authority, renewable authority, to get polygraph examinations of agents now, pre-employment. I think that will be a very positive goal and we are certainly in favor of that, and also additional financial background matters. Yes, sir.

Senator GRAHAM. Mr. Mollen talked about the issue of mobility within the workforce in order to break up this "us versus them" issue. There is another aspect of mobility within the Customs Service, and that is, a person is felt to be hired to work at a specific site, like the JFK airport or the port of Long Beach. Should consideration be given to a geographic mobility over a period of employment of Customs agents so they do not become so site-specific?

Mr. KEEFER. I believe that Customs looks at these things in different ways. Agents expect to move around quite a bit, and should anticipate that. That is a part of their job description. Inspectors and other personnel may not have that expectation and that plays a considerable role, as well as money, in the rotation issue for them. That is an issue that we are studying very closely right now.

Senator GRAHAM. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Mr. Parolisi, and you, Mr. Tarr, and maybe others will comment, too, OPR, I think you said in your report, did not uncover any evidence of organized corruption within Customs. But it also concluded that the true extent of corruption cannot be accurately determined. Is there a way for Customs to determine the extent and nature of corruption within the agency?

Mr. PAROLISI. Senator, that is a very interesting question. One of the problems that I think exists when one tries to determine the level of corruption, is there is not a standard definition of what corruption is. You have all these different variations of what constitutes corruption.

So, the first problem you have, is identifying and defining what we mean by corruption. The second problem, as I see it, is there is a whole universe of information out there that goes unreported, so you truly do not know the total population of complaints.

Many instances of misconduct and corruption take place which are never reported to the agency. So, it is very difficult to get your

arms around those two things in order to make a truly accurate assessment of the level of corruption in any organization, including the Customs Service.

What you can do, is you can look at trends and patterns, you can look at statistical data, which are indicators of what direction you are proceeding in. But it is very difficult, in my view, to accurately give a definite position on where the agency is as it relates to the level of corruption.

The CHAIRMAN. Mr. Tarr?

Mr. TARR. One of the issues with corruption, it is kind of like trying to answer the question of how much counterfeit money there is in circulation. You are not really sure. You can look at some trends and some indicators and those sorts of things.

I think what Mr. Parolisi talked about is something that needs to be looked at. What are the kinds of issues, or lifestyles, or indicators that Customs' management can take a look at to see if a person is susceptible or vulnerable to corruption.

A natural extension of that thought is, quite frankly, particularly on the southwest border, it seems to me, that it is a staffing issue, where the pay grades are not that great, there is not a lot of mobility between those folks who work for the Customs Service along the border, and, therefore, perhaps the temptation may be greater in some of those areas. So, it is a broad issue, a broad question, but certainly the profiling, and indicators, and things of that nature might be something to look at.

The CHAIRMAN. Let me go back a minute to you, Mr. Parolisi. You talked about trends and statistics. Does Customs have anything in place that enables them to determine such trends?

Mr. PAROLISI. Well, when I was conducting the review, which was almost a year ago, I believed that Customs did not have that apparatus in place. But, under Mr. Keefer's and Mr. Kelly's direction, we have a new unit within the Internal Affairs Division. It is a Computer Analysis Division.

Plans are in place to make those things possible, to conduct those types of proactive approaches to identifying trends and patterns. I believe it is in the works and should be up and running very shortly.

The CHAIRMAN. As I mentioned, I know I have some additional questions. We will submit them in writing. We will keep the record open until 7:00 tonight.

I want to express my appreciation for you being here. Again, I apologize for the long delay. We particularly welcome your expertise, your Honor. Thank you for coming.

Thank you very much.

Senator MOYNIHAN. Thank you very much.

The CHAIRMAN. We will now call forward the second panel that we are pleased to have here. Jack Bradshaw is the corporate vice president and director of Ethics and Compliance at Motorola; Jerry Cook is the vice president of International Trade, Sara Lee Knit Products Group; and John Moore is the senior vice president of the Siecor Corporation.

Mr. Bradshaw, we will start with you, please.

STATEMENT OF JACK BRADSHAW, CORPORATE VICE PRESIDENT AND DIRECTOR OF ETHICS AND COMPLIANCE, MOTOROLA, INC., SCHAUMBURG, IL

Mr. BRADSHAW. Chairman Roth, Senator Moynihan, Senator Graham, thanks for the opportunity to come to speak on the challenge of global compliance, which is the subject of the hearing.

I have been asked to discuss for the committee how a large organization such as my corporation creates and maintains an effective compliance program. I think, although I will be talking generically, the relevance to the panel comments we have just heard will be clear.

One very important challenge of this expanding global commerce that is presented to a large corporation is compliance with a lot of laws at the many borders that their products cross. Customs' laws and practices are among these.

Many of you know my company, Motorola, by its products such as cell phones, two-way pagers, two-way radios, and semi-conductors. We have about 130,000 employees. We are a global enterprise, with people in 45 countries, and we market around the world. Last year, we imported over $4 billion into the U.S., making our corporation one of the largest importers in the country.

We view, at Motorola, formal compliance programs as an obligation of corporate governance. But we also believe that investing in compliance programs makes good sense, good business sense.

In 1989, at the direction of the Motorola CEO—and it is important to note that the CEO was involved—I initiated a company-wide program to ensure compliance with government contracting laws. I have been at the compliance game in Motorola for 10 years.

In the mid-1990's, we applied the same approaches for compliance programs in Customs and in export controls, and our environmental compliance programs use similar practices.

We refined our model for government compliance programs in this decade into a management strategy. We used it to ensure compliance with several laws and other internal corporate policies.

Over the years, other companies have asked us to share with them, and we have done that. We have hosted benchmarking sessions and we have learned, ourselves, in that process.

Let me turn, briefly, to the specific elements of Motorola's global compliance program. They are pretty simple to list, and I will just list them.

First, is senior management commitment. I think you will see the relevance to some of these things we have just heard here.

Second, is a clear, I call it, fixing of responsibility; who is going to be accountable for what? We have to have appropriate staffing. We have heard about staffing here earlier as well. Training. Written policies and compliance programs, assessment and feedback, and doing something with the results of the assessment.

And, not to be forgotten, renewal. These things do not get created and run by themselves. They need to be renewed from time to time.

Now, I could comment in detail about each of those. I will not, but I do want to emphasize two of those elements. Those are senior management commitments and assessment. Compliance does not just happen. It is easy for the boss to say, "follow the rules." That really is the easy part.

But senior people must continually emphasize by word, but also, and I believe especially, by deed the importance of the program. Their belief in compliance is particularly important because costs and benefits are basically impossible to measure. You have to believe it and take it on faith.

At Motorola, our senior management has shown commitment in a variety of ways: participation in many compliance conferences, making training videos, supervising, and they have hired the skills and paid the money to create compliance programs.

Now, the second element beyond senior management commitment I want to emphasize is assessment. That is a process of making sure you get the results you expect.

I spent a career in the military. An old soldier one time said that soldiers do well those things the commander checks. There are an awful lot of things we want to do, but if you do not go back and check they just do not do it, particularly they do not do it well. It does not matter how pretty the compliance plan and the policies are if you do not check to see if they are working.

Just the knowledge that the company cares enough to dedicate resources to our performing assessments will, by itself, have a positive effect.

At Motorola, we perform assessments internally and with external assistance in a variety of ways: self-audit, peer reviews, benchmarking. Then, of course, there is the interaction with the Customs Service and, I might add, not just in the U.S., but in many, many countries around the world.

Now, let me conclude that remark about assessment by emphasizing, again, feedback. Having found that something needs to be improved is important to improvement. It is almost worse not to know that you have got problems than to know that you do and not fix them.

We seek continuous improvement. We are well-known, we think, and justifiably, we hope, for our quality programs. We take that same approach to compliance: continuous improvement.

Now, we believe that instituting a compliance program, which costs, we know, several millions of dollars annually just for Customs, is a good investment.

I would be happy to answer your questions if you have any, and I want to thank you again for the opportunity to share these thoughts with you.

[The prepared statement of Mr. Bradshaw appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Bradshaw.

Mr. Cook?

STATEMENT OF JERRY COOK, VICE PRESIDENT, INTERNATIONAL TRADE, SARA LEE KNIT PRODUCTS GROUP, WINSTON-SALEM, NC

Mr. COOK. Thank you, Mr. Chairman. I want to thank the committee for this opportunity to comment on the U.S. Customs Service, joint industry programs related to interdiction, and the security of our merchandise.

I am the vice president of International Trade for Sara Lee Branded Apparel, and recently have been reappointed to the U.S.

Treasury Department Advisory Committee on Commercial Operations, U.S. Customs Service, and I am the chair of the Sara Lee Customs Council.

Sara Lee Branded Apparel is the largest wearing apparel company in the United States, with brands such as Haines, Haines Her Way, Platex, Bali, Wonder Bra, Champion, L'Eggs, and Just My Size.

Sara Lee Branded Apparel is an active member and a participant with the U.S. Customs Service in the Business Against Smuggling Coalition.

One of the key partnerships in the joint program with the U.S. Customs Service has been the interdiction and the hinderance of illegal narcotics and shipments. The very presence of illegal narcotics is a threat to the well-being of our employees, service providers, our investment, and our supply chain. We have a corporate policy and place a high importance on a drug-free environment, a drug-free cargo, and drug-free operations.

This partnership with U.S. Customs extends from the headquarters through the import specialist, local inspectors, and, recently, to the overseas assistance by the U.S. Customs Service.

In certain countries and locations we have co-developed new shipping techniques based on the feedback and the assistance we received from the U.S. Customs Service and our private security operations and key service providers.

For instance, in the country of Colombia, the combined and coordinated efforts with our foreign operations, the foreign inland trucking operator, our U.S. vessel operator, the port operations in Miami, and our U.S. inland carrier have developed one of the first cargo routes for us from Colombia to the United States that has the lowest risk assessment for the insertion of illegal narcotics.

The Business Against Smuggling Coalition, the BASC, program has been so successful that the U.S. Customs Service has assisted in the joint development and the creation of the U.S. and Colombian industry groups to form the Business Against Smuggling Coalition chapters in the country of Colombia.

In Mexico, we have developed and continued to redevelop improved operational techniques based on the information assistance we receive directly from the Customs Service to prevent and reduce our exposure of threats related to the illegal insertion of narcotics and our U.S.-Mexican operations.

The use of dedicated and uniquely outfitted trailers and a fleet of trucks and drivers, accompanied by private security, have significantly thwarted attempts at the insertion of illegal narcotics and highjackings.

The constant pressure by criminal elements to use innocent and unsuspecting individuals and unwilling corporations' equipment requires a constant awareness and partnership with the U.S. Customs Service.

During fiscal year 1998, the Customs' efforts overseas and industry partnership participants have assisted in 82 foreign interceptions and 42,000 pounds of narcotics being detained from the United States from abroad.

The American Counter Smuggling Initiative, ACSI, in July of 1988, started the Americas Counter Smuggling Initiative team

members in Cartegena. Colombia provided training to the Colombian anti-narcotics police on targeting methods and examinations abroad on commercial shipments.

Shortly after the training, the Colombian anti-narcotics police in Cartegena seized over 14,000 pounds of cocaine shipment in 192 metal spools of nylon thread bound for the U.S.

In the area of advanced technology, Customs needs continued funding. Mr. Chairman, the use of new technology for the non-intrusive inspection is critical to our joint mission to deter and cease illegal narcotics from being shipped to the United States and abroad.

The U.S. Customs Service personnel will no longer be subjected to the grueling task of inspection of cargo by physical unloading and reloading of trailers in less than ideal work environments.

In short, the non-intrusive technology assists us and our operations, while providing the highest degree of integrity against illegal narcotics.

Mr. Chairman, in summary, we have learned from our experiences, from the unfortunate experiences of others as well as our own. We are convinced that the assistance of the U.S. Customs Service is critical to our mission to service our customers by providing integrity in our cargo shipments.

Separately, in the MOD Act, with automation, the passage of the MOD Act created a potential government and industry facilitation. The movement of manufactured components in a finished product require more fluid environment than we currently have today.

The industry and governments are both seeking the same, specific data elements in a time-sensitive environment to determine the acceptability of a given commercial shipment essential to the business community to advance the automation of data collection, data processing, and data retrieval as quickly as possible, as well as to move data requirements to better mirror the business process.

In closing, Mr. Chairman, the industry partnership program to reduce the importation of illegal narcotics is important to us. We need the valued assistance and cooperation of the Customs Service.

Finally, I would just like to take a special note to the Chairman and fellow committee members and comment kindly on the past favorable action of the Caribbean Basin Initiative, and hope that this, too, will see it pass this year.

I appreciate the opportunity, and would be happy to answer questions.

[The prepared statement of Mr. Cook appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Cook.

Mr. Moore?

STATEMENT OF JOHN S. MOORE, SENIOR VICE PRESIDENT, SIECOR CORPORATION, HICKORY, NC

Mr. MOORE. Thank you, Mr. Chairman, Senator Moynihan, and Senator Graham.

I have been asked to relate to the committee how Customs and my company worked on a drug smuggling operation together, and what we did afterwards.

I am a senior vice president, working for a U.S. Fortune 500 company and an international technology company. I manage RWC, one of the divisions of these companies.

In 1992, I was informed by U.S. Customs that the general manager of my company reporting to me had a relationship with organized crime and was a conspirator to import 1,300 pounds of cocaine. The general manager used our company's paperwork to assist in the smuggling and it reflected RWC, my company, as importer of record.

The shipment was diverted as soon as it entered the United States and never physically shipped to our property. Customs contacted our company and notified us that Customs was conducted a controlled delivery, which they described as a surveillance of the shipment to its ultimate destination, in an attempt to identify and arrest those responsible for smuggling the drugs.

This operation took several months, during which time we complied with Customs fully. We ran our company as if nothing was amiss, contrary to our own internal policies upon discovery of improper conduct and misuse of company property and information. Our company complied with all Customs Service official requests for documentation and information, also including search warrants.

Our review of the events and documentation provided by Customs confirmed that the general manager exerted his control and authority to accomplish what was done. It should be noted that what had occurred is in no way standard operating procedure within our company, and it was not normal for the general manager to handle the situation himself, as others in our organization normally handle paperwork and the other routines mentioned above.

Once Customs and RWC reviewed the paper trail, it was obvious that something highly suspect had taken place. It was also obvious that others not affiliated with our company were involved.

The general manager was relieved of his duties as soon as Customs provided the evidence to us of the violation of United States law, and Customs declared the proactive phase of their investigation complete. The general manager, after making a full confession to Customs' special agents, was eventually indicted and convicted of unlawfully smuggling cocaine. It is understood he is still serving his sentence of 10 years in a Federal penitentiary.

The experience of our company working with Customs was positive and professional from day one. While the actions of one individual disturbed us greatly, we complied fully with the requests of Customs. Maintaining a business as usual manner was difficult at best, but rewarding in the end.

We kept Customs fully aware of the general manager's activities while the investigation took place, and continually followed Customs' advice. We were prepared to testify in court, if need be.

We feel that the program would have been detected and prevented the unauthorized use of RWC's name but for the power and control entrusted to this one individual at a remote location. None of the specific actions which took place were suspicious enough to warrant detailed investigation on our part. Financial records and inventory records would have revealed nothing.

Since these events have taken place, our company has taken several measures to help prevent any such reoccurrence. The events

that took place could have resulted in grave consequences for our business. Our parent company or our customers could have been upset and even walked away. The seriousness of the events caused us to review all internal compliance measures and policies, as well as the departments and people who are charged with audit and enforcement.

Internal compliance is stressed more than ever, and we pride ourselves in learning from this experience. Every single employee is made aware, in writing, of our position on compliance with all company policies and procedures, as well as U.S. law.

Some of the important actions taken to strengthen internal compliance include: transportation now being centralized, and preferred carriers must have contracts with our company; external consultants have been brought in to review internal Customs compliance on all trade issues; policies and procedures have been developed by consultants specific to our operations; a system has been put in place to monitor and comply with any change in Customs' reporting requirements and to ensure trade compliance; we employ a corporate compliance administrator to interface with outside consultants, Customs, and to train and advise our internal personnel.

Finally, less than 1 year from the time we relieved the general manager of his duties, we shut down the remote location and moved all of our operations within our factory.

All of the above-listed items help ensure we are doing our very best to eliminate import activities which could have a major negative impact on our company, our customers, and our employees.

[The prepared statement of Mr. Moore appears in the appendix.]

The CHAIRMAN. Thank you, Mr. Moore.

Mr. Bradshaw, let me ask you, what lessons can Customs learn and apply to its own operations from corporate compliance models such as yours at Motorola?

Mr. BRADSHAW. I was impressed, actually, to hear the previous panel and to have heard from things said by the new Commissioner, that senior management at the Customs Service has taken ownership for these things and have said the right things and have initiated the right programs.

If there is a lesson to be learned beyond that, it is to hang in there through what can be a long journey, actually, toward a compliance program to continue that same sort of commitment.

I would just reiterate my remark about assessment. There are many, many ways to know how you are doing, but you must deliberately engage in measuring yourself and use outside assets as you can to keep attention on the program.

The CHAIRMAN. Mr. Moore, the committee, of course, applauds the assistance you gave Customs in helping to bring those responsible for smuggling to justice. But are there any additional areas in which you think Customs could supplement its efforts against drug smuggling?

Mr. MOORE. I would think that there needs to be more exposure of what U.S. Customs does to U.S. business. A lot of this is sort of unknown. As one of the former panelists mentioned, many companies like to sweep these things under the rug, and they cannot be swept under.

Also, I would urge U.S. Customs supporting the use of the Customs compliance administrator or officer in any company doing importing. It is obvious that Mr. Bradshaw's and Mr. Cook's companies are doing that, and that is to be applauded.

The CHAIRMAN. And you, Mr. Cook. What are the primary lessons to be learned from your experience working with Customs? What worked, why, and what needs to improve?

Mr. COOK. I guess the first thing that we have learned with Customs, is that there are many dedicated professionals. Rolling up your sleeves and sitting down with them at the port and the different locations and walking them through what you are trying to do, and how, is the first and most important step. Then getting them involved with you is critical.

We have learned that the opposition on the other side is a lot more sophisticated than we tend to want to give them credit for. They win by doing small things in big ways.

As far as the future and how to make things better, our view is very simple. That is, there needs to be a working relationship with Customs. It cannot be an adversarial relationship. We applaud the Commissioner and the Customs Service for continuing on their side to work with industry.

I think the next big step is working abroad, both with the foreign governments, the foreign customs services, and letting the U.S. Customs Service have a more proactive role in modeling the outstanding behavior they do in this country for other countries, and to develop that joint relationship. Without that, you leave U.S. businesses alone to do that, and we really need their assistance.

The CHAIRMAN. Senator Moynihan?

Senator MOYNIHAN. Thank you, Mr. Chairman.

Gentlemen, I found your testimony extraordinarily rewarding. I found Mr. Bradshaw's title, director of Ethics and Compliance at Motorola, particularly interesting. You can either teach or you can do it, I suppose.

But a point. The Customs Service was established in 1789 as "the collector and protector of the revenue." Well into this century, it provided most of the revenue of the Federal Government, and still collects $22 billion a year.

Yet, in the press and such, even in some of your testimony, the issue is, how many pounds of cocaine did we seize last week? This is something personal with me, but I think we want to be careful how much of a burden we place on institutions like Customs with regard to matters such as this which we do not control. I have commented, last year we had a conference up at Yale on 100 Years of heroin. The Bayer Company obtained a trademark for heroin in 1898. It was a cough medicine. I think you will find one of these in your mail, too, Mr. Chairman. The Merck Company, which puts out that wonderful manual on medicine, began theirs in 1899, their first.

Among their products they tell you is available, you can have cocaine hydrochloride-Merck. The doses are 1.5 grains; maximum dose is 6 grains daily. The antidotes include morphine, alcohol, and ammonia. That is how much we knew about this fine product from a fine manufacturer of pharmaceuticals.

This is not going to go away. If you think so, you are wrong. It is not going to respond to paramilitary efforts. It might respond to medical research. These all began as medicines, you see. It is something almost lost to us.

What I would like to ask is, in your obviously genuine experience, how well is Customs performing its primary mission, which is trade facilitation? How can you get your things in and out? I was fascinated, Mr. Cook, by your suggestion that Customs could take some of its techniques abroad and pass the word, as it were.

Could I just ask that general point? Do you find that they work with you to get your product moving?

Mr. COOK. I would be happy to make the first answer on it. I think the Customs Service, for us, is very involved in trade facilitation. They provide a lot of counsel for us, solving problems we have in the U.S. and helping us with interpretations of classification with other countries, which is becoming one of the larger trade barriers that we are faced with today.

I think one of the biggest advocates or things that could help the Customs Service is their new automation system. Today, the data collection is encumbering trade, and it is going to get worse before it gets better. I think if we could do one thing, and that is to give them a new system, the old frame is wearing and showing some wear and tear on it. We direly need to move to a 24-hour process.

Senator MOYNIHAN. Could I ask you if we could get something in writing from you about this question you just described of classification?

Mr. COOK. Yes, sir.

Senator MOYNIHAN. It is obviously a bigger issue than we know. It is good to hear from somebody who knows about it.

Mr. Moore?

Mr. MOORE. Customs has worked very well with us. We are a smaller division, but we export our products to 55 countries. We import some goods and we actually use a Customs broker who works closer than us with Customs. Our measurement devices upset customers. If they do not get our goods or we do not get ours, you tend to get upset. The frequency of that has been minuscule. Customs has worked with us very well.

Senator MOYNIHAN. Sir?

Mr. BRADSHAW. I could support that same view. In fact, I am happy to tell you that essentially all of our relationships with the Customs Service are in the trade facilitation area and not in some of the other areas which have been the subject of testimony today. I can tell you, in the last four and 5 years, the Service has done, in my mind, quite a good job of facilitating trade. I believe that the Modernization Act is responsible for that. It changed the attitude and procedures of the Service, and also changed corporations such as ours, making the point that there is a shared responsibility.

I can discern, in that time, that the Service has, indeed, reached out in a variety of ways to help the importing community understand how to do the job, and do it right themselves. I can cite the assessments which are difficult for some importers, but we found them very useful, and the broker management which gives us one voice in the Customs Service. So, we think there has been a lot of success there.

Senator MOYNIHAN. Well, Mr. Chairman, if either Mr. Bradshaw or Mr. Moore wanted to add, in writing, something about this facilitation, I, for one, would very much appreciate it.

The CHAIRMAN. Could I ask a related question? As I understand it, just-in-time delivery has become increasingly important.

Senator MOYNIHAN. Yes. We had this discussion previously.

The CHAIRMAN. That is right. I just wonder, are your companies using just-in-time delivery, and what kind of experience have you had with imports or exports?

Mr. BRADSHAW. Well, when the question came up before, I guess it was very clever, because I wrote down JIT on my paper here because a company such as ours with manufacturing facilities, major ones in the U.S., and high-tech feeder plants, semiconductor plants in particular and radio component plants around the world, depend vitally on a process which we call just in time.

That means that components and materials need to arrive at our plants in this country just in time. The option to maintain large inventories is too costly for companies to be competitive.

That is why I say, one of the challenges of global trade that is sometimes overlooked is the challenge to deal with the complexities of crossing borders—hundreds of borders, actually—around he world for finished product and for components, and just in time depends upon it. I can say that, at least in this country, the relationship we have with the Customs Service makes that possible for us.

Senator MOYNIHAN. Mr. Chairman, this is important. We were talking about it last week, that the economics taught in American universities 30 years ago, on the business cycle, heavily depended on the accumulation of inventory, that led to a slow-down, then finally a back-up, and that is how you got your business cycle.

The business cycle has, to an extraordinary degree, diminished or disappeared because of this just in time business. There is no inventory accumulation. But if the Customs did not work, my God! We think the Y2K is a problem. It is very interesting.

The CHAIRMAN. It is, indeed.

Senator Graham?

Senator GRAHAM. Thank you, Mr. Chairman.

I want to start by commending Mr. Cook for his closing remarks about CBI. I share with you the feeling of the importance of that. I know that that feeling is shared by the leadership of this committee, and hope that we can see some affirmative action soon on that too-long-delayed issue.

One of the things that the Customs Service has increasingly relied on are procedures at the foreign point of dispatch of goods which facilitate the movement once those goods arrive in the United States, things like providing to the Customs Service at the port of arrival a listing of all of the items that are on a particular airplane or ship so that Customs' review can be expedited.

Could you comment, from your own experience, as to how well those activities that are external to the United States have contributed to facilitation of processing once the goods arrive in the United States?

Mr. COOK. Our experience has been particularly in the air movement because we air a lot of product in and out of the Caribbean

back to Miami. You can get the identification of the shipper and the commodities.

Getting the exact quantity gets to be a little more complicated because of air and wind conditions. You may have a 90,000 payload ready to go and the air and winds change and you have to strip out 20,000 pounds to get the plane off the ground.

So, I think the ability to provide the information in advance of the shipment today has been our focus, and I think that helps the Customs Service and their ability to do pre-selectivity of an arriving shipment, of who the shipper is, who the receiver is, the commodities that are on it.

I think it also makes it difficult in air shipping today though, because of the way cargo is put in a container and wrapped, to really open it up and go through it. That is why the higher technology, the scanning, the x-ray equipment, is really needed to help them facilitate and look at it, and the use of K-9s has been very important in air programs.

Senator GRAHAM. I assume that all three of the companies that you represent use multiple sources of transportation and points of entry. Could you comment on the consistency with which Customs carries out its responsibilities?

For example, are there some ports that are seen to be particularly good and, therefore, are a preferred point of entry as opposed to others, which may generate problems of delay or other impediments to the flow of goods?

Mr. MOORE. We use multiple ports, mostly on the east coast. We have not had a problem with that. Actually, it boils down to, we would like to use the southernmost port before it goes through the Panama Canal, the last point before it heads through the Panama Canal. Importing, we use the west coast. We have not used the Gulf much. But west coast, east coast. It appears to be pretty consistent. I cannot recall a repetitive problem at one port as opposed to another.

Mr. BRADSHAW. I cannot tell you of a specific in that way. We do not make any effort, frankly, to measure it. Again, an occasional anecdote. But, basically, we use several ports. We use two and three heavily, and it just happens to be that that suits the flow of our product into the country.

We use expediters that carry a lot of our semiconductor imports out of Asia and into the U.S. through Alaska. That is where they land, and that is the port we use. We use Miami a lot, we use L.A. a lot, but we do not make any effort to compare them.

The only inconsistency we find from time to time is perhaps in the classification issue, but it is really not a problem.

Mr. COOK. Our experience has been, as far as consistency, it is fairly consistent port to port. A lot of our port selection is based particularly in Miami, because there has been a very good drug net, essentially, establish in the Port of Miami. We like to have that cleaning process occur when we come in, and we have a very good relationship with the set team there.

So, we have a preference for using the Port of Miami for a lot of reasons, but, overall, it really gets——

Senator MOYNIHAN. Mr. Cook, that was the correct answer.

Mr. COOK. Well, it is our major port for that reason.

Senator GRAHAM. I knew that the Chairman would select only wise persons to give us testimony, and that has been demonstrated.

Mr. COOK. But, overall, the biggest challenge going forward is really hours of operation.

Senator GRAHAM. Mr. Cook, I think you mentioned the issue of automation and coming into the modern era of data collection and management.

That is an issue before the Congress because the Customs Service, based on the Modernization Act, has now made a recommendation for a new system. They have also made a recommendation as to how to pay for it, which includes some increase in access fees by the users.

Could you comment on the system that the Customs Service has recommended, and their proposed method of financing it?

Mr. COOK. Let me give you these two comments back. One, we are high supporters that it is time to replace the Customs' system and have every confidence that they know best how to replace the tasks and build the new automation system. We take no issue with their process and their design.

As far as the funding, we know in our own system, if you are going to build it, it is going to cost money. We would leave that up to the Customs Service and the Congress on how to get the funding. We highly support funding. The earlier the funding, this year, next year, and the sooner it is implemented, the sooner we can all benefit from that.

Senator GRAHAM. Thank you.

The CHAIRMAN. Thank you, gentlemen. We appreciate your very meaningful testimony.

Senator MOYNIHAN. Very good.

The CHAIRMAN. We will call upon you in the future. Commissioner Kelly, it is nice to have you here.

Commissioner KELLY. Thank you.

The CHAIRMAN. The committee is in recess.

[Whereupon, at 12:30 p.m., the hearing was concluded.]

APPENDIX

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

PREPARED STATEMENT OF GEORGE BARDOS

INTRODUCTION

Mr. Chairman and members of the Committee, thank you for the opportunity to discuss the technical elements relating to the funding of the Automated Commercial Environment. Vastera is dedicated to the research and development of a commercial enterprise software application that automates various elements of International Trade Logistics.

We are one of the many software vendors or in-house developers for Customs interfaces like the current ABI system. The trade uses these Customs interfaces to "pass over the fence" trade and statistical data via electronic communication. This communication is critical to the movement of goods. Our software and others software vendors integrate to Customs systems both on the inbound and outbound side. Development and maintenance of these interfaces is costly to the Trade.

What Vastera would like to impress upon the Committee is the cost and resources required to develop, test and certify these interfaces to US Customs. Each time a "new" release is completed by US Customs the Trade must write the code or logic for the new or improved functionality and test internally at our own cost. Then once developed the software vendors must test with Customs before going live or becoming certified. To complicate matters even further, the importer themselves must also install, test and become certified with Customs before sending transactions to Customs. This ensures that merchandise is not hung up at the border due to a software issue. This takes time, funding and resources from the private sector.

During the current planned phased implementation of ACE over the next four years, the Trade will continuously need to develop and test the new functionality as it is released by US Customs. This is a continuous resource requirement and cost to the Trade. The Trade cannot sustain a seven-year implementation of ACE—it must be completed as quickly as possible with as few releases as possible.

It is also important to note that as a software vendor, Vastera and others will need to maintain at least four interfaces to Customs over the next four years. These include AES, ABI, ACE and possibly ITDS. This requires multiple record layouts to multiple systems, until such time as one interface can be used. This requires maintaining four systems to accomplish import/export transactions within the US. As you can imagine this requires software, hardware, technical support and expertise from the import/export community to ensure the migration to the new systems and functionality is done timely and cost effectively. One less interface with Customs will be required, the quicker ABI is replaced by ACE. This is very important to the Trade Community.

Each interface and release is costly to the trade community. It is drain on already scarce internal IT resources and hardware.

CUSTOMS PROVEN ABILITY TO DEVELOP SOFTWARE SOLUTIONS

The people associated with the creation and maintenance of the ACS system should be very proud of their achievement. For any large scale software system to support its user base for 15 years under the constant demand of more throughput, must be considered a highly successful system.

Customs has the ability to manage, design, develop, deploy and support software systems such as the Automated Export System (AES). Vastera recently became certified under the AES program. We worked with our assigned Customs contact, who facilitated and answered any questions that arose. This process mechanism coupled

with clear, accurate and complete documentation made the certification process smooth. This kind of integration is not always so smooth. In fact, integration between computer systems has been so difficult, that a new cottage industry has recently been born. This further demonstrates Customs ability to design and deploy systems that are considered by industry to be a difficult task.

ACE PROJECT PLAN AND ARCHITECTURE

Customs phased rollout of functionality, combined with a methodology to decide which functionality and which ports should receive it first, is a sound plan. It shows evidence that, first of all, a prioritization methodology exists. Secondly, it shows that Customs understands the importance of an early impact on the user community and its associated benefit compared with its associated development costs. In simpler terms, Customs has a plan for how to determine what functionality returns the biggest bang for the buck. This is a sign of a mature development organization that understands the business result is the end game.

Although the ACS system has been serving the trade community for 15 years, the technological and regulatory landscape has changed greatly during that time. The personal computer was not yet ubiquitous and the Apple Macintosh was just being introduced. Improvements in software design and development tools, hardware advancements, and software paradigms have dramatically changed the software development process from what it was 15 years ago. In order to accommodate for new requirements and/or accommodate for greatly increased transaction volumes, both of which are true in regards to the ACS, it is far easier to redesign a new system rather than try to patch or augment an existing system. It is no surprise that Customs has come to the same conclusion regarding ACS.

In Vastera's opinion, the ACE technical architectural foundation is sound. The centralization of the time critical transaction processing tasks is a sound decision. Designing for performance considerations and analyzing bottlenecks become much easier and more versatile in a centralized processing environment. Equally as sound is the decision to offload the non-time critical analysis tasks. This allows for the segregation of the specific data that must be analyzed, while not impacting the systems performing the time sensitive operations. All too often, transaction processing software systems are brought to a crawl because the systems designers neglected to take into consideration the impact of report and analytical processing. The design put forth by Customs accommodates for this common mistake.

CMM LEVEL 2 ATTAINMENT

Let me say that Vastera is a proponent of the Software Engineering Institute's (SEI) Capability Maturity Model (CMM). Anytime a measurement process is introduced into the software development life cycle, more predictability will be added to the process. Furthermore, the metrics gathered from this process could be used to further refine the development process going forward. Although Vastera does not have any formal experience implementing or evaluating CMM, we do understand its principles.

So, while we believe that the introduction of discipline into the development process is generally a good thing, we also believe that the decision to do so cannot be made in a theoretical vacuum. That is, specifically speaking the current state of the world must be examined in order to make a judicious software project decision. In order to measure the cost of the time delay we must consider the following elements.

We know that the current system (ACS) has experienced outages during the last 18 months. We know that this system is the lifeblood that controls approximately 8.8 billion dollars worth of merchandise flowing across our borders. We know that this flow of goods affects the livelihood of countless workers. US manufacturers depend on Just In Time deliveries to keep assembly lines running and avoid the costs of carrying raw materials inventory. We know that the flow of goods is expected to double by the year 2005. We know that ACS cannot be effectively enhanced to accommodate for this increased traffic. We know that if the ACS system fails, the flow of goods will be effectively stopped. We know that every day that ACE funding and implementation is delayed, is another day of increased risk of an outage of ACS. These facts merit consideration. ACE is the insurance policy and must be purchased before the tragedy occurs.

Vastera interfaces with the major ERP and warehousing software systems throughout the world, the certification processes vary, but not one of these world class software vendors require CMM Certification. This is not the norm for the software industry and Customs should not be held to this standard. Also, the Customs Modernization Act promises automation to support the regulations and Customs

programs, it doesn't specify that CMM Level 2 is required. It seems that GAO is asking for this late in the game.

The first question to ask: What is the risk? Delaying the ACE project until CMM Level 2 is achieved will add considerable time and money to the project. The CMM process is not easy to implement and is generally more difficult for larger organizations. The money required is certainly quantifiable, but the additional time is more difficult to measure.

CONCLUSION

I believe that the current state of the ACS system, coupled with the projected growth of border transactions, puts American importers and exporters at severe risk.

I believe that Customs has demonstrated a proven track record of successful software project deliveries.

I believe that the ACE project plan and technical architecture are fundamentally sound.

And finally I believe that while CMM Level 2 attainment is a beneficial goal, the project delays and additional costs associated with achieving this goal is not warranted given the current state of ACS.

The Trade should not be asked to support multiple Customs systems, and multiple ACE Releases requiring development and implementation costs and resources. Customs should implement ACE within four years or less with few releases to the Trade. Keeping internal Customs releases separate from external trade releases.

Based on these conclusions I recommend that Congress fund Customs Automation as soon as possible.

PREPARED STATEMENT OF JACK O. BRADSHAW

Mr. Chairman and Members of the Committee, thank you for the opportunity to discuss creation of government compliance programs in the private sector.

Reporting to the General Counsel and Chief Financial Officer at Motorola, my office oversees company-wide, global compliance programs in the areas of Ethics, Customs, Export Controls and Government Contracting.

Motorola is one of the largest importers in the United States, with annual volumes of over 70,000 entries and entered value in excess of $4 Billion annually.

Currently, Motorola has 130,000 employees, annual revenues of $30 Billion, over 1,000 locations in 45 countries, and 65 manufacturing facilities in 17 countries. We market our products all over the world. To sustain success we must be an agile manufacturer, able quickly to shift production from one plant to another. We must be an agile marketer, able to serve any market from any source.

WHY HAVE GOVERNMENT COMPLIANCE PROGRAMS?

Motorola was built on the key belief of uncompromising integrity in everything we do. Fostering a corporate culture shared by employees throughout the world, this belief is at the very heart of our compliance programs.

We recognize that complex, ever-changing government rules which vary by country—combined with our own organizational complexity—mean that compliance does not "just happen." Saying "follow the rules" is easy—but it is not enough. Making sure that it actually happens requires structured processes and active management. Our government compliance programs are an investment to provide this structure.

Effective compliance programs help to ensure our status as a good corporate citizen in countries throughout the world. The improved coordination and management in these areas which results helps, in turn, to reduce cycle times and costs. Only in this way can we achieve our fundamental objective of Customer Satisfaction.

ELEMENTS OF A COMPLIANCE PROGRAM

Each of our compliance programs has common fundamental characteristics:

1. Commitment by senior management, who set the expectation for compliance and remain involved in oversight.
2. A corporate policy, with supporting plans and procedures.
3. Assignment of specific responsibilities within organizations.
4. Dedication of resources, including people, systems, training and outside experts.
5. Compliance assessment and feedback mechanisms, to identify and monitor corrective actions.
6. Coordination and information-sharing, through councils, conferences, peer networks.

7. Renewal, which is conscious refreshment of compliance programs driven by management, organizational changes and changes in regulatory requirements.

THE ROLE OF COMPLIANCE PLANS

We have found clear communication to be the key to success in our compliance programs. For this reason, we require that business units and facilities document their compliance programs in the form of compliance plans. Each plan is a reference document for employees, describing the elements of the specific organization's compliance programs as described above.

Approved by senior management, communicated throughout the organization, and updated as required, the plan is a written "roadmap" to ensure that the organization is focussed to follow the rules and to attain continuous improvement. Through this communication tool, each individual within the organization understands his role in assuring compliance.

Although customs laws can vary greatly among countries, compliance plans are an effective communication vehicle and management device for operations in any country, tailoring the contents to the specific regulatory requirements.

We recognize that it is not easy to keep busy senior managers consciously involved in compliance activities. Thus, we require that plans be submitted by the organization's senior manager, or on his or her behalf, to the Corporate Office and that management keeps the plan up to date through periodic review. This practice provides evidence of management commitment, and it adds some discipline to the process. We also gain the benefit of a corporate review, which promotes consistent approaches to common challenges and provides a valuable basis for sharing solutions.

ASSESSMENT AND IMPROVEMENT

An effective compliance program must include processes to verify that what management expects is happening in their organizations is what is actually happening. We call this "assessment." Without it, there is no assurance that the organization is in compliance.

Equally as important as assessment is the need to identify and communicate areas for improvement, followed by monitored implementation of corrective measures. An assessment program without this meaningful feedback activity can lead to the disastrous situation in which an organization has evidence of areas that are deficient and does not take action to correct them.

Assessment takes many forms in Motorola's compliance programs. Our policies require periodic "self-assessment" in which an organization measures its own levels of compliance and control. Organizations typically develop standardized self-assessment programs for their operations. We also arrange for peer exchanges in which compliance managers from different organizations meet to review each other's programs.

The corporate staff also makes on-site visits that include assessment of compliance programs. The Corporate Audit Department provides independent and critical measurement. External assessments include reviews by consultants or outside counsel. And, of course, there are government audits and reviews.

One further source of informal organizational assessments occurs during compliance councils and conferences in which compliance professionals interact, share ideas and best practices. Usually every attendee finds several ideas to improve his compliance programs.

Some assessments are primarily qualitative, testing existence of and adherence to procedures, for example. Some contain quantitative transaction testing. Most good assessment programs contain a blend of qualitative and quantitative review.

An effective feedback program includes:

1. Clear identification of issues discovered and specific corrective measures.
2. Assignment of individuals responsible for implementing the corrective measures, along with target completion dates.
3. Monitoring of actual implementation of corrective measures by the appropriate levels of management.
4. Follow-up verification at an appropriate time after the corrective measures have been implemented.

A high level of various types of assessment programs, along with strong feedback programs place the organization, and executives charged with our governance, in a good position to be confident that our internal controls are functioning properly and that deficiencies are being identified and corrected in a well structured way.

COSTS AND BENEFITS OF COMPLIANCE

All companies have limited resources. Management wants to know what they are getting for their investment. This poses a continual challenge to compliance managers, because measurement of costs and benefits in this area are virtually impossible.

An effective compliance program must permeate the organization and receive some time and attention from people well beyond those who are paid specifically for compliance activities. The cost of time from these additional contributors, however, cannot be practically measured.

The main benefit of compliance programs is prevention of law violations. It is not possible to quantify the financial impact of a legal issue that has never arisen because the organization has a strong compliance program.

Here again we see the direct linkage between senior management commitment and ongoing support and the quality of compliance programs. Management must have the faith and belief that instituting a compliance program represents a worthwhile investment and makes good business sense. Motorola views the cost of our customs compliance program, which we estimate to be several millions of dollars annually, as an investment that results in good corporate citizenship, customer satisfaction and reduced overall shipment costs and cycle times.

HOW LONG DOES IT TAKE?

Implementing and maintaining an effective compliance program should be viewed as a journey rather than a destination.

For example, the basic elements of our customs compliance program include a global, company-wide customs compliance policy, standards of internal control, self-assessment guidelines and involvement of Motorola's internal audit function. We began implementation of these some years ago. In time, supporting plans, procedures and controls were established within our major businesses and importing operations around the world. Full implementation of these elements can take several years.

On an ongoing basis, we maintain the program through training, self-assessment and broker management. We continuously address specific technical issues including valuation, classification and country of origin issues. The process of coordination among importing operations in country is an ongoing one.

It is important, even essential, that compliance programs be "renewed" from time to time. They never become mature. Senior management must continue to support, sponsor and oversee them. An important driver of renewal is internal and external change. We continuously evaluate changes in government regulations. We also respond internally to an ever-changing organization, mix of products and distribution strategies. Our compliance programs are modified accordingly in this spirit of renewal.

CONCLUSION

Our compliance programs help us to satisfy our fundamental objective of Customer Satisfaction. Among our most important customers are law enforcement agencies in governments throughout the world—including the US Customs Service. Our compliance programs assure that, just as we partner with governments to provide communications solutions, we partner to pursue a shared goal of compliance.

PREPARED STATEMENT OF MICHAEL CHERTOFF

I am delighted to appear before this Committee as part of today's oversight hearing into the enforcement activities of the United States Customs Service.

I served for over a decade as a federal prosecutor in the Southern District of New York and the District of New Jersey, culminating in my appointment as United States Attorney for New Jersey from 1990–1994. During that time, I worked with the Customs Service on a variety of investigations and cases, including narcotics trafficking, money laundering, and export control violations. In addition, I supervised investigations involving a large number of other law enforcement agencies and task forces, including long-term cases directed at organized crime and white collar crime. Finally, as a member of the Attorney General's Advisory Committee of United States Attorneys from 1991–1994, I had the opportunity to participate in policy planning at the highest levels of the Department of Justice. This experience has provided me with a perspective on law enforcement planning and evaluation which I hope that this Committee will find helpful.

I.

As part of its mandate to oversee the activities of the Customs Service, this Committee is naturally concerned about the value of Customs' enforcement priorities and the success of its strategies. How a law enforcement agency selects performance benchmarks and how it evaluates its activities are crucial to the success of the agency's mission. Unfortunately, sometimes the drive to accurately measure performance results in shifting an agency's priorities to those activities which are most easily gauged quantitatively, and away from objectives that are equally or more important, but less easily measured.

An example of this phenomenon appears in the government's effort to eradicate traditional organized crime. In my view, that effort over the last two decades has been one of law enforcement's paramount successes. Traditional organized crime has been driven from labor unions and legitimate industries, and its hierarchy has been repeatedly decimated. One reason for this success is that law enforcement recalibrated its tools for evaluating the success of its mission.

During the 1970s, government prosecutors and investigators had individual successes convicting organized crime figures for specific crimes. Too often, however, the crime families simply replaced the convicted members with new members. As a result, the Government made little actual progress dismantling the structure and long-standing organizational power of these criminal syndicates. Part of the problem was that the FBI's enforcement priorities were driven by the need to generate good statistics: large numbers of arrests and indictments. An agent had the incentive to gravitate to and focus on investigations with the potential for fairly quick arrests and indictments in large numbers. An agent who worked a long time on a single case yielding only a handful of arrests would be at a comparative disadvantage.

But as the decade closed, farsighted FBI and Justice Department officials realized that the way to dismantle organized crime was to target its leaders and the institutions that they used to maintain their power. This project required long-term strategic operations, aimed at a relatively small number of high level bosses, and using long-term investigative techniques such as electronic surveillance, deep undercover operations, and ongoing physical surveillance. To be successful, these investigations would have to pass up opportunities to make quick arrests in favor of building one or two large cases charging the top echelon criminals. As a statistical matter, this approach might only yield a fraction of the arrest numbers that might be obtained the old-fashioned way. But as a strategic matter, convicting a handful of mob bosses and captain dealt a far more crippling blow to organized crime than convicting a much larger number of dispensable underlings.

Furthermore, these officials soon came to the realization that the most effective effort for law enforcement might sometimes require turning away from arrests altogether toward a focus on building civil racketeering cases that would put corrupt unions and companies under court supervision. Some agents were surprised when they found themselves building cases that led not to defendants in handcuffs but to court orders placing trustees in charge of previously mob-dominated entities. But my experience is that these agents became converted to the new approach when they saw how successful these trusteeships could be in ridding institutions of domination by organized crime.

The results speak for themselves: Since the early 1980s, the Department of Justice convicted the Commission of La Cosa Nostra; the hierarchies of every one of the five New York families, the hierarchies of La Cosa Nostra families from Boston and Philadelphia to Chicago and Kansas City. Organized crime influence was reduced, if not eliminated, from a large number of labor unions and businesses. And yet the agents working on these significant structural cases probably had lower arrest and indictment statistics than they would had they worked during the same period on a large number of one-shot cases. Fortunately, the leadership of the FBI and the Department of Justice understood that performance should be measured not just by measuring the number of investigations and prosecutions, but by evaluating their strategic quality instead.

II.

Against this background, let me address the issue of planning and evaluation in the context of the Customs Service.

In setting enforcement goals and performance standards, the Service, and Congress, should bear in mind that Customs enforcement entails both a reactive component and a strategic component. What I mean by reactive enforcement is the protection of the borders against penetration by contraband and/or dangerous materials, and interception and seizure of such materials when encountered. The critical strategic element of reactive enforcement is the identification of those points of entry

where there is greatest vulnerability, and deployment of the Service's limited resources to achieve maximum protection, interdiction, and deterrence.

In contrast, strategic enforcement is aimed at reducing illegal imports (and illegal exports) across the border through disruption of organizations that carry out illegal transportation activities. So, for example, long term investigations or undercover operations that target narcotics trafficking or money laundering groups may involve little activity at U.S. borders; instead, these operations protect those entry points by removing the criminal organizations that finance or execute the illegal exportation or importation through these points.

Recognizing the distinction between reactive enforcement and strategic enforcement, and capitalizing on their distinct values, is important for an agency like Customs, because the process of setting goals and standards is different for the former than for the latter. Reactive enforcement tends to be opportunistic, localized, and short-term. That is to say, law enforcement responds to opportunities as presented by specific acts of smuggling or importation; activity is concentrated in and around a specific airport, seaport or border location; seizure or arrest is accomplished in a matter of hours or, at most, days. Moreover, in evaluating the effectiveness of reactive enforcement, quantitative measurement can be a significant (although not exclusive) benchmark for enforcers' performance. Every kilo of drugs seized is one kilo of drugs that will not enter the country. Therefore, seizing 10 kilos is by definition more significant than seizing five. Thus, a plan for reactive enforcement of laws against narcotics smuggling, for example, necessarily involves the following: identifying the best opportunities by deploying resources at those points of entry which are most vulnerable from a historical, geographic, and volume standpoint; assigning responsibility for enforcement at the local level; measuring success by comparing trends of arrests and seizures over comparatively short-term periods; placing significant weight on numbers of arrests or seizures of contraband in comparison with historical rates and current smuggling trends.

This sort of approach, however, is ill-suited to setting goals and standards for strategic enforcement. As illustrated by the experience in fighting organized crime outlined above, for strategic enforcement numbers do not translate into effectiveness. Far more important than numbers of arrests or seizures are removal of high-level, sophisticated organizers of illegal activity, or cleansing of institutions—for example, banks—that are facilitating ongoing criminal behavior. Strategic enforcement requires a qualitative approach that sets as goals incarcerating indispensable criminal leaders or eliminating corruption of financial institutions.

Thus, strategic enforcement does not await opportunities presented by criminal activity. Rather, a strategic enforcement plan: seeks out criminal organizations and tries to pre-empt criminal behavior using such techniques as controlled deliveries of contraband; cultivation of informants; undercover operations; electronic surveillance; coordinates operations not locally but nationally or even internationally; involves long-term, intensive efforts, in which the time horizon for success is measured over several years, rather than days; places greatest weight on incapacitating key criminal figures or entities.

Accordingly, the process of planning, benchmarking and evaluating reactive enforcement should be treated as distinct from that applied to strategic enforcement. The former is driven by the need to match resources with short-term threats, requires flexible deployment of resources, and measures success to a large degree by considering trends in people or contraband apprehended. The latter is driven by identifying long term threats, requires commitment of personnel and effort over a sustained time period, and evaluates success through the incarceration of high-level criminals or the eradication of criminal institutions. Both forms of enforcement, however, are vital in a comprehensive effort to combat international crime; official ignore either at their (and our) peril.

III.

As long as Customs pursues reactive and strategic enforcement objectives, it is appropriate to use both the reactive and strategic planning and evaluation models in setting goals and measuring performance with regard to those objectives. What Customs and this Committee should avoid, however, is mixing up these objectives and approaches. More specifically, we should avoid letting the need to measure how law enforcement achieves its goals skew the choice of what those goals should be.

As the evolution of organized crime strategy shows, the quantitative approach has a particularly appealing quality. Because quantitative measurement seems rigorous and precise, and lends itself to easy comparison, managers often gravitate to quantitative evaluation. But, as demonstrated above, the quantitative approach is suitable for a reactive law enforcement program, not for a strategic program. Over-

emphasis on numerical measurement, therefore, creates a strong incentive to devote resources and effort to reactive enforcement where "success" is more readily demonstrated. The result is that strategic enforcement gets shortchanged.

In my view, the planning process should begin with a threshold decision about how much effort the agency should devote to reactive as opposed to strategic enforcement. Once that decision is made, the process of setting goals and measuring performance should proceed separately for each program, with an understanding that success under each program must be evaluated distinctly. Without that type of explicit commitment, the strategic enforcement program will be hostage to constant erosion of resources in favor of the more quantifiable reactive program.

So, the reactive law enforcement planners should track historical data and use current intelligence to project patterns of transportation of contraband, and set objectives for the interdiction of that contraband. Data on seizures and arrests, as well as information about regional markets for illicit substances, should by used to track law enforcement success by region and on a regular basis. The agency should be flexible in redeploying resources when, for example, importation trends shift geographically.

On the other hand, strategic law enforcement planners—working with other law enforcement agencies—should identify criminal organizations which play a major role in transporting illegal substances or in repatriating the proceeds of crime. The agency should commit adequate resources over the long-term to achieve the objective of dismantling specific criminal groups and breaking their grip on legitimate institutions. Evaluation should rely not only on compilation of raw data on markets for illegal substances, but should consider the extent to which major criminal figures have been convicted or driven from access to legitimate financial institutions. This kind of assessment, of course, will require a nuanced understanding of the internal dynamics of the targeted groups. It will also require the patience to recognize that success may not become apparent within a single annual budget cycle.

That leaves the fundamental question: How should Customs balance its reactive and strategic roles? Plainly, reactive enforcement must remain a core Customs function since no other agency is assigned the mission of protecting against illegal importation. But should Customs continue to operate a strategic program aimed at large scale money laundering or narcotics organizations? Perhaps there is an argument that other law enforcement agencies are adequately suited to conduct strategic investigations, and that Customs is merely duplicating effort. My view—based on personal experience but not on any comprehensive study—is that Customs plays a distinct and important role in strategic investigations because of its institutional knowledge about smuggling, its opportunities to develop informants, and its singular focus on protecting the country against illegal importation (and exportation). But if Customs is to continue to play this invaluable role, the Service should explicitly and consciously set goals and evaluation benchmarks that are tailored to the special features and demands of its strategic law enforcement effort.

PREPARED STATEMENT OF JERRY COOK

Good Morning. My name is Jerry Cook. I am Vice President of International Trade for Sara Lee Branded Apparel. I have recently been re-appointed to the US Treasury Department's Advisory Committee on Commercial Operations of the United States Customs Service. I am the chair of the Sara Lee Customs Council. Additionally, I serve on the Board for the United States-Mexican Chamber of Commerce Mid-Atlantic Chapter, member of the Joint Industry Group and serve on the Board of the United States Apparel Industry Council. I want to thank the Committee for this opportunity to comment on the U.S. Customs Services joint industry-government programs related to interdiction and security of our merchandise.

Sara Lee Branded Apparel is the largest wearing apparel Company in the United States. Some of our apparel Brands are: Hanes, Hanes Her Way, Playtex, Bali, Wonder Bra, Champion, Legg's and Just My Size. Sara Lee Branded Apparel is an active member and participant with the Business against Smuggling Coalition with U.S. Customs (BASC).

Our success in wearing apparel is directly related to our ability to develop and implement an effective supply chain servicing our worldwide customers' demand. Our on-going ability to incrementally expand our product selections successfully is directly related to trade successes like the Canadian Free Trade Agreement, NAFTA, Israeli Free Trade Agreement and the Caribbean Basin Initiative. In each program, one of the key agencies assisting companies is the United State Customs Service.

In the balance of my testimony, I will present several comments, observations and suggestions related to the United States Customs Service role working with Industry.

One of the key partnerships Sara Lee Branded Apparel has benefited from, is the joint program with the U.S. Customs Service on the interdiction and hindrance of illegal narcotics. I sincerely believe that the private sector needs the assistance of the U.S. Customs Service and related agencies to deter illegal narcotics from being illegally inserted in our cargo/merchandise or operations. The very presence of illegal narcotics is a threat to the well being of our employees, investments and supply chain.

We have a corporate policy and place high importance on a drug-free environment, drug-free cargo and drug-free operations. From the late 1980's to the present, we have worked closely with the many professionals of the U.S. Customs Service to define and redefine our procedures, techniques, locations, service providers and practices to ensure the integrity of our international shipments. This partnership extends from the Customs Service headquarters through import specialist, local inspectors at the port of entry and recently to overseas assistance. We sincerely believe that in the drug enforcement arena, we must go beyond traditional expectations to one of effective partnerships that yield a supply chain clean and free of corrupting practices and threats of illegal substances.

In certain countries and locations we have co-developed new shipping techniques based on the feedback and assistance we receive from the U.S. Customs Service, private security operations and key service providers. Key partnerships have emerged in both the Caribbean Basin in countries like Colombia and Jamaica as well as in Mexico.

Our efforts extend beyond the U.S. border back to the foreign country and foreign operations. In many operations we utilize additional private security, security equipment and canine resources to thwart those who would attempt to take advantage of our employees, their families, our operations or our cargo/shipments. The illegal trafficking of illegal narcotics places at risk many unsuspecting people and investments in harms way. The partnership with our suppliers and the U.S. Customs Service is unique.

For instance, in the country of Colombia, the combined and coordinated efforts with our foreign operations, foreign in-land trucking operator, U.S. ocean vessel operator (Seaboard Marine), the port operations in Miami and our U.S. in-land carrier (Salem Carriers, Inc.), have developed one of the first cargo routes from Colombia to the United States with the lowest risk assessments for illegal narcotics being inserted in the container and successfully shipped into the United States.

BUSINESS AGAINST SMUGGLING COALITION (BASC)

In fact, the program has been so successful that the U.S. Customs service has assisted in the joint development and creation of the U.S. and Colombian Industry to form a Business Against Smuggling Coalition (BASC) in Colombia. The BASC chapters in Colombia include Bogota, Cartagena, Medellin, Cali and Barranquilla. The U.S. Customs service alone with private corporations have been successful in extending the security awareness and assisting in expanding the BASC to Costa Rica as well as U.S.-Mexican border sites/cities like Laredo, Nogales, El Paso, McAllen and Miami, Fl.

On November 20, 1998 an event commemorating the official inauguration of the first BASC chapter in Colombia was held in Cartagena. Among the attendees for this event were the President of Colombia, the U.S. Ambassador to Colombia, U.S. Customs Service Commissioner Raymond Kelly, several of Colombia's Cabinet Ministers, our key service provider, Seaboard Marine, as well as many members of the Colombian military and private/corporate BASC members.

In Mexico, we have developed and continue to re-develop improved operational techniques based on information and assistance from the U.S. Customs Service to prevent exposure and threats related to the illegal insertions of illegal narcotics in our U.S.-Mexican Operations. The use of dedicated and uniquely outfitted trailers and a fleet of trucks and drivers accompanied by private security have significantly thwarted attempts at the insertion of illegal narcotics.

Additionally, the attempts related to inserting illegal narcotics abroad have a direct correlation on attempted thefts and threats on employees, families, investments and service providers in the United States. At some point in the supply chain, the illegal narcotics, if inserted abroad, must be successfully removed in the United States. The constant pressure by criminal elements to use innocent and unsuspecting individuals or corporations equipment requires constant awareness and partnering with the U.S. Customs Service.

In April of this year, our U.S. in-land trucking Service provider (Salem Carriers, Inc.) participated in a combined U.S. Customs, Texas Department of Public Safety and local law enforcement operations to conduct a joint operation in the Laredo area that successfully intercepted illegal narcotics (cocaine and marijuana) coming into the United States. Additionally, several arrests were achieved of those involved in the illegal distribution.

INDUSTRY PARTNERSHIP PROGRAM (IPP)

In FY98, participants in the Industry Partnership Programs (IPP) provided information to the U.S. Customs Service, which resulted in 54 domestic seizures totaling 21,217 pounds of narcotics. During FY98, Customs efforts overseas and the Industry Partnership Participants, have assisted in 82 foreign intercepts of 42,665 pounds of narcotics detained for the United States from abroad.

AMERICAS COUNTER SMUGGLING INITIATIVE (ACSI)

In July of 1998, the Americas Counter Smuggling Initiative (ACSI) team members in Cartagena, Colombia provided training to Colombian Anti-Narcotics Police on targeting methods and examination techniques for commercial shipments. Shortly after the training, Colombian Anti-Narcotics Police in Cartagena seized over 14,000 pounds of cocaine in shipment of 192 metal spools of nylon thread.

In January 1999, representatives from the Cartagena BASC Chapter visited with U.S. Customs officials in the Port of Miami, Fl in an effort to better understand the risk and techniques used to ship illegal narcotics abroad and to enhance the best practice models to deter illegal narcotics.

ADVANCED TECHNOLOGY NEEDS CONTINUED FUNDING

Mr. Chairman, the use of new technology for Non-intrusive Inspection is critical in our joint mission to deter and cease illegal narcotics from affecting our operations, our shipment and our employees. The engagement of these new devices will expedite cargo sampling and detection of illegal narcotics. Trailers will not be subjected to traditional drilling and handling. U.S. Customs Service personnel will not be subjected to the grueling task of inspection of cargo by physical unloading and re-loading trailers in less than ideal work environments. In short, the non-intrusive technology assists our operations with through-put concerns while providing the highest degree of integrity against unwarranted insertion of illegal narcotics in the shipment and risk to our employees and service providers.

Our ability to apply the latest technological solutions accompanied with the assistance of the U.S. Customs Service to identify our exposure areas is critical. The assistance of the U.S. Customs Service, along with our own efforts, essentially reduces risk to employees, their families and to our service providers. The reduction of theft and deterrence of illegal narcotic trafficking reduces the other risks often associated with illegal narcotic trafficking.

Mr. Chairman, in summary we have learned from our experiences and from the unfortunate experiences of others that we can not move cargo internationally without the protection and assistance of agencies seeking to prevent and stop the movement of illegal narcotics. I am convinced that this is a shared interest and can best be achieved by an active supply chain informed and involved with the risk and strategies to effectivley thwart the smuggling of illegal narcotics.

Over the past four years, these industry programs have not only provided information which resulted in the seizure of over 167,000 pounds of narcotics, but reduced the risk to employees and individuals involved in legitimate international commerce. In FY98, the US Customs Service seized over 1,000,000 lbs. of narcotics. Though roughly 25% of the total narcotics were seized in commercial cargo, it is a constant vigil to protect against illegal insertions of narcotics. Critical to this effort is to inform the supply chain of the risks and the necessary steps it should undertake to protect against illegal narcotics. Seeking better partnerships and getting other key agencies involved should only reduce risk to U.S. businesses and U.S. citizens.

Mr. Chairman, I want to express other key areas that are essential to good long-term management and relationship with U.S. Customs Service.

MODACT & AUTOMATION

With the passage of the MODACT, a potential government and industry facilitation was created. The daily requirements to support and achieve customer satisfaction are increasing the need for the supply chain to become more responsive and more predictable.

The movement of manufactured components and finished product require a more fluid environment. Industry and governments are both seeking specific data elements in a time-sensitive environment to determine the acceptability of a given commercial shipment. The movement of required data in advance of a shipment is as critical as the automated collection and processing the data to U.S. Customs as is to the private sector.

Commercial cargo is dependent on predictable and timely releases accompanied by selective enforcement and secures supply chain management. It is essential to the business community to advance the automation of data collection, data processing and data retrieval to advance as quickly as possible as well as to move data requirements to better mirror more of the business processes.

The shift in many corporations to compliance groups continues to emerge into more central compliance and operational groups. The current dilemma on advanced automated export and import processing and reconciliation present substantial obstacles to both industry and government. The need for expanded hours of operation is also critical to supply our customers' demands. U.S. Customs Service automation accompanied by expanded hours of operations by both U.S. and foreign Customs operations will provided an effective use of infrastructure and can assist in reducing the congestion at the borders.

In closing Mr. Chairman, the Industry Partnership Program to reduce the importation of illegal narcotics is important to us because we can not do it alone. We need the valued assistance, cooperation and the joint leadership by the U.S. Customs Service. Likewise, I believe the joint Industry cooperation has opened the ability to move the partnership internationally where the supply-side begins.

Finally, I want to say thank you, Mr. Chairman and fellow Committee members for the Committee's past favorable action on the much-needed Caribbean Basin Enhancement legislation. I hope we will be able to achieve a successful conclusion this session on the Caribbean Basin Trade Enhancement legislation.

I appreciate the opportunity to present my views to the Committee and welcome your questions.

Thank you.

PREPARED STATEMENT OF HON. ORRIN G. HATCH

[MAY 13, 1999]

Mr. Chairman, I welcome your initiative in extending the Customs Service oversight process. For too many years, we've treated Customs as an orphan. They deserve much better. Their mission is far too important, and the great majority of their field and headquarters staffs are far too involved in managing activities critical to our foreign trade and commerce, the efficient control of legitimate arms exports, defense against drug trafficking, and many other law enforcement as well as revenue collecting functions.

I believe your initiative will continue to produce results, Mr. Chairman. Thanks to your timely review last year, we deployed more Customs inspectors to the often-ignored northern ports of entry, and vastly expanded the Customs Service's access to new and better technology.

[One of my staff visited the Los Angeles Airport [LAX] port of entry in 1996; he reported that the computer hardware equipment was so antiquated that the screen on the CRT was unreadable, and the decibel level of the printer so loud that you couldn't listen on the telephone or even speak and be heard in close conversation . . . it was as if Customs inspectors at LAX were being denied the opportunity to see or hear the intelligence needed to do their jobs. He returned this past November to the same site and reported a complete upgrade of technology].

It's the technology issue that concerns me at the moment, which I will address in my question for Commissioner Kelly. More specifically, we need efficient, labor-saving, user safe, and cost-effective non-intrusive technologies along the Southwest U.S. border and in the so-called "Southern Tier," stretching from Southern California to Puerto Rico. There are more than 35 ports of entry along this frontier. To provide the level of staffing needed to manually inspect entering and departing trucks and other vehicles, and at a rate conducive to good business practices, is almost a superhuman effort. I have therefore long promoted cooperation with DOD. In my own state of Utah, I saw how x-ray systems were usefully employed since 1988 to inspect crated weapons under the INF Treaty. (This was done at a Utah company, Hercules Aerospace, which produced the motors for the old Pershing intermediate range missiles). I was very pleased to see Customs begin exploring the use

of these systems many years ago. But I am still concerned about the progress of putting these types of systems on line.

Let me be more specific: Customs will need mobile, non-intrusive X-ray or "electron voltage" penetrating systems, for safe use and at acceptable prices. It would seem to me that the emphasis ought to be placed on mobility, for reasons mentioned above. Secondly, since we're operating in the very high photon energy ranges . . . involving frequency cycles in ranges of ten to the eighteenth power . . . and, for certain systems, at the gamma ray level, shielding users from radiation is a high and costly priority. In my judgment, Customs and DOD should not be spending taxpayer money on systems that are "gold-plated," we ended that process with the $450 hammers, or so I thought. Rather, I would hope that we can find systems that have flexible switching, allowing for different levels of electron voltage, depending on the inspection target, and which are both less costly and more safe.

Mr. Chairman, I didn't intend to get quite so technical. However, no one should misconstrue our desire to help Customs do its job better as a 1970's-era, DOD contract abuse opportunity.

I look forward to hearing from our witnesses.

PREPARED STATEMENT OF HON. ORRIN G. HATCH

[MAY 18, 1999]

Mr. Chairman, I join you in welcoming our witnesses. Customs enforcement is an issue that affects my interests on both this and the Judiciary Committees. We have heard much regarding the statistical workload of this agency. Some of Customs' accomplishments are legendary.

Customs is probably one of the most business-like agencies in this company town. And today's presentation demonstrates that. Customs uses the latest management techniques and philosophies for both internal operations and in monitoring trade and drug trafficking. They use sophisticated statistical procedures to determine where and when to husband their scarce resources to meet threat probabilities. They wisely assess costs to their operations and can even predict the "future value" of their resource commitments. It is staggering to realize that this relatively small agency manages nearly 450,000 importing company "accounts" that amount to $900 billion in transactional value.

And, Mr. Chairman, I hasten to add that the value of imports, since the enactment of the Mod Act in 1994, has grown from $589 billion to $918 billion, up 56 percent. This compares with our GDP which rose 18 percent during the same period, meaning that imports are increasing three times the rate of GDP growth. Trade is the fastest growing of the four pillars of our economy, the other three are consumer spending, government spending, and gross private domestic spending.

Today's meeting will complement last week's hearing on Customs' commercial operations, where we uncovered some of the more serious resource gaps affecting Customs' ability to optimize its performance still further. The resource deficiencies discussed then affect the enforcement performances that we consider today. Congress ought to pay careful attention to this because in Congress we bear responsibility when an agency's workload outpaces its capabilities to respond.

Mr. Chairman, I take a special interest in the on-going GAO review of Customs operations. More specifically, I will be looking for information that shows the effectiveness of the deterrent effects which we built into the Customs Modernization Act. You will recall that, during the long six-year period that we drafted the act, I opposed the excessive criminalization of offenses. Rather, I sought a Customs mission of informed compliance, meaning that every effort should be made to create incentives for compliance after the information was provided to the company. I believe Customs has done that. But there remain, in my judgment, a high enough number of "high-risk" importers and exporters that it becomes evident that self-policing will not work for everyone. For the hard-core law breakers, we need deterrents to crime, like the inevitability of prosecution. On this point, I need much more information. And I need to know if Customs is getting the cooperation that the agency needs from the Justice Department.

I look forward to hearing from our witnesses and thank the Chair.

PREPARED STATEMENT OF HON. ORRIN G. HATCH

[MAY 24, 1999]

Mr. Chairman, I want to commend the initiative that you took to look into reports of corruption in the Customs Service. At a time when we depend on Customs as our forward deployed troops against traffickers in the drug war, the reported criminal

activity by our operatives has grave consequences. Not only do wrongdoers within the Customs Service demean the fine work done by the overwhelming number of Customs personnel, but they further imperil the effectiveness and mission of our nation in eliminating this insidious threat to our society and the well-being of every American.

These are not issues that can be easily waved off as something that's inevitable in this type of drug trafficking climate. We all know that drug traffickers offer tempting propositions to many law enforcement officials; but we also know that these same devoted men and women in our anti-trafficking forces, with very few exceptions, the exceptions that concern us here today, are too concerned about the consequences for our country to fall prey to these elements.

With the permission of the Chair, I would like to present my questions for reply in writing from the Treasury witness.

I thank the chair.

PREPARED STATEMENT OF RANDOLPH C. HITE

Thank you for inviting me to participate in today's Customs Service oversight hearing. My statement will focus on Customs' Automated Commercial Environment, better known as ACE. Through ACE, Customs intends to implement much needed improvements in the way it currently enforces import trade laws and regulations, and assesses and collects import duties, taxes, and fees, which total $22 billion annually.

The need to leverage information technology to improve the way that Customs does business in the import arena is undeniable. Customs' existing import processes and supporting systems are simply not responsive to the business needs of either Customs or the trade community, whose members collectively import about $1 trillion in goods annually. These existing processes and systems are paper-intensive, error-prone, and transaction-based, and they are out of step with the just-in-time inventory practices used by the trade. Recognizing this, Congress enacted the Customs Modernization and Informed Compliance Act, or "Mod" Act, to define legislative requirements for improving import processing through an automated system.[1]

Customs fully recognizes the severity of the problems with its approach to managing import trade and is modernizing its import processes and undertaking ACE as its import system solution. Begun in 1994, Customs' estimate of the system's 15-year life cycle cost is about $1.05 billion, although this estimate is being revised upwards. In light of ACE's enormous mission importance and price tag, Customs' approach to investing in and engineering ACE demands disciplined and rigorous management practices. Such practices are embodied in the Clinger-Cohen Act of 1996[2] and other legislative and regulatory requirements, as well as accepted industry system/software engineering models, such as those published by the Software Engineering Institute (SEI).[3]

Unfortunately, Customs has not employed such practices on ACE over the last 5 years. Our February 1999 report on ACE,[4] upon which my testimony today is based, describes serious ACE management and technical weaknesses. The weaknesses that we reported are: (1) building ACE without a complete and enforced enterprise systems architecture, (2) investing in ACE without a firm basis for knowing that it is a cost effective system solution, and (3) building ACE without employing engineering rigor and discipline. My testimony will address each of these points as well as our recommendations for correcting them. To Customs' credit, its leadership has agreed with our findings, has initiated actions to implement our recommendations,

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[1] Customs refers to Title VI of the North American Free Trade Agreement Implementation Act (Public Law 103–182, 19 U.S.C. 1411 et seq) as the Customs Modernization and Informed Compliance Act or "Mod" Act.

[2] Although the Clinger-Cohen At (Public Law 104–106) was passed after Customs began developing ACE, its principles are based on practices that are widely considered to be integral to successful information technology (IT) investments. For an analysis of the management practices of several leading private and public sector organizations on which the Clinger-Cohen Act is based, see Executive Guide: Improving Mission Performance Through Strategic Information Management and Technology (GAO/AIMD–94–115, May 1994). For an overview of the IT management process envisioned by Clinger-Cohen, see Assessing Risk and Returns: A Guide for Evaluating Federal Agencies' IT Investment Decision-making (GAO/AIMD–10.1.13, February 1997).

[3] Software Development Capability Maturity Model℠ (SW–CMM®) and Software Acquisition Capability Maturity Model℠ (SA–CMM®). Capability Maturity Model℠ is a service mark of Carnegie Mellon University, and CMM® is registered in the U.S. Patent and Trademark Office.

[4] Customs Service Modernization: Serious Management and Technical Weaknesses Must Be Corrected (GAO/AIMD–99–41, February 26, 1999).

and is committed to seeing that these actions are completed before investing huge sums of money in the system.

ACE: A BRIEF HISTORY

Customs began ACE in 1994, and its early estimate of the cost and time to develop the system was $150 million over 10 years. At this time, Customs also decided to first develop a prototype of ACE, referred to as NCAP (National Customs Automation Program prototype), and then to complete the system. In May 1997,[5] we reported that Customs' original schedule for completing the prototype was January 1997, and that Customs did not have a schedule for completing ACE. At that time, Customs agreed to develop a comprehensive project plan for ACE.

In November 1997, Customs estimated that the system would cost $1.05 billion to develop, operate, and maintain throughout its life cycle. Customs plans to develop and deploy the system in 21 increments from 1998 through 2005, the first four of which would constitute NCAP.

Currently, Customs is well over 2 years behind its original NCAP schedule. Because Customs experienced problems in developing NCAP software in-house, the first NCAP release was not deployed until May 1998—16 months late. In view of the problems it experienced with the first release, Customs contracted out for the second NCAP release, and deployed this release in October 1998—21 months later than originally planned. Customs' most recent dates for deploying the final two NCAP releases (0.3 and 0.4) are March 1999 and September 1999, which are 26 and 32 months later than the original deployment estimates, respectively. According to Customs, these dates will slip farther because of funding delays.

Additionally, Customs officials told us that a new ACE life cycle cost estimate is being developed, but that it was not ready to be shared with us. At the time of our review, Customs' $1.05 billion estimate developed in 1997 was the official ACE life cycle cost estimate. However, a January 1999 ACE business plan specifies a $1.48 billion life cycle cost estimate.

CUSTOMS HAS BEEN DEVELOPING ACE WITHOUT A COMPLETE ENTERPRISE SYSTEMS ARCHITECTURE

At the time of our review, Customs was not building ACE within the context of an enterprise systems architecture, or "blueprint" of its agencywide future systems environment. Such an architecture is a fundamental component of any rationale and logical strategic plan for modernizing an organization's systems environment. As such, the Clinger-Cohen Act requires agency Chief Information Officers (CIO) to develop, maintain, and implement an information technology architecture. Also, the Office of Management and Budget (OMB) issued guidance in 1996 that requires agency IT investments to be architecturally compliant. These requirements are consistent with, and in fact based on, information technology management practices of leading private and public sector organizations.

Simply stated, an enterprise systems architecture specifies the system (e.g., software, hardware, communications, security, and data) characteristics that the organization's target systems environment is to possess. Its purpose is to define, through careful analysis of the organization's strategic business needs and operations, the future systems configuration that supports not only the strategic business vision and concept of operations, but also defines the optimal set of technical standards that should be met to produce homogeneous systems that can interoperate effectively and be maintained efficiently. Our work has shown that in the absence of an enterprise systems architecture, incompatible systems are produced that require additional time and resources to interconnect and to maintain and that suboptimize the organization's ability to perform its mission.[6]

We first reported on Customs' need for a systems architecture in May 1996 and May 1997.[7] In response, Customs developed and published an architecture in July and August 1997. We reviewed this architecture and reported in May 1998 that it was not effective because it was neither complete nor enforced.[8] For example, the architecture did not;

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[5] Customs Service Modernization: ACE Poses Risks and Challenges (GAO/T-AIMD-97-96, May 15, 1997).

[6] Air Traffic Control: Complete and Enforced Architecture Needed for FAA Systems Modernization (GAO/AIMD-97-30, February 3, 1997).

[7] Customs Service Modernization Strategic Information Management Must Be Improved for National Automation Program To Succeed (GAO/AIMD-96-57, May 9, 1996) and Customs Service Modernization: ACE Poses Risks and Challenges (GAO/T-AIMD-97-96, May 15, 1997).

[8] Customs Service Modernization: Architecture Must Be Complete and Enforced to Effectively Build and Maintain Systems (GAO/AIMD-98-70, May 5, 1998).

(1) fully describe Customs' business functions and their relationships,
(2) define the information needs and flows among these functions, and
(3) establish the technical standards, products, and services that would be characteristic of its target systems environment on the basis of these business specifications.

Accordingly, we recommended that Customs complete its enterprise information systems architecture and establish compliance with the architecture as a requirement of Customs' information technology investment management process. In response, Customs agreed to develop a complete architecture and establish a process to ensure compliance. Customs reports that its architecture will be completed in May 1999. Also, in January 1999, Customs changed its internal procedures to provide for effective enforcement of its architecture, once it is completed. Until the architecture is completed and enforced, Customs risks spending millions of dollars to develop, acquire, and maintain information systems, including ACE, that do not effectively and efficiently support the agency's mission needs.

CUSTOMS HAS NOT BEEN MANAGING ITS INVESTMENT IN ACE EFFECTIVELY

Effective IT investment management is predicated on answering one basic question: is the organization doing the "right thing" by investing specified time and resources in a given project or system. The Clinger-Cohen Act and OMB and GAO guidance together provide an effective IT investment management framework for answering this question. Among other things, they describe the need for:

(1) identifying and analyzing alternative system solutions,
(2) developing reliable estimates of the alternatives' respective costs and benefits and investing in the most cost beneficial alternative, and
(3) to the maximum extent practical, structuring major projects into a series of increments to ensure that each increment constitutes a wise investment.

Customs did not satisfy any of these requirements for ACE. First, Customs did not identify and evaluate a full range of alternatives to its defined ACE solution before commencing development activities. For example, Customs did not consider how ACE would relate to another Treasury-proposed system for processing import trade data, known as the International Trade Data System (ITDS), including considering the extent to which ITDS should be used to satisfy needed import processing functionality. Initiated in 1995 as a project to develop a coordinated, government-wide system for the collection, use, and dissemination of trade data, the ITDS project is headed by the Treasury Deputy Assistant Secretary for Regulatory, Tariff and Trade Enforcement. The system is expected to reduce the burden federal agencies place on organizations by requiring that they respond to duplicative data requests. Treasury intends for the system to serve as the single point for collecting, editing, and validating trade data as well as collecting and accounting for trade revenue. At the time of our review of ACE, these functions were also planned for ACE.

Similarly, Customs did not evaluate different ACE architectural designs, such as the use of a mainframe-based versus client server-based hardware architecture. Also, Customs did not evaluate alternative development approaches, such as acquisition versus in-house development. In short, Customs committed to and began building ACE without knowing whether it had chosen the most cost-effective alternative and approach.

Second, Customs did not develop a reliable life cycle cost estimate for the approach it selected. SEI has developed a method for project managers to use to determine the reliability of project cost estimates. Using SEI's method, we found that Customs' $1.05 billion ACE life cycle cost estimate was not reliable, and that it did not provide a sound basis for Customs' decision to invest in ACE. For example, in developing the cost estimate, Customs did not (1) use a cost model, (2) account for changes in its approach to building different ACE increments, (3) account for changes to ACE software and hardware architecture, or (4) have historical project cost data upon which to compare its ACE estimate.

Moreover, the $1.05 billion cost estimate used to economically justify ACE omitted relevant costs. For instance, the costs of technology refreshment and system requirements definition were not included (see table 1). Exacerbating this problem, Customs represented its ACE cost estimate as a precise point estimate rather than explicitly disclosing to investment decisionmakers in Treasury, OMB, and Congress the estimate's inherent uncertainty.

TABLE 1: ESTIMATED COSTS OMITTED FROM CUSTOMS' ACE COST-BENEFIT ANALYSIS

Excluded cost description	Excluded cost estimate
Hardware and software upgrades at each port office (e.g., desktop workstations and operating systems, application and data servers, database management systems).	$73 to $172 million
Security analysis, project planning and management, and independent verification and validation	$23 million
Requirements definition, component integration, regression testing, and training.	No estimate available

Customs' projections of ACE benefits were also unreliable because they were either overstated or unsupported. For example, the analysis includes $203.5 million in savings attributable to 10 years of avoided maintenance and support costs on the Automated Commercial System (ACS)—the system ACE is to replace. However, Customs would not have avoided maintenance and support costs for 10 years. At the time of Customs' analysis, it planned to run both systems in parallel for 4 years, and thus planned to spend about $53 million on ACS maintenance and support during this period. As another example, $650 million in savings was not supported by verifiable data or analysis, and $644 million was based on assumptions that were analytically sensitive to slight changes, making this $644 million a "best case" scenario.

Third, Customs is not making its investment decisions incrementally as required by the Clinger-Cohen Act and OMB. Although Customs has decided to implement ACE as a series of 21 increments, it is not justifying investing in each increment on the basis of defined costs and benefits and a positive return on investment for each increment. Further, once it has deployed an increment at a pilot site for evaluation, it is not validating the benefits that the increment actually provides, and it is not accounting for costs on each increment so that it can demonstrate that a positive return on investment was actually achieved. Instead, Customs estimated the costs and benefits for the entire system—all 21 increments, and used this as economic justification for ACE.

Mr. Chairman, our work has shown that such estimates of many system increments to be delivered over many years are impossible to make accurately because later increments are not well understood or defined. Also, these estimates are subject to change in light of experiences on nearer term increments and changing business needs. By using an inaccurate, aggregated estimate that is not refined as increments are developed, Customs is committing enormous resources with no assurance that it will achieve a reasonable return on its investment. This "grand design" approach to managing large system modernization projects has repeatedly proven to be ineffective across the federal government, resulting in huge sums invested in systems that do not provide expected benefits. Failure of the grand design approach was a major impetus for the IT management reforms contained in the Clinger-Cohen Act.

CUSTOMS HAS NOT BEEN MANAGING ACE SOFTWARE DEVELOPMENT/ACQUISITION EFFECTIVELY

Software process maturity is one important and recognized measure of determining whether an organization is managing a system or project the "right way," and thus whether or not the system will be completed on time, within budget, and deliver promised capabilities. The Clinger-Cohen Act requires agencies to implement effective IT management processes, such as processes for managing software development and acquisition. SEI has developed criteria for determining an organization's software development and acquisition effectiveness or maturity.

Customs lacks the capability to effectively develop or acquire ACE software. Using SEI criteria for process maturity at the "repeatable" level, which is the second level on SEI's five-level scale and means that an organization has the software development/acquisition rigor and discipline to repeat project successes, we evaluated ACE software processes. In February 1999,[9] we reported that the software development processes that Customs was employing on NCAP 0.1, the first release of ACE, were not effective. For example, we reported that Customs lacked effective software configuration management, which is important for establishing and maintaining the integrity of the software products during development. Also, we reported that Customs lacked a software quality assurance program, which greatly increased the risk of ACE software not meeting process and product standards. Further, we reported that Customs lacked a software process improvement program to effectively address

[9] Customs Service Modernization: Ineffective Software Development Processes Increase Customs System Development Risks (GAO/AIMD–99–35. February 11, 1999).

these and other software process weaknesses. Our findings concerning ACE software development maturity are summarized in table 2.

TABLE 2: SUMMARY OF ACE SOFTWARE DEVELOPMENT MATURITY

Key process areas	Satisfied	Not satisfied
Requirements management		X
Software project planning		X
Software project tracking and oversight		X
Software quality assurance		X
Software configuration management		X

Note: These represent five of six level 2 key process areas in SEI's Software Development Capability Maturity Model. We did not evaluate ACE in the sixth level 2 key process area—software subcontract management—because Customs did not use subcontractors on ACE.

As discussed in our brief history of ACE, after Customs developed NCAP 0.1 in-house, it decided to contract out for the development of NCAP 0.2, thus changing its role on ACE from being a software developer to being a software acquirer. According to SEI, the capabilities needed to effectively acquire software are different than the capabilities needed to effectively develop software. Regardless, we reported later in February 1999 [10] that the software acquisition processes that Customs was employing on NCAP 0.2 were not effective. For example, Customs did not have an effective software acquisition planning process and, as such, could not effectively establish reasonable plans for performing software engineering and for managing the software project. Also, Customs did not have an effective evaluation process, meaning that it lacked the capability for ensuring that contractor-developed software satisfied defined requirements. Our findings concerning ACE software acquisition maturity are summarized in table 3.

TABLE 3: SUMMARY OF ACE SOFTWARE ACQUISITION MATURITY

Key process areas	Satisfied	Not satisfied
Software acquisition planning		X
Solicitation		X
Requirements development and management		X
Project office management		X
Contract tracking and oversight		X
Evaluation		X
Transition and support		X
Acquisition risk management		X

Note: These represent seven level 2 key process areas in SEI's Software Acquisition Capability Maturity Model. We also evaluated one key process area associated with the "defined" level of process maturity (level 3)—acquisition risk management.

CUSTOMS HAS INITIATED ACTIONS TO IMPLEMENT OUR RECOMMENDATIONS FOR STRENGTHENING ACE MANAGEMENT

To address ACE management weaknesses, we recommended that Customs:

(1) analyze alternative approaches to satisfying its import automation needs, including addressing the ITDS/ACE relationship;

(2) invest in its defined ACE solution incrementally, meaning for each system increment (a) rigorously estimate and analyze costs and benefits, (b) require a favorable return-on-investment and compliance with Customs' enterprise systems architecture, and (c) validate actual costs and benefits once an increment is piloted, compare actuals to estimates, use the results in deciding on future increments, and report the results to congressional authorizers and appropriators;

(3) establish an effective software process improvement program and correct the software process weaknesses identified in our report, thereby bringing ACE software process maturity to a least an SEI level 2; and

(4) require at least SEI level 2 processes of all ACE software contractors.

In commenting on our February 1999 report, the Commissioner of Customs agreed with our findings and committed to implementing our recommendations. In April 13, 1999 testimony, the Commissioner outlined several actions Customs has under-

[10] GAO/AIMD–99–41, February 26, 1999.

way to improve ACE project management and address our recommendations.[11] In brief, Customs:

(1) plans to acquire the services of a prime contractor that is at least SEI level 3 certified to help Customs implement mature software processes and plan, implement, and manage its modernization efforts, including ACE;

(2) plans to hire a Federally Funded Research and Development Center (FFRDC) to support solicitation, selection, contract award, contract management, and ongoing oversight of the prime contractor;

(3) has hired a contractor to update and improve the ACE life cycle cost estimate;

(4) has retained an audit firm to provide independent reviews of Customs' methodology for estimating ACE costs and revised cost/benefit analysis;

(5) has engaged a contractor to update and improve the ACE cost/benefit analysis by addressing our concerns, including use of ITDS as the interface for ACE;

(6) plans to perform additional cost/benefit analyses of ACE increments and analyze alternative approaches to building ACE; and

(7) plans to ensure that each ACE increment is compliant with Customs' enterprise systems architecture.

CONCLUSIONS

Successful systems modernization is absolutely critical to Customs' ability to perform its trade import mission efficiently and effectively in the 21st century. Systems modernization success, however, depends on doing the "right thing, the right way." To be "right," organizations must (1) invest in and build systems within the context of a complete and enforced enterprise systems architecture, (2) make informed, data-driven decisions about investment options based on expected and actual return-on-investment for system increments, and (3) build system increments using mature software engineering practices. Our reviews of agency system modernization efforts over the last 5 years point to weaknesses in these three areas as the root causes of their not delivering promised system capabilities on time and within budget.[12]

Until Customs corrects its ACE management and technical weaknesses, the federal government's troubled experience on other modernization efforts is a good indicator for ACE. In fact, although Customs does not collect data to know whether the first two ACE releases are already falling short of cost and performance expectations, the data it does collect on meeting milestones show that the first two releases have taken about 2 years longer than originally planned. This is precisely the type of unaffordable outcome that can be avoided by making the management and technical improvements we recommended.

To Customs' credit, it fully recognizes the seriousness of the situation, has quickly initiated actions to begin correcting its ACE management and technical weaknesses, and is committed to each of these actions. We are equally committed to working with Customs as it strives to do so and with Congress as it oversees this important initiative.

This concludes my statement. I would be glad to respond to any questions that you or other Members of the Committee may have at this time.

PREPARED STATEMENT OF JAMES E. JOHNSON

Thank you Mr. Chairman, Senator Moynihan, and members of the Committee. It is an honor for me to be here today in support of the United States Customs Service and Customs' efforts to carry out its intricate, dual responsibilities of facilitating international trade and pursuing aggressive enforcement of the law.

With me today is Raymond W. Kelly, Commissioner of the U.S. Customs Service, and Nancy S. Killefer, the Assistant Secretary for Management and Chief Financial

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[11] Statement of Commissioner Raymond, W. Kelly, Commissioner of the Customs Service, Authorization Hearing with the Customs Service Before the House Committee on Ways and Means Trade Subcommittee, April 13, 1999.

[12] Tax System Modernization: Management and Technical Weakness Must Be Corrected if Modernization is to Succeed (GAO/AIMD–95–156, July 26, 1995); Tax System Modernization: Actions Underway but IRS Has Not Yet Corrected Management and Technical Weakness (GAO/AIMD–96–106, June 7, 1996); Tax Systems Modernization: Blueprint Is a Good Start but Not Yet Sufficiently Complete to Build or Acquire Systems (GAO/AIMD/GGD–98–54, February 24, 1998); Air Traffic Control: Immature Software Acquisition Processes Increase FAA System Acquisition Risks (GAO/AIMD–97–47, March 21, 1997: Air Traffic Control: Complete and Enforced Architecture Needed for FAA Systems Modernization (GAO/AIMD–97–30, February 3, 1997); and Air Traffic Control: Improved Cost Information Needed to Make Billion Dollar Modernization Investment Decisions (GAO/AIMD–97–20, January 22, 1997).

Officer of the Department of the Treasury. I ask the Chairman's consent that my written statement be entered in full into the official record of these proceedings.

INTRODUCTION

As each year passes, the world becomes a more complex and a more dangerous place. The danger to law enforcement personnel is brought home to all of us this week as we mark Police Week and honor those who have sacrificed their lives in service to our Nation. Customs' vital place within this law enforcement community and in the service it provides to the country makes this an important hearing. We thank the Committee for its continuing interest in, and support for the U.S. Customs Service.

This is a unique moment in Customs' long and proud history. It faces daunting challenges based upon a mission that, on the one hand, requires the facilitation of legitimate commerce and travel while, on the other, requires the greatest vigilance in countering attempts to smuggle narcotics and other contraband into our country.

For our nation on the whole, the falling of trade and other barriers has had the positive effect of increasing the flow of legitimate goods and honest travelers across borders. It also, however, has created more demands on Customs, which constantly must guard against drug traffickers who might seek to hide their illicit products in ostensibly legitimate cargo. For Customs, this has meant a heightening of the challenges it faces as either the first welcome to the honest traveler or the first line of defense against the dishonest.

Customs is meeting these trade and enforcement challenges in large part through the dedication and professionalism of its people. It also, however, is moving into a better position to respond to challenges because of its willingness to adopt changes that will make an already strong agency that much stronger.

One of its most powerful agents of change is its Commissioner. Through his entire professional career and, most notably for purposes of this hearing, as Under Secretary for Enforcement and Commissioner of Customs, Raymond Kelly has had a unique capability of evaluating an organization, reinforcing those elements proven to be constructive, and overhauling those in need of repair. His ability to make change work for an organization has always led to a more productive workforce, more accountable management, and better service to the public.

In the case of Customs, the Commissioner is pursuing his agenda for change through development of a detailed action plan that he actually began developing while serving as Under Secretary. The action plan includes tangible goals for improvements in the organization's structure, management, and operations.

My remarks today will focus mainly on the Department's role, particularly that of the Office of Enforcement, in providing support to Commissioner Kelly and Customs as they pursue the action plan and perform Customs' mission in an environment of constrained budgets and increasing demand for services.

THE ROLE OF THE OFFICE OF ENFORCEMENT

Our support of Customs and its mission comes in a variety of forms, two of which are policy guidance and operational oversight. By enhancing both, we help ensure that Customs performs its mission as safely, professionally, and effectively as possible.

Policy oversight

The Office of Enforcement is actively involved in the development of Customs-related programs such as Operations Hardline, Gateway, and Brass Ring, as well as the Border Coordination Initiative. These programs will better ensure that Customs has the tools it needs and deserves to combat narcotics trafficking.

In addition, Enforcement works with Customs in the development and maintenance of vital public-private partnerships to enhance trade, revenue collection, and industry compliance, most notably through the Commercial Operations Advisory Committee (COAC). This advisory committee was established several years ago at the initiative of this Committee. It provides Treasury, and the Customs Service, with the perspectives and advice of the private sector groups affected by Customs' operations. Over the years, COAC has been highly influential on issues such as development of an automated export reporting system, and streamlining of Customs procedures.

Committee members also have assisted us in organizing efforts within the trade community to keep drugs out of commercial shipments. Committee members were leaders in creating the Business Anti-Smuggling Coalition and the Border Carrier Initiative, both of which have effectively involved members of the international trade community in self-policing efforts.

Additionally, Customs has sought to leverage private sector resources to assist us in meeting our goals. For example, at the Federal Express hub in Memphis, Tennessee, Customs is able to use on-site resources to assist in clearing packages entering and leaving the United States.

Our support of Customs extends to the international arena, where we work to obtain cooperation of other governments on issues vital to Customs, including counternarcotics cooperation and the harmonization of Customs procedures. We also are creating a single International Trade Data System for the collection, use, and dissemination of information on international trade. One of our most important efforts is working with Customs to modernize its existing automated commercial system through the development of a new Automated Commercial Environment (ACE), which will be critical to meeting trade processing needs of the future.

We also provide policy guidance to Customs and all of the Treasury bureaus on operational issues. Policies created through such guidance include the Use of Force Policy, Guidelines for Sensitive Undercover Operations, and General Guidelines on the Use of Cooperating Individuals and Confidential Informants. Consistent policies allow the various law enforcement agencies to work more effectively and safely together on task forces.

In addition, to strengthen policy coordination among Customs, other bureaus, and the Department, such mechanisms as the Treasury Enforcement Council, the Treasury Terrorism Advisory Group, and the Financial Crime Steering Committee and Working Group have been established at the Departmental level. The Office of Enforcement also promotes coordination with other agencies through representation of Customs and other bureaus at interagency meetings involving Justice, the National Security Council, ONDCP, and the Department of State.

Office of professional responsibility

To further enhance day-to-day operational oversight, we created the Office of Professional Responsibility (OPR) within the Office of Enforcement. OPR is structured to have a Senior Oversight Advisor responsible for direct oversight of each enforcement bureau and office. In addition, OPR will have advisors who deal exclusively with crosscutting issues, such as internal affairs, inspection, training, and EEO.

While relatively recent in origin, OPR already has focused a great deal on the Customs Service in an effort to support and improve the agency's pursuit of its mission. Immediately upon creation of OPR, it was tasked with performing a top-to-bottom, year-long review of the Customs Office of Internal Affairs and its processes. The report was released to the Congress in February 1999. The recommendations in OPR's report, most of which have already been implemented by Commissioner Kelly, will help dramatically improve Customs' internal affairs capability.

Through OPR and the constant attention of senior policy makers, the Office of Enforcement will ensure that the type of focus brought to the Internal Affairs review will continue as Customs seeks to improve all of its operations.

Strategic planning process

Treasury is committed to using the strategic planning process to accomplish our goals and guide budget formulation and resource allocation. The Secretary, Deputy Secretary and the Under Secretary for Enforcement were personally involved in the development of Treasury's FY 1997–2002 Strategic Plan.

Working closely with the Office of Management and Treasury's law enforcement bureaus, the Office of Enforcement evaluated the missions and unique characteristics of the bureaus and formulated broad policy goals for the Department's law enforcement mission. These policy goals were discussed with enforcement bureau heads in two planning off-sites chaired by the Secretary in June 1997. Based on the Secretary's guidance, Enforcement established priorities for Customs at that time to: (1) prevent drugs from entering the country; and (2) ensure the highest percentage of compliance to tariff and trade laws. Customs, as well as the other bureaus, then developed strategic plans which were reviewed, refined, and approved by the Department.

The strategic plans provide direction for the budget formulation process and lay the foundation for performance planning. Beginning in FY 1997, Treasury defined performance goals for each budget activity and integrated into our budget justification the proposed performance plan for the budget year, and the final performance plan for the current year. Thus, budget justification documents request resources under each budget activity and are linked to their respective performance goals and supporting performance measures.

In addition, Enforcement is also working to coordinate law enforcement measures with other agencies. During 1998, the Offices of Enforcement and Management jointly created the Law Enforcement Performance Measures Working Group to for-

malize the intra-agency coordination of law enforcement measures. While there is much to be done in this area, Customs worked with the Department of Agriculture and the Immigration and Naturalization Service to develop the interagency goal of clearing international air passengers in 30 minutes or less, while improving enforcement and regulatory processing.

As the Committee is aware, the performance measurement process throughout the government is continuing to evolve. However, we are making a concerted effort to measure and assess bureau performance in a proactive manner that is linked to resource allocation. Equally important, we are striving to assure the presentation of key measures that reflect program results rather than the traditional output oriented or workload measures. We share the Committee's goal of ensuring that we have the right measures and incorporating them in our budget process.

As the performance measurement system evolves, we continue to assess how accurately the measures in question reflect organizational effectiveness. Currently, the measures judge success only as meeting a precise numeric goal, without reference to how close a bureau comes to achieving that goal.

Thus, in FY 1998, Treasury law enforcement achieved approximately 63 percent of its 115 performance targets. For its part, the Customs Service met approximately 46 percent of its 48 performance targets for FY 1998. If one includes those measures where the Treasury law enforcement bureaus' performance was at least 90 percent, 83 percent of the measures were met, and for Customs in particular, their performance was at 79 percent. We are reviewing these results to determine how we can work with Customs to improve its overall performance. As part of this review, we are looking to determine whether the measures set were appropriate and that the measures accurately reflect program results. To this end, Enforcement has worked with Customs to refine its targets for FY 2000. As this process continues, we expect to make further improvements in future presentations.

As the amount and quality of performance data grows more robust, Treasury will continue to formulate its budget proposals based on concerns about gaps in performance. In many cases, demand-driven workload may be challenging the capacity to achieve acceptable results. Despite a tremendous increase in its responsibilities, Customs is making the best possible effort to achieve its goals. Automation is critical to Customs' ability to enhance its efficiency and continue to meet its goals. That is the principal reason the ACE initiative is so vital. Other cases may also justify resource enhancements for sensible investments in technology that improve productivity while also improving quality (e.g., non-intrusive inspection equipment for ports and border crossings). We are committed to working closely with the Committee in making these assessments.

CONCLUSION

In summary, the Treasury Department is proud—and I am personally proud—of the contributions that the U.S. Customs Service has made and continues to make to this Nation. Treasury and Customs have defined goals and objectives to ensure excellence in protecting our borders, defeating financial crimes, and facilitating international commerce and passenger service. Increasingly realistic strategies and goals, effective law enforcement and compliance, and a commitment to work in partnership with the regulated commercial community toward modernization, will enable Customs to make great strides in meeting current challenges and to begin preparations for the daunting challenges facing us in the 21st century.

PREPARED STATEMENT OF WILLIAM A. KEEFER

Chairman Roth and distinguished Members of the Committee, thank you for the opportunity to appear before you. As the Assistant Commissioner of Internal Affairs for the United States Customs Service, I am pleased to have been invited here today to discuss Commissioner Kelly's actions to reinforce the organizational integrity of the Customs Service.

As you are aware, I joined the Customs Service as Assistant Commissioner for Internal Affairs in February of this year. Prior to assuming my responsibilities with this agency, I was a career federal prosecutor. I served as Interim United States Attorney in the Southern District of Florida and as Deputy Chief of the Public Integrity Section at the Department of Justice. In my 23 years as a federal prosecutor, I investigated, prosecuted or supervised hundreds of corruption cases involving individuals that ranged from agency clerks to federal judges. I dealt with virtually every internal affairs, professional responsibility and Inspector General's office in the federal government. While in the Miami United States Attorney's office, I was directly involved in some of the best—and worst—Customs Internal Affairs investigations

and prosecutions. In short, I know what it takes to successfully investigate and prosecute federal law enforcement corruption.

When I assumed my new position with the Customs Service, Commissioner Kelly's directive was clear: help him institute any and all measures necessary to ensure the highest standards of integrity throughout the agency. Mr. Chairman, I am committed to that goal and welcome the challenge. Misconduct by Customs employees will not be tolerated under my watch.

Before addressing the reforms we are undertaking to ensure the highest caliber of professional standards and ethics within the agency, I would like to take a moment to describe our employees. The vast majority are well-trained, highly motivated and competent professionals who devote their lives to carrying out what may be the most diverse and complicated mission of any agency in the federal government. Every internal and external review of Customs has concluded that no systemic corruption exists within the agency. These same reviews conclude that 99 percent of our workforce are women and men of the highest integrity. While instances of corruption in Customs are few, however we may not have always done a good job in responding to allegations of misconduct. That is changed.

We all know about the corrupting influences that Customs employees face daily. We are committed to institutionalizing a system that will discourage our employees from succumbing to those temptations and which will detect and punish those who violate our laws or regulations. We want everyone to understand the rules as well as the consequences of any illegal or improper activities. We are making changes that will remain in place regardless of who heads the agency in the future.

As we implement the reforms necessary to ensure greater integrity and responsibility on the part of all employees, we know you will be watching as you carry out your oversight responsibilities. We welcome that oversight and we want all our employees to understand that there will be oversight of their activities as well.

Before I was appointed Assistant Commissioner, Mr. Kelly, who was at the time Under Secretary of the Treasury for Enforcement, had already undertaken an intensive and focused review of all internal investigative and disciplinary processes within the agency. In addition, to elevate the issue of integrity to the highest rung of the agency ladder, Commissioner Kelly took several important steps. First, he placed my office—the Office of Internal Affairs—under his direct supervision. As a result, I report directly to the Commissioner; there is no intermediary between us. It is my job to keep him fully informed of integrity issues and investigations, and to make recommendations on how to strengthen and professionalize the Internal Affairs mission. As you know, Commissioner Kelly demands top to bottom accountability from his people. He wants to know what the problems of his agency are. He wants solutions, not excuses.

In addition to elevating my office, the Commissioner elevated other important positions in Internal Affairs as well. He created a Senior Executive Service level Deputy Assistant Commissioner position for Internal Affairs. That person will work closely with me to ensure managerial control and operational effectiveness. He also elevated the position of the Regional Special Agents in Charge to SES levels, giving those positions parity with other federal law enforcement agencies. These new, permanent positions will attract the highest caliber of applicants throughout Customs. The benefit to Internal Affairs will be immediate and lasting. Mr. Chairman, I believe these actions underscore the personal priority and strong commitment the Commissioner places on rooting out corruption within the agency. Let me take a moment to describe some of the reforms that Commissioner Kelly is implementing:

REPORTING MISCONDUCT

The Commissioner's review showed that the process for reporting misconduct was flawed. Under the old system, the options for reporting misconduct were diverse and often confusing. Some allegations were made in the form of a passing comment to any available supervisor. Others were made in writing or through direct contact with the Office of Internal Affairs. And some types of allegations were not required to be reported to Internal Affairs at all. The procedures for documenting these allegations, where they existed at all, were similarly broad. To correct the problem, every allegation of misconduct, without exception, is now being reported directly to my office. Every allegation is now being tracked by my office. This new procedure is simple, unambiguous and ensures accountability.

To make this process work efficiently, my office is now staffed with a small cadre of specially trained intake officers who make an initial determination regarding the seriousness of each reported allegation of misconduct, including whether it is time-sensitive or places the mission, personnel, or resources of the Customs Service in immediate danger. Allegations of misconduct are scrutinized daily by an Intake Re-

view Group of Headquarters-level Internal Affairs agents and Labor and Employee Relations Specialists. This team of experts decides whether and where to refer the allegation for further action. This standardized process focuses reporting of suspected misconduct and alleged criminal activity in a way which guarantees the most effective response. In addition, a 24-hour toll-free hotline and operations center has been created and is staffed by Internal Affairs personnel to facilitate the timely reporting of allegations of misconduct.

DOCUMENTATION AND TIME LIMITS

The new allegation intake system triggers two important processes to ensure greater accountability. First, a retrievable computer record will be created that will follow the allegation from receipt to final disposition. Second, a clock will begin ticking. For noncriminal allegations, specific time limits have been incorporated into the intake system to govern when appropriate referral, investigation, reporting and final action must be completed. Managers will be held accountable for compliance with these deadlines. Furthermore, criminal investigations will be more closely supervised. The quality and timeliness of these investigations are of particular concern to me. Failure to exhaust viable leads or to interview knowledgeable witnesses is inexcusable. An untimely report is often a useless report. These are failings of supervision, both in the field and at Headquarters, and will not be tolerated. We will require frequent case reviews by field supervisors, which will be tracked by Headquarters. Each noncriminal Report of Investigation will be reviewed by attorneys at Headquarters before being approved by me, and every Report of Investigation will include a clear finding for each allegation investigated by Internal Affairs. The new standards and review process will serve to focus and improve the quality of the Internal Affairs work product.

TRACKING CASES

Perhaps the most deficient area of Internal Affairs was our inability to track a case from its inception to final disposition. Cases investigated by Internal Affairs and then referred to management for administrative disposition were virtually impossible to follow. Our new automated Case Management System will merge the investigative and discipline case tracking systems and provide us with the tools to monitor the status and disposition of all cases. I am not overstating the importance of the new tracking system when I say it is the key to ensuring accountability on all levels.

SPECIAL INVESTIGATIVE UNIT

An Internal Affairs special investigative unit is being formed at Customs Headquarters to handle the most serious and high-level cases. This rapid response team will consist of a cadre of highly experienced agents at the GS-14 level, which is a unique status for nonsupervisory personnel. These agents will be tasked with the investigation of critical incidents worldwide, and they will report directly to me. They will also quickly and efficiently handle misconduct investigations of SES and GS-15 personnel when the Inspector General returns these cases to Customs for investigation. There will be no foot-dragging when high-level employees and high-profile matters are investigated by this new unit.

ROTATION

As you all know, there is always a degree of tension between investigators and internal affairs personnel in every law enforcement agency. To improve cooperation and effectiveness between these units, the Commissioner has instituted a rotation process of senior agents between the two offices, including GS-13s, 14s and 15s. This rotation will enhance agents' understanding of investigative processes and build a talent pool of future agency leaders. We respectfully disagree with the Inspector General's recent conclusions regarding rotation between Internal Affairs and the Office of Investigations. The clear majority of Internal Affairs investigations do not involve Office of Investigations agents. For that minority which does, a clear recusal policy and strong supervision will overcome any legitimate questions concerning a lack of objectivity by Internal Affairs.

STREAMLINING

To improve efficiency and enhance accountability for our anti-corruption efforts, the Commissioner has restructured the Internal Affairs field operation, reducing the number of regions from five to four. The most important restructuring will take place along the critical Southwest Border. Under the new plan, the entire Southwest

Border will fall under the control of a single Regional Special Agent in Charge. This will provide a single voice to effectively and efficiently deal with corruption issues on this long and very crucial border.

Retaliation and the fear of retaliation have been persistent allegations at Customs. Some employees have expressed fear of retaliation by their managers if they report misconduct to Internal Affairs for investigation. We are taking measures to address this issue. First, specific training about retaliation and the Whistleblower Protection Act will be made a part of the Internal Affairs Basic Course beginning June 21, 1999. Second, in appropriate investigations, Internal Affairs agents will specifically advise managers whom they interview about the rules prohibiting retaliation against their employees. Third, I will work with my fellow Assistant Commissioners to make sure that retaliation allegations are aggressively and effectively investigated and resolved through the disciplinary process.

As the Commissioner has stated previously, the way Customs administers discipline has been revamped as well. For the first time, a service wide Disciplinary Review Board will screen all substantiated investigations and recommend appropriate discipline in all serious cases.

Furthermore, the accountability of the deciding official has been made very clear, and disciplinary action will be tracked in the field and at Headquarters. Under the new system, discipline at Customs will be swifter and more consistent.

In conclusion, there is nothing more important to law enforcement than integrity. Corruption endangers law enforcement agents, undermines public confidence, and facilitates other crimes. My job—to make sure that Internal Affairs does a better job in attacking this insidious menace—is clear.

Mr. Chairman and Members of the Committee, I thank you for your time and attention and I am now prepared to answer your questions.

PREPARED STATEMENT OF RAYMOND W. KELLY

Chairman Roth, Senator Moynihan, and Members of the Finance Committee. I am pleased to have the chance to appear before the Committee today. I believe these oversight hearings are extremely important to the future of our agency. We at Customs continue to look for the support and guidance of this Committee and of the Congress as this Service moves forward in carrying out its complex and important mission. As Commissioner of Customs, I am fully aware of the critical role of oversight in improving the performance and integrity of our Executive Branch agencies, and I look forward to the exchange of ideas that will be generated during the course of these proceedings.

The men and women of the Customs Service work hard to do their jobs well in a time of exploding international trade and travel. The numbers of people and goods passing through our ports continue to spiral. In 1998 we processed over 19 million trade entries, close to 2 million more than 1997, and approximately 955 billion dollars worth of goods. Four hundred and sixty million passengers moved through our inspection areas last year, 13 million more than the prior year. Despite these unprecedented numbers, Customs continued to seize illegal drugs in record quantities. At the same time, the agency tackled new threats to our citizens and our national security—including Internet child pornography and the smuggling of nuclear material.

Before President Clinton nominated me to Commissioner, as Under Secretary for Enforcement at the Treasury Department, I began to work with Customs senior management on developing a list of issue areas that required priority attention. That list became the basis for a document we call Action Plan 1999, a concise summary of the focal points of our attention. Some of the most critical areas covered in the Action Plan are Integrity, Discipline, Accountability, Training, Passenger Services, and Automation. I should add that our Action Plan is a living document. It is constantly updated as new reforms are identified and as others have been completed. To ensure that there is follow-up on the items in the Action Plan, we designated our Management Inspection Division to oversee compliance with this effort.

Our reform initiatives are comprehensive, and cover everything from personnel issues, to management methods, to technology. They are designed both to address weaknesses in Customs, and prepare the agency for the challenging era of global trade ahead.

Our new Customs mission statement reflects these changes, and places a high priority on our values and our responsibilities:

We are the guardians of our Nation's borders—America's frontline;

We serve and protect the American public with integrity, innovation, and pride; and

We enforce the laws of the United States, safeguard the revenue, and foster lawful international trade and travel.

We began by focusing on integrity in our workforce. Customs, with its vast responsibility for enforcing our nation's drug statutes, has a duty to ensure that its corruption fighting efforts are second to none. Accordingly, we conducted a full review of the Customs Office of Internal Affairs, the focal point of our integrity efforts. We named a new Assistant Commissioner for Internal Affairs, a seasoned prosecutor and former acting U.S. Attorney who also served as Deputy Chief of the Public Integrity Section at the Justice Department. We've also reassigned some of the best investigators in the Customs Service to Internal Affairs, and have made rotations through this office a positive stop on the promotion track for all agents. To further verify our reforms, we're soliciting the counsel of a former Assistant Director of the Federal Bureau of Investigation, as well as the Director of the Office of Professional Responsibility at the Department of Justice.

To underpin our efforts in Internal Affairs, we replaced a weak, fractured and inconsistent employee allegation and disciplinary process with a new, integrated system. It includes a computer-tracking program that is designed to stop integrity and disciplinary problems from falling through the cracks.

New accountability standards for all managers will help to secure our reforms. In the past, decision-making authority was delegated to 301 ports of entry all across the country. We have changed this by expanding the authorities and responsibilities of the Directors of our Customs Management Centers, the regional offices that oversee all the activities of a port. We've also developed a mandatory self-inspection program. In the past, comprehensive inspections of our ports and agent offices were conducted every 5 to 6 years. Now field managers must provide their own assessments of their operations every 6 months. Their evaluations, in turn, will be checked and verified by Headquarters every 18 to 24 months. By paying attention to top-level oversight in our field operations, we will eliminate any ambiguity about who is ultimately responsible for getting the job done.

Integrity cannot be instilled through discipline and accountability alone. It must be reinforced through training. We created a new Office of Training, an office that did not exist previously, to centralize our training initiatives. Enhanced training will be instituted for both in-service and new employees. This includes cultural awareness and sensitivity training for new Customs inspectors, as well as integrity training for all employees. We consider this initiative so important that we've created a new, assistant commissioner-level post to head this office.

We're counting on these and other internal reforms to yield tangible results in areas such as passenger services, the most visible side of Customs. For millions of travelers, their first, and perhaps only contact with the Customs Service is at the international arrival areas of airports and seaports across the country. That experience must be as efficient, courteous, and professional as possible, and at the same time serve as an effective deterrent to smugglers.

In the past, Customs had been faulted for poorly communicating its inspection policies to the travelling public. In response to this criticism, we commissioned a leading independent consultant to review our air and seaport passenger inspection areas. This study yielded many valuable recommendations, which we're implementing now. They include such practical improvements as streamlining our Customs declaration forms, displaying better signs in our inspection areas, and improving the way we communicate with travelers. In addition, passengers can fill out response cards that are directed to Headquarters, and contact a new Customer Service Center that we've established in Washington. In addition to fielding passenger comments and complaints, the Service Center will serve as a collection point for data and trend analysis about our field operations.

The most sensitive and challenging area of passenger services for Customs, however, remains the personal search. While at times unpleasant, the personal search is the most effective method available to us today to counter the growing trend in body smugglers, those persons who try to conceal drugs either on or in their bodies. Last year Customs seized over two and a half tons of illegal narcotics smuggled by this means. The personal search is admittedly an unpleasant procedure, and one that is by no means foolproof. To minimize the discomfort associated with this countersmuggling tactic, Customs has turned to technology. We've deployed new body-scan technology in two major airports, John F. Kennedy in New York and Miami International. These devices, similar to common X-ray machines, limit or abolish the need for invasive physical contact during a personal search. Customs has asked for more funding for this and other technology from the Congress in the President's FY 2000 budget proposal.

However, no amount of technology can protect against racial bias. Allegations have been made that Customs has been targeting specific ethnic groups when select-

ing passengers for personal searches. As Commissioner, I take these charges very seriously. They must be heard and investigated. To ensure that we examine this issue thoroughly and impartially, we've asked a high-level commission of prominent public leaders to review our personal search tactics. The Customs Personal Search Review Commission will have unfettered access to Customs facilities and employees, and will submit its findings directly to the Commissioner's office. To aid the Commission and Customs, we've begun collecting extensive, detailed data on every personal search we conduct. This will be carried out on a daily basis and will allow us to develop a national database against which we can check allegations and measure trends and indicators.

With the help of the Commission, all aspects of this issue will be brought to the fore. There is simply no place for bias, or even the perception of bias, in the U.S. Customs Service. If substantive evidence is found that Customs personnel have engaged in any form of racial bias, we will take swift and decisive action.

From an operational standpoint, there is no issue more critical to Customs future than automation. It is the heart and soul of our commercial operations, and the key to our relationship with the all important trade constituency. The Congress has been and continues to be the most important outside agent of change in this area for Customs, specifically with its passage of the Customs Modernization Act in 1993.

Today's hearing offers Customs the chance to provide the Congress with perhaps the most comprehensive assessment of our modernization efforts to date. It could not come at a better time. Customs is now at a critical juncture in its efforts to meet the mandates established under the Modernization Act, and we look forward to this opportunity to update the Committee.

TRADE OPERATIONS

In fiscal year 1998, Customs processed over 19.7 million shipments of merchandise entering the United States. With current personnel resources, Customs was able to physically examine only about 3% of these shipments. By 2005, this trade volume is expected to double. In the next 6 years, Customs will have to process roughly 40 million shipments of merchandise. The staggering growth in trade, coupled with the expectation that growth in personnel resources will remain flat, means that 6 years from now, Customs will be able to examine only a little over 1% of the cargo entering this country.

This is a sobering thought. The risk of noncompliant, illicit, or even dangerous cargo crossing our borders and reaching the public is great. To address this risk, Customs has developed a comprehensive risk management strategy and redesigned its trade processes to make the most effective use possible of the resources we have. Implementing this strategy, however, requires enabling legislation and the support of modern, sophisticated automation. The legislation was provided largely in the form of the Customs Modernization and Informed Compliance Act (hereafter referred to as the Mod Act), which passed with the NAFTA legislation in December 1993. Acquiring the automated support to fully implement the risk management strategy, trade compliance redesign, and the Mod Act has been and continues to be a challenge.

RISK MANAGEMENT

In an environment where nearly $1 trillion of imports enter this country every year, managing the risk in trade compliance means dispensing with low-risk, compliant trade rapidly and concentrating our resources on noncompliant or high-risk trade. In response to this environment, Customs has developed a fully-integrated trade risk management program. Through this program, Customs manages risk by analyzing data and information to identify areas where the risk of noncompliance is greatest and applying our resources accordingly.

Key components of this risk management program are Primary Focus Industries, Compliance Measurement, Compliance Assessment and Account Management.

PRIMARY FOCUS INDUSTRIES

Our risk management program incorporates a primary focus industry (PFI) approach. Customs deliberately focuses resources on PFIs to ensure that we devote particular attention to trade areas that merit the highest priority because of such factors as revenue, quota and domestic industry impact. The PFIs are agriculture, automobiles, communications, critical components (bearings and fasteners), footwear, production equipment, steel, textiles and apparel.

COMPLIANCE MEASUREMENT

Customs measures the compliance rate of all goods entering the United States by using statistically valid sampling techniques to select cargo shipments to examine. Through these examinations, Customs develops a picture of compliance levels for all imports and pinpoints areas where the most serious trade violations occur. In 1998, the compliance rate for imports in PFIs increased from 83% to 84%, while the overall compliance rate for imports remained at 81%.

Customs has recently refined compliance measurement by factoring materiality into the analysis of compliance problems. Recognizing that all violations of trade law are not equal and t ıat some violations require a more vigorous response than others, Customs convened two task forces, one internal and one in cooperation with the trade community, to determine the types of discrepancies to be considered materially significant, as opposed to letter-of-the-law discrepancies. This new methodology was applied to the 1998 compliance measurement. Considering only the significant discrepancies, the compliance rate was 89% overall, and 90% for imports in the primary focus industries.

COMPLIANCE ASSESSMENT

Compliance assessment is another major tool that Customs uses to identify risk and develop corrective actions. During a compliance assessment, Customs assesses an importer's internal controls through statistical sampling and validation of import transactions. Customs uses compliance assessments on the largest importers (those importing at least $10 million per year), which covers most of the major importers in primary focus industries.

In the three years since Customs initiated the compliance assessment program, 200 assessments have been completed, while 187 are in progress. Customs has succeeded in assessing a substantial segment of the importing community. These companies account for 23.5% of all imports (by value) and 43% of PFI imports.

In addition to the assessment of risk resulting from these compliance assessments, Customs has recovered $100 million in revenue through this program. Approximately $70 million of this amount came from importers disclosing their own discrepancies and submitting the resulting duties.

ACCOUNT MANAGEMENT

Our account management program enables Customs to manage companies in their totality rather than dealing with them strictly on a transaction by transaction basis. Customs assigns account managers to work with the largest importers to improve their levels of compliance. Account managers strive to ensure uniformity in Customs actions affecting importers, serve as agents for educating importers on compliance issues, and work closely with their accounts on correcting and monitoring compliance problems.

The account management program covers a broad segment of the importing community. Currently, 25 national account managers handle 159 accounts, representing 25% of the value of all imports and 32% of entry-line volume. By assigning account managers to these larger importers, Customs maximizes the impact of this program since increasing compliance among this group of importers will hr ve a substantial effect on compliance rates overall. In addition to these national accounts, Customs is also using the account management approach for 300 smaller accounts that are managed by teams in ports throughout the country.

Each of these national programs allows Customs to collect and analyze data to identify noncompliance and its root causes, to develop and implement solutions, and to monitor the effectiveness of our efforts and progress toward our goals. Using them together in a deliberate, systematic fashion constitutes the heart of Customs risk management program for trade.

TRADE COMPLIANCE REDESIGN

Risk management programs have an integral role in Customs comprehensive effort to redesign cargo processing. The cornerstone of this effort is a dramatic shift from a work environment centered on reviewing individual cargo transactions to a highly automated, account-based focus. This shift is an inevitable result of our need to manage trade risks and modernize operations to keep pace with the explosive growth of international trade, advancements in automation, and Mod Act mandates.

Customs laid the foundation for a new era of highly automated, account-based processing by launching the Automated Commercial Environment (ACE) prototype in April 1998. More than 40,000 shipments have cleared Customs using ACE in its first year of operation. Each of these shipments benefited from the fastest, most effi-

cient cargo clearance and examination procedures available to importers who demonstrate high compliance with trade laws. ACE cargo gets released based solely on electronic shipment data, which eliminates cargo paperwork, speeds up cross-border traffic and frees up Customs inspectors to devote more time to law enforcement and less time to handling paper.

The ACE prototype is proof of the theory that Customs can rapidly clear cargo while ensuring a high level of compliance with trade laws. This balance of facilitation and enforcement is only possible through employing our risk management programs in combination with enhanced automation. Customs and the trade community are eager to proceed with further ACE development so that the successes of the ACE prototype can be repeated for all types of cargo transactions and the full potential of the Mod Act can be realized.

COMMITMENT TO IMPLEMENTING THE CUSTOMS MODERNIZATION AND INFORMED COMPLIANCE ACT (MOD ACT)

Customs has made significant progress in implementing the Mod Act. All major component areas—automation, enforced compliance, informed compliance, and legal—have been the focus of a concerted implementation effort. The following summary describes developments in each of these areas:

AUTOMATION

Full implementation of the automation elements of the Mod Act requires capabilities beyond what our legacy system, the Automated Commercial System (ACS) can provide. Almost all of these elements require extensive computer programming and infrastructure improvements at the Customs data center and in field locations throughout the country.

Of the eight automated programs provided for in the Mod Act, five are prototypes currently undergoing field testing and one has been fully tested and awaits approval for implementation. These include: reconciliation, electronic periodic payment, remote location filing, violation billing, automated protests, and the National Customs Automation Program (NCAP) account based declaration (also known as the ACE prototype). The remaining two, electronic bonds and drawback, are in development.

ENFORCED COMPLIANCE

Customs has addressed violations of trade law through a series of enforced compliance initiatives that utilize interdisciplinary teams, nationally coordinated enforcement actions and sophisticated data analysis techniques. Of 13 projects concerning enforced compliance elements of the Mod Act, ten have been implemented, two are currently being prototyped, and one is a proposal under final review. Major enforced compliance initiatives include:

Enforce Evaluation Teams.—a new concept that brings investigative and operational staff together on teams that jointly review potential or confirmed compliance problems and select appropriate enforcement responses. These teams have been established in 12 locations and implementation at all 47 service ports is anticipated for later this year. The full impact anticipated from implementing the enforce team concept will not be realized without enhancements to the existing automated system.

Company Enforced Compliance Process.—an enforcement program designed to systematically review those companies with low compliance measurement rates. Of the 43 companies reviewed in FY 98, 70% have shown signs of improvement. Customs has identified 130 additional candidates for this program.

Interventions.—initiatives designed to confront major trade issues through nationally coordinated actions, ranging from informed compliance assistance to investigations. Approximately 50 interventions have been conducted or are in progress.

INFORMED COMPLIANCE

Informed compliance has been integrated into the way Customs does business and remains an ongoing program of information, outreach and education. Customs has instituted seven of nine major initiatives intended to support the informed compliance elements of the Mod Act. Two initiatives are still being tested. Implemented programs include compliance measurement, national and port account management, compliance assessment, the importer compliance monitoring program, and the Multiport Approach to Raise Compliance (MARC 2000) initiatives. Collectively, these initiatives have fundamentally changed the way Customs interacts with the trade community by promoting increased cooperation and information exchange to improve compliance levels.

Customs has further demonstrated its commitment to promoting informed compliance through a comprehensive outreach program. Since the Mod Act passed, Customs has issued over 58,000 rulings, approximately 7,500 classification reviews, and 35 informed compliance publications. Customs also has held 136 national seminars to educate the trade community on a variety of compliance topics and publishes an official trade and informed compliance magazine, Global Trade Talk, which has a circulation of more than 10,000. Customs supplements all of these outreach activities with our web site, where the trade can readily access up-to-date information on trade programs and compliance issues.

LEGAL

Customs has issued final regulations, requested public comment on proposed regulations, or is conducting ongoing tests on all major Mod Act proposals that can be done under the existing automated system. Implementation of the Mod Act-related regulations is substantially complete. Fifteen regulation packages have been finalized and issued. These include recordkeeping, drawback, seizures, and an increase in the informal entry limit to $2,000. The remaining 11 are in various stages of the rulemaking process, with regulations governing laboratory accreditation and vessel boarding in final review.

CHALLENGES

While Customs has made substantial progress, in varying degrees, in all aspects of the Mod Act, it is nonetheless hampered in its ability to fulfill the "spirit" of the legislation. By this we refer to our mandate to match a changing business world's needs with an equally sophisticated and streamlined approach to trade processing. Our primary challenge in this regard is the lack of modern automation.

This inadequacy has forced Customs to implement modern business practices that require modern automated solutions using an antiquated automated system. As a result of having to work within the structure of a cumbersome and outdated legacy system (ACS), automation elements of the Mod Act are implemented with only partial automated support and with less efficiency than intended. Without significant investment in modern automation, these Mod Act programs will continue to rely heavily on manual processing support, and will therefore most likely remain in prototype status.

TRADE PARTNERSHIPS

The Mod Act requires that Customs consult with the trade community prior to proposing or drafting regulations and prototyping certain programs. Customs welcomes the input of the trade community into the formulation process and actively seeks their involvement through fora such as the Trade Support Network (TSN), a broad spectrum of the trade community that works with Customs on ACE development.

While this level of consultation results in longer implementation time frames for regulations and programs, it does ensure that Customs and the trade work in tandem on new rules and processes.

TRADE OPERATIONS SIMPLIFICATION PROPOSALS

Despite the far-reaching operational improvements supported by the Mod Act, many areas of trade operations remain extremely complex and technical. We believe that some of these areas would benefit from major simplification efforts. Two of these areas where the Committee could provide assistance are the tariff schedule and drawback.

A SIMPLIFIED TARIFF

The current U.S. tariff is so large that it requires two volumes and contains approximately 20,000 different classification numbers for imported products. This complexity exists even though duty-free products account for almost one-half of the total value of U.S. imports and are expected to account for an even larger share as a result of the remaining Uruguay Round tariff reductions. Furthermore, despite the enormous complexity of the tariff, we expect importers to have at least a 90% overall compliance rate for their product classifications, and at least a 95% rate for primary focus industry products, such as textiles or steel. Not surprisingly, many importers are having difficulty reaching this level of compliance.

The growth of duty-free imports and the inherent difficulties importers face in mastering product classification increasingly bring into question the need for a highly complex U.S. tariff. As you know, the Chairman of the Ways and Means Commit-

tee has requested that the U.S. International Trade Commission (ITC) conduct a study on tariff simplification. The ITC has just issued a draft simplified tariff schedule. We support their initial effort, and we are working closely with them in suggesting additional simplifications. The final ITC report is due to Ways and Means in July 2000.

We believe that if the simplified tariff were enacted, classification compliance rates could improve by five percentage points or more. That could result in a reduced examination rate for many of the more compliant companies. We hope that the Finance Committee would support the required legislation to enact a simplified tariff.

DRAWBACK

Customs is aware of the Committee's concerns regarding the highly complex drawback program. Any program that involves over $500 million per year in refunds by the government will always be the subject of disagreements on eligibility, documentary requirements, and timing. As you know, Customs worked very closely with the trade community in developing and implementing the new drawback regulations. Although this industry-government collaboration resulted in an outstanding program that earned a "Hammer Award" from Vice-President Gore, this effort was very time consuming and resulted in almost 250 pages of final regulations.

We believe that the drawback statute could benefit from a simplification exercise, and if it is the Committee's wish, Customs would be happy to participate in any such effort.

LONG-TERM COMMITMENT TO THE AUTOMATED COMMERCIAL ENVIRONMENT (ACE)

Investments in trade modernization remain a priority for Customs. Continued reliance on the 16-year old Automated Commercial System (ACS) will subject both Customs and the trade to risks of degraded service. ACS relies on old technology that is costly to maintain and is not conducive to supporting the requirements of the reengineered trade compliance process. In the period from mid-September 1998 through early-March 1999, ACS experienced significant processing slow downs that adversely affected the trade's ability to process entries quickly and cost-effectively. Recent investments at the Customs data center will alleviate the problems in the short term. However, we can anticipate reoccurrences of these problems without additional and substantial investments at our data center; in a modernized data network technology; and in personal computers and desktop software to support our field personnel.

Customs is committed to the development of the Automated Commercial Environment (ACE) as our commercial system for the 21st century. ACE is necessary for several key reasons: to cope with the enormous growth in international trade; to meet legislative requirements for informed compliance; to improve financial controls over the more than $21 billion in revenue collected annually; and to meet the requirements articulated by the trade and Customs field personnel as part of the trade process reengineering effort.

Given the size of the investment that ACE represents, it has received substantial scrutiny. As a result, a number of issues have been raised about Customs ability to manage such a large project. We take these concerns seriously, and have implemented a series of actions to strengthen our ability to make investment decisions and manage ACE and all other information technology projects.

To improve project management, Customs has:

Hired a Chief Information Officer (CIO) with extensive experience in enterprise architecture and major systems acquisition;

Reorganized the Office of Information Technology to provide for improved accountability and program control. An important element of the reorganization was the establishment of staff offices for Technology and Architecture, Strategic Planning, Program Monitoring, and Resource Management that are responsible to the CIO for: improved investment management; further progress on the enterprise architecture; enhanced controls over software development; and the development and implementation of software process improvement plans;

Hired a Federally Funded Research and Development Center (FFRDC) to assist with system acquisition and development planning, evaluation and oversight; and

Plans to acquire the services of a prime contractor to help plan, implement, and manage its information technology modernization efforts. The contractor will be responsible for implementing mature software development processes which Customs will adopt, and will assume the risks associated with delivering functional components of ACE and other software projects. Modeled after the experience of the Internal Revenue Service in addressing concerns about its tax modernization efforts, Cus-

toms will utilize the experience of the FFRDC from prime contractor acquisition strategy, to bidding and selection, to award and contract management. The FFRDC will also provide support to Customs in overseeing prime contractor performance. Customs intends to give this the highest priority, with the goal of having a contract in place within 12 months from the time of initiation. However, before the contract process begins, Customs needs a commitment on a reliable source of funding.

To improve the management of the investment in ACE, Customs has:

Engaged a contractor to update and improve the ACE cost-effectiveness analysis (CEA) which will be available for external review in the coming weeks. This CEA will incorporate analytical approaches responsive to direction previously provided by General Accounting Office staff, including reflecting use of the International Trade Data System as the trade interface for ACE. However, Customs recognizes that still more work is required beyond the current effort and commits to follow-on work that will a) analyze the cost effectiveness of ACE functional increments; and b) rigorously analyze alternative approaches to building ACE; and

Engaged Klynveld Peat Marwick Goerdeler Limited Liability Partnership (KPMG) to provide an independent review of Customs methodology and assumptions for software development and infrastructure costs. KPMG's preliminary review found our approaches for cost estimation to be sound and appropriate. KPMG is now reviewing the completed CEA referenced above and advising on the follow-on work.

We will work closely with the General Accounting Office on concerns regarding the appropriate level of architecture definition. As part of its investment management process, Customs has initiated a documented review process that ensures that all proposed investments comply with its architecture standards and are not redundant of other information technology projects.

It's important to note that the continuing controversy surrounding ACE is masking the urgency of making the necessary investments in infrastructure modernization required for Customs to meet its mission responsibilities. Approximately 54% of estimated costs associated with ACE are for software development and maintenance over an eight-year period. The rest of the investment is required to replace an outdated and problem plagued data network, to acquire additional computing capacity at the Customs data center, and to provide for regular updating of desktop computing capabilities necessary to stay abreast of rapidly changing technology. Almost all of these infrastructure investments would be necessary even if Customs is forced to continue to rely on the outdated ACS.

The limitations imposed on Customs infrastructure modernization is also adversely affecting our efforts to combat narcotics smuggling, screen international travelers, and provide automated mission support to aid management controls and operational efficiencies.

YEAR 2000 PROGRAM

Customs depends heavily on its computer systems to provide timely, accurate, and reliable information. This function is critical to the agency's capacity to fulfill its trade and enforcement responsibilities. It was therefore crucial to avoid any potential problems from the Year 2000 situation confronting electronic systems everywhere.

Customs has been very successful in achieving its goal to get all its critical systems Year 2000 compliant. This was managed within budget, in accordance with prescribed General Accounting Office (GAO) and Treasury guidelines. It was also achieved ahead of deadline dates, and without negative impact or interruption of daily operations and services.

Approximately 21 million lines of program code were successfully renovated and tested. This code, in addition to system software, is currently operational. Customs also identified, tested, and evaluated over 5,000 non-information technology (non-IT) assets for compliancy. These included facility systems, portable radios, lab equipment, building security systems, and other such products having date-related functions. We ensured the continuity of our business operations, and submitted to the Treasury Department business quality assurance plans. We checked, upgraded, or replaced nearly 19,000 personal computers for Year 2000 compliance, and replaced 300 telephone systems and 156 voice mail systems.

In previous testimony before the House of Representatives Committee on Ways and Means (February 24, 1999), GAO reported that Customs had made good progress to date in addressing its Year 2000 problem, thanks in large part to the effective program management structures and processes that it has in place. This program remains on schedule, and outlines plans for the completion of all remaining tasks.

RESOURCE ALLOCATION

Customs contracted with Price Waterhouse Coopers to develop a resource allocation model for the entire agency. The decision to contract for the development of the model was made due to the ability of the consultant to provide a specific range of expertise and technical skills not available within Customs.

Customs was faulted in two GAO audits for not having a consistent resource allocation methodology. Past practices were focused on isolated projects or events, and did not look at the agency as a whole. Nor was there a systematic method of establishing linkages between various occupations in the agency. For example, hiring decisions for one particular set of employees were not analyzed for their impact on other sets, in terms of additional support needed.

The contractor did not produce a staffing allocation table for Customs. The contractor only developed the methodology and the software for Customs to use in determining resource requirements. The model is not a substitute for management decision making. Rather, it is an additional tool for helping Customs to determine its needs and to analyze how changes in one area of operation might affect others throughout the agency.

USER FEES

The FY 2000 budget request includes two new user fee proposals. They are:

Passenger processing fee

The President's FY 2000 budget proposes to increase the fee paid by travelers arriving in the United States by commercial aircraft and commercial vessel, and to remove certain exemptions from this fee. Proceeds of the fee increase would partially offset Customs costs associated with air and sea passenger processing. Subsequent to the budget submission, authorization legislation will be transmitted to allow the Secretary to increase the fee paid by air and sea passengers and to remove existing exemptions from this fee. In order for Customs to be able to collect $312.4 million for FY 2000, collections would have to begin on July 1, 1999.

Automation modernization fee

The FY 2000 budget also proposes to establish a user fee for Customs automated systems. Proceeds of the fee will offset the costs of modernizing Customs automated commercial operations and an international trade data system, and would become available after FY 2000. Subsequent to the budget submission, authorization legislation will be transmitted to allow the Secretary to establish a fee for the use of Customs automated systems.

CUSTOMS ENFORCEMENT OPERATIONS

In addition to its mission of managing the flow of legitimate trade and travel across U.S. borders, Customs also has a very broad enforcement mission—encompassing drug smuggling, money laundering, international child sexual exploitation and child labor, antiterrorism, and violations of U.S. import and export trade laws.

It is a tremendous challenge to protect U.S. citizens and industry from these crimes (the majority of which are high priorities of the Administration and Congress) while not unduly impeding the movement of law-abiding persons and compliant goods. It becomes even more daunting in the face of ever increasing levels of trade, expanding responsibilities, and changing threats.

Recognizing this challenge, the Mod Act legislated that industry assume greater responsibility to ensure maximum compliance with the trade laws. By working in partnership with industry, Customs would be able to reduce cases of inadvertent noncompliance. This would then free up enforcement resources to address willful violators in the trade and other high-priority enforcement areas. We are beginning to see the benefits of this approach. Aggressive industry outreach and partnership programs have increased the compliance rates of our primary focus industries. However, with the continued increases in international trade and travel have come increased opportunities for criminal activities in areas over which Customs has jurisdiction.

The magnitude of the problem we are charged with addressing is enormous. Customs seizes more drugs than any other Federal agency—but our share represents only perhaps 20% of the amount of cocaine available to enter the U.S. Last year, Customs seized over $426 million in monetary instruments. A banner year by any agency's standards. But this success pales in comparison to the magnitude of the problem—estimated to be in the trillions of dollars, globally. Despite our impressive accomplishments, we are only scratching the surface.

MEASURING THE EFFECTIVENESS OF OUR ENFORCEMENT OPERATIONS

Measuring the effectiveness of our enforcement efforts is a challenge that continues to place Customs and our sister law enforcement agencies in a unique and somewhat difficult position. The principal challenge to developing realistic enforcement measures is defining the universe. Unlike the commercial side, where importers are forthright in declaring merchandise and paying duties, enforcement's targeted population, by its very nature, is deceitful. Willful violators of the law do not submit manifests detailing how many pounds of cocaine they are bringing into the country or how many millions of dollars they are taking out. Without a baseline against which to compare our efforts, traditional measures such as arrests, seizures, indictments, and convictions, are limited in their value. None account for displacement or deterrence, and others, like indictments and convictions, are highly dependent upon factors beyond our control.

Notwithstanding these obstacles, Customs has taken the charge of developing meaningful performance measures, to include outcome measures, very seriously. Not because the Results Act mandates it, but because it is the right way to do business. The public's confidence must be earned through responsible and sound decision making, enhanced productivity and, above all else, unquestionable integrity through accountability.

In keeping with this philosophy, we believe our most notable success has been with our counterdrug and money laundering strategies. Over the last year and a half, we have been developing a measure called the Cost of Doing Business. In essence, this outcome measure will track the costs incurred by criminal organizations to smuggle drugs into the U.S. and to launder money. Our theory is that the risk imposed by law enforcement is the principal factor in the cost of these illicit activities. As the risk of apprehension and seizure increases, cost will increase consequentially. By monitoring costs across the entire spectrum of modes, methods and geographic areas, we can accurately gauge the effectiveness of our efforts.

As noted above, the risk assumed by the violator is contingent upon our effectiveness in enforcing the law. However, there is some breaking point where the risk will outweigh the reward. What that point is exactly, we do not know. We can reasonably assume, however, that these levels do exist and that as we improve our effectiveness, more and more criminals will be forced out of business.

Beyond that, there appear to be other benefits of increasing transportation costs for imported drugs. Strong evidence exists to support the view that increased costs at the wholesale level directly affect consumption. Economists believe that increased costs at the import level will cascade through each segment of the distribution sequence and culminate at the retail level. Street dealers respond by either raising prices or reducing purity.

Various studies have shown that drug consumption decreases with a commensurate increase in price or a decrease in purity—even for highly addictive substances such as heroin and cocaine. For instance, researchers have found that, at a minimum, cocaine consumption decreases by 1% for every 2% increase in price. Therefore, we believe a causal relationship exists between our enforcement efforts and consumption.

Customs is very enthusiastic about these measures. Recently, we completed a feasibility study of cocaine transportation costs. It has been reviewed by econometricians and statisticians in the counterdrug research community and all support our conclusions that this is a viable measure. We are now in the process of collecting historical data to analyze how these costs have changed in relation to the employment of our enforcement resources. The feasibility study for the Cost of Laundering Money is underway—we expect similar results.

In the outbound arena, Customs has developed measures to determine our effectiveness in targeting export cargo violations. Baselines have been set and we will work toward improving our efficiency rates. In addition, Customs continues to measure the increased number of currency, munitions, high technology, and Office of Foreign Assets Control (OFAC) seizures made in the passenger and cargo arena. Recognizing that better outcome measures are necessary, Customs strives to automate the export process to provide better targeting information and to increase resources to augment enforcement efforts.

ALLOCATION OF OUR ENFORCEMENT RESOURCES

There are three factors that determine where and how we allocate our enforcement resources: workload, performance, and national priorities.

Threat is the principal component of enforcement workload. Determinants of threat include: proximity to the U.S. border; the number of arriving international passengers, vehicles, containers, aircraft, vessels and the level of threat they present

by virtue of their country of origin or point of embarkation; and demographic factors of the office's area of responsibility. Historically, Customs has used intelligence assessments and information based observations, such as a high caseload or high seizure rate, to evaluate threat. There are limitations, however, in relying solely on this type of information. While intelligence is a critical component of evaluating threat, it is qualitative in nature and cannot be incorporated into quantitative models. Also, while data such as seizures and caseload are indicators of threat, they are dependent, in part, upon resource levels. This results in a circular argument when solving for resource requirements and limits their utility when used as a workload factor in resource allocation models.

To provide managers with a more objective and quantitative means of determining threat, Customs has developed standardized threat assessments to evaluate the relative level and distribution of the threat within our Special Agent in Charge (SAIC) and Resident Agent in Charge (RAIC) offices. Although these standardized threat assessments do not provide an empirical determination of the threat level, they do provide us with a sense of where, geographically, our high threat areas are and how the threat is distributed among our priority enforcement mission areas. These standardized threat assessments have already proven themselves as a very useful resource allocation tool. They are currently being used by our Office of Investigations as an instrument in determining Special Agent staffing needs at our SAIC and RAIC offices. Our ability to carry out the recommendations of these resource allocation evaluations is limited, however, due to relocation funding constraints. We are in the process of developing standardized threat assessments for our foreign offices, as well.

When evaluating workload, we must also account for inherent interdependencies among our enforcement officers. For example, a large part of the workload of our special agents is driven by the results of our inspectors. When an inspector discovers a violation, it is referred to a special agent. The special agent opens an investigation to determine the source of the crime, identify additional co-conspirators and parlay the inspector's success into additional and even more substantial results.

Quantitative performance measures, such as seizures, arrests, indictments and case load, are compared against workload factors to assess each office's performance and results relative to its workload. Recognizing the inherent limitations of these output measures, evaluations must take into consideration qualitative factors, such as the quality and impact of our investigative cases, the quality of our enforcement results, and narrative intelligence assessments regarding the threat. Eventually, upon completion of the data collection and analysis process, the Cost of Doing Business measures will also be factored into these evaluations.

The magnitude of our enforcement responsibilities, combined with nominally stagnant resource levels, requires that final decisions regarding the allocation of resources be made in the context of national priorities. These priorities are established based on Presidential and Congressional guidance, directives and strategies.

SUMMARY

Members of the Committee, Customs is committed to fulfilling the mandates laid out before it by the Mod Act of 1993. We have done our best to carry out our obligations as far as we possibly can without the essential component that is still lacking—a new automated system. That system, ACE, will allow Customs to become fully modern and stay fully modern. As long as we are working with the outdated ACS system we will remain handicapped, and incapable of fully meeting our legislative requirements.

The explosion in global trade underscores this critical need. The total percentage of goods that Customs can examine is declining dramatically. Our capacity to focus on high-risk goods, and to maximize the resources we have at hand, must increase. By managing risk we not only improve the efficiency of the flow of trade through our borders. We also provide a vastly improved national defense against the scourge of drugs and the threat of tainted and fraudulent products.

Customs has taken dramatic steps to ensure that our modernization efforts are competent, well managed, and up-to-date. We have worked closely with the private sector on both the design and the technical specifications involved in trade modernization. And we will continue to do so through entities such as the Trade Support Network, our federally funded research and development center, the Mitre Company, and the private contractor we will hire when resources are made available. We've restructured our Office of Technology, appointed capable and experienced leaders for this project, and reviewed our cost and accounting methods with an independent consultant. We've also run a series of prototypes for a new automated system that has met with great praise from the private sector.

We believe we have a sound strategy for modernization, one that is in step with a changing world's trade and enforcement needs. Customs looks forward to working with the Congress to ensure that this strategy is fully implemented.

PREPARED STATEMENT OF CHARLES MORGAN KINGHORN

Mr. Chairman and Members of the Subcommittee:

My name is Morgan Kinghorn and I am a partner with PricewaterhouseCoopers (PwC). I am pleased to have this opportunity to discuss how the U.S. Customs Service is improving the linkage between its performance and its resources.

Last year, the U.S. Customs Service partnered with PwC to develop a Resource Allocation Model that would enable the Customs Service to improve the methods by which it allocates resources. With the full participation of Customs leadership, we demonstrated that it is possible to develop a model which can assist a large and diverse organization such as the Customs Service in determining its resource requirements by location and by activity, and do so on the basis of results. The completion of the model met the objectives of the Commissioner to establish a stronger strategic framework upon which to make improved decisions regarding resources within the Customs Service.

The delivery of the model marks the beginning of new staffing analysis opportunities for the U.S. Customs Service. The next step for Customs is to set the model's assumptions and analyze current model results by comparing them to proposed resource needs received from the field.

Today, I will describe the model, the suggested process by which Customs can use the model, and suggested next steps.

OVERVIEW OF THE RESOURCE ALLOCATION MODEL

Under the Government Performance and Results Act (GPRA), organizations within the federal government are required to link resource requirements with results. An objective, data-driven link between resource requirements and results can greatly assist the federal government in making more informed budgeting decisions.

The U.S. Customs Resource Allocation Model was designed to take advantage of this link by using the most recent year of historical performance measurement data as a baseline and combine that information with assumptions about future workload drivers to allow them to predict future resource requirements.

In order to develop the model, the project team, composed of both PwC and Customs staff met the following objectives:

Integrated data from eight Customs data sources;

Linked Customs' performance measurements to occupations performing specific activities;

Developed analysis and performance measurement methodologies that can be reapplied to future data, and can identify and avoid significant data issues;

Developed user-friendly what-if capabilities that can be applied to the analysis output; and

Provided user documentation to allow Customs to use and modify the model on an ongoing basis.

PwC also worked with Customs personnel to obtain corporate agreement on which current performance measures were linked to each occupation and the activities they perform. This allowed PwC and Customs to create a new performance measurement analysis methodology. This new methodology links the following data for each core occupation:

Activities that these occupations perform;

Workload that drives the work of these occupations; and

Average amount of time that is required to complete these activities

This "performance map" as we call it, details workload drivers, workload assumptions, and activity time data sources for all of Customs core functions and core occupations. It was also designed so that future efforts can include a link between the existing data and results and total threat data, which can also have a significant impact on how Customs may want to apply their resources. Given the short timeframe of the project and the significant effort required to identify and collect the data, the inclusion of result and total threat data in the model will be a future consideration for Customs. In the meantime, Customs can subjectively link workload and activity time assumptions to results and total threat as part of the overall Resource Allocation Process.

Model Description

The model can be used as a Customs-wide tool to determine the optimal number of positions by the 8 core occupations and over 400 core locations. Core occupations are defined as those occupations which directly perform one of the four core functions (Passenger Processing, Trade Compliance, Outbound, Enforcement). They are:

Inspectors;
Agents;
Import Specialists;
Canine Enforcement Officers (CEOs);
Entry Specialists;
Regulatory Auditors;
Pilots; and
Marine Enforcement Officers (MEOs).

Other occupations were included into a category labelled as Mission Support and a ratio was developed to represent the relationship between the selected occupations and their support requirements. The model is flexible so that it allows Customs to control all of the variables, which would influence the allocation of their personnel.

The completion of the Resource Allocation Model is a significant first step in the development of a complete Customs-wide staffing process. The model's focus is on predicting future staffing needs using the current year's data as the baseline and then setting assumptions based on the predicted change of key performance measures. Customs is currently completing the Resource Allocation Process by setting the key performance measure assumptions and reviewing the model output.

Data sources & data quality improvement

Like in most organizations, performance data at Customs is contained in a number of different systems often not well integrated because, historically, people only wanted to look at specific data for specific purposes. PwC and Customs designed the model and the new methodology as a tool to assist in the establishment of corporate staffing levels, across function, occupation and location. We wanted to do so using a consistent set of performance measurements. The data for these performance measurements is now integrated from 8 different data sources, which collect data from over 400 field locations. While it was not within the scope of our project to assess data integrity at Customs, PwC has witnessed three factors, which act to improve the quality of Customs' performance measurement data.

First, functionality within the model provides the capability to identify and analyze potential data issues, as they occur. For example, the model will highlight data mismatches when attempting to combine data from two sources to perform calculations;

Second, as with any data which is used to actually make decisions, we anticipate that greater effort will be made by all individuals in Customs to ensure the correct data is being used to make decision which impact their ability to staff; and

Finally, as the Resource Allocation Model and its methodology are communicated throughout Customs, data entry at field locations is expected to improve. We anticipate that the actual use of the data in the Resource Allocation Process will incent those providing the data to ensure its accuracy.

In short, the model will assist Customs in its on-going efforts to increase the integrity of its program data.

SUMMARY

The Resource Allocation Model improves the Customs' previous methods of allocating and justifying resources in several ways:

First, it is a Customs-wide model, providing a predicted number of positions required for all of Customs locations and occupations;

Second, it is based on established and agreed upon key performance measurements. The model, therefore, uses a consistent set of assessment factors from year to year; and

Finally, it was developed using input from both headquarters and field staff and assumptions can be set based on input from both headquarters and field staff.

The Customs model was a unique answer to the difficult questions:

How do I objectively justify the need for resources;

What happens to my resource requirements if I can improve my operations in terms of timeliness; and

What happens if I have increased demand across the board or at a particular location?

In the beginning of the project, PwC made an attempt to locate a generic resource allocation methodology, which could answer these questions for Customs. However,

given Customs' diverse set of goals, no existing methodology could be applied. As a result, PwC developed the performance measurement analysis methodology and applied it to create the Customs Resource Allocation Model. Thanks to the time and effort dedicated to the project by all of Customs personnel, including the Commissioner, the Resource Allocation Model provides the objective foundation for determining the optimal level of staffing at each of Customs' locations. This model

Allows Customs to begin using corporate information to make better-informed decisions regarding the distribution and magnitude of their staff;

Allows Customs to challenge old staffing assumptions;

Facilitates the continued improvement in data quality; and

Creates a process, which requires the yearly updating of the assumptions that drive staffing decisions.

The model still requires the use of professional judgement, the analysis of risk factors, and common sense. It is not intended as a tool simply to run and take its results blindly, without discussion and analysis. We at PricewaterhouseCoopers believe that the completion of this model is a significant first step in more objectively determining the optimal level and allocation of staffing resources. Once Customs finalizes the process and incorporates results and threat data into the model output, it will complete the objective link between resources and results.

Mr. Chairman, this completes my statement. I would be pleased to answer any questions at this time.

PREPARED STATEMENT OF MALCOLM E. MCLOUTH

Exceeding the 10% growth rate in international trade in the United States, Florida's cargo trade has already doubled this decade. Between 1990 and 1997, Florida's international trade increased by 110%. Seaports were responsible for approximately two thirds of Florida's international trade. Containerized cargoes increased 148% during the same time period. Cargo growth at the major deep-water ports of Jacksonville, Port Everglades and Miami is projected to continue at a conservative 5% per year. These numbers allow for the recent downturn in trade between Latin America and Florida and the growth in trade between Europe, Asia, Africa and Florida. Attached are two graphs prepared by the Florida Ports Council; the first (Figure 1) from data provided by the Florida Trade Data Center and the second (Figure 2) from data provided by each of Florida's fourteen deep-water seaports is the rapidly growing container ship movements in Florida ports.

Florida also has the world's busiest cruise ports which, along with cargo, is expanding rapidly. In FY 1999, U.S. Customs is expected to be available to clear and process a total of eight million passengers and crew arriving from foreign destinations at the ports of Canaveral, Miami, Ft. Lauderdale, Palm Beach, Tampa and Key West. The attached (Figure 3) depicts the expected volume of passenger and crew Customs clearances that the three largest Florida ports will experience from 1999 through 2002. Clearance processing of both cargo and passengers is impacted by available U.S. Customs staffing and support equipment. Being most familiar with Port Canaveral, I will describe our growing needs for additional U.S. Customs services.

Currently, U.S. Customs staffing in Port Canaveral consists of two supervisors, two enforcement officers, six part-time and six full-time inspectors and a canine assigned to cruise and cargo operations for a total of 18 positions. In comparison, Miami has a staff of about 120 positions with 75 being assigned to cruise ship operations. It is only through innovative scheduling and a dedicated Customs staff that Port Canaveral has been able to meet the challenges to date. The port authority staff has worked closely with U.S. Customs during the design of highly efficient cruise terminals and, when requested, the hiring of supplementary guards. We also recognize that Customs has been required to take on additional responsibilities to meet the drug interdiction goals imposed by Congress and we fully support their efforts. Understandably, with the port's rapid growth of cruise and cargo support requirements being placed on a limited Customs staff, something has had to give and its impact on operations at Port Canaveral follows:

1. Due to lack of personnel to cover both the debarkation of ship crew and cruise passengers, Customs has had to impose crew or support services access windows as follows:

Crew (early clearance)	30 minutes between 7:00am and 8:00am.
Passenger/Baggage only	8:00am to 10:30am.
Crew (late clearance)	After 10:30am and continuous monitoring by Customs until the ship departs.

2. The Canaveral Customs staff, due to its small size, has very limited flexibility to allow changes in a window once adopted except in times of emergencies. Typical problems created for the cruise line is with suppliers and ship repair workmen who, for one reason or another, have been delayed and are now forced to wait until the passengers are cleared. By design, scheduling priority is given to the passengers over the crew to ensure they are off in time to make connecting transportation. But the crew, with their need for off-ship banking, shopping, telephone calls, postal and recreational requirements needs as much time as possible and are unhappy employees if confined onboard ship for an extra two to four hours.

3. A negative perception exists in the cruise industry that the Canaveral Customs staff is tighter, more picky and inflexible in their enforcement of basic Customs regulations. This is both positive and negative. Positive is the fact that enforcement of Customs regulations at Canaveral is necessary for effective drug interdiction. On the negative side, lack of operational flexibility with the ship crew and staff as compared with other major cruise ports in the State of Florida is entrenched in the minds of our cruise line customers.

4. The lack of staffing by Customs at Canaveral is a public relations disaster waiting to happen. The Customs staff already utilizes allowable overtime up to the maximum and when an inspector is ill or training is involved, the difficulties encountered by this very thin staff is readily apparent. The two supervisors are regularly called upon to assist in covering routine operations affecting efficiency. Pre-passenger analysis and targeting also suffers. The Customs staff at Port Canaveral is already spread too thin and the slightest added workload and/or staffing problems will result in major delays in the processing of cruise passengers and ship crew.

Port Canaveral's growth in the past has been significant and can be expected to continue. The attached graph of multi-day passenger and crew debarkation shows where we are today and where we expect to be in the next three years related to Florida's two other major passenger cruise ports (Figure 4). The Canaveral Customs staff is aware of the port's confirmed scheduled expansion plans for FY 2000 as well as what can be expected through FY 2002 as the many new cruise ships under construction are added to the Florida based cruise fleet. Also impacting Port Canaveral's growth is the maxing out of the capacity of the two South Florida ports listed. U.S. Customs' response to this information at the local level has been, in the case of Fast Ferries, which is the most immediate need, "We just won't be able to handle it on a continuous basis because we don't have the overtime." or in the case of the *Disney Wonder*, "If we don't get more staff, we will only be able to handle two cruise ships at one time and the third one will have to wait until we are finished." A two to four hour delay in debarking passengers would be catastrophic for cruise ship operation and at the same time keeping the crew on the ship would lead to serious labor problems. Customs didn't even wish to speculate as to how to handle the *Sovereign of the Seas* with its added 350,000 per year passenger and crew clearances when it arrives for 3- and 4-day itineraries starting in June 2000. Added to the Canaveral Customs workload, is the fact that the port has recently completed a new $9 million container facility to service all of Central Florida. Once this container facility becomes operational in the next 60–90 days, additional Customs manpower will be needed to process container imports and exports. In discussions with Customs, the immediate need for at least six new positions at Canaveral has been suggested.

Throughout these trying times, the Port Canaveral operations and management staff have been in close contact with U.S. Customs management personnel at all levels in the State of Florida. We are the first to applaud their cooperative efforts in trying to make a bad situation and lack of personnel work and at the same time do all the other duties required such as drug interdiction. You couldn't ask for a better Customs staff but they desperately need more personnel.

Port Canaveral has also recognized the serious funding problems that U.S. Customs has encountered at the national level due to the elimination of COBRA funding for cruise ships as a result of the NAFTA trade agreements. The elimination of the $5.00 user fee head tax for cruise passengers over nine months ago was recognized by the International Council of Cruise Lines (ICCL) and the major cruise ports, including Port Canaveral, as a serious problem that needs to be rectified by the U.S. Congress. After six months of negotiations last year, it was concluded that a $1.75 per passenger user fee would be acceptable by all parties and legislation to

that extent was drafted, passed by the U.S. House but failed to obtain the necessary unanimous consent at the close of the 1998 U.S. Senate session. Subsequently, the House has re-passed the Bill, H.R. 435 and the Senate Finance Committee has approved companion Senate Bill 262 but it is yet to be passed by the full Senate due to a minor disagreement regarding the importation of a specific dye which has nothing to do with the COBRA funding. Without this funding, we have been told by Customs that we would lose five positions at Port Canaveral and 30 plus positions in Miami. This, in effect, would literally shut down Canaveral and Miami as cruise ship ports. Other ports would suffer as well if the user funding for cruise ship passenger processing is not re-instated in the next 30–60 days. The urgency of this situation is apparent. However, even with the passage of this legislation, it is limited to 50 new inspectors to be spread over all U.S. cruise ports. Looking at the numbers presented, one can see that this limited number of additional inspectors will be quickly absorbed and in the year 2000, the problem will re-occur unless the number of Customs staff is allowed to increase. The revenue being collected at $1.75 per cruise passenger would be increasing but Customs would be obligated to seek congressional authorization to raise the limitation of 50 inspectors. Utilizing previous data presented, Figure 5 is attached showing the Customs user fee revenue that is expected to be generated in Port Canaveral in FY 2000 through 2002. Not included in the data presented today are the emerging cruise ports of Tampa, Palm Beach and Key West. In discussions with Customs, we learned that at the Port of Tampa, they are also in dire straits and they have already maxed out on their Customs overtime. As it stands right now, unless the passage of this law is not swiftly attended to in the U.S. Senate, the cruise industry in Florida will suffer a serious reversal and a press feeding frenzy will result. It is important to recognize the $11.6 billion cruise industry impact on the U.S. economy (Figure 6).

At the suggestion of Florida Senator Bob Graham, President Clinton created a commission to study crime and security at American seaports. The Graham Commission on Seaport Crime and Security will focus on terrorism, drug trafficking, auto and cargo theft, illegal immigration, food safety and other problems. The commission will be reporting to the President in one year. The Florida Ports Council supports Senator Graham's commission on seaport crime and security and it's worth noting that the State of Florida appropriated $1.7 million in 1999 to perform a security analysis at seaports. In addition, the Florida legislature has set aside sufficient monies on a matching fund grant program to Florida ports to provide for the purchase of facilities to x-ray containers so Customs officials can have a better indication of what is in the container to assure it matches the manifest. The program with the acronym, S.T.A.R. will be operational in all the major container ports in the State of Florida, including Port Canaveral, by the first of next year. At Canaveral, we are hoping that one of the results of the Graham commission and seaport analysis is to develop new uniformity between Florida ports relating to Customs' enforcement activities.

Thank you so much for allowing me to address the Senate Committee on Finance and hopefully the information I have provided will be of use in your deliberations.

Florida Trade
1991-1997

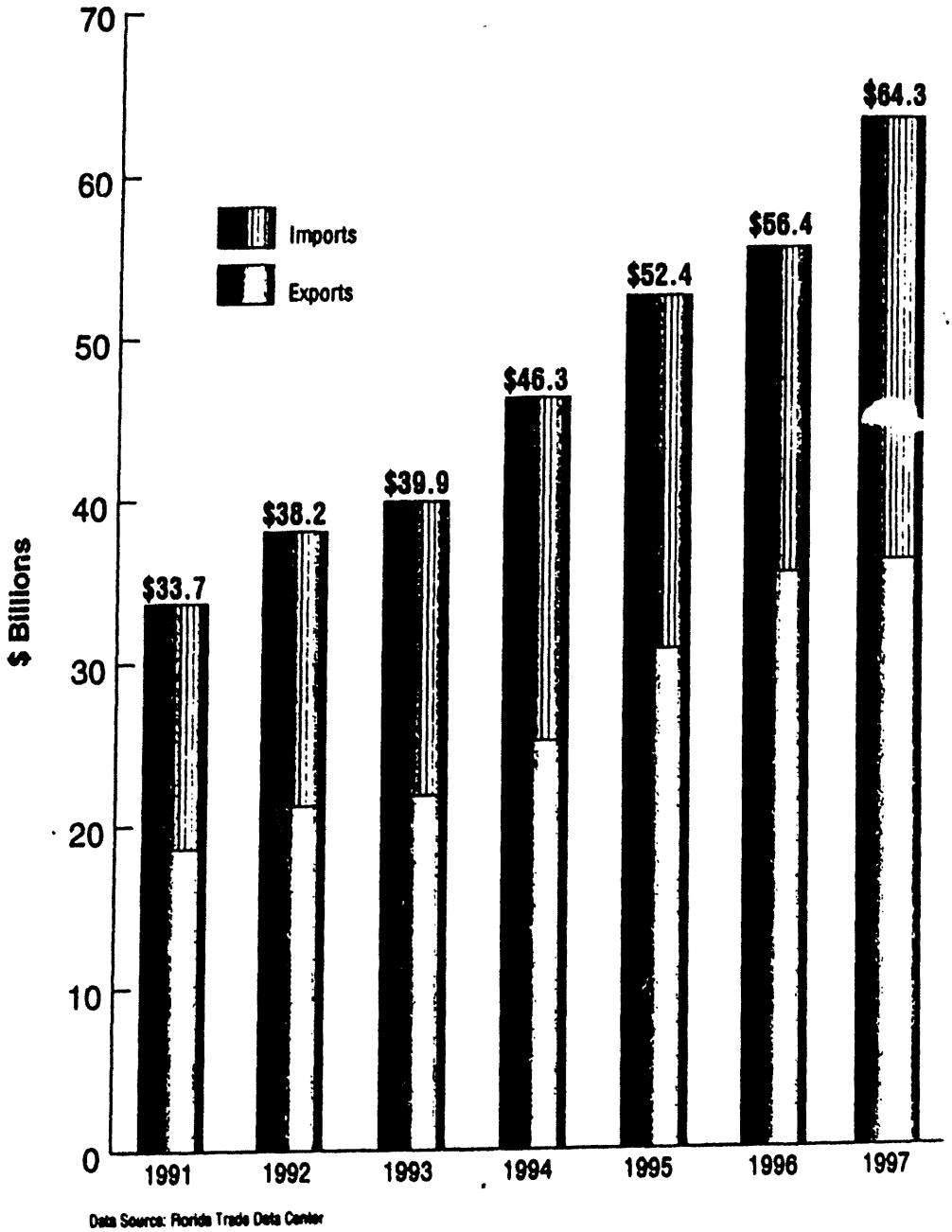
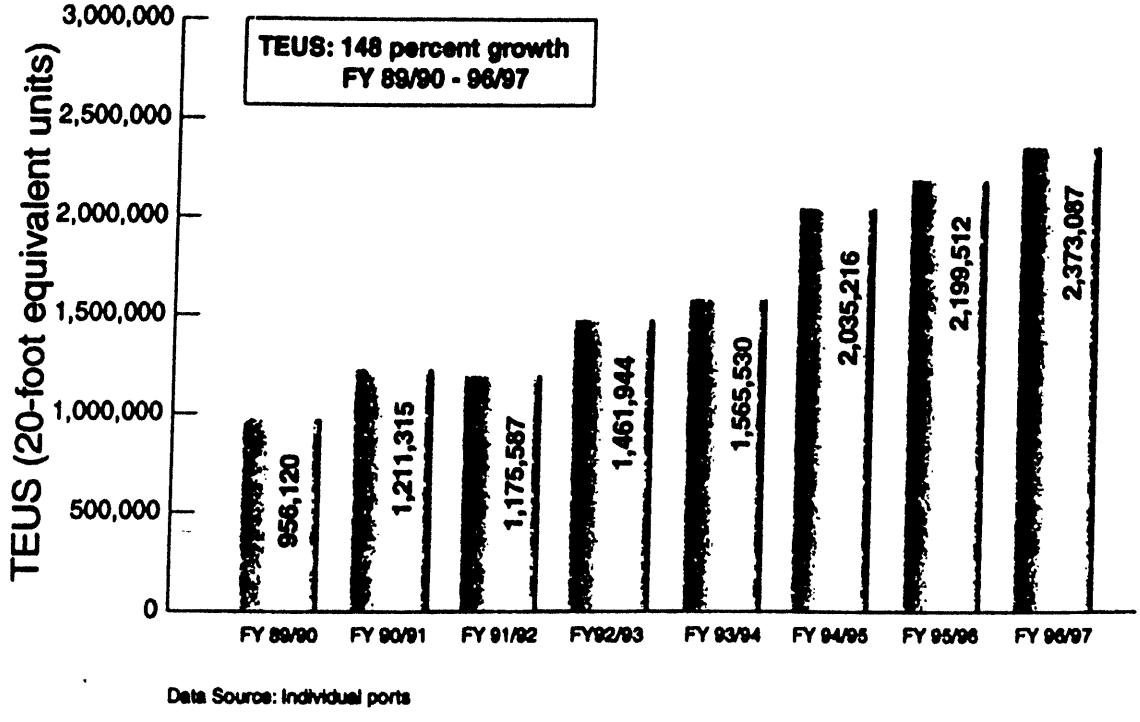


Figure 1

Container Movements
1990-1997



Data Source: Individual ports

Figure 2

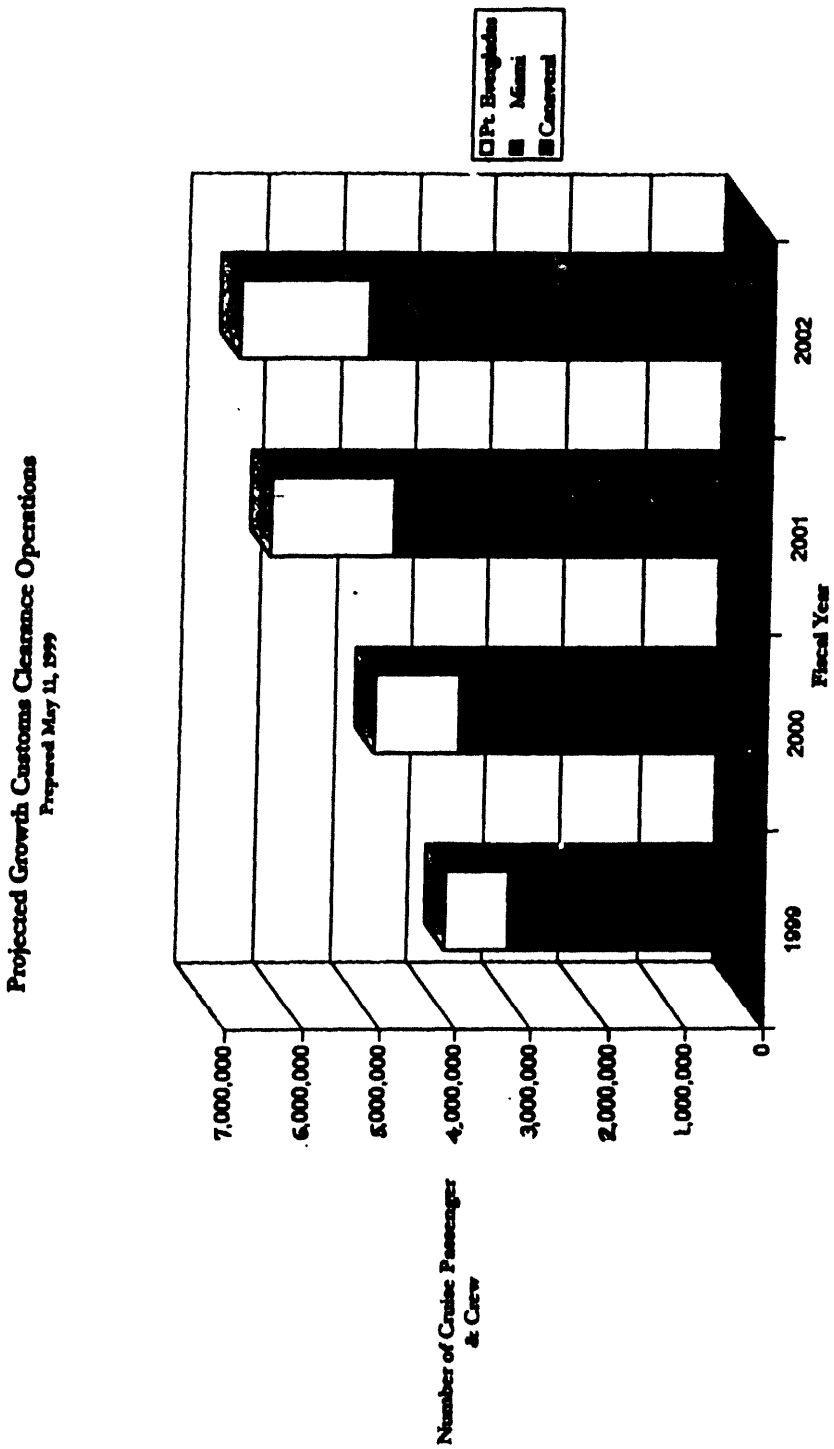

Projected Growth Customs Clearance Operations
Prepared May 11, 1999
Pt. Everglades
Miami
Canaveral
7,000,000
6,000,000
5,000,000
4,000,000
3,000,000
2,000,000
1,000,000
0
1999
2000
2001
2002
Fiscal Year
Number of Cruise Passenger & Crew

Figure 3

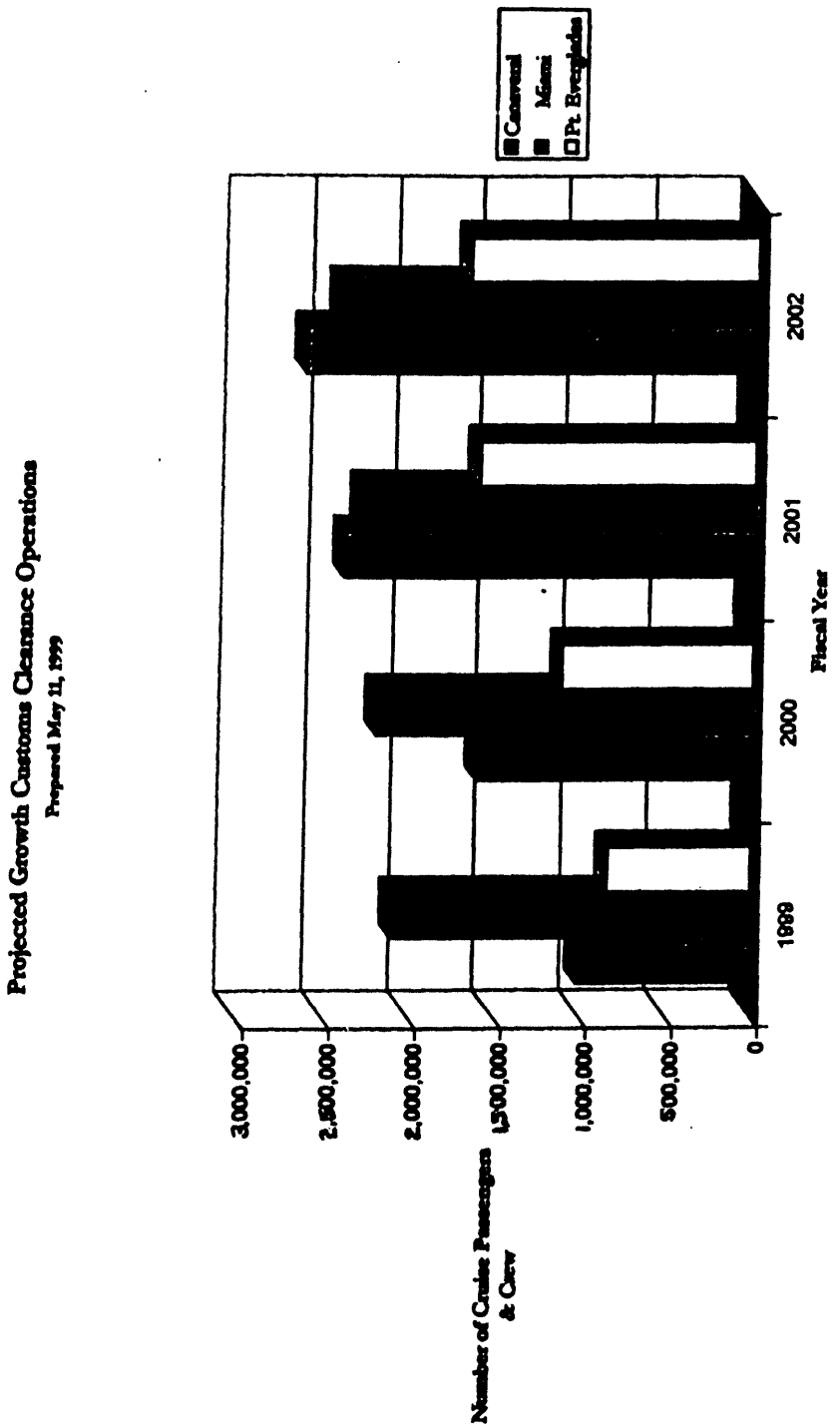

Projected Growth Customs Clearance Operations
Prepared May 11, 1999
Canaveral
Miami
Ft. Lauderdale
3,000,000
2,500,000
2,000,000
1,500,000
1,000,000
500,000
0
Number of Cruise Passengers & Crew
1999
2000
2001
2002
Fiscal Year

Figure 4

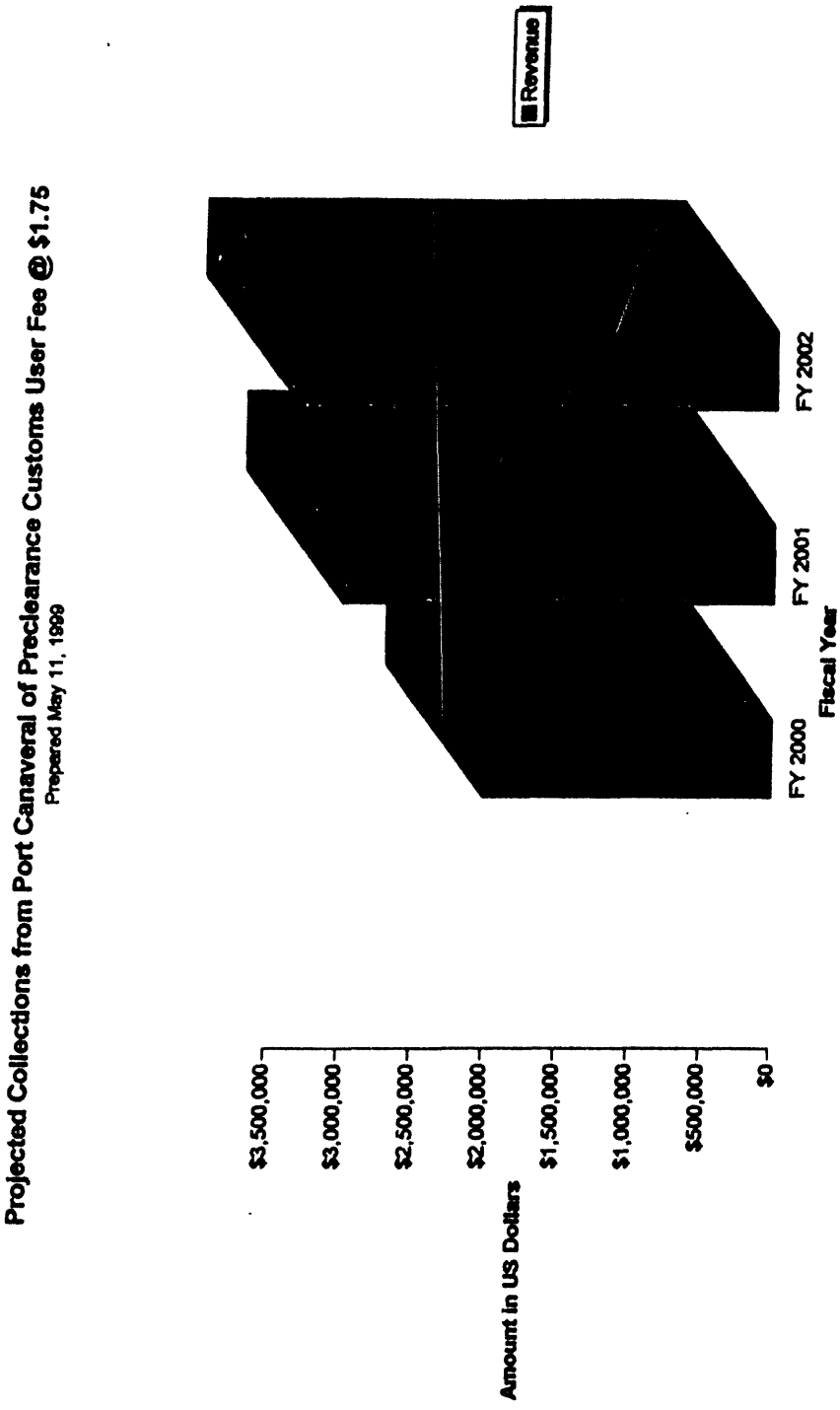

Projected Collections from Port Canaveral of Preclearance Customs User Fee @ $1.75
Prepared May 11, 1999
Revenue
$3,500,000
$3,000,000
$2,500,000
$2,000,000
$1,500,000
$1,000,000
$500,000
$0
Amount in US Dollars
FY 2000
FY 2001
FY 2002
Fiscal Year

Figure 5

Impact of North American Cruise Industry on U.S. Economy in 1997

A recently completed study, conducted by PricewaterhouseCoopers (PwC) and Wharton Economic Forecasting Associates (WEFA), examined the total impact of the North American cruise industry in the United States. It quantified the economic contributions and examined the extensive links which the industry has with other businesses and industries throughout the United States.

PwC managed the project and was responsible for collecting all the cruise-related expenditure data and quantifying the direct economic impact of the cruise industry. WEFA utilized its economic and industry models to calculate the economic impacts throughout the U.S. economy in 1997. The WEFA analysis used the PwC estimates of direct spending by the cruise industry and its passengers and quantified the impact of this spending on all sectors of the U.S. economy.

The following provides a detailed outline of the study's conclusions regarding the cruise industry's revenues and expenditures in 1997. These figures represent the economic impact of the North American cruise industry.

➢ Direct spending of the cruise lines and their passengers on goods and services produced in the United States in 1997.	$6.6 billion
➢ Total economic impact of the cruise lines, its passengers, and its U.S. suppliers in 1997.	$11.6 billion
➢ These expenditures generated jobs in the U.S.	176,433 U.S. jobs
➢ Direct industry expenditures included purchases from major U.S. industries such as airline transportation, food and beverage, business services, energy, and financial services.	
➢ This economic impact touched virtually every segment of the U.S. economy. Those industries most heavily impacted are summarized below.	
• Airline Transportation	$1.8 billion
• Transportation Services[1]	$1.2 billion
• Business Services[2]	$1.0 billion
• Energy[3]	$988 million
• Financial Services[4]	$698 million
• Food & Beverage	$607 million

[1] *This primarily includes travel agents, ground transportation, and U.S.-based excursions.*

[2] *This includes such services as advertising, management consulting, engineering and architectural services, computer hardware, and software services, etc.*

[3] *This includes fuel, utility services, and oil and gas mining.*

[4] *This includes banking, investment, and insurance services.*

Analysis conducted by: Pricewaterhouse Coopers
Wharton Economic Forecasting Associates

Figure 6

PREPARED STATEMENT OF MILTON MOLLEN

DEAR SENATOR ROTH: I appreciate your invitation to appear before the Senate Finance Committee to testify on the issue of Customs Management, and, more particularly with regard to the specific issue of combating corruption within the Customs Service.

Obviously, corruption is not a recent invention. One might reasonably argue its history goes back to the Garden of Eden. Corruption in various forms has plagued society down through the ages. It is of particular concern when it infects law enforcement agencies. A major mission of law enforcement agencies is to enforce the law and to inspire public confidence in the integrity of the government to which the public has entrusted the power to govern.

However, while we might hope for better, the fact is that law enforcement agencies mirror and reflect society at large, its strengths and its weaknesses. Most law enforcement personnel are trustworthy, dedicated and committed to honorably fulfilling their responsibilities. However, some are weak, vulnerable and susceptible to the temptation of "easy" money. Others are just plain venal, who view public service as a means of using their power to illegally enrich themselves. When we factor into the equation the enormous amounts of money involved in drug trades and money laundering, one can readily understand the concern about maintaining the integrity of the Customs Service and the necessity for constant vigilance and for the creation and maintenance of internal and external safeguards to protect that integrity.

I would, therefore, offer a few thoughts as to those means which are most likely to achieve the goals of deterring corruption within the Customs Service to the fullest extent possible, and to finding it and rooting it out where it exists. These suggestions are based upon my experience and observations of many years in the executive and judicial branches of government, most recently as Chairman of the New York City Commission to Investigate Allegations of Police Corruption and the Anti-Corruption Procedures of the Police Department, more commonly known as the Mollen Commission.

I strongly believe that the battle to combat corruption in an agency such as the Customs Service must be comprehensive and multi-faceted. It must commence with the recruitment process by reaching out for and attracting the right kind of candidates, and conducting proper and expeditious investigations prior to appointment. Thereafter, there must be appropriate training with emphasis on integrity in terms of adequate time devoted to such training and with effective substantive material utilizing updated technology. The training should not be confined to newly appointed agents; there should be refresher courses at appropriate intervals.

After the agents are sent into the field, it is essential that there be effective supervision. I recognize that this is not easily achieved in an agency which is spread out as widely as is the Customs Service; however, I believe that with a leadership firmly and totally committed to maintaining the integrity of the Service, the goal can and will be achieved. Obviously, the leadership must be given adequate resources in order to accomplish this objective. But, I am convinced that with reasonable appropriation of funds and with prudent management, the mission can be accomplished.

I am firmly convinced that with adequate resources, and the implementation of a policy of strict accountability at each level of authority, a leadership fully committed to the maintenance of integrity will succeed in achieving that goal.

At this point, I would take note of two actions taken by Commission Kelly which I believe are salutary and important in spreading the right message and in effecting positive changes within the Service. One was his altering the chain of command to provide for direct reporting by the Assistant Commissioner for Internal Affairs to the Commissioner. This change in process should result in the
Commissioner being constantly informed and aware of any integrity or misconduct problems in the Service and enable him to take prompt and effective action.

Secondly, I have been informed that Commissioner Kelly is instituting a selective form of rotation in and out of Internal Affairs. I believe that this approach will assist in changing the culture within the Service in a positive way.

In order to be truly effective, the effort to combat corruption must alter in a positive manner the existing culture within the Service. It has been my observation that in most law enforcement agencies there is a strong tendency to resent and hold in contempt the Internal Affairs Units. A policy of rotating agents into Internal Affairs should ameliorate the customary perception and lead to a more effective and more cooperative relationship between Internal Affairs and the other agents.

Lastly, I should like to address the most important issue of sustaining the durability of any program for promoting integrity implemented by Commissioner Kelly. I have known Commissioner Kelly for approximately ten years and I have total faith

in his integrity and in his ability. I have enormous respect for him professionally and high regard for him personally. I have no doubt that he will do his utmost to meet the challenge of improving the system for maintaining the integrity of the Customs Service. However, my studies of and experiences with the struggle to achieve and maintain the integrity of law enforcement agencies led clearly and strongly to the conclusion, that an essential ingredient in the long range success in combating corruption is the existence of some form of effective outside monitoring of the internal efforts in confronting corruption. Most institutions are reluctant to, as they see it, expose their dirty laundry in public. They find all kinds of rationalization to buttress their failure to make public what they perceive to be their shortcomings. Furthermore, I am firmly convinced that if there exists an outside entity to monitor and review their success or failure in combating corruption, it will result in a more sustained and more effective campaign to deter and root out corruption.

I have been informed that presently there exists two possible instrumentalities for accomplishing this important result. One is the Inspector-General for the Treasury Department and the other is the Office of Professional Responsibility. It may well be that either or both may well provide the most successful means to accomplish the desired objective. But, of one thing I have no doubt. To achieve the most effective means of establishing a long range, on-going successful method of combating corruption, it is essential that there exist a permanent outside monitor to work alongside of and in cooperation with the Commissioner in the difficult task of successfully confronting corruption and fulfilling the Customs Service responsibility to the people of our country.

I hope that these observations are of some assistance to your distinguished committee in its efforts in addressing the Custom Services' management issues.

With best wishes for a successful hearing.

PREPARED STATEMENT OF JOHN S. MOORE

I am a Senior Vice President, working for a U.S. Fortune 500 company and an international technology company. I manage RWC, one of the Divisions of these companies.

In 1992, I was informed that the General Manager of RWC, reporting to me, had a relationship with organized crime and was a conspirator to import 1300 pounds of cocaine. The General Manager used RWC paperwork to assist in the smuggling and it reflected RWC as the importer of record. The shipment was diverted as soon as it entered the United Sates and never physically shipped to RWC property. Customs contacted our company and notified us that Customs was conducting a "controlled delivery," which they described as a surveillance of the shipment to its ultimate destination in an attempt to identify and arrest those responsible for smuggling the drugs.

This operation took several months, during which time we complied with Customs fully. We ran our company as if nothing was amiss, contrary to our own internal policies upon discovery of improper conduct and misuse of company property/information.

Our company complied with all Customs Service official requests for documentation and information of RWC, including search warrants.

Our review of the events and documentation provided by Customs confirmed that the General Manager exerted his control and authority to accomplish what was done. It should be noted that what occurred was in no way standard operating procedure within our company. It was not normal for the GM to handle this situation himself, as others in our organization would normally accomplish these tasks. Once Customs and RWC reviewed the paper trail, it was obvious that something highly suspect had taken place. It was also obvious that others not affiliated with our company were involved.

The General Manager was relieved of his duties as soon as Customs provided the evidence to us of the violation of United Sates law and Customs declared the proactive phase of their investigation complete.

The General Manager, after making a full confession to Customs Special Agents, was eventually indicted and convicted of unlawfully smuggling cocaine. It is understood that he is still serving his sentence of ten years in a federal penitentiary.

The experience of our company working with Customs was positive and professional from day one. While the actions of one individual disturbed us greatly, we complied fully with the requests of Customs. Maintaining a "business as usual" manner was difficult at best but rewarding in the end. We kept Customs fully aware of the General Manager's activities while the investigation took place and contin-

ually followed Customs' advice. We were prepared to testify in court should that have been necessary.

We feel that the program would have been detected and prevented the unauthorized use of RWC's name but for the power and control entrusted to this one individual at a remote location. None of the specific actions, which took place, were suspicious enough to warrant detailed investigation on our part. Financial records and inventory records would have revealed nothing unusual.

Since these events have taken place, our company has taken several measures to help prevent any such reoccurrence.

The events that took place could have resulted in grave consequences for our business. Our parent company or our customers could have been upset enough to "walk away." The seriousness of the events caused us to review all internal compliance measures and policies as well as the departments and people who are charged with audit and enforcement. Internal compliance is stressed more than ever and we pride ourselves in learning from this experience. Every single employee is made aware, in writing, of our position on compliance with all company policies and procedures as well as U.S. law.

Some of the important actions taken to strengthen internal compliance include.

1. Transportation is now centralized and preferred carriers have contracts with our company.
2. External consultants have been brought in to review internal Customs compliance on all trade issues.
3. Policies and procedures have been developed by consultants specific to our operations.
4. A system has been put in place to monitor and comply with any change in Customs reporting requirements to insure trade compliance.
5. We employ a corporate compliance administrator to interface with outside consultants, Customs, and to train and advise internal personnel.
6. Less than one year from the time we relieved the General Manager of his duties, we shut down the remote location and moved all those operations to our factory.

All of the items listed above help insure we are doing our very best to eliminate import activities which could have major negative impact on our company, our customers, and our employees.

What can others learn from our experience?

Communicate with and know your employees. Formally instruct them on the Company Mission and Values. Have them know the consequences of non-compliance;

Consider the power you give individuals carefully, especially at remote or small operations. Insure that audit trails are present and audited on a regular basis;

Watch for signs that things may be amiss. Follow up on any irregularities that you know of or that you suspect;

Get help when you feel you need it. Resources like Customs are there to help and more than willing to do so in a positive and professional way; and

Realize that the events detailed earlier could happen to you and be prepared to deal with it.

Thank you.

PREPARED STATEMENT OF HON. DANIEL PATRICK MOYNIHAN

[MAY 25, 1999]

On Thursday, December 17, 1998, our Chairman wrote Commissioner Kelly expressing concern over the serious allegations of Customs' misconduct that had appeared in the Miami Herald four days earlier. The Commissioner's response was swift and decisive. On Monday, December 21," the Commissioner assured the Chairman that he shared those very concerns. He wrote:

> In response to the Miami Herald article of December 13, on the same Sunday the story was published I directed the Deputy Commissioner to investigate the allegations contained in that report. The charges levied in that piece are very serious and warrant an expeditious review.

And the Commissioner asked the Committee to assist him in his efforts by forwarding any additional allegations of misconduct that might come to the Committee's attention. If I may quote the Commissioner again,

> Corruption within the ranks of any law enforcement agency undermines public confidence and poses a real threat to the safety of the vast majority of honest personnel. I do not condone it in any fashion. I intend to crush it.

Commissioner Kelly has backed up those statements with actions. In December, he informed the Committee that he had reassigned the current head of Internal Affairs and restructured the internal review process. On February 16, 1999, the Commissioner appointed William Keefer, with 20 years of experience in prosecuting public corruption and organized crime cases, as the new Assistant Commissioner of Internal Affairs.

I look forward to hearing from Mr. Keefer this morning about the measures that Customs has put in place to ensure that any future allegations of misconduct will also be promptly investigated and misdeeds appropriately punished.

Sixty-four percent of Customs' 17,263 employees are assigned to the Office of Field Operations, the vast majority in far-flung locations. They are exposed daily to the temptation of easy money, with Headquarters, in some cases, thousands of miles away. There will be isolated instances of misconduct. Commissioner Kelly has vowed to crush" them, and he should have this Committee's full support.

Attachments.

THE COMMISSIONER OF CUSTOMS

WASHINGTON, D.C.

May 24, 1999

The Honorable William V. Roth, Jr.
The Honorable Daniel Patrick Moynihan
Committee on Finance
U.S. Senate

Dear Senators:

I am in receipt of the recently-completed Special Report by the Treasury Inspector General (IG) on the United States Customs Service. We understand the Committee's request for this investigation was initiated on December 17th, 1998, in response to *The Miami Herald* article of December 13, 1998 entitled "U.S. CUSTOMS: A CULTURE OF FAVORITISM."

I would like to take this opportunity to apprise the Committee of actions we have taken to respond to the findings in the IG report. First, as you know, Customs immediately undertook an internal investigation of the allegations made in *The Miami Herald* article. The results of our review of those allegations were provided to the Committee on January 14, 1999. That same information was also provided to the Inspector General prior to his review. The Inspector General's findings on the *Herald* allegations essentially concurred with ours, that most of these cases were not properly handled. In those instances where we were able, we have reopened cases.

Integrity at the Customs Service is my top priority. While every review of Customs to date has concluded that no systemic corruption exists within the agency, various reports, including the IG report, have pointed out weaknesses and/or deficiencies in the Office of Internal Affairs (IA). Therefore, one of the first efforts I initiated as Commissioner was a review of the operations of the Office of Internal Affairs to the assess weaknesses and vulnerabilities in order to improve the manner in which we conduct investigations into misconduct and impose discipline on agency employees who violate our policies, procedures or the law. As a result of that review, we have now implemented new, greatly strengthened internal affairs procedures and systems which demand accountability and provide us with the tools to monitor all cases from their inception to final disposition. I believe this new system will correct the deficiencies identified in the IG's Special Report.

Below are some of the specific measures that I have instituted which directly address the major findings identified in the IG Report.

CASE MANAGEMENT/QUALITY OF INVESTIGATIONS

IG Findings: The IG review of Internal Affairs investigations identified a lack of supervisory review at both the field office and Headquarters level which contributed to an inferior quality of investigative work. Allegations of misconduct that would have been more appropriately handled by IA were referred to management for inquiry:

New Customs Policies:

- William Keefer, the new Assistant Commissioner of Internal Affairs and a career federal prosecutor, is responsible and accountable for the proper functioning of the IA unit and reports directly to me.

- All allegations of misconduct will now be reported to Headquarters. Each allegation will be reviewed on a daily basis by a special team of experts in Headquarters who will determine whether and where to refer the allegation for further action.

- All time and mission critical allegations of misconduct of top level personnel and cases referred back to IA by the IG will be handled by a new Special Investigative Unit, composed of highly experienced agents, which is housed in the Office of Internal Affairs at Headquarters.

- An improved case management system has been established which will merge the investigative and administrative case tracking systems and allow us to track all cases from inception to final resolution.

- A 24-hour fully-staffed hotline has been instituted to ensure timely and efficient reporting of allegations to Headquarters.

TIMELINESS OF INVESTIGATIVE REPORTS

IG Findings: The IG review indicated a number of instances in which IA investigations failed to comply with proper reporting requirements as outlined in the Customs Internal Affairs Handbook. The Handbook requires that an interim report of Investigation (ROI) be completed within three working days after any substantive investigative activity and a closing ROI within ten working days after the final investigative activity.

New Customs' Policies:

- The new intake system for reporting allegations of misconduct triggers a time clock which will be strictly adhered to. Managers will be held accountable for ensuring that these time constraints are met. Headquarters will be able to monitor the timeliness of required actions through a retrievable computer record.

- Criminal investigations will be more closely supervised, and frequent file reviews by supervisors in the field, tracked by Headquarters, will ensure a more timely and accountable process. Failure to exhaust viable leads or to interview knowledgeable witnesses will not be tolerated.

- Each non-criminal report of investigation (ROI) will be reviewed by an Assistant Chief Counsel for legal sufficiency before being approved by the Assistant Commissioner for Internal Affairs.

- Each ROI will include a finding for each allegation investigated by Internal Affairs.

MANAGEMENT INQUIRIES

IG Findings: Less serious allegations of misconduct are referred by IA back to Customs managers for further examination and appropriate action. IG review identified allegations of serious misconduct initially referred to IA for investigation that were subsequently referred to management for action. These referrals are known as management inquiries. An independent, objective and impartial person, senior in authority should conduct a management inquiry. There are no published directives for conducting management inquiries within the Customs Service and there is no oversight review by Internal Affairs of closed management inquiries.

New Customs Policies:

- Specific criteria have been developed to determine which cases will remain in IA and which will be referred to management for further action.

- Allegations of misconduct will be reviewed daily by a team of experts at Headquarters and approved by the Assistant Commissioner for Internal Affairs before being referred to management.

- A Customs directive dated April 13, 1999 details the conduct of management inquiries and mandates Internal Affairs oversight.

DISCIPLINARY PENALTIES

IG Findings: Disciplinary penalties were inconsistently applied in a number of instances. The inability of Customs to equitably administer discipline according to its established Table of Offenses and Penalties contributes to a lack of confidence in the disciplinary process and fosters the perception of favoritism.

New Customs Policies:

- Customs-wide Discipline Review Boards (DRBs) have been established to ensure that discipline is administered in a fair, uniform and consistent manner. The DRBs are composed of a pool of trained managers. These rotating teams will review cases of serious misconduct, and determine the appropriate level of discipline thereby providing greater consistency and objectivity in administering actions against offenders.

- A new plain-English Code of Conduct is being written which will be accompanied by an improved Table of Offenses and Penalties that states what actions will result from specific types of misconduct.

- A Discipline Handbook for employees and managers to explain the process and rules and responsibilities is being developed.

- A "bright line" memo, which will be distributed to all Customs employees, is in the final stages of preparation. The memo will clearly outline a "bright line" of the types of conduct which are inconsistent with continued employment with the Customs Service.

- Past records and personnel files of employees will be reviewed prior to consideration for promotion or merit awards. Final decisions on selections will be made by Assistant Commissioners after reviewing all relevant information contained in an employee's file.

ROTATION OF SPECIAL AGENTS

IG Finding: The IG review found that there was no standard policy on the issue of special agent rotation between the Office of Investigation (OI) and Internal Affairs (IA). IG review also found that Customs policy of rotating agents within the same geographical area could call into question the objectivity of IA agents and undermine employee confidence in any integrity program.

New Customs Policies:

- A rotation process of senior agents, including GS-13s, 14s and 15s, between OI and IA has been established to improve the cooperation and effectiveness between these units. This rotation will enhance agents' understanding of investigative processes and build a talent pool of future agency leaders.

- We respectfully disagree with the IG's conclusions regarding rotation of agents within the same geographical area. The clear majority of IA investigations do not involve OI agents. For that minority which does, a clear recusal policy and strong supervision will ensure objectivity.

EMPLOYEE INTERVIEWS

IG Finding: Most of the employee concerns about integrity uncovered by the IG during its interview process of 500 Customs employees -- timeliness of investigations, investigations by management, impartiality, the role of IA -- have been addressed above. The remaining issue of great concern to employees was the fear of retaliation by management when reporting abuses.

New Customs Policy: To reduce employee fears of retaliation by managers if they report misconduct, several policies have been implemented.

- Specific training about retaliation and the Whistleblower Protection Act will be made a part of the Internal Affairs Basic Course beginning June 21, 1999.

- All agency employees received a memorandum announcing the whistlebower hotline, located in my office, which will provide employees with information on how and where to report allegations of misconduct.

- All agency employees have been provided with a pamphlet on whistleblower protections prepared by the Office of Special Counsel.

- In appropriate investigations, Internal Affairs agents will specifically advise managers whom they interview about the rules prohibiting retaliation against their employees.

- The Assistant Commissioner for Internal Affairs is working with the other Assistant Commissioners to ensure that retaliation allegations are aggressively and effectively investigated and resolved through the disciplinary process.

I hope you will agree that the efforts we have undertaken or are in the process of undertaking effectively respond to the concerns raised in the Inspector General's report. I want to assure you that our process for improving the operations of the Office of Internal Affairs and our disciplinary procedures is ongoing. We intend to continue to implement changes that will enhance the effectiveness of our operations and ensure greater integrity and accountability at every level of the agency.

I am enclosing for your information a series of memoranda which address changes in agency policies and procedures.

Sincerely,

Raymond W. Kelly

Raymond W. Kelly
Commissioner

Enclosures
Memorandum, Discipline, December 24, 1998
Memorandum, Delegation of Selection Authority, January 12, 1999
Memorandum, Delegation of Selection Authority # 2, January 27, 1999
Memorandum, Reforms to the Customs Investigative and Discipline Programs, February 25, 1999
Customs Directive No. 51735-010, Dated April 13, 1999

THE COMMISSIONER OF CUSTOMS

WASHINGTON, D.C.

December 24, 1998

PER-1-HRM:LER CP

MEMORANDUM FOR ALL MANAGERS AND SUPERVISORS

FROM: Commissioner

SUBJECT: Discipline

Since becoming Commissioner of Customs, I have on numerous occasions and in a variety of forums expressed my views on employee integrity and conduct. I firmly believe that as law enforcement professionals, we are all accountable to a high standard of ethical and professional conduct. I take employee misconduct and discipline seriously and I plan to exercise personal oversight of the Customs discipline program. I will also hold all managers, from the senior level to the first line supervisor, accountable for taking appropriate disciplinary action when necessary.

Of course, the goal of any organization is to have employees maintain the highest standards of personal and professional conduct. However, as with any large workforce, we must expect instances of misconduct to occur. Our obligation is to act swiftly and fairly in addressing this misconduct with appropriate sanctions. When we can demonstrate that: 1) we take misconduct seriously; 2) employees and supervisors alike are subject to the same rules and the same process; and, 3) everyone involved is treated fairly and consistently, I am convinced that acts of misconduct and the resulting requirement for discipline will diminish.

In order to ensure that we meet these three objectives, I have called for a series of reviews and recommendations relating to the administration of discipline. In upcoming weeks, you will see the results of these activities; however, in the meantime, please be aware of the following actions and requirements:

Reporting arrests: As you know, all employees who are arrested or detained in connection with any violation of Federal, state or local law are required to report such matters to management which, in turn, is responsible for referring the reports to Internal Affairs. In addition to this

reporting requirement, I am establishing new and additional requirements that all arrests involving Customs employees be reported to the Assistant Commissioner with authority over the employee and to the Office of Human Resources Management (HRM) for review of official personnel records in coordination with Internal Affairs, and monitoring of employment and pay status.

Reporting discipline to Headquarters: I am also establishing a reporting requirement for all disciplinary activity. Offices will be required to report disciplinary activity through their servicing Labor and Employee Relations staffs to HRM on a monthly basis beginning after the first of the year. HRM will consolidate the information and provide me with detailed activity reports reflecting agency-wide discipline administration. Further information regarding both reporting requirements will be forthcoming.

Publicizing discipline: I am directing that relevant information from the referenced disciplinary activity reports be disseminated to all employees in an effort to both educate and inform. Published information will feature types of misconduct and resultant penalties, trend analysis, and breakouts reflecting disciplinary activity by organization, position and supervisory status.

All reports of discipline will be appropriately sanitized to protect individual privacy.

Review of process and delegations: I have asked the Integrity Advisory Board, led by the Deputy Commissioner, to review the disciplinary process from start to finish and assess areas of vulnerability as well as areas of potential opportunity for improvement. Areas to be assessed include reporting procedures, investigative jurisdiction and training, case tracking and management, delegations of authority and settlement. The Board is expected to provide specific recommendations for ensuring discipline is administered throughout Customs with the greatest possible degree of consistency and fairness.

As managers, we have a special obligation to act in response to misconduct within our organization, and to conduct ourselves, individually, in the manner we expect of all employees. I call upon each of you to join me in carrying out these obligations in a way that will ensure the highest standards of integrity and professionalism in the Customs Service. Our commitment to public service demands nothing less.

UNITED STATES GOVERNMENT
Memorandum

DEPARTMENT OF THE TREASURY
UNITED STATES CUSTOMS SERVICE

DATE: JAN 12 1999

FILE: PER-1-H:HRM MW

MEMORANDUM FOR ALL ASSISTANT COMMISSIONERS

FROM: Assistant Commissioner
Human Resources Management

SUBJECT: Delegation of Selection Authority - Interim Guidance

As you are aware, we have been working with your Program Management Staffs to develop procedures to effect the delegations of selection authority outlined in the Commissioner's memorandum of December 24, 1998. We appreciate you and your staff's cooperation and want to clarify, as an interim measure, several issues that have arisen.

- As indicated in the Commissioner's memorandum, an applicant's entire past record is to be reviewed prior to selection. Since there can be a significant work effort associated with compiling this information, HRM will assume responsibility for collecting relevant information from within HRM records and from other offices, including Internal Affairs. In order to avoid confusion, your staffs should not attempt to retrieve records on individuals; instead, continue to deal with your servicing staffing specialist.

- In order to manage this process as effectively as possible, we would like to clarify that HRM will be responsible for setting effective dates and making firm employment offers. Since coordinated clearances are required for these positions, please ensure that your staffs do not set effective dates without specific authorization from HRM.

- We are now developing procedures for your review of the applicant(s) under consideration for selection. If there is information identified in the review of records which raises relevant concerns about a candidate's background, prior conduct or suitability for the position being filled, it will be forwarded to you for consideration. We will provide further guidance on this aspect of the process in the near future. However, in all cases, you will receive documentation related specifically to the applicant's experience, supervisory reference checks, and

other information that we jointly determine you will need in order to exercise selection authority in a meaningful way. We are working with your staffs to identify the types of information and the referral procedures that make the most sense for your organization and the types of positions being filled.

- Until we can finalize these procedures, we will, at a minimum, conduct reviews of records for all candidates recommended for selection since the Commissioner's memorandum, as well as candidates who are in various stages of pre-appointment, for all positions covered by the memorandum. If effective dates had been tentatively established, no action should be taken until we re-confirm these dates with your staffs. As we expect the vast majority of candidates to clear all records checks, these reviews should not delay processing the actions.

- Since selection authority for all positions outlined in the memorandum now rests solely with the Assistant Commissioners, effective immediately, any actions forwarded for selection by your subordinates are considered to be recommendations. Selections you have made personally since the Commissioner's memorandum will be subject to the review process described above.

- Positions covered by the Commissioner's memorandum are subject to its requirements regardless of the way the position is filled. That is, the staffing method (e.g., merit promotion, reassignment, result of settlement agreement, accretion of duties) utilized to fill a position covered by the memorandum does not alter the delegation of authority and associated responsibilities.

- The memorandum referred to "Entry level positions for all core occupations". We would like to clarify the intention of this category, which is to include any entry into the occupation, regardless of grade. For example, an inspector being appointed as an agent, GS-1811-9, would be considered entry into a core occupation and would be covered by the memorandum.

We will continue to work with you and your staffs to streamline this process. Should you have any questions, please contact Ms. Melanie Willford, (202) 927-2519.

Deborah J. Spero

cc: Deputy Commissioner
Chief Counsel
Special Assistant to the Commissioner (EEO)
Chief of Staff

UNITED STATES GOVERNMENT
Memorandum

DEPARTMENT OF THE TREASURY
UNITED STATES CUSTOMS SERVICE

DATE: JAN 2 7 1999

FILE: PER-1-H:HRM MW

MEMORANDUM FOR ALL ASSISTANT COMMISSIONERS

FROM: Assistant Commissioner
Human Resources Management

SUBJECT: Delegation of Selection Authority - Interim Guidance #2

Recently we provided you with a January 12, 1999, memorandum (copy attached) which contained interim guidance related to the Commissioner's Delegation of Selection Authority memo. Because of additional decisions made by the Commissioner, we are issuing supplemental guidance on this matter. You are reminded that the provisions of the December 24, 1998, and January 12, 1999, memoranda are in effect.

- Entry into these occupations/positions have been added to the coverage outlined in the Commissioner's memorandum of December 24, 1998:

Intelligence Research Specialist	Senior Special Agent, GS-1811-13
Marine Enforcement Officer	Air Enforcement Officer
Technical Enforcement Officer	Detection Systems Specialist
Staff Officer at Headquarters(GS-1890)	Seized Property Officer & Specialist

- All overseas positions regardless of organizational location, including details in excess of 6 months and assignments to Preclearance locations, are now included in the coverage.

- Only the following types of actions are **excluded** from the process:

  - Reassignment actions within a covered occupation/category <u>without</u> relocation (within the same commuting area). For example, an Inspector, GS-1890-9, Chicago to Inspector, GS-1890-9, Chicago is the only type of reassignment action that would be excluded from the process.

- Discipline Review Board reassignment actions.

- Individuals' reappointments as summer hires (i.e., the initial appointment is covered, but successive years are excluded).

In addition to the actions described in the attached memorandum, the following types of actions are also **included** in the process:

- All actions involving a change to lower grade when the new position is a covered position/category.

- Appointments of all limited duty Customs Inspectors, since these individuals may be converted to full-time permanent Inspectors at a later date.

- Selection of Customs employees from Office of Personnel Management certificates for covered positions/categories.

- Reinstatements of former Customs employees to any covered position/category.

- Re-entry into a core occupation; for example, as a result of failure at Glynco or possession of previous experience.

- Actions involving Co-op students when hired for a covered position, and/or converted to a covered position.

We are continuing to work with you and your staffs to streamline this process. Should you have any questions, please contact Ms. Melanie Willford, (202) 927-2519.

Please feel free to distribute this memorandum and the attachment to your subordinate managers.

Deborah J. Spero

Attachment

cc: Deputy Commissioner
Chief Counsel
Special Assistant to the Commissioner (EEO)
Chief of Staff
CMC Directors

THE COMMISSIONER OF CUSTOMS

WASHINGTON, D.C.

February 25, 1999

MEMORANDUM FOR ALL CUSTOMS EMPLOYEES

FROM: Commissioner

SUBJECT: Reforms to the Customs Investigative and Discipline Programs

Over the past few months, you have been hearing about reviews of the processes and policies for investigating misconduct and taking disciplinary action. You will be hearing more about the results of these reviews in the upcoming weeks. However, I wanted to take this opportunity to give you an overview of the more significant changes, so that as the details are provided, you can understand how everything fits together.

Why are we making these changes? Before describing the changes, I would like to share with you the underlying reasons for them. These can be summed up in two words - **fairness** and **consistency.** Although the vast majority of our workforce will never be investigated or disciplined, when it happens, those who are the subjects of the process have a clear and compelling interest in making sure that they are treated fairly.

Sometimes people don't realize that those who are not themselves the subjects of an investigation or discipline also have a strong interest in seeing these processes work fairly and consistently. We all want to see investigations handled quickly and professionally; we want employees to be exonerated if an investigation reveals no wrongdoing. And, if there has been misconduct, we want to see penalties imposed that are appropriate to the nature of the misconduct.

Do our processes meet the fairness and consistency tests? Not completely. Even though the majority of disciplinary actions are taken appropriately, many people believe that the process isn't fair or consistent. For processes to work, employees need to have faith in them. We have had several teams looking at every aspect of investigations and discipline. While the teams did not identify any individual process that is truly "broken", they believe that collectively we need some changes to ensure that safeguards, controls and checks and balances are brought into the systems. They have made a series of recommendations that will reform the processes to ensure greater fairness and consistency.

How will our processes be changed?

The investigative process:

- a new, simple but all inclusive system for reporting misconduct to Internal Affairs;

- consistent use of criteria to determine the matters that IA will investigate and those they will refer to management;

- daily review of allegations, at Headquarters, to decide if they should be investigated or referred for management action;

- creation of a special unit in IA to handle investigations of high level officials and matters critical to the Service;

- improvements to the investigative process and training of the IA workforce;

- a new program for "administrative inquiries", using specially trained fact-finders to conduct inquiries into allegations referred to management and not subject to a formal IA investigation.

The discipline process:

- establishment of a Customswide Discipline Review Board (DRB) - drawn from a pool of trained managers, three-member DRBs will review cases of serious misconduct, and determine the proposed discipline; DRBs will provide greater consistency and objectivity across the Service in this important phase of the discipline process;

- a "plain English" Code of Conduct, in easy-to-understand and job related terms for Customs employees, and annual training on the requirements;

- an improved Table of Offenses and Penalties that provides clear guidance on ranges of penalties for specific acts of misconduct;

- an articulated and defined "bright line" describing conduct that we in Customs will not tolerate at any organizational level or by any employee;

- a discipline handbook for employees and managers to explain the process and roles and responsibilities.

General program improvements:

- an enhanced whistleblower information program, staffed in the Office of the Commissioner that will provide employees and managers with information on their rights and responsibilities, and oversee training;

- new delegations of authority, elevated to the necessary levels to ensure consistency and accountability in making decisions on discipline;

- systematic analysis of statistics on allegations and resultant actions to identify trends, improvements, and issues for review in the investigative/discipline processes.

When can we expect to see the changes begin?

These reforms will be implemented over the next few months. More detailed information will be provided on each area, so that employees and managers will have complete information in advance of any changes. Also, we will keep NTEU informed of upcoming changes and work with them closely on implementation, keeping in mind both our bargaining obligations and our partnership objectives.

Although you will be hearing much more about the enhancements to our investigative and discipline processes, I would like to stress again the underlying reasons for these changes - to promote fairness and consistency. As I have often stated, the employees of the Customs Service have some of the most important and difficult jobs in the Federal Government. You should have confidence in all of the personnel processes that are designed to support you in carrying out our mission. You, and the public we serve, deserve no less.

CUSTOMS DIRECTIVE NO. 51735-010

DATE: April 13, 1999

ORIGINATING OFFICE: IA:IPD
SUPERSEDES:
REVIEW DATE: April 2001

ADMINISTRATIVE INQUIRIES

1 PURPOSE. This directive establishes policy and responsibilities for conducting administrative inquiries into allegations which are referred to Assistant Commissioners (AC) by the Office of Internal Affairs (IA).

2 POLICY. Currently, allegations made against Customs employees are dealt with in a nonuniform manner. Incidents and allegations that are neither criminal in nature nor considered serious misconduct may be reported to IA at a manager's discretion. Managers may ask for a fact finder to look into these matters and decide whether or not to take disciplinary action. There is no dependable system in place for reporting the occurrence of an administrative inquiry or the disciplinary action that is taken pursuant to an inquiry. Additionally, for incidents or allegations that are turned over to fact finders for administrative inquiry, there is no established, uniformly trained cadre of fact finders from which responsible officials can select. As a result, reports are of variable quality and time frames for completion are indeterminate and often excessively lengthy. Consequently, disciplinary actions are often delayed to the detriment of the Customs Service and its employees. This directive outlines standardized procedures to be followed in referring, assigning and processing administrative inquiries.

3 AUTHORITY/REFERENCES. Customs Directive 099 1510-003, January 12, 1994; U.S. Customs Service Administrative Inquiry Guidebook, March 29, 1999.

4 PROCEDURES.

4.1 This directive establishes procedures for:

4.1.1 referring allegations to responsible officials for fair, objective, uniform, and timely conducting of and reporting on administrative inquiries, and;

4.1.2 selecting and training a cadre of fact finders.

5 RESPONSIBILITIES.

5.1 The Office of Internal Affairs will receive and log allegations. Those allegations that IA does not investigate will be referred to the appropriate AC for administrative

inquiry. Within 3 days of receiving a referral, the AC will review the facts contained in the referral and determine whether to:

5.1.1 take no action;
5.1.2 resolve the issue independently without assigning a fact finder; or
5.1.3 assign a fact finder to conduct an administrative inquiry.

5.2 If no action is taken by the AC or the AC resolves the issue independently without assigning a fact finder, the AC will notify IA in writing as to the respective decision. All no action proposals will be processed through the AC/Headquarters self-inspection team for final review.

5.3 If the AC determines, however, that an administrative inquiry is necessary, the following general guidelines should be adhered to in deciding on one of the two following options:

5.3.1 If the allegation:

5.3.1.1 has been previously reported (a repeat offense);
5.3.1.2 appears to be systemic in nature;
5.3.1.3 involves any form of harassment; or
5.3.1.4 is of sufficiently high interest to generate media or executive level scrutiny.

5.3.2 The fact finder should be assigned from Headquarters or a self-inspection team and report to the AC or designate.

5.4 If the allegation does not meet any of the criteria in paragraph 5.3.1, and is a local area incident, the fact finder should be assigned from the field and report to the Principal Field Officer, i.e.; Special Agent in Charge, Director of Field Operations (Customs Management Center), Director, Strategic Trade Center.

5.5 In either of the above two instances where a fact finder will be designated to conduct an administrative inquiry, the AC will issue an authorization order to the fact finder.

5.6 A cadre of trained fact finders, comprised of GS-13/14/15 management officials, will be formed from throughout the Customs Service. Each AC will provide a designated number of fact finders for this cadre in proportion to the size of the office. AC's will be responsible for periodically assessing the number of fact finders needed to accomplish the administrative inquiry mission. Additionally, AC's will project training needs in order to maintain a viable fact finder workforce. Those who are selected to be

In this cadre of fact finders must have a minimum 6 years tenure with the U.S. Customs Service, no recent or pending disciplinary action, good oral and written communication skills, and a working knowledge of Customs laws, rules, and regulations.

5.7 All fact finders will receive standardized training, with courses developed and instructed by IA, Labor and Employee Relations (LER), and Counsel. Each AC will maintain a roster of trained fact finders within his or her office, and will draw from this pool of fact finders as needed. IA will provide to all AC's at the conclusion of each training session a list of the fact finder graduates. AC's must be cognizant of the need to monitor the frequency of assigning individual fact finders, equalizing the number of times fact finders conduct administrative inquiries. Equalization must be achieved so that individuals and their offices are not unfairly burdened by disproportionate absences caused by the responsibility of fact finding.

5.8 Depending on the nature of a referral and operational and geographic considerations, AC's may determine a fact finder should be assigned from an office outside the AC's chain of command, to assure the highest degree of fairness and objectivity. This action, however, must be coordinated with the AC from which the fact finder is being requested.

5.9 Once assigned to perform an administrative inquiry, fact finders will conduct an assessment as soon as possible after the referral in order to formulate an administrative inquiry plan. IA, LER, or Counsel may be contacted as necessary by the fact finder during any stage of the inquiry process. LER may provide guidance regarding personnel data, contract or disciplinary issues, and assistance with the administrative inquiry plan, while Counsel may give legal advice. All information received by fact finders during an administrative inquiry is for official use only, and may be discussed and disseminated only among those with a need to know.

5.10 Within 45 days after receiving the authorization order from the AC, fact finders must complete and distribute through the Treasury Enforcement Communications System (TECS) a draft Administrative Inquiry Report (AIR) to IA for review and approval. Upon IA approval of the AIR and the fact finder conclusion reached, the fact finder will then submit a hard copy AIR to the assigning AC. Fact finders will follow all requirements concerning the writing and formatting of an AIR, as contained in the Customs Administrative Inquiry Guidebook.

5.11 Assistant Commissioners will determine appropriate action either through immediate action, delegation to subordinate management, or referral to the Disciplinary Review Board. Upon completion of all actions regarding an administrative inquiry, the AC will ensure the AIR is destroyed according to standard security procedures for sensitive documents.

5.12 Upon final disposition by the deciding official, LER will enter this action in the Disciplinary and Adverse Action Tracking System (DAATS), which will close the administrative inquiry in TECS. LER will maintain all administrative inquiry documents and all original attachments in accordance with the records retention schedule.

Commissioner of Customs

PREPARED STATEMENT OF VINCENT J. PAROLISI

Thank you Mr. Chairman, Senator Moynihan, and members of the Committee for inviting me to testify on the findings and recommendations contained in the Office of Professional Responsibility's (OPR) report An Assessment of Vulnerabilities to Corruption and Effectiveness of the Office of Internal Affairs, U.S. Customs Service.

I completed this review when I was the Internal Affairs Advisor at the Department of the Treasury's Office of Professional Responsibility and a principal member of the OPR assessment team. I have been an employee of the United States Customs Service since May 9, 1999. Prior to commencing my federal service, I served for more than 20 years in progressively higher command positions within the New York City Police Department's Internal Affairs, Inspection, and Intelligence Divisions.

The purpose of OPR's review was to conduct "a comprehensive review of integrity issues and other matters related to the potential vulnerability of the United States Customs Service to corruption, to include an examination of charges of professional misconduct and corruption as well as analysis of the efficacy of departmental and bureau internal affairs systems," pursuant to Congressional directive.

The review began under the direction of Raymond W. Kelly, then Under Secretary for Enforcement at the Department of the Treasury. While Under Secretary, Mr. Kelly recognized many management deficiencies within Customs, and took action to improve the level of integrity and professionalism within the organization. Mr. Kelly became the Commissioner of the U.S. Customs Service, and James E. Johnson was confirmed as the new Under Secretary (Enforcement) and continued to direct OPR's review. After moving to Customs, Commissioner Kelly remained involved in the review process. Over the past several months, Commissioner Kelly has acknowledged and agreed with many of the findings and recommendations in this report, and has implemented changes consistent with OPR's recommendations.

The OPR conclusions in the report were formed by obtaining and reviewing relevant publications, commission reports, and studies on corruption to gain a broad perspective on the subject matter. In addition, OPR conducted more than 50 interviews with Customs employees, including senior headquarters management personnel, and made several field visits to Internal Affairs offices along the Southwest border. We also consulted with other federal and local law enforcement agency personnel, including several U.S. Attorney's offices experienced in anti-corruption operations and strategies. We analyzed pertinent statistical data for Fiscal Years 1995, 1996 and 1997, covering: staffing levels; number of allegations received; types and categories of allegations; number of investigations opened and closed; sources of the allegations; subjects of the allegations; and disciplinary results. Finally, OPR reviewed and evaluated 36 randomly selected closed internal investigations conducted by the Office of Internal Affairs to determine the level of investigative proficiency.

OPR did not uncover any evidence of systemic corruption within Customs. It did conclude, however, that the most formidable corruption threat facing Customs is the illegal drug trade. OPR also found that the Office of Internal Affairs is more reactionary than proactive in detecting and combating corruption.

Finally, OPR identified eight factors which have weakened Customs' ability to confront issues of corruption. The following is a brief overview of those findings and recommendations:

ORGANIZATIONAL ALIGNMENT OF INTERNAL AFFAIRS

Until recently, the Office of Internal Affairs was on the same organizational level as Customs' other ten Assistant Commissioner offices, reporting to the Commissioner through the Deputy Commissioner. Given the confidential and sensitive nature of the work performed by Internal Affairs, it is imperative that this office report directly to the Commissioner. Furthermore, a direct reporting relationship demonstrates an agency's commitment to the investigative function of Internal Affairs, and assures that the Commissioner receives all pertinent information concerning integrity operations without any restrictions. OPR recommended that the Commissioner realign the Office of Internal Affairs to give the Assistant Commissioner of Internal Affairs direct access to the Commissioner. This recommendation has already been implemented by Commissioner Kelly.

LEADERSHIP WITHIN THE OFFICE OF INTERNAL AFFAIRS

OPR found that Customs' Office of Internal Affairs required new leadership. The mission of Internal Affairs is complex and demanding and requires aggressive leadership, which we found lacking. OPR recommended that the Commissioner select a new Assistant Commissioner of Internal Affairs. In December 1998, Commissioner

Kelly selected Mr. William Keefer, who you have just heard from, as the new Assistant Commissioner of Internal Affairs.

CONFLICT BETWEEN THE OFFICE OF INVESTIGATIONS AND THE OFFICE OF INTERNAL AFFAIRS

Conflicts between the Office of Investigations (OI) and the Office of Internal Affairs (IA) has significantly interfered with the successful performance of Internal Affairs' operations. OPR recommended that the Commissioner establish conflict resolution strategies to rebuild positive relationships between these offices. In February of this year, Commissioner Kelly issued a memorandum mandating cooperative measures be instituted between the two offices and subsequently, the Assistant Commissioners for both Internal Affairs and Investigations jointly signed a memorandum to IA and OI Special Agents in Charge, outlining working agreement standards and rules of cooperation and communication.

RECRUITMENT AND HIRING PRACTICES OF CUSTOMS INSPECTORS AND PERIODIC REVIEW INVESTIGATIONS OF ALL CUSTOMS EMPLOYEES

A uniform nationwide process is needed to assure consistency in the recruitment and hiring of Customs inspectors. Shortcomings in monitoring practices have resulted in a backlog of approximately 5,600 Periodic Review Investigations of employee background reinvestigations. These investigations are an important tool in assessing the appropriateness of continued employment and the potential for corruption. OPR recommended that Customs continue its work with the Quality Recruitment and Hiring initiative and take affirmative action to resolve the backlog of Periodic Review Investigations. In response to OPR's recommendations, Customs has appointed a National Recruitment manager, and Commissioner Kelly has reprogrammed funds to eliminate the backlog in the Periodic Review Investigations over a two-year period.

INTEGRITY TRAINING

Integrity training for Customs employees is inadequate for deterring corruption. OPR recommended that Customs create an Office of Training to coordinate and implement agency wide training and that the Assistant Commissioner of Internal Affairs should work cooperatively with this new office to ensure that adequate integrity training becomes a priority for all Customs' employees. Prior to the release of the OPR report, Commissioner Kelly created the Office of Training and Development at the Assistant Commissioner level and will soon be announcing the appointment of the new Assistant Commissioner for Training.

APPLICATION AND ADMINISTRATION OF DISCIPLINE

Customs' disciplinary system is fragmented, resulting in perceived inequities in the application of discipline. At the time of the OPR's review, there were three separate internal processes for adjudicating discipline based on the organizational assignment of the offending employee. Furthermore, the database used to record and track disciplinary cases does not allow for comparisons or analysis of disciplinary matters. OPR recommended that Customs redesign its disciplinary database system to provide information for evaluation and comparisons, and that it establish a uniform internal mechanism for the adjudication of administrative discipline. In response to these recommendations, computer redesign is currently underway to integrate the Internal Affairs' Case Management System with the Office of Human Resources Disciplinary and Adverse Action Tracking System. This integrated system will allow for comprehensive data capture within a single query for specific allegations received, investigative findings, and the disciplinary results applied. In addition, service-wide Disciplinary Review Boards have been implemented.

USE OF CUSTOMS AND INS PERSONNEL AT PRIMARY INSPECTION LANES ON THE SOUTHWEST BORDER

Since 1979, Customs and the Immigration and Naturalization Service (INS) have shared the commitment to staff primary inspection lanes at various Southwest border ports of entry. The lack of direct supervisory control and accountability by su-
isory personnel over inspectors outside of their respective agencies can be a
kness in the overall management and integrity efforts on the Southwest border.
ıddress this and other concerns, the Commissioner of Customs and the Commis-
er of INS implemented the Border Coordination Initiative (BCI). OPR rec-
ıended that the Commissioners of Customs and INS build upon the strong foun-
on of BCI to minimize incidents of corruption. Customs is planning to work

closely with INS to aggressively implement further areas of joint coordination under the BCI initiative.

ASSESSMENT OF THE OFFICE OF INTERNAL AFFAIRS

OPR also conducted a quantitative and qualitative assessment of the Office of Internal Affairs and found that Internal Affairs is not focusing sufficient attention on more serious criminal investigations nor effectively using its investigative resources. A significant number of recommendations were made to correct these deficiencies, to include: centralizing the operation of Internal Affairs' Case Management System at headquarters; establishing guidelines to prevent the downgrading of allegations from a higher class to a lower class; conducting more self-initiated (proactive) internal investigations; greater use of confidential informants; and the creation of a Quality Assurance Unit within Internal Affairs to monitor and review each completed investigation to ensure compliance with investigative standards set by the Assistant Commissioner of Internal Affairs. Internal Affairs has established an Intake Review Group at headquarters, which will have the responsibility to assess and process all allegations in a structured, uniformed environment.

As noted in OPR's report, there is no one strategy or solution to the problem of corruption. There must be a synergistic approach to combating corruption; therefore, OPR's recommendations should be viewed as complementary strategies to enhance Customs' ability to perform its anti-corruption mission. It is also important that Customs undertake an agency wide initiative to increase the level of corruption awareness of all Customs employees so they can participate and have a role in preventing and combating corruption. OPR commends Customs' recent efforts to become proactive in preventing and detecting possible corruption, and believes Commissioner Kelly's strong leadership will have a lasting, positive impact on the U.S. Customs Service.

I appreciate the committee's interest in this very important issue and believe that this committee's continued oversight of the Customs Service is not only warranted, but an added benefit in the fight against corruption.

This concludes my formal statement. I look forward to answering any questions the committee may have. Thank you.

Office of Internal Affairs
Answers to Senator Hatch

Could you please tell the committee what specific steps are being taken to correct the following identified deficiencies?

- Is their (sic) a manual for conducting investigations, and is it regularly updated, annotated and disseminated?

The manual which outlines the procedures and processes to follow in conducting integrity investigations is the Internal Affairs Special Agent Handbook. The Handbook is contained on-line, and updated with new information and procedures as necessary. Input to the Handbook is via the Customs InfoBase system, which allows for necessary changes to be made on a monthly basis. InfoBase also provides immediate access to any part of the Handbook by authorized personnel.

- What procedures have been put into place to ensure that whistleblowers are fully protected?

The Commissioner of Customs issued a memorandum to all Customs employees on April 14, 1999, which was followed by Customs Directive 51735-012, dated April 30, 1999. The purpose of the memorandum and subsequent Directive was to provide to all employees a definition of Whistleblowing, and outline the rights, obligations, and privileges afforded to employees under the Whistleblower Protection Act. Employees were also provided copies of a pamphlet, "The role of the Office of Special Counsel,' which explains the role of the U.S. Office of Special Counsel in cases involving Whistleblowers.

The Directive also announced the establishment of the U.S. Customs Service Whistleblower Protection Program. Under this program, a toll-free Whistleblower Hotline was created as a source for employees to obtain additional information regarding Whistleblowing and as a means for employees to obtain points of contact to report Whistleblower disclosures and allegations. Also announced in the directive was the creation of a position of Whistleblower Program coordinator, which is located on the Commissioner's staff. The main responsibility of the Whistleblower Program Coordinator is to administratively oversee the Customs Whistleblower Protection Program.

How is the Office of Internal Affairs staffed? Are agents regularly rotated? Are their career performances used as determinants of their suitability for assignment to Internal Affairs?

The Office of Internal Affairs is funded for 382 positions, of which 193 are criminal investigators (agents). The mix of agents, investigative support personnel and other positions varies based on mission priorities and available funding. Over the past three years, a de facto rotation of agents through promotions, normal reassignments, and directed reassignments between the Office of Internal Affairs and Investigations has occurred at an annual rate of approximately 19 percent. In May 1999, the Commissioner of Customs ordered the implementation of a formal rotation, affecting 92 agents between both offices.

An agents investigative and career performance is used as one evaluation tool for assignment to IA. In seeking highly qualified and experienced investigators to work on sensitive integrity cases, successful investigative history, a clear background, and application of specialized investigative skills are all highly sought determinants for suitability as IA agents.

PREPARED STATEMENT OF JAMES D. PHILLIPS

Mr. Chairman and members of the Senate Finance Committee, I appreciate the opportunity to appear before you today to present the views of the Canadian/American Border Trade Alliance.

The CANADIAN/AMERICAN BORDER TRADE ALLIANCE (Can/Am BTA) is a transcontinental/bi-national broad-based organization with participation from all 22 states on or near the U.S./Canada Border (from the State of Washington to Maine including Alaska) plus the Canadian provinces with a combined network which involves over 60,000 companies and organization in their individual memberships. Can/Am BTA participants; include producers; shippers; brokers; mode transportation providers; bridge and tunnel operators; chambers of commerce; business and trade corridor associations; economic development and government agencies.

Over the past ten years I have had first-hand opportunities to participate and experience most aspects of U.S. Customs and INS border protection and facilitation activities onsite at a number of U.S./Canada border crossing locations.

U.S. CUSTOMS WORKLOAD INDICATORS

U.S./Canada two-way trade, "is the largest trading partnership" in the world. It is the fastest growing segment of major economic activity in the global economy. It is a fundamental element of U.S. economic viability which directly translates to job creation and is critical to the continued growth of the U.S. economy.

In 1988, the year "before" the Free Trade Agreement was implemented, U.S./Canada Trade was $194 billion. Since then U.S./Canada Trade has doubled and is now crossing our Northern Border at the rate of $40 million every hour reaching $387 billion in 1997 (see attached chart).

At the Northern Border U.S. Customs processes:

62% of the total trucks (growing at 11% per yr.);

85% of the trains;

40 million privately owned vehicles (⅓ of national total); and

104 million passengers and pedestrians (23% of national total).

Total containers (1994–1996) increased at an annual growth rate of 8%. Of more timely importance, containers processed in 1997 increased 44% over 1996 and in 1998 was increased 33% over 1997.

In the last three years, commercial entries increased at an annual growth rate of 11%. The current number of authorized U.S. Customs Inspectors working on the Northern Border is essentially the same number employed in 1980. The formal entries on the Northern Border have increased sixfold since 1980 from 1 million to 6 million a year.

NARCOTICS THREAT—NORTHERN BORDER CONSIDERATION

In the period 1996 to 1998, the number of narcotics seizures have increased at an annual growth rate of 19%, the majority occur on the Southern and Southwestern Borders. However, several factors are at work portending future escalation threats on the Northern Border where U.S. Customs Inspection staffing remain at 1980's levels. Threats encompass:

1. A change in current Cargo traffic along the Northern Land Border. Whereas previously U.S. Customs found that the majority of cargo processed along the Northern Border originated in Canada, changes in maritime shipping patterns "now" results in cargo crossing which originates anywhere in the world. Cargo arriving by vessel is now offloaded at one of several new large container ports in Canada and travels to the U.S. by truck or rail entering at a Northern Border land port;

As the size of these large ocean vessels increase (some vessels now carry 8,000 containers requiring 4,000 or more trucks to unload) to arrive in Canada with cargo destined for U.S. delivery. This is an increased opportunity "Threat" for Customs and one which will need to be addressed through the same aggressive means Customs has undertaken to address smuggling in other venues. The fatal flaw to providing effective and appropriate response to this new situation is lack of adequate staff and resources to meet current needs much less this new threat to the U.S. Origin reviews by Customs also significantly affects duty collection. With the current Customs understaffing on the Northern Border, capability to perform adequate investigation is a concern;

2. Current escalation of hydroponically grown marijuana. It is understood that this species is exceedingly potent and commands a street price in the U.S. of $4,000 a pound double that of the street price in British Columbia where it is being grown. The necessary additional enforcement/inspection to combat this situation without

benefit to added staff is resulting in traffic congestion delays of 1 to 2 hours at the major Washington State/British Columbia crossings; and

3. Additional U.S. Customs staff and resources (plus that of other federal agencies) have rightfully been authorized on the Southern Borders in order to combat major levels of narcotics activity. As they succeed in their mission, the specter of increased illegal trafficking being initiated through the under-staffed Northern Land Border (as the "weakest link" alternative) is raised.

VIEW OF THE NORTHERN BORDER SITUATIONS

From extensive observations and exposure to U.S. Customs border crossing activities and counsel with CAN/Am BTA members, who make their livelihoods on and at the border I offer this testimony to provide information for your review and consideration.

In the early '90 border crossing infrastructure lane capacity and plaza constraints were a major limitation along with lack of adequate U.S. Customs staffing at the Michigan and New York Bridge and Tunnel crossings which carry 70% plus of the total U.S./Canada trade and traffic.

In the past six years, the Michigan and New York crossing operators have made or are making $750 million of new investment in capacity additions and improvements (and may I add that no public or tax funds are used).

During the same six year period, quantum leaps were made in technology development and utilization by both operators and federal agencies active at the border for automatic toll collection, transponders computerization, systems development, enforcement equipment, and techniques, license plate readers, biometrics, remote port entry techniques, video cameras, voice analyzers and NATAP and NCAP pilots achieving seamless commercial passage under selective conditions. These technical developments however are just scratching the surface since enough funding is not currently made available in U.S. Customs Appropriations to actually activate these devices on the Northern border in any volume.

Much improvement in inter-governmental agency cooperation and modernization (especially U.S. Customs and INS cooperation, Agriculture and U.S. Customs cooperation and FDA computerization) has been achieved with more to be done.

The Canada/United States Accord on Our Shared Border agreement commenced in February 1995 which continues to result in increased cooperation harmonization, exchange, shared training, equipment and joint facilities between U.S. and Canadian agencies. This essential bi-national initiative needs to continue to be given priority to finalize achievable improvements which are of paradigm shifting importance. U.S. Customs has recently appointed a Northern Border Coordinator for increased focus on work with Canada. This initiative is welcome and will enhance progress. In spite of the aforementioned positive improvements, some of which are of historic proportions, while communities and private sector entities have stepped up, current authorized U.S. Customs and INS staffing cannot service the existing required border crossing lane capability. The downside of the success in the array of mentioned improvements is that they "mask" the need for added staff by averting outright crises which would occur without these improvements.

For the past two years, the Bridge and Tunnel operator members of the Can/Am BTA unanimously report that U.S. Customs understaffing is by far the number one cause (coupled with INS to a slightly lesser degree) of congestion and non-operation of in-place crossing processing lanes. This is echoed in the Central and Western regions at Northern Land Border crossings. Perhaps the most telling example is at the Rainbow Bridge in Niagara Falls, New York where new facilities were constructed doubling the primary inspection lanes to remove long standing choke points and accommodate large, new increased traffic demands from Canadian Casino gaming. No new permanent U.S. Customs inspectors have been provided so the new capacity remains essentially unused while traffic congestion and time delays mount.

Because of current inadequate funding levels, U.S. Customs has to make "lose/lose" choices continuously at the Northern Land Border crossing, i.e., operate a passengers car lane vs. a truck lane and when both are needed and when an illegal activity/seizure occurs, make a choice to close one or both types of primary lanes in order to provide staff to handle the seizure.

Trade and tourism are critical to the U.S. economy. Both are growing annually in double digits while inspection agency staffing is capped on the Northern border leaving the crossings area communities to "deal with the resultant congestion and delays" within each individual state.

At land borders crossings in the State of Washington, Montana, North Dakota, Minnesota, Michigan, New York, Vermont and Maine, routinely half of the existing

primary inspection booths (in total) remain closed due solely to understaffing of U.S. Customs and INS inspectors.

U.S. Customs has dual important missions neither of which should be comprised.

1. Enforcement and interdiction of illegal goods and activities to protect the Country.

2. Facilitation of legal trade and tourism which contributes directly to economic growth, taxes and job creation.

U.S. Customs should and must do both, but current imposed funding constraints prohibit their ability to effectively do so.

The Southern Border has a proven serious protection threat with narcotics and illegal aliens. In the period 1990–1998 every additional U.S. Customs position authorized by Congress was directed to the Southern Border. Total U.S. Customs inspection staffing on the Southern Border more than doubled and they need even more personnel.

In deploying all new resources to the Southern Border the Northern border was forced to "make do." Actual work load demands in every category grew sharply. Customs has done "yeomen duty" with what they were given to work with. Today their staff is over extended.

Enforcement's protect our populace and cannot be sacrificed. It is mission number one but not at the expense of sacrificing facilitation. The current situation for Customs to provide adequate, much less appropriate, services at current funding levels is untenable. They are continually forced to choose on the facilitation side i.e., air vs sea vs land; Northern Border vs Southern Border and passenger vs cargo.

These critical areas cannot continue to be "either/or."

The Northern border embodies 40% of the total 301 ports/crossing in the U.S. but has only 14% of the currently deployed inspectors who perform 33% of the national Customs workload. The total current primary inspection on the entire Northern Land Border is under 900 (men and women), the same level it was in 1980. Compare that to the 500 required inspectors currently staffing JFK Airport. The "shortage" of Northern Border customs inspectors is not a "media event" as it would be for Southern border drug activity or massive delays at busy airports but are just as real.

RECOMMENDATIONS

A perspective for funding U.S. Customs operations

A retrospective view of actual Customs Commercial Processing growth in the period from 1993 to 1997 reflects: The number of importers increased 66%; the value of imports increased 32%; the number of entries increased 35% and the total revenue (the collection of duties, taxes and fees) actually increased 4% to $22.6 billion in 1997.

It was predicted in 1989, when the Free Trade Agreement with Canada was about to be introduced phasing duties out over 10 years, that gross duty collection by U.S. Customs would substantially decrease thus reducing the revenue available to the government for spending purposes. Since neither duty collected or the mandated Merchandise Processing Fee is dedicated to cover the costs of collection, enforcement and related expenses before utilizing it for general spending programs, history shows that other priorities have usurped the ability to provide appropriate funding to the critical collection related operational cost necessities i.e. U.S. Customs. The current situation will only get substantially worse. If the current approach to funding Customs isn't changed with trade volume growth projected to increase 10% a year thru 2005, Customs current processing workload, already dangerously underfunded, will be double what it is today.

Since unexpectedly, U.S. Customs continues to collect approximately $20 billion annually in duty fees today in spite of the full implementation of FTA duty removal and the NAFTA provisions as well, one could make the case that this is found money. This duty "income" should first be appropriated to cover the duty "collection cost" which include the annual operating budget of U.S. Customs related to Trade and Commercial activities including the required new Commercial Automation System development, Operation Cost, System Maintenance and upgrades.

It would amount to—less than 13 cents of each dollar—of duty income actually collected each year by U.S. Customs, to fund the entire U.S. Custom's Annual budget ($1.71 billion for 1999), plus the additional $300 million a year needed for new commercial automation and $250 million a year needed for the desperately required increased staff, technology and equipment proposed in Senator Moynihan's Bill S. 219, coupled with Senator Gramm's Bill.

This view reflects that additional user fee generation is in fact not related to covering adequate cost to operate U.S. Customs, but for the non related programs currently benefiting from being funded with Duty revenue.

Duty is collected from trade and manufacturing activities which translate directly to economic growth, tax generation and most important "Job Creation."

Airport preclearance positions

It is of great concern that U.S. Customs will "not be able" to meet the demand for service this summer in its Canadian preclearance program unless a legislative remedy such as that contained in S. 262 is enacted.

When the enhanced U.S. Customs user fee provision under NAFTA expired on September 30, 1997, U.S. Customs lost the funding mechanism for twenty-six existing preclearance positions in Canada. Since that time, I understand that U.S. Customs, at the request of Congress, has maintained existing services by increasing overtime and sending personnel to Canada on temporary duty. Having experienced a forty-percent increase in air passenger traffic since 1994. U.S. Customs faces a growing demand for services. U.S. preclearance officers in Canada now inspect more than 9 million U.S. air passengers each year.

Recognizing that it could take between two and three months to fill the aforementioned twenty-six positions prompt enactment of legislation to fund these positions is indicated. U.S. Customs cannot and should not be expected to continue to provide preclearance inspection services without having a proper funding mechanism in place.

Constrained or eliminated preclearace operations in Canada would have an extensive negative effect on U.S. tourism. We urge authorization of continued use of positions to maintain effective service to the traveling public.

U.S. Customs automation modernization

Automation is integral to the competitive movement of goods internationally thus is a necessity not an option.

The continued success of the U.S. Economy and U.S. Job Creation growth are based in large part on the effective and efficient facilitation and enforcement of U.S. border trade.

In order for the U.S. Customs Service to effectively carry out it's mission and responsibilities it must be provided with appropriate resources to operationalize the necessary automation capability.i.e., to efficiently facilitate and enforce Border trade activities upon which the U.S. Economy and JOB creation depend.

The current Automated Commerical System (ACS) process is outdated and over burdened. It is estimated $1.2 billion is required over the next 4 yrs to provide a critically needed replacement system ACS before it impeds trade.

The President's budget proposes a "new additional" user fee to fund this effort in an amount that would take far too many years (8 to 10) to accomplish thus risking system failure resulting in shutdown or serious interruption of U.S. Border Trade. The imposition of a new user fee as proposed by the President's budget appears to be in violation of NAFTA provisions and is unconscionable since industry has already provided funds.

Industry already pays a mandated Merchandise Processing Fee ($800 million a year as it has for the past ten years) which "is not" but should be appropriated" to provide the funds for U.S. Customs automation needs.

Needs oversight

In past years U.S. Customs continued to request resources for increased inspection and cargo personnel, technology and equipment which has not survived elimination from the final budget request presented to Congress so that you are unaware of repeated statement of needs.

In the role of oversight it suggested that the Senate Finance Committee receive a copy of all original budget request "directly" to allow for an assessment of the "deletion rationale" (for the critical needs of U.S. Customs) made in the budget process.

While Section 110 of the 1996 IIRIRA Legislation is not in itself a subject of this hearing, it is relevant to state that the proposed additional Customs staffing provided for in Senator Moynihan's Bill S. 219 and Senator Gramm's Bill and the INS staffing provided for in Senator Abraham's Bill (S. 745), will far more effectively deter potential and real terrorist, narcotic and illegal alien activities than Section 110 will ever do while avoiding logistic nightmares and border gridlock, which Section 110 in its present form will cause.

The Southern Border needs and deserves every U.S. Customs position it has and more as proposed. The Northern Border need is even more acute, but while remaining at 1980 levels is perhaps less apparent on the surface. The Northern Border now has less than half of the inspector positions of those on the Southern Border. Yet

just the Detroit Port processes more commercial transactions than ALL the Southern Border ports combined. My point is that additional Customs staff is needed at both the Northern and Southern Land Borders for different reasons. It is a wise and prudent investment in the present and future of our country.

I appreciate your invitation to appear before you today to present a unified voice of the Northern Border private sector Trade and Tourism community describing the U.S. Customs Northern Border resource shortfall and trade facilitation needs which impact directly on maintaining and increasing U.S. Trade and jobs both of which affect the U.S. economy.

PREPARED STATEMENT OF NORMAN J. RABKIN

Mr. Chairman and Members of the Committee: I am pleased to be here today to discuss work we have done addressing efforts by the U.S. Customs Service to interdict drugs, allocate inspectional personnel, and develop performance measures. For the most part, our testimony is based on products we have issued on each of these subjects since 1997. You also asked us to discuss Customs' action plan for resolving management problems. Our discussion of the action plan is based on (1) interviews with Customs officials from its Office of Planning, Management Inspection Division, and Office of Strategic Trade and (2) our examination of the several versions of the plan.

Created in 1789, the U.S. Customs Service is one of the federal government's oldest agencies. Customs is responsible for collecting revenue from imports and enforcing customs and other U.S. laws and regulations. Customs collects revenues of about $22 billion annually while processing an estimated 15 million import entries and 450 million people who enter the country. A major goal of Customs is to prevent the smuggling of drugs into the country by creating an effective drug interdiction, intelligence, and investigation capability to disrupt and dismantle smuggling organizations. Customs' workforce totals almost 20,000 employees at its headquarters, 20 Customs Management Centers, 20 Special Agent-in-Charge offices, and 301 ports of entry around the country.

DRUG INTERDICTION

Our work on Customs' efforts to interdict drugs has focused on four distinct areas: (1) internal controls over Customs' low-risk cargo entry programs; (2) the missions, resources, and performance measures for Customs' aviation program; (3) the development of a specific technology for detecting drugs; and (4) Customs drug intelligence capabilities.

Low-risk cargo entry programs

In July 1998, at the request of Senator Dianne Feinstein, we reported on Customs' drug-enforcement operations along the Southwest border of the United States.[1] Our review focused on low-risk, cargo entry programs in use at three ports—Otay Mesa, California; Laredo, Texas; and Nogales, Arizona. To balance the facilitation of trade through ports with the interdiction of illegal drugs being smuggled into the United States, Customs initiated and encouraged its ports to use several programs to identify and separate low-risk shipments from those with apparently higher smuggling risk. One such program is the Line Release Program, designed to expedite cargo shipments that Customs determined to be repetitive, high volume, and low risk for narcotics smuggling. The Line Release Program was first implemented on the Northern border in 1986 and was expanded to most posts along the Southwest border by 1989. This program requires importers, brokers (companies who process the paperwork required to import merchandise), and manufacturers to apply for the program and to be screened by Customs to ensure that they have no past history of narcotics smuggling and that their prior shipments have been in compliance with trade laws and Customs' commercial importing regulations. In 1996, Customs implemented the Land Border Carrier Initiative Program, which required that the Line Release shipments across the Southwest border be transported by Customs-approved carriers and driven by Customs-approved drivers. After the Carrier Initiative Program was implemented, the number of Southwest Border Line Release shipments dropped significantly.

At each of the three ports we visited, we identified internal control weaknesses in one or more of the processes used to screen Line Release applicants for entry into the program. These weaknesses included (1) an absence of specific criteria for deter-

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[1] Customs Service Drug Interdiction: Internal Control Weaknesses and Other Concerns With Low-Risk Cargo Entry Programs (GAO/GGD–98–175, July 31, 1998).

mining applicant eligibility at two of the three ports, (2) incomplete documentation of the screening and review of applicants at two of the three ports, and (3) lack of documentation of supervisory review for aspects of the applicant approval process. During our review, Customs representatives from northern and southern land-border cargo ports approved draft Line Release volume and compliance eligibility criteria for program applicants and draft recertification standards for program participants.

The Three Tier Targeting Program—a method of targeting high-risk shipments for narcotics inspection—was used at the three Southwest border ports that we visited. According to officials at the three ports, they lost confidence in the program's ability to distinguish high- from low-risk shipment because of two operational problems. First, there was little information available in any database for researching foreign manufacturers. Second, local officials doubted the reliability of the designations. They cited examples of narcotics seizures from shipments designated as "low-risk" and the lack of a significant number of seizures from shipments designated as "high-risk." Customs suspended this program until more reliable information is developed for classifying low-risk importations.

One low-risk entry program—the Automated Targeting System—was being pilot tested at Laredo. It was designed to enable port officials to identify and direct inspectional attention to high-risk shipments. That is, the Automated Targeting System was designed to assess shipment entry information for known smuggling indicators and thus enable inspectors to target high-risk shipments more efficiently. Customs is evaluating the Automated Targeting System for expansion to other land-border cargo ports.

Aviation program

In September 1998, we reported on Customs' aviation program missions, resources, and performance measures.[2] Since the establishment of the Customs Aviation Program in 1969, its basic mandate to use air assets to counter the drug smuggling threat has not changed. Originally, the program had two principal missions: Border interdiction of drugs being smuggled by plane into the United States and law enforcement support to other Customs offices as well as other federal, state, and local law enforcement agencies.

In 1993, the administration instituted a new policy to control drugs coming from South and Central America. Because Customs aircraft were to be used to help carry out this policy, foreign counterdrug operations became a third principal mission for the aviation program. Since then, the program has devoted about 25 percent of its resources to the border interdiction mission, 25 percent to foreign counterdrug operations, and 50 percent to other law enforcement support.

Customs Aviation Program funding decreased from about $195 million in fiscal year 1992, to about $135 million in fiscal year 1997—that is, about 31 percent in constant or inflation-adjusted dollars. While available funds decreased, operations and maintenance costs per aircraft flight hour increased. Customs Aviation Program officials said that this increase in costs was one of the reasons they were flying fewer hours each year. From fiscal year 1993 to fiscal year 1997, the total number of flight hours for all missions decreased by over one-third, from about 45,000 hours to about 29,000 hours.

The size of Customs' fleet dropped in fiscal year 1994, when Customs took 19 surveillance aircraft out of service because of funding reductions. The fleet has remained at about 114 since then.[3] The number of Customs Aviation Program onboard personnel decreased, from a high of 956 in fiscal year 1992 to 745 by the end of fiscal year 1997.[4]

Customs has been using traditional law enforcement measures to evaluate the aviation program (e.g., number of seizures, weight of drugs seized, number of arrests). These measures, however, are used to track activity, not measure results or effectiveness. Until 1997, Customs also used an air threat index as an indicator of its effectiveness in detecting illegal air traffic.[5] However, Customs has discontinued use of this indicator, as well as some other performance measures, because Customs determined that they were not good measures of results and effectiveness. Having

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[2] Customs Service: Aviation Program Missions, Resources, and Performance Measures (GAO/GGD–98–186, Sept. 9, 1998).

[3] Customs' fleet should increase because additional aircraft were funded in the Fiscal Year 1999 Omnibus Consolidated and Emergency Supplemental Appropriations Act, P.L. 105–277, 112 Stat 2681–553, 2681–583.

[4] Staffing for the Aviation Program is expected to grow to 817 in fiscal year 2000, according to Customs' latest budget justification.

[5] The air threat index used various indicators, such as the number of stolen and/or seized aircraft, to determine the potential threat of air drug smuggling.

recognized that these measures were not providing adequate insights into whether the program was producing desired results, Customs said it is developing new performance measures in order to better measure results. However, its budget submission for fiscal year 2000 contained no new performance measures.

Pulsed Fast Neutron Analysis Inspection System

The pulsed fast neutron analysis (PFNA) inspection system is designed to directly and automatically detect and measure the presence of specific materials (e.g., cocaine) by exposing their constituent chemical elements to short bursts of subatomic particles called neutrons. Customs and other federal agencies are considering whether to continue to invest in the development and fielding of this technology.

The Chairman and the Ranking Minority Member of the Subcommittee on Treasury and General Government, Senate Committee on Appropriations, asked us to provide information about (1) the status of plans for field testing a PFNA system and (2) federal agency and vendor views on the operational viability of such a system. We issued the report responding to this request on April 13, 1999.[6]

Customs, the Department of Defense (DOD), the Federal Aviation Administration (FAA), and Ancore Corporation—the inspection system inventor—recently began planning to field test PFNA. Because they were in the early stage of planning, they did not expect the actual field test to begin until mid to late 1999 at the earliest. Generally speaking, agency and vendor officials estimated that a field test covering Customs' and DOD's requirements will cost at least $5 million and that the cost could reach $8 million if FAA's requirements are included in the joint test. Customs officials told us that they are working closely with the appropriate applicable congressional committees and subcommittees to decide whether Customs can help fund the field test, particularly given the no-federal-cost language of Senate Report 105–251.[7] In general, a complete field test would include (1) preparing a test site and constructing an appropriate facility; (2) making any needed modifications to the only existing PFNA system and its components;[8] (3) disassembling, shipping, and reassembling the system at the test site; and (4) conducting an operational test for about 4 months. According to agency and Ancore officials, the test site candidates are two seaports in California (Long Beach and Oakland) and two land ports in El Paso, Texas.

Federal agency and vendor views on the operational viability of PFNA vary. While Customs, DOD, and FAA officials acknowledge that laboratory testing has proven the technical feasibility of PFNA, they told us that the current Ancore inspection system would not meet their operational requirements. Among their other concerns, Customs, DOD, and FAA officials said that a PFNA system not only is too expensive (about $10 million to acquire per system), but also is too large for operational use in most ports of entry or other sites. Accordingly, these agencies question the value of further testing. Ancore disputes these arguments, believes it can produce an operationally cost-effective system, and is proposing that a PFNA system be tested at a port of entry. The Office of National Drug Control Policy has characterized neutron interrogation as an "emerging" or future technology that has shown promise in laboratory testing and thus warrants field testing to provide a more informed basis for deciding whether PFNA has operational merit.

Federal counterdrug intelligence coordination efforts

At the request of the Subcommittee on National Security, International Affairs and Criminal Justice, House Committee on Government Reform and Oversight,[9] in June 1998 we identified the organizations that collect and/or produce counterdrug intelligence, the role of these organizations, the federal funding they receive, and the number of personnel that support this function.[10] We noted that more than 20 federal or federally funded organizations, including Customs, spread across 5 cabinet-level departments and 2 cabinet-level organizations, have a principal role in collecting or producing counterdrug intelligence. Together, these organizations collect

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[6] Terrorism and Drug Trafficking: Testing Status And Views on Operational Viability of Pulsed Fast Neutron Analysis Technology (GAO/GGD–99–54, Apr. 13, 1999)

[7] Senate Report 105–251 (July 1988) on the fiscal year 1999 Treasury and General Government Appropriations bill directs the Commissioner of Customs to enter into negotiations with the private sector to conduct a field test of the PFNA technology at no cost to the federal government.

[8] The existing (prototype) PFNA system is located at the vendor's plant in Santa Clara, CA.

[9] This is now the Subcommittee on National Security, Veterans' Affairs and International Relations of the House Committee on Government Reform.

[10] Drug Control: An Overview of U.S. Counterdrug Intelligence Activities (GAO/NSIAD–98–142, June 25, 1998).

domestic and foreign counterdrug intelligence information using human, electronic, photographic, and other technical means.

Unclassified information reported to us by counterdrug intelligence organizations shows that over $295 million was spent for counterdrug intelligence activities during fiscal year 1997 and that more than 1,400 federal personnel were engaged in these activities. The Departments of Justice, the Treasury, and Defense accounted for over 90 percent of the money spent and personnel involved. Customs spent over $14 million in 1997 on counterdrug intelligence, and it is estimated that 63 percent of its 309 intelligence research specialists' duties involved counterdrug intelligence matters.

Among its many missions, Customs is the lead agency for interdicting drugs being smuggled into the United States and its territories by land, sea, or air. Customs' primary counterdrug intelligence mission is to support its own drug enforcement elements (i.e., inspectors and investigators) in their interdiction and investigation efforts. Customs is responsible for producing tactical, operational, and strategic intelligence concerning drug-smuggling individuals, organizations, transportation networks, and patterns and trends. In addition to providing these products to its own drug enforcement elements, Customs is to provide this information to other agencies with drug enforcement or intelligence responsibilities. Customs is also responsible for analyzing the intelligence community's reports and integrating them with its own intelligence. Customs' in-house collection capability is heavily weighted toward human intelligence, which comes largely from inspectors and investigators who obtain information during their normal interdiction and investigation activities.

RESOURCE ALLOCATION

In 1998, we reported on selected aspects of the Customs Service's process for determining its need for inspectional personnel—such as inspectors and canine enforcement officers—for the commercial cargo or land and sea passengers at all of its 301 ports.[11]

Customs officials were not aware of any formal agencywide efforts prior to 1995 to determine the need for additional cargo or passenger inspectional personnel for its 301 ports. However, in preparation for its fiscal year 1997 budget request and a new drug enforcement operation called Hard Line,[12] Customs conducted a formal needs assessment. The needs assessment considered (1) fully staffing all inspectional booths and (2) balancing enforcement efforts with the need to move complying cargo and passengers quickly through the ports. Customs conducted two subsequent assessments for fiscal years 1998 and 1999. These assessments considered the number and location of drug seizures and the perceived threat of drug smuggling, including the use of rail cars to smuggle drugs. However, all these assessments were focused exclusively on the need for additional personnel to implement Hard Line and similar initiatives; limited to land ports along the Southwest border and certain sea and air ports considered to be at risk from drug smuggling, conducted each year using generally different assessment factors, and conducted with varying degrees of involvement by Customs' headquarters and field units.

We concluded that these limitations could prevent Customs from accurately estimating the need for inspectional personnel and then allocating them to ports. We further concluded that, for Customs to implement the Results Act successfully, it had to determine its needs for inspectional personnel for all of its operations and ensure that available personnel are allocated where they are needed most.[13]

We recommended that Customs establish an inspectional personnel needs assessment and allocation process, and Customs is now in the process of responding to that April 1998 recommendation. Customs has awarded a contract for the development of a resource allocation model, and Customs officials told us that the model was delivered in March 1999 and that they are in the early stages of deciding how to use the model and implement a formal needs assessment system.

PERFORMANCE MEASURES

Under the Results Act, executive agencies are to develop strategic plans in which they, among other things, define their missions, establish results-oriented goals, and

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[11] Customs Service: Process for Estimating and Allocating Inspectional Personnel (GAO/GGD–98–170, Apr. 30, 1998); Customs Service: Inspectional Personnel and Workloads GAO/GGD–98–170, Aug. 14, 1998); and Customs Service: Inspectional Personnel and Workloads GAO/T–GGD–98–195, Aug. 14, 1998).

[12] Operation Hard Line was Customs' effort to address border violence and drug smuggling through intensified inspections, improved facilities, and advances in technology.

[13] Government Performance and Results Act of 1993, P.L. 103–62.

identify strategies they plan to use to achieve those goals. In addition, agencies are to submit annual performance plans covering the program activities set out in the agencies' budgets (a practice which began with plans for fiscal year 1999); these plans are to describe the results the agencies expect to achieve with the requested resources and indicate the progress the agency expects to make during the year in achieving its strategic goals.

The strategic plan developed by the Customs Service addressed the six requirements of the Results Act. Concerning the elements required, the mission statement was results oriented and covered Customs' principal statutory mission—ensuring that all goods and persons entering and exiting the United States do so in compliance with all U.S. laws and regulations. The plan's goals and objectives covered Customs' major functions—processing cargo and passengers entering and cargo leaving the United States. The plan discussed the strategies by which Customs hopes to achieve its goals. The strategic plan discussed, in very general terms, how it related to annual performance plans. The plan discussed some key factors, external to Customs and beyond its control, that could significantly affect achievement of the strategic goals, such as the level of cooperation of other countries in reducing the supply of narcotics. Customs' strategic plan also contained a listing of program evaluations used to prepare the plan and provided a schedule of evaluations to be conducted in each of the functional areas.

In addition to the required elements, Customs' plan discussed the management challenges it was facing in carrying out its core functions, including information and technology, finance, and human resources management. However, the plan did not adequately recognize Customs' need to improve financial management and internal control systems, controls over seized assets, plans to alleviate Year 2000 problems,[14] and plans to improve computer security.[15]

We reported that these weaknesses could affect the reliability of Customs' performance data.

Further, our initial review of Customs' fiscal year 2000 performance plan showed that it is substantially unchanged in format from the one presented for 1999. Although the plan is a very useful document for decisionmakers, it still does not recognize Customs' need to improve its internal control systems, control over seized assets, or plans to improve computer security.

You asked us to comment on the performance measures proposed by Customs, which are to assess whether Customs is achieving its goals. Customs has included 26 performance measures in its fiscal year 2000 performance plan. These measures range from general information on the level of compliance of the trade community with trade laws and Customs' regulations (which Customs has traditionally used) to very complex measures, such as transportation costs of drug smuggling organizations. Many of these complex measures were still being developed by Customs when the fiscal year 2000 performance plan was issued. In addition, Customs did not include performance targets for 8 of the 26 measures in its fiscal year 2000 plan.

ACTION PLAN

You asked us to discuss Customs' action plan, which is a document comprised of action items to resolve management problems. Commissioner Kelly originated the action plan; all assistant commissioners and office directors were asked to submit a list of actual or perceived management problems in Customs. The action plan is organized around 31 categories ranging from "integrity" to the "Mod Act implementation," and the May 1999 version had 219 items under the 31 categories. Since 16 of the items are listed under more than one category, there are 203 discrete items. For each action item, the plan currently includes the (1) date initiated, (2) responsible office(s), and (3) status. If more than one office is responsible for an action, one of the offices is designated as the lead office. Twenty-one offices within Customs are responsible for taking the lead on resolving the action items. The number of items that the offices are responsible for ranges from 1 to 37. The first action plan was issued in February 1999 and has since been updated three times.

According to the plan, it is Customs' intention to implement all action items included in the plan by 2000. Customs' Director for Planning is to manage and monitor the plan on an ongoing basis. He told us that items are usually added at the

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[14] Customs has established effective Year 2000 programs management controls, including structures and processes for Year 2000 testing, contingency planning, and Year 2000 status reporting. See *Year 2000 Computing Crisis: Customs Has Established Effective Year 2000 Program Controls* (GAO/AIMD–99–37, Mar. 29, 1999).

[15] See *Customs Service: Comments, on Strategic Plan and Resource Allocation Process* (GAO/T–GGD–98–15, Oct. 16, 1997) and *Results Act: Observations on Treasury's Fiscal Year 1999 Annual Performance Plan* (GAO/GGD–98–149, June 30, 1998).

behest of the Commissioner. The Management Inspection Division (part of the Office of Internal Affairs) is responsible for verifying and validating the items that have been reported as completed, including determining whether the action taken was effective. The action plan of May 7—the latest version available—shows that 91 of the 203 items had been completed; 110 were ongoing, pending, or scheduled; and 2 had no description of their status.

Overall, use of this kind of management tool can be very helpful in communicating problems and proposed solutions to executives, managers, and the Customs Service workforce, as well as to other groups interested in Customs such as this Committee and us.

Mr. Chairman, this completes my statement. I would be pleased to answer any questions.

PREPARED STATEMENT OF HON. WILLIAM V. ROTH, JR.

[MAY 25, 1999]

This is the third of the Committee's oversight hearings on the performance of the U.S. Customs Service. In our past two hearings, we looked at select issues related to Customs' commercial operations and its enforcement mission. This third hearing will examine Customs internal management and certain issues affecting corporate compliance with the customs laws.

Our first panel of witnesses will discuss the Customs internal affairs function. The credibility of Customs, whether in its commercial operations or enforcement, depends on its reputation for integrity. There can be no doubt that central to this proposition is the Customs Service's ability to effectively police itself against corruption and mismanagement.

While Commissioner Kelly has taken important first steps to address these concerns, the question remains whether Customs has the necessary internal mechanisms in place to sustain his proposed reforms. In addition, it is clear that strong external oversight, from this Committee as well as from the Treasury Inspector General, will play an important role in ensuring that Customs decisively and effectively addresses these problems.

This past December, I asked the Treasury Department's Office of Inspector General (OIG) to review allegations made concerning mismanagement at Customs, particularly in its disciplinary process. The OIG investigation identified serious weaknesses within Customs Internal Affairs, including poor tracking of misconduct allegations, an ineffective disciplinary program and a fear of retaliation from management for the reporting of wrongdoing.

The Treasury Department's Office of Professional Responsibility (OPR) recently published its own assessment of Customs Internal Affairs, which identified similar weaknesses in Custom's internal management and disciplinary program, as well as deficiencies in Customs integrity training.

Today, we will hear from Judge Milton Mollen—who conducted a comprehensive review of corruption and internal affairs within the New York Police Department—on what it takes to establish a solid foundation for internal affairs within a law enforcement agency. We will then hear the results of the OIG and OPR reviews as part of the testimony of our first panel. Finally, the new Assistant Commissioner of Customs for Internal Affairs will discuss the reforms instituted by Commissioner Kelly to address the concerns raised regarding Customs' management of its disciplinary process and internal affairs function.

On our second panel, we will address an equally important topic confronting Customs and the trade community—that of corporate compliance. There, we will hear about the level of investment and resources required to satisfy the Mod Act standards for informed compliance. We will also hear about the challenge members of the trade community face when smugglers find ways to infiltrate the operations of legitimate businesses to conduct their illegal transactions. Finally, we will hear how Customs can leverage its resources by partnering with industry in joint efforts to combat smuggling and effectively move the border offshore for enforcement purposes.

PREPARED STATEMENT OF SENATE PROTECTED WITNESS (FORMER SMUGGLER)

Thank you for the opportunity to continue an effort I began several years ago, assisting in the war on drugs in which I was once a participant.

I was a narcotics smuggler for over twenty years. After I was arrested by Customs for smuggling a large amount of cocaine, I agreed to cooperate with the government. This included, offering my knowledge to Customs Inspectors to assist in targeting shipments for narcotics. It is because of this continued cooperation that I am before you today.

I was educated at an Ivy League institution, and soon after I began employment with a United States intelligence agency in a capacity unrelated to my later smuggler activity. During the Vietnam Era, while in this employment, I was held as a prisoner of war for two years by the Communists.

In the early 1970's I decided to start a legitimate seafood business. Unfortunately this business venture did poorly and failed, but it was during this time that I became aware of how little interaction there was with Customs while operating on the high seas. I followed the allure of easy money and decided to enter the narcotics smuggling business.

I offered to solve an essential part of the smuggling puzzle. I provided the "transportation bridge" which closed the gap between the supply and great demand for drugs. I was the middle man who would receive the drugs from the cartels in South and Central America and smuggle them into the United States where I would turn them over to the local distributors in charge of packaging and dealing to the streets.

As with any business, smuggling is driven by profit, and it is determined by subtracting the cost of physically moving the drugs from the amount of money negotiated for the transportation. Smuggling is less expensive when there is little resistance crossing the border.

For example, when the drugs were destined to enter the United States at a border or port that was not heavily policed by Customs, then the smuggling method does not have to be as sophisticated. It is less expensive to smuggle a thousand pounds of marijuana in an open fishing boat than hidden in an ocean container. These additional costs are absorbed by the smuggler.

The goal of the smuggler is to lower transportation costs and pocket as much money as possible. This forces smugglers to "shop" ports in an effort to find the weak link in Customs armor. This becomes a shell game because as soon as the smugglers find this opening, they exploit it until customs reacts, forcing the smugglers to find a new entry way. This is apparent in the methods and ports I utilized during my smuggling career.

My first smuggling venture involved over 10,000 pounds of marijuana. Because the Customs presence in the Caribbean at the time was scarce I was able to use a fishing vessel without secret compartments.

After that successful operation, all future undertakings were targets of opportunity, meaning that I would exploit the weakest area in Customs resources at the time, usually in vessels through the Caribbean. From the late 1970s to the early 1980s, I smuggled over 500,000 pounds of marijuana into the United States valued at approximately $125 million dollars.

During this time period, I experimented with dropping cocaine out of airplanes to waiting boats. After limited success I had some bad luck and the drugs were dropped to the wrong location and lost.

As the emphasis began to focus on the Caribbean and Customs began making large seizures with a concentrated effort of airplanes and "go fast" boats I moved operations to New York City where I smuggled over 400,000 pounds of marijuana in just over 3 years. One venture resulted in the off-loading of 100,000 pounds of marijuana across the Hudson River from the World Trade Center.

I also moved to smuggling cocaine hidden in containerized cargo into the New York seaports. Finding logical products and a country of origin that would not raise red flags were important factors in being successful.

I developed a relationship with Italian organized crime in New York City and I was able to infiltrate a Fortune 500 company who did a great deal of importing. The company did not realize that I was able to import hundreds of kilograms of cocaine valued at $81 million dollars hidden within their shipments.

Before I was arrested. I attempted to smuggle a load of cocaine through this company but the Customs Inspectors noticed a paperwork discrepancy and discovered approximately 1000 kilograms of cocaine, valued at $130 million dollars. I was arrested by Customs Special Agents during an undercover operation and decided to cooperate and use my knowledge to help further Customs efforts.

I was sentenced for my role in smuggling this load of cocaine and was released from custody two years ago. While I was working closely with the Customs agents who arrested me, I promised them that when I was released from jail my cooperation would continue, and I would continue to assist in any way possible.

I was asked to make observations on drug related areas in which I have experience and there is one in particular regarding Customs' mission. Aside from the

physical placement of inspectors and agents, an important element in the war is intelligence. During my smuggling days and time in prison, I met many people who had their drugs seized and were arrested. The common thread to their downfall was almost always prior information by Customs, DEA or the FBI. Information should be an invaluable element when targeting cargo and people for narcotics. As an alumni of the intelligence community I fully understand how vital timely information is when targeting and infiltrating organizations at all levels.

In closing, I hope that I have been helpful in describing the smugglers abilities to exploit openings created by placement of Customs officers and resources. I understand and accept the condemnation that I have brought upon myself through a lifetime of smuggling. However, I would like to make clear that since the day I was arrested I have not looked back in my efforts to assist in the battle against narcotics smuggling.

Thank you for this opportunity and I hope I can answer any questions.

PREPARED STATEMENT OF LAWRENCE W. SHERMAN

Mr. Chairman and Senators, I thank you for the opportunity to testify to you today about the strategy for evidence-based policing as applied to the U.S. Customs Service. While I can claim no special expertise in the work of the Customs Service, I can claim three decades of working with police agencies around the world to improve the measurement and achievement of greater public safety. Since I began my career as a research analyst with the New York City Police Department, I have had the opportunity to work with over thirty police agencies and eleven foreign governments, including the United Kingdom, the Netherlands, Israel, Saudi Arabia, Hungary, Australia, Korea, Finland, Taiwan, Canada, and the United Arab Emirates. I have served as a consultant to local police agencies in Minneapolis, Kansas City (MO), Houston, Philadelphia, Baltimore, Milwaukee, Newark (NJ), Indianapolis and several counties in Maryland. I currently serve as an advisor on Behavioral Sciences to the FBI Academy in Quantico, as well as to numerous business corporations.

The central theme running throughout all my work with these organizations has been evidence: the systematic measurement of any claim about the nature of problems and the effectiveness of solutions. I have argued that government in general is driven far too much by theory and not nearly enough by facts. Because we fail to invest in the discovery of evidence, we waste the taxpayers' money by arguing over theories rather than testing them. Without that investment, we are flying blind, unaware of the consequences of choosing alternative methods for accomplishing our goals.

The question of the effectiveness of Customs enforcement is a prime example of the need for evidence. No one knows how much contraband is smuggled into the country at each of the ports of entry, nor how much that volume changes at each port from year to year. Without any measurement of that crucial denominator, it is impossible to tell whether increases in the seizures of contraband result from increasing volume of smuggling or more effective detection methods. It is impossible to tell whether decreases in seizures result in less effective detection methods, or more effective deterrence of smuggling at that port. Nationwide, the lack of measured changes in smuggling over time makes the establishment and meeting of numeric enforcement goals a meaningless exercise in bean-counting. Smuggling is by definition a crime committed in secret. No cry of "stop thief" is heard to add to the FBI's annual count of reported crime. No dead bodies present themselves for explanation. While the consequences of smuggling can be pernicious, they are not so easily measured as answering the telephone calls to 911. This problem is far from unique. Income tax evasion, drug dealing, and other crimes share the so-called "victimless" character of smuggling. The only "victimless" thing about these offenses, of course, is the lack of a complainant who experiences immediate harm and reports the offense to law enforcement authorities. Even that system of counting crime is unreliable, since street crime with direct victims is under-reported.

Our solution to the street crime reporting problem has been to invest in evidence. For over two decades, federal appropriations have supported the measurement of unreported victimization by means of the National Crime Victimization Survey. This national survey is administered annually by the U.S. Census Bureau under contract to the Bureau of Justice Statistics of the U.S. Department of Justice. It provides an important check on the trends in crime using methods that are unaffected by police practices, practices which can affect rates of voluntary reporting and police recording of crimes. It is not as useful as it might be for police operations, however, because it is not conducted on a city-by-city basis, or even within large cities on a precinct-by-precinct basis. Similarly, the measurement of drug use in this country

has been supported for some two decades by federally funded, annual surveys of high school students, as well as national compilation of medical data and other indicators of harms caused by illegal drugs.

The measurement of income tax evasion was once assisted by the Taxpayer Compliance Measurement Program, by which the Internal Revenue Service estimated the rates of tax evasion by occupation, geographic region, and other dimensions that could help guide enforcement operations more effectively. The federal government of Australia has just launched a multi-million dollar series of experiments for comparing different methods of encouraging greater compliance with tax laws.

I understand that the US Customs Service has on occasion conducted one-time random samples of persons entering the U.S., and has been able to produce some estimates of the percentage of smuggled drugs seized for single areas or ports of entry. My point is that this method can be of far greater use if it is conducted on a regular basis, with separate surveys for each of the port of entry.

SYSTEMATIC MEASUREMENT AND TESTING PROGRAM (STAMP)

I would recommend that the Senate authorize the expenditure of funds sufficient to produce annual estimates of the volume and nature of contraband smuggled into the US, as well as the characteristics or "profiles" of cargo and persons involved in the acts of smuggling.

These estimates should be produced by stratified random sample selections of cargo and persons for a full search. While the searches themselves should be conducted by Customs Service personnel using standard methods, the selection of cargo and persons for searching should be performed in consultation with the Customs Service by an independent organization specializing in the conduct of survey research, a field which has an elaborate and complex scientific methodology. This organization should also develop what is called the sampling "frame," or lists of possible units for full search from which samples can be selected. Finally, the organization should be responsible for reporting to the Congress on the results of the searches and extrapolated estimates about the nature and trends of smuggling, using full information from the Customs Service about the results of the searches conducted in support of the proposed Systematic Testing and Measurement Program (STAMP).

The U.S. Census Bureau is ideally qualified for the Customs STAMP program, but other organizations are also qualified. The two key principles of selecting such an organization are that it be independent of any operational responsibility for the Customs Service, and that it be highly qualified in technical knowledge of sampling and survey research. The latter point is especially important with respect to the development of smuggling "profiles," which could be objective indicators of the most productive foci for allocating scarce enforcement resources.

The issue of law enforcement profiles in this country has become a very sensitive one in all areas of drug enforcement. I suggest that one reason for this sensitivity has been the failure to invest in evidence. Most profiles are based on theories, and not on the kinds of facts that can be produced by sample surveys. Searches conducted at a higher rate on persons of a certain nationality or race will always seem unfair. Searches focused on persons whose characteristics on ten or twenty dimensions gives them a mathematically estimated high risk of carrying contraband should not seem unfair, especially if the decisions are driven by a substantial investment in discovering the highest risk persons. If that evidence is based on a truly random sample, in which all persons have an equal probability of being selected, then the use of non-random but highly accurate criteria for selecting suspect persons and cargo for search should be manifestly fair.

Here are some of the characteristics that could be measured by the Customs STAMP surveys, and factored into a mathematically weighted and computerized profile without becoming overly intrusive to arriving citizens or visitors:

Clothing (multiple dimensions).
Number of bags.
Kind of baggage.
Age.
Gender.
Number in party.
Presence or absence of children.
Occupation.
Number of times entered or exited the country.
Employment status and size of employer organization.
Specific country where each trip to US originated.
Last country visited prior to entry to US.

Each of these characteristics can be scanned into a computerized data file at the point of the immigration check. By the time the person (or cargo) clears customs the computer can advise the Customs Service of the risk level of the person. Depending on resource availability, different thresholds could be set for different levels of search.

Conducting surveys for every port of entry—or perhaps all but the very smallest—would allow far more than creation of port-specific smuggler risk factors. It would also allow an evaluation of Customs performance at each port in terms of a ratio of contraband detected to estimated contraband smuggled. Hypothetically, if JFK airport in New York detects and intercepts an estimated 10% of all drug shipments, while LAX in Los Angeles intercepts only 5%, the ratio suggests important questions of oversight for both the executive of the Service and the Congress.

COSTS

The costs of a Customs STAMP program may seem high, especially if a separate survey of 1,000 or more persons or cargo items is conducted in each port of entry every year. But the costs of not mounting this program are even higher. Not knowing whether more or fewer Customs agents are needed has enormous costs, either in taxpayer dollars or in harm done to the country. The ratio of the cost of the proposed program to the overall Customs appropriation is minuscule.

But however it is conceived, the basic point is that there is no such thing as free evidence. If we want to know how effective our Customs Service operations are, we must be willing to do what every publicly held corporation in the nation does: commission an independent firm to perform an independent assessment of the bottom line.

Thank you for the opportunity to address these important questions.

PREPARED STATEMENT OF KEVIN M. SMITH

Mr. Chairman, Members of the Committee: my name is Kevin Smith and I am the Director of Customs Administration for General Motors Corporation. In that capacity, I am responsible for ensuring that GM's import and export operations comply with all relevant customs requirements in the United States. I want to thank you for giving me the opportunity to be here today to share GM's views on the modernization of US Customs automated systems.

Last year alone, GM filed close to 500,000 Customs entries—or about 2.5% of the total entries reported to Customs, 450,000 crossed the Canadian or Mexican land borders, with about ninety percent of those carried on trucks. In the US, most of GM's customs filings are made electronically. However, the current process is still unnecessarily cumbersome and subject to delays that can create unnecessary costs.

Right now, more than 30 percent of GM's entries are shipments of $2,500 or less. Yet, each of these entries requires a separate declaration with detailed reporting requirements.

The Customs entry process now in effect is based on practices established in the 1950's and 1960's and systems put in place in the early 1980's. Most US. Customs entries require the presentation of paper invoices to obtain the release of goods. These invoices are created from the electronic data maintained by importers and shippers purely so that they can be handed to Customs officers and brokers, who then retype the information into other electronic systems. With arcane practices such as this, it is understandable that the private sector would embrace the Customs Modernization Act of 1993.

The Mod Act, as it has come to be called, established the National Customs Automation Program to modernize US Customs Service software and implement programs to enhance and streamline customs processes. These programs included import activity summary statements, remote entry filing and reconciliation of prior entries. The Mod Act also stipulated that the Customs Service seek the participation of the private sector—brokers, importers and carriers, etc.—in the development of these new systems. However, the benefits of the Mod Act did not come without a cost. In return for the promised programs, much of the responsiblity—as well as the cost—of commercial customs operations was transferred to the private sector.

Unfortunately, funding shortages have slowed the development of the promised systems, while the existing systems have become alarmingly unreliable. Last year the current system (the Automated Commercial System or ACS) suffered a number of interruptions creating serious problems in the nation's ports. For GM, such delays can be extremely costly because they interrupt the flow of parts required for our just-in-time production system. These missing parts can cause assembly line shutdowns, costly rework of our vehicles, and idling of our work force.

Although we have been disappointed generally with the pace at which new Customs automated systems are being developed, we are impressed with the performance of a number of prototypes that have been introduced to test future systems. GM, Ford and DaimlerChrysler are participating in one of these prototypes, a new automated customs process for entering and releasing goods crossing US land borders. This new system is based on the use of electronic data used in our normal business processes.

Although this prototype has required a considerable investment from us, both in time and money, we think it has been a great success. Currently GM and Customs are processing over 2000 shipments a week through the ports of Port Huron and Detroit, Michigan, and Laredo, Texas, with this prototype. In our opinion, the success of this project can be traced to the willingness of Customs to seek out the participation and support of customs users in developing this program and the cooperative spirit that evolved as the project moved ahead. Throughout the process, the Customs Service has used a disciplined managerial approach and worked closely with all those affected—including brokers, carriers and customs software developers—to make sure the end product would work well, is user friendly and efficient to operate.

Our most immediate concern is to keep the current Automated Commercial System (ACS) running to prevent delays in US Ports of Entry. Unless the necessary funding is provided, we are at risk of a serious and prolonged failure of this system that could adversely impact many businesses and jobs.

We ask the support of this Committee for the complete development of the next generation of customs automation programs, including remote filing, periodic statement processing and reconciliation, and the full implementation of the National Customs Automation Program. In our view, this would require funding, including adequate appropriations in the Fiscal Year 2000 budget, to support the continuation of current prototypes and to fully implement the new system within four years.

General Motors opposes establishing a new user fee as a source of funding. The private sector has already taken on many costly new responsibilities as a result of the Mod Act. More important, we already are paying to support the operations of the US Customs Service through the general taxes that we pay. And, more specifically, importers are paying $800 million annually in Merchandise Processing Fees and over $20 billion in import duties.

Again, I would like to thank the committee for the opportunity of appearing here today and I would be happy to answer any questions.

PREPARED STATEMENT OF MICHAEL C. TARR

Chairman Roth, Members of the Committee, I appreciate the opportunity to discuss with you today the results of our recent investigation at the U.S. Customs Service. On Sunday, December 13, 1998, The Miami Herald published a Special Report entitled "U.S. CUSTOMS: A CULTURE OF FAVORITISM." On December 17, 1998, the Chairman of this Committee, Senator Roth, requested that our office conduct an independent review of the allegations outlined in The Miami Herald article concerning the Customs Service's "ability to effectively assess allegations of mismanagement within the agency, and impose appropriate discipline where warranted."

Since this request related directly to the allegations of agency mismanagement and inappropriate disciplinary practices dating back to 1986, the Office of the Inspector General (OIG) concentrated its initial phase of the review on files relevant to the allegations in the article. The purpose of the review was to determine the effectiveness of investigations conducted by the U.S. Customs Office of Internal Affairs; review the basis for the claims of management failure; and assess the application of penalties based upon established policies within the Customs Service.

In further discussions with this Committee, it was requested that we expand the scope of our review to include additional Internal Affairs investigations and address additional concerns regarding employee perceptions of Customs Internal Affairs. We visited Internal Affairs offices in 13 cities and reviewed 395 closed investigations for fiscal years 1997 and 1998. These reviews were conducted to determine if similar deficiencies, as those addressed by The Miami Herald, were also present in other offices. We conducted over 500 interviews of Customs employees concerning the role of Internal Affairs, the application of discipline within Customs, and the fear, if any, of retaliation from management for reporting wrongdoing.

During our review of 50 Internal Affairs files relating to individuals named in The Miami Herald article, we found evidence that Customs Internal Affairs investigators did not exhaust all relevant leads or interview all knowledgeable witnesses that

may have substantiated or refuted an allegation. The inadequacies identified during our review suggest that the lack of supervisory review at both the field office and headquarters level contributed to an inferior quality of investigation. We found a number of instances in which Internal Affairs investigations failed to comply with proper reporting requirements stated in the Customs Internal Affairs Handbook.

We identified serious misconduct allegations that were initially referred to Internal Affairs for investigation that were subsequently referred to Customs management for inquiry. We found there are no published directives for conducting management inquiries within the Customs Service and there is no oversight review by Internal Affairs to ensure thoroughness. We also found the use of management inquiries exposed the sources of the allegations, which may tend to erode employee confidence of the Internal Affairs process. We determined that disciplinary penalties were inconsistently applied. Customs inability to equitably administer discipline fosters the perception of favoritism. We found that awards and promotions were issued to employees who were subjects of Internal Affairs investigations. This is a direct violation of Customs policy.

In expanding the scope of our review, we requested Internal Affairs provide a comprehensive and complete report from their automated Case Management System listing all closed internal investigations for fiscal years 1997 and 1998. We determined the Case Management System report did not conform with field office files and, in many instances was inaccurate and incomplete.

We reviewed 395 closed Internal Affairs files and found many of the same problems that we identified in our *Miami Herald* review. Investigations failed to comply with proper reporting requirements, lacked thoroughness, timeliness, and did not receive quality management review.

During our interviews with over 500 Customs employees, many expressed their lack of confidence in the Internal Affairs program. Concerns were raised regarding impartiality, confidentiality, and investigative quality. Some employees were fearful of retaliation from management for reporting alleged wrongdoing to Internal Affairs and were concerned that Internal Affairs forwarded too many allegations to management for inquiry.

Our review disclosed that there was no standard policy on the issue of special agent rotation between the Office of Investigations (OI) and the Office of Internal Affairs. However, Customs is currently proposing rotating special agents between OI and Internal Affairs by reassigning the agents within the same geographic area. The OIG believes that this proposal may call into question the objectivity of Internal Affairs agents. In addition, it may give the impression of agents investigating themselves. Objectivity is critical to overall employee confidence and the Customs integrity program.

The problems we found in our review of Customs are issues which the OIG should have identified over the years. Had a thorough oversight process occurred, some of the problems would have been identified sooner, and others less likely to have occurred as a result. We have made some organization and staffing changes during the past year, and we are undertaking other initiatives to re-establish a firm understanding of the oversight role of the OIG with Customs.

The OIG believes that the challenge of any substantial and long-lasting change in Customs must be management led and policy driven. We look forward to assisting Customs and sharing the responsibility to bring about the changes necessary.

Chairman and members of the Committee, this concludes my testimony. I would be pleased to answer any questions that you may have at this time.

DEPARTMENT OF THE TREASURY,
Washington, DC, May 25, 1999.

From: Michael C. Tarr, Acting Assistant Inspector General For Investigations.
To: Katherine Quinn, Senate Committee on Finance.
Subject: Requests for Inclusion in the Public Record.

Based on issues that were discussed on May 25, 1999, before the Senate Committee on Finance that focused on the effectiveness, integrity, and accountability in Customs operations, the Department of Treasury, Office of the Inspector General (OIG), requests the following be made part of the public record.

1. In the May 20, 1999 OIG Special Report on the United States Customs Service, the OIG stated "The OIG believes the Customs proposal concerning the rotation of agents between OI and IA in the same geographic area may call into question the objectivity of IA agents." At no time did the OIG indicate in its report or during testimony given before the Committee that it was opposed to the rotation of special agents between OI and IA.

2. In its May 20, 1999, OIG Special Report on the United States Customs Service, the OIG indicated that "There are no published directives for conducting management inquiries within the Customs Service and there is no oversight review by Internal Affairs of closed management inquiries to ensure thoroughness." During testimony given before the Committee by the Customs Assistant Commissioner for Internal Affairs, William Keefer indicated that he disagreed with the OIG finding. Keefer stated that Customs had implemented a policy effective April 13, 1999. On February 1, 1999 and March 3, 1999 the OIG confirmed with Customs at the headquarters and regional levels that Customs had no policy.

PREPARED STATEMENT OF ROBERT M. TOBIAS

Chairman Roth, Ranking Member Moynihan and Members of the Committee, my name is Robert M. Tobias, and I am the National President of the National Treasury Employees Union (NTEU). On behalf of the men and women of the United States Customs Service who enforce our trade laws, collect duties on imported goods, and fight to curb the flow of illegal narcotics and contraband into our country, I would like to thank you for this opportunity to submit our Union's views on Customs Service operations.

The mission of the United States Customs Service has developed over the 210 years of the Agency's existence. Beginning primarily as a collector of duties on imported goods, the Customs Service has transformed into a front line Agency for drug interdiction. The Agency's responsibilities include enforcing hundreds of trade laws and regulations, classifying and appraising imports, interdicting drugs, dismantling international conspiracies to launder money, smuggle arms, counterfeit money and exploit children on the Internet. Customs employees must keep products out of the United States that have been manufactured with child labor. On the Southern Border, Customs employees must enforce statewide automobile emissions standards for vehicles regularly entering the United States. We have tasked Customs employees with an important enforcement mission, while requiring that they facilitate trade and travel and keep pace with burgeoning commerce.

Over the past few years, legitimate imports have grown at double digit rates, but the Agency's staffing levels have remained relatively static. The technology necessary to clear products and cargo for entry into the United States and accurately record all of the information has not been made available to the Customs employees. Without attention to the sorely lacking staffing levels and the critical need for technology upgrading, Customs Service employees will have difficulty continuing their dual missions of enforcement and trade facilitation. Moreover, we must pay attention to the needs and morale of the rank and file who perform the Agency's work in this ever changing trade environment, so we can fully identify the problems in Customs Service operations and develop adequate solutions that will best serve the Agency and the American public.

TECHNOLOGY

Currently the Automated Commercial System known as ACS is on the brink of failure. The system is about 15 years old, subject to slowdowns and brownouts. Employees who now rely on computer technology to perform most of their job, deserve to have the most efficient and productive system available to them. We must bring Customs' technology into the 21st Century whether it be providing funds for the Automated Commercial Environment (ACE), passenger x-ray equipment at airports or vehicle gamma ray machines at land borders. Upgrading technology is necessary and overdue.

IMPORT SPECIALISTS

Customs import specialists are responsible for determining the classification, appraisal value and admissibility of products coming into the United States. Their work is demanding, ever-changing and extremely technical. An import specialist must be able to interpret the Tariff, review financial records, analyze legal decisions, be familiar with foreign currencies and the Metric System, and have technical expertise in a particular line of commodity specialization. These men and women interact daily with private attorneys, accountants, and corporate executives. They protect domestic industries by enforcing quotas and trademark and copyright laws. The import specialist position begins at a GS–5 with a career ladder to the GS–7/9/11 levels. In response to the recent explosive growth in trade, the enactment of the Customs Modernization Act in 1994, as well as many other laws, the responsibilities and necessary technical abilities of Customs import specialists have in-

creased tremendously. Yet their salary structure and position description have not reflected the GS–12 graded workload they must perform regularly.

Barry Braverman is an import specialist at JFK International Airport. He has worked in the position for over 25 years. He has told me about the added responsibilities of the position and the new demands made of him and his co-workers in response to the doubling of legitimate imports in the United States. He has had to master computer skills and design and use countless codes, data bases and spread sheets to keep pace with the Automated Commercial System. There is not a aspect of his job that does not require reliance on the computer.

In addition to mastering computer skills, import specialists must understand complex new international trade agreements. These include the General System of Preferences, the Caribbean Basin Initiative, the United States-Israel Free Trade Act, the Andean Trade Preference Act, and, of course, NAFTA. The NAFTA alone involves three countries and three languages. One general note in NAFTA is over 120 pages long. Import specialists are tasked with enforcing these type of agreements and understanding their complexities.

New programs at Customs require that import specialists work side by side with regulatory auditors and national account managers who are graded at the GS–12 and GS–13 levels. Very often they are performing the same work. Import specialists must possess the technical abilities of these higher graded employees because their assessments of rate of duty, classification and quota applicability have national impact on the importers they examine. The NAFTA verification teams, joint verification teams (JVTs), compliance assessment teams (CATs) and enforcement evaluation teams (EETs) require import specialists to perform more complex assessments and classifications and to implement the Customs Modernization Act (Mod Act). Import specialists are long overdue for increased salaries and recognition for their newly required skills, technical expertise and professional judgment. They must be provided with the proper tools and compensation if their important work is to be done efficiently and effectively.

TRADE COMPLIANCE REDESIGN

Under the Mod Act, Customs' informed compliance program places the burden on importers and brokers to determine, using reasonable care, the duty owed on their merchandise. Customs' import specialists will review an entry after the merchandise has been conditionally released into the United States by Customs. Working from the back end of an entry has created a difficult situation for the import specialist who must follow strict time frames and procedures to recover revenue or order redelivery on the products. There simply is not enough personnel performing this valuable work to properly assess the entries and ensure that the laws and regulations are being followed. To adequately shift the burden of compliance to importers and brokers without losing enforcement abilities, more personnel must be dedicated to the work of the import specialists. Employees' morale is impacted by their effectiveness in bringing importers into compliance with the trade laws. We must give the import specialists the tools to facilitate trade, but also the enforcement assistance to enforce the laws. Import specialists review product for adherence to child labor standards, copyright laws, proper markings and many consumer safety requirements. In addition to the inadequacy of their grade structure, import specialists have many concerns about the procedures and time limitations on their ability to do their job. There must be an appropriate balance between facilitation of trade and enforcement of our trade laws.

INSPECTIONAL PERSONNEL

Customs Inspectors and Canine Enforcement Officers (CEOs) present the first line of defense to the illegal importation of drugs and contraband across our borders. They are literally on the front lines at air, sea and land ports. They have been assaulted by travelers, shot at, dragged to their death by cars running ports, threatened and accosted Very recently, a Customs Inspector in Puerto Rico was shot because he was recognized as a Customs enforcement official. At the very height of a career, and even after twenty-five years of dedication to the Customs Service, an average inspector will make a base salary of about $40,000 per year.

Employees of the Customs Service, like their law enforcement counterparts around the country, are committed to the eradication of drug abuse in America. They risk their lives in the war on drugs, and sadly, many have died in that battle. Their job is demanding and dangerous. Customs inspectors carry weapons and undergo mandatory firearms training. They are taught to make arrests. They learn defensive tactics for protecting themselves from dangerous criminals with whom they may come face to face. Despite a record of unparalleled achievement in so many law

enforcement areas, the Customs inspectors and canine enforcement officers still do not qualify for federal law enforcement status. As in past years, NTEU will continue its efforts to enact legislation (H.R. 1228 and S. 718) to end this disparity. We believe that denying the brave men and women of the Customs Service the same employment rights of their counterparts in the DEA, FBI and Border Patrol is unjust.

Cargo shipments and passengers cross our borders at all times of the day and night, and Customs Inspectors must be there to process them. Most Customs Inspectors and CEOs around the country are expected to work at a minimum three different shift schedules. A shift one week may be as ordinary as 8 a.m. to 4 p.m., but the next week it may be as disruptive to the body clock and family life as 5:15 a.m. to 1:15 p.m. or even 3 a.m. to 11:00 a.m. We will continue to adamantly oppose all misguided proposals that reduce the night pay differentials of Customs enforcement personnel who are asked to do more work with inadequate staffing and technology.

INSPECTOR ROTATION

Factors including the uncertainty of irregular hours and the requirement to work overtime have contributed to a high turnover rate among the Customs inspection ranks. These turnover rates lead to increased training costs for the Agency. After being hired by Customs, many young Inspectors complete the training program, gain valuable on the job experience and move to positions with the Department of Justice, the Secret Service, the FBI or with state or local government, where they are guaranteed all the benefits of being a law enforcement officer.

I recently testified before the House Treasury Appropriations Subcommittee on the issue of Customs integrity where the subject of mandatory Customs Inspector rotation was discussed. NTEU has been clear that requiring geographic rotation for Customs Inspectors will have a devastating impact on the mission of the Agency, as well as the lives of the Inspectors and their families. There is no empirical evidence to show that uprooting experienced Customs officers and moving them around the country will lead to a reduction in corruption. In any case, Customs has stated that there is no systemic corruption problem to address, so a rotation program would be an astoundingly expensive endeavor that would do more harm than good. Implementation of a mandatory rotation scheme would contribute to the difficulty Customs has in attracting new hires in their inspection ranks. I believe retention problems would be insurmountable in light of the relatively low salaries, constant shift work and dangerous nature of the job.

COLLECTIVE BARGAINING

Evidence clearly demonstrates that the men and women of the Customs Service need better resources to better perform their mission. But, there is no evidence to show that the mission of interdicting drugs is impaired when the Customs Service lives up to the collective bargaining provisions it has negotiated. On the contrary, Customs and NTEU have an impressive working relationship. In 1998, the Customs and NTEU received the John N. Sturdivant Partnership Award in recognition of their contributions to reinventing government through labor-management cooperation. This year the parties have been nominated for the Office of Personnel Management Director's Award for Outstanding Alternative Dispute Resolution (ADR) programs focusing on resolving employee workplace disputes.

No federal agency, including the Customs Service, would enter into labor contracts that it believes interfere with its mission. There is nothing in the current contract that hinders the interdiction of drugs or contraband. In fact, we have worked closely with Customs on many special programs, including Operation Brass Ring, that have resulted in record amounts of drugs seized in short periods of time.

PERSONNEL FLEXIBILITIES

NTEU has been on the front lines for years fighting for sensible and intelligent personnel reform in federal agencies. Our goal is and will continue to be to maximize the role of the employees in shaping and designing new personnel systems that enable federal employees and agencies to work more efficiently and effectively.

In his testimony during the first day of these hearings, Customs Commissioner Raymond Kelly told Committee Members that he would like certain personnel flexibilities granted to Customs which would allow Customs to better perform its mission. Specifically, he requested that the Agency be exempt from government wide merit principles and procedures for hiring Customs employees. Additionally, he mentioned support for a three-year probationary period for Customs new recruits. In light of all the information learned about Customs management during these hearings, and considering that the Commissioner has moved to centralize operations and remove discretion from field management, these specific proposals are mis-

guided and inappropriate. We would oppose these flexibilities for the Customs Service.

Customs has not demonstrated a need to be exempt from regular competitive service hiring procedures. The current government wide competition that follows these merit principles guards against discriminatory behaviors and bad motives in the hiring process. Very few agencies have excepted service hiring authority because merit principles should govern the selection of employees into the federal service and the competition should be open and fair to all candidates. We have struggled for decades to avoid mistreatment and discrimination in government hiring. Granting excepted service hiring to the Customs Service would be a giant step back to the darker days of non-merit based selection. This would be unwise and detrimental to the work force.

Time and again, Customs employees complain about reprisal and fear of retaliation from supervisors for disclosing fraud, waste and mismanagement at the Customs Service. Currently, there are many cases before the United States Office of Special Counsel in which Customs employees have asked for whistle blower protection from retaliation by Customs management. Commissioner Kelly even recognized the need to better protect whistle blowers. He announced that he has established a telephone line to the Headquarters for reporting mismanagement and other Agency problems to Internal Affairs. He has appointed an Assistant Commissioner of Internal Affairs to ensure integrity of employees and that proper procedures and reporting is followed for all complaints. He is attempting to centralize the disciplinary process by proposing a disciplinary review board at the Headquarters level to ensure uniform treatment of all employees. His actions signal to me that he is not entirely comfortable with the decisions made by lower level supervisors regarding treatment of employees in these matters. Allowing these same supervisors to fire employees without just cause up to three years after their appointment to the Service will undoubtedly have a chilling effect on the work force that will undermine Commissioner Kelly's attempts to ensure protection for whistle blowers. Any move to give supervisors broader discretion to fire employees without cause will only generate more distrust and cynicism among the very employees whose commitment and dedication will be needed to make Customs operations better.

Customs employees should not be required to work for the Agency for three years without job security. The Agency has not demonstrated that any of its employees work in positions that would require three year probationary periods. Generally, probationary periods are longer than one year for a very narrow set of positions within the federal government. These positions include scientists and researchers whose work is experimental and performed in stages. Results of their efforts can not be known or reviewed for long periods of time. In these very specific cases, the employees' work and value to the government can not be measured or assessed within one year.

These conditions do not exist for front line enforcement personnel at the Customs Service. Customs officers undergo about ten weeks of formal training prior to being assigned a duty station. Once they pass the training, they are put to work. Supervisors have several months to evaluate the new inspectors and canine enforcement officers for their suitability for their jobs. It is foolish to allow supervisors to ignore their responsibility to adequately supervise their employees and recognize a poor performer for three years. We would never want an employee who can not do the job to continue in the position for three years before a supervisor made a decision to fire him. That is not good for the employee, for the Customs Service and especially not for the American people.

I know that the more than 13,000 Customs employees represented by the NTEU are capable and committed to the Customs mission. They are deserving of more resources and technology and the chance to have meaningful input into the discussions of personnel reforms that will impact them the most. I look forward to working with this Committee in the future and to providing the insight and perspective of the men and women of the Customs Service.

Mr. Chairman, thank you for the opportunity to submit the views of the National Treasury Employees Union on this matter. I applaud you and the other members of the Committee for taking a closer look at the resource needs and operations of the Customs Service.

PREPARED STATEMENT OF S.F. VALE

Mr. Chairman, my name is Sam F. Vale and I am here to testify on behalf of the Border Trade Alliance (BTA). The BTA has a number of proposals that we believe are essential in order to provide U.S. Customs with the necessary tools and re-

sources to carry out its trade and law enforcement missions along our nation's borders.

Mr. Chairman, the Border Trade Alliance is a grass-roots organization that was formed in 1986 to facilitate trade between Canada, the United States and Mexico. The BTA Legislative Agenda for the 106th Congress addresses the U.S. Customs Service and particularly those issues that directly affect the flow of legitimate trade and commerce across our southwest and northern borders.

The U.S. Customs Service must have the necessary inspection personnel and state-of-the-art technologies to carry out its increasingly difficult mission. To this end, the BTA is strongly endorsing the legislation introduced by Senator Phil Gramm of Texas (S–658) which if approved and fully funded, would provide Customs with its first major inspection personnel increase in nearly five years. This bill would authorize Customs to increase the necessary personnel and acquire essential technology to reduce delays at our border crossings with Mexico and Canada and move towards a Customer Service Standard of no more than a 20 minute wait at the border, while dramatically increasing our anti-drug and trade compliance efforts at both borders. The bill will allow our Federal inspection agencies to open all existing primary lanes during peak hours of operation at the land ports of entry, while enhancing our important national anti-drug efforts. We particularly support Section 201:Customs Performance Report of this bill, which calls for Customs to report on its progress in reaching the goals outlined by the bill, as well as requiring enhanced cooperation with the trade community.

Since April of 1998, and with the support of the U.S. Customs Service, the BTA and other Federal agencies with border-related missions, have been meeting together in open sessions to reach common ground on how best to address the issues of waiting times; drug enforcement; environmental policies and infrastructure needs along the border; as well as immigration policies that will efficiently accomplish our legitimate enforcement objectives. Our purpose is to reach concrete solutions for facilitating the legitimate flow of commerce across our borders, while ensuring that the flow of illegitimate commerce in narcotics and illegal immigration is stopped. Many of the recommendations that we are making today, Mr. Chairman, are the direct result of this important dialogue with the U.S. Customs Service, the Immigration Naturalization Service, the Department of State; the Food and Drug Administration; the General Services Administration; the Drug Enforcement Administration; Environmental Protection Agency, the Department of Agriculture, even the embassies of Canada and Mexico, and representatives of the four Southwest Border Governors.

Mr. Chairman, Customs needs a substantial increase in both personnel and technological tools to improve both missions.

Let's take a look at the number of trucks entering the United States at some of our ports on the Northern and Southern borders during Fiscal Year 1998. The Ambassador Bridge in Detroit, the busiest commercial port of entry on our Northern border, and Laredo, Texas, the biggest commercial port of entry on our Southern border, both saw over 1 million trucks crossing the border. Both were increases from fiscal year 1997.

Let me give you just one example that unfortunately is more the rule than the exception with regard to how traffic affects waiting times at our ports of entry.

For San Ysidro, California, the largest non-commercial port on the southern border, on January 5, 1999, the average length of the line of vehicles waiting to cross the border was 85 and the wait time was approximately 27 minutes. The average length of the line increased to 180 vehicles and up to 47 minutes by January 30th of this year. And on weekends the situation got even worse, with the numbers increasing to as high as 180 vehicles and 61 minutes in waiting times to cross the border into the United States. Without increased Customs Service inspection staffing at ports of entry along our southwest and northern borders, numbers like those at San Ysidro will only get worse.

Mr. Chairman, as a president of a company that owns and operates an international bridge port of entry and as a border businessman, I face daily the challenge of the movement of legitimate commerce into the United States against an underfunded and understaffed U.S. Customs Service. We are not alone in facing this systemic impediment to economic growth in our border regions.

From fiscal year 1992 through fiscal year 1997, Customs estimated that the number of commercial trucks entering the United States from Mexico increased by more than 50%, with rail traffic increasing by an overwhelming 115% in this same time frame. Traffic from Canada to the United States has enjoyed a similar dramatic increase. The formal commercial entries on the Northern border have grown sixfold since 1980, from 1 million to 6 million a year. Add to these facts that over 121 million automobile crossings and 340 million pedestrians crossed both borders and you

can see that the U.S. Customs Service needs a significant number of employees to keep up with the growing pace of border trade and tourism.

Mr. Chairman, as pointed out at the beginning of this testimony, the BTA has a number of proposals to address the situation faced by our borders. We have included for your review several attachments describing other key issues on the following subjects:

Upgrading and maintenance of the Automated Commercial System (ACS), the U.S. Customs Service's outdated computer system. We are supporters of the Coalition for Customs Automation Funding. We agree with its position that funding for Customs' automation efforts should be accomplished from appropriations. Like many other members of the Coalition, we do not take a position on whether the ultimate replacement for ACS should be Automated Customs Environment (ACE) or International Trade Data Systems (ITDS), but it is important that each be given appropriate consideration. We have attached testimony presented by the BTA to the House, Ways and Means Trade Subcommittee on April 13, 1999 on this subject.

We should all agree about the need for infrastructure improvements along the border. We have included for your review a report prepared by the BTA outlining needed Southern Border Port Capital Improvements. Because of time limitations and the more complex nature of the infrastructure needs along our border with Canada, we have not made a port by port infrastructure analysis along this border. However, we clearly support similar improvements at the ports of entry along the Northern Border.

We support the need to repeal the implementation of Section 110 of the 1996 Illegal Immigration Reform Act. As currently proposed, the implementation of this section will further burden an already undermanned U.S. Customs Service. To that end we support S. 745 sponsored by Sen. Abraham from Michigan. However, while the implementation is something we oppose we agree that there must be found some mechanism to adequately control our borders to prevent people who enter legally from overstaying their visa and becoming illegal immigrants. We have attached for your review our position paper on Sec. 110 and some possible alternatives.

The Gramm and Abraham bills, if coupled with the requisite appropriations, would tackle these problems head-on and provide U.S. Customs with the requisite workforce and technologies to carry out their dual missions of facilitating trade and halting the flow of illegal drugs at our borders. We urge the Committee to incorporate the major components of both bills into the final Customs Authorization legislation this year, and work with your colleagues on the Senate Appropriations Committee to provide the appropriate level of fiscal year 2000 appropriations to carry out your staffing and technology recommendations.

Some examples of the consequences of inadequate Customs staffing and funding are as follows:

1. The import lot at the Bridge of the Americas in El Paso has posted hours of operation from 6:00 am to 5:00 pm. However, U.S. Customs personnel close up the import dock inspection facility between 4:00 and 4:30 pm daily. Trucks entering the import lot immediately after closing must wait until 10:00 am the following day to have their documentation cleared or trucks inspected. The delay costs the shipper and American consumer money. U.S. Customs does not have the staff nor the budget to keep this important port of entry open enough hours to process the increasing amount of trade coming from Mexico.

2. In April 1999 the Peace Bridge in Buffalo, New York saw 6000 trucks cross through its port on a peak day. An increase of 8% over the previous year, double what was expected. Even though all the lanes were in use, back-ups occurred at the crossing and more staff is necessary to keep up with the tremendous amounts of traffic.

3. Frigoríficos Especializados de Tuxpán, a Mexican Company specializing in frozen perishable products recently decided to send its products via sea instead of routing them through the southwest border . . . its products were spoiling in the long waits to cross the border. Though their decision to ship by sea bodes well for ports on the East Coast, this example illustrates the lengths companies will go to in order to avoid costly delays at the border.

4. As reported to the Coalition for Customs Funding, General Motors estimates that their assembly lines can only operate for four hours if trade is halted at the border. Caterpillar estimates its production will shut down after a couple of days.

These are but a few examples illustrating the need for a fully funded and staffed Customs Service. OUR INTERNATIONAL TRADE IS OUTGROWING OUR RESOURCES.

Thank you, Mr. Chairman, for this opportunity to share our views with the committee.

COMMUNICATIONS

STATEMENT OF THE AIR COURIER CONFERENCE OF AMERICA

This statement is submitted by the International Committee of the Air Courier Conference of America ("ACCA") in conjunction with the Senate Finance Committee's series of oversight hearings on issues relating to the U.S. Customs Service. ACCA is the trade association representing the air express industry; its members include large firms with global delivery networks, such as DHL Worldwide Express, Federal Express, TNT Skypack International Express and United Parcel Service, as well as smaller businesses with strong regional delivery networks, such as Global Mail, Midnite Express and World Distribution Services. Together, our members employ approximately 510,000 American workers. Worldwide, ACCA members have operations in over 200 countries; move more than 25 million packages each day; employ more than 800,000 people; operate 1,200 aircraft; and earn revenues in excess of $50 billion.

The express industry specializes in time-sensitive, reliable transportation services for documents, packages and freight. It is a relatively new and rapidly expanding industry, having evolved during the past 25 years in response to the needs of global international commerce. Express delivery has grown increasingly important to businesses needing to use "just-in-time" manufacturing techniques and supply-chain logistics in order to remain internationally competitive. The express industry has revolutionized the way companies do business worldwide and has given a broad-based application to the just-in-time concept. Producers using supplies from overseas no longer need to maintain costly inventories, nor do business persons need to wait extended periods of time for important documents. In addition, consumers now have the option of receiving international shipments on an expedited basis. Increased reliance on express shipments has propelled the industry to average annual growth rates of 20 percent for the past two decades.

ACCA is pleased that the Finance Committee is examining various issues regarding U.S. Customs, because Customs administrations play a critical role in ensuring expeditious movement of goods across borders and consequently are critical to our industry's ability to deliver express international service. To give a sense of the size of our industry in U.S. trade—and as a customer of U.S. Customs—the express industry accounts for roughly 25 percent of all Customs formal and informal entries. In addition, express operators enter more than 10 million other manifest entries on low-value shipments, plus millions of clearances on letters and documents. In short, American business is dependent upon our industry, and we are dependent upon an efficient and effective Customs Service.

These comments focus on the following issues being examined by the Finance Committee: Customs' automation programs and the funding mechanisms for these efforts, and Customs' user fees.

IT IS ESSENTIAL TO THE U.S. ECONOMY THAT CUSTOMS' NEXT-GENERATION AUTOMATION SYSTEMS BE BROUGHT ON-LINE RAPIDLY

ACCA commends U.S. Customs for the impressive strides it has made in the last 12 months with respect to its approach to automation. Most important in this regard is Customs' resuscitation of the Trade Support Network, through which it has actively consulted with the express industry and other members of the trade community on the development of its next-generation automated system, the Automated Commercial Environment (ACE). While many important issues with respect to ACE remain to be decided, ACCA is encouraged that Customs appears genuinely committed to working with the trade community to develop its next-generation automation system.

ACCA believes that Customs is moving in the right direction with ACE. If Customs adheres to its current plans, ACE should provide the functionality and enhanced automated abilities—processing of data, remote entry filing, account-based systems, reconciliation, etc.—mandated by the Customs Modernization Act. Customs also plans to incorporate into ACE features that will enable Customs to adjust and upgrade the system as technology developments warrant, rather than having to create entirely new automation programs every few years.

As the Finance Committee knows, the current Customs automation system—the Automated Commercial System, or ACS—is in desperate need of replacement. The system is rapidly nearing the end of its life span and is increasingly subject to brownouts. ACCA is extremely concerned about the impact of future brownouts and even blackouts because the express industry, more than any other mode of transportation, relies on automation. We have invested tens of millions of dollars in automated systems designed to expedite shipment and delivery of goods within an express timeframe. For our industry to survive and expand, automation is critical. Without automation, thousands upon thousands of shipments every day would fail to be processed in time to meet their express delivery deadlines, stranding thousands of individuals and small, medium and large businesses who rely on our industry to provide them with the parts and components they need on a just-in-time basis to keep their manufacturing lines in operation; the computers, telecommunications and other equipment they need to keep their offices running; the blueprints they need to keep their construction projects on schedule; or the critical-care pharmaceutical and medical devices they need to provide urgent patient care.

In short, an interruption in Customs' automation programs would devastate our ability to meet our express delivery deadlines and would harm a significant portion of the U.S. economy. As an illustration of this, think back to the havoc wreaked throughout the U.S. economy by the UPS strike in 1997.

THE CLINTON ADMINISTRATION'S PROPOSAL FOR A USER FEE TO FUND AUTOMATION PROGRAMS IS ILL-CONCEIVED AND ILL-ADVISED

ACCA is extremely concerned that the Clinton Administration budget fails to acknowledge the critical importance to the U.S. economy of maintaining and improving an automated Customs environment. The budget proposed a new user fee to pay for automation, with the expectation that this would generate $163 million in the next fiscal year. This proposal fails to acknowledge the true cost of developing ACE and also fails to acknowledge the fact that the trading community has been and continues to pay an enormous annual stipend in the form of the merchandise processing fee (MPF) that should be directed to U.S. Customs' operations, including automation programs.

First, with respect to the true cost of ACE development: Customs estimates that the trade portion of ACE will cost roughly $1.2 billion if the program is developed over four years. The Administration's proposal would therefore only provide approximately half of the money needed for the first year of development. The costs of ACE development will be far greater than $1.2 billion if the project is stretched over more than four years. Furthermore, given the imminent obsolescence of ACS, the trade community and the U.S. economy simply cannot wait more than four years for development of ACE.

Second, with respect to the trade community's annual contributions to the U.S. Treasury: throughout the 1990s, U.S. importers have paid MPF on most imports into the United States. MPF revenues total about $800 million annually. When first imposed, the MPF was challenged as being illegal under the GATT; it was determined that the surcharge would be consistent with GATT requirements only if it was directly related to the costs of U.S. Customs' operations. Notwithstanding the subsequent U.S. modifications of the MPF to bring it into GATT compliance and the U.S. assertion that the purpose of the MPF is indeed to offset Customs' operating costs, the fact remains that MPF revenues have not been channeled to U.S. Customs. Instead, they have gone to the general revenue fund of the U.S. Treasury.

ACCA urges Congress to acknowledge this, as well as the critical importance of this issue to the U.S. economy, by appropriating MPF monies specifically for the development of ACE over the next four years.

THE COST OF REIMBURSABLES TO THE EXPRESS INDUSTRY HAS GROWN OUT OF BALANCE AND THE SYSTEM NEEDS TO BE ALTERED

Turning now to the issue of user fees, the express industry is in a unique situation because we pay for dedicated Customs resources at our facilities. In order to obtain inspectional services whenever needed at our hub and express consignment facilities, the express industry agreed 12 years ago to pay "reimbursables" to Cus-

toms. These fees are supposed to cover the costs to Customs of providing inspectors when needed. However, in recent years the cost of reimbursables has escalated well beyond what we envisioned, to the point where reimbursables have become a serious burden on the express industry. In fact, the industry has grown so much in the past 12 years that today collections under the MPF from this industry would more than cover the cost of providing inspectional services when needed to the express operators. We should note, by the way, that the express industry's principal competitor, the U.S. Postal Service, pays no reimbursables. Rather, U.S. Customs pays the Postal Service for the privilege of being on-site at its international mail clearing facilities.

Recently, Customs has expanded even further the scope of services for which it is billing the express industry. For example, the express industry fought for several years for a technical correction to the law that would permit Customs to provide additional inspection personnel at our facilities during daytime hours in response to the industry's request, and that provision was finally enacted in 1996 as part of Public Law 104–295. Now, however, Customs has deliberately misinterpreted the provision as allowing it to bill for all daytime services, whether requested or not. Clearly, it was never the intention of the industry or of Congress in enacting this provision to provide a windfall to Customs to bill for services which it routinely provided free of charge in the past and which it continues to provide free of charge to all other members of the transportation industry. Furthermore, Customs has indicated to us that it plans to expand its billing for export-related services, even though there is no legal authority for it to do so.

Reimbursable charges cost the industry close to $20 million last year—and the bills are mounting rapidly. On top of that, the express industry generated almost $75 million in MPF in 1998. Since the MPF collected already exceeds the cost of services provided by Customs for express operations, the reimbursables system represents a hidden tax that is borne by the express industry and that is ultimately paid by U.S. importers.

It bears noting that, when we first agreed to pay reimbursables years ago, Customs considered express facilities to be a special service divorced from the mainstream of U.S. commerce and, to a great extent, that was true. Today, however, the express industry is an integral part of the U.S. economy and its demise, as noted in this statement, would harm a wide swath of U.S. commerce. In addition, the express industry has pioneered automation innovations for Customs that enable Customs to process express shipments far more efficiently than it can for any other mode of transportation, while retaining high rates of compliance.

We believe that a resolution to this issue will require legislative action, and ACCA expects to be approaching members of the Finance Committee soon to discuss ways to redress this situation.

STATEMENT OF THE AIR TRANSPORT ASSOCIATION OF AMERICA

[SUBMITTED BY CAROL B. HALLETT, PRESIDENT AND CHIEF EXECUTIVE OFFICER]

Mr. Chairman and Members of the Committee, I appreciate the opportunity to offer written testimony on behalf of the Air Transport Association (ATA) concerning the Administration's proposal to increase the U.S. Customs Service User Fee and to create a new user fee for the use of Customs automated systems.

ATA represents the major U.S. passenger and cargo air carriers in the United States. Our members transport approximately 95 percent of the passengers and goods transported by air on U.S. flag airlines. Last year, the U.S. airline industry safely and successfully carried over 600 million passengers. The Federal Aviation Administration (FAA) predicts that that number will reach one billion passengers by 2010.

ADMINISTRATION PROPOSAL

I would like to address the Administration's proposal to increase the Customs User Fee and to create a new user fee for the use of Customs automated systems.

In August, 1997, at a meeting between U.S. Customs Service staff, House Trade Subcommittee staff, and ATA, Customs stated that the true cost of preclearing an airline passenger was approximately $3.25. Earlier this year, Assistant Secretary Lubick testified that the cost was over $5.00, implying adequate justification for the Administration's request to increase the fee to $6.40 per passenger. Mr. Chairman, doesn't it strike you as odd that in 18 months new found costs have almost doubled Customs' cost per passenger? With inflation so low, how could government be so inefficient as to result in its costs rising so much in excess of the CPI. In all candor,

we think you should be particularly suspicious of the basis for these new found costs.

We doubt there is adequate justification for these proposed "user fee" increases. They are tax increases masquerading as user fees. As you know, airlines and the traveling public already pay more than their fair share in taxes and fees.

In 1998, 54 million international passengers paid the Customs user fees. FAA predicts that this number will likely double by 2010. With these dramatic increases in international air travel, revenues from the Customs user fee, and other taxes and fees will grow substantially. The question is, can Customs or Treasury efficiently use these fees at the rate they are currently collected, or, is the proposed fee increase just a tax increase?

PURPOSE OF THE USER FEE

Mr. Chairman, the collection of the Customs user fee on every international air passenger ticket has helped the Customs Service to make improvements in passenger processing over the years. However there are many restrictions on the use of the funds which need to be addressed. We suggest the establishment of a government/industry oversight committee, to assess the uses of these monies and to make recommendations for improvements. Through a useful government/industry dialogue, real gains can be made in Customs processing.

Additionally, the COBRA fee, which funds a baseline of Customs airport staffing, is highly restricted in its use. We would propose and strongly support the removal of some restrictions, however, the fees generated should continue to be segregated from the general fund and reserved specifically for air and sea passenger-related Customs inspection activity. The removal of restrictions on spending for staffing will allow Customs the flexibility it needs to respond to transportation industry needs, trends, growth, and changes. The use of these funds should be clearly limited to activities that benefit the overall provider of the funds—air and sea passengers. Therefore, unrelated activities or operations without a nexus to air and sea passenger inspection, should not have access to the funds.

ADMINISTRATION'S NAFTA TAX

The Administration has proposed once again to remove the existing exemptions from the Customs user fee for passengers originating in Canada, Mexico, and the Caribbean. This exemption exists to promote good will between North American nations and we appreciate Congress' recognition of their special status within North America. But to extend benefits through NAFTA, on the one hand, and then take them away, on the other, suggests that this proposal is just a NAFTA tax.

Just as with NAFTA, Open Skies agreements dismantle barriers with countries like Canada to facilitate the flow of people across our shared borders. The adjacent islands of the Caribbean also deserve an exemption because of their unique status within the Americas. Preclearance operations utilize the highest levels of Customs processing efficiencies without sacrificing our national commitment to law enforcement. Imposing the Customs user fee on these passengers does not advance these efforts.

Lastly, Customs user fees collected from air passengers are being used for non-air passenger processing, such as land border overtime. These revenues are not used exclusively for the benefit of the persons paying the fee. Thus, industry participation through a user fee advisory committee would enhance the appropriate and efficient use of these resources.

CUSTOMS AUTOMATION ENHANCEMENT FEE

We want to commend the on-going efforts of Customs to bring its procedures and processes into the 21st Century. International cargo and passengers encounter border crossings at air and sea ports, as well as land locations; all of which have one thing in common—a crossing of national boundaries.

The result of crossing that imaginary line, specifically for air cargo, is an off-the-chart spike in increased transportation time, costs, and communication requirements. In like manner, the number of participants involved in the transaction increases significantly, creating the need to coordinate activities with numerous transportation partners and government agencies at both origin and destination with similar, if not identical, information.

Unfortunately, after thorough review and consultation with our member airlines, we cannot support the Administration's proposal to introduce an automation enhancement fee for the Customs automated systems. Notwithstanding our opposition to the fee, we want to remain actively engaged with the Administration and Con-

gress in identifying the right mechanisms to develop our common goals to improve the information processing system.

It is important to recognize that there are other influences that inhibit further engagement by air carriers in Customs automation development, specifically the Automated Commercial Environment (ACE). It is our view that Customs' current Automated Commercial System (ACS) and the current path of ACE produces a magnification of existing problems inherited from a manual document process. Converting a document into an electronic data format does not take full advantage of automation and information technology development. No less can be said of the recent Automated Export System (AES) implementation; the system attempts to automate a flawed export document process. As a result, a multitude of problems has surfaced for Customs and the trade community.

Furthermore, several problems intrinsic in the Automated Manifest System (AMS-Air) for imports have been carried over to AES. For example, the attempt to reconcile trade data with transportation data in AMS-Air has been consistently difficult, thereby increasing processing costs and delaying cargo movement. It remains an elusive goal after more than nine years of operation.

Having said that, we have several areas of concern related to ACE and AES development that are made worse by continuing frustrations with Customs' current import system, AMS-Air. While we want to develop a fully paperless automated manifest process, industry-wide participation in ACE may be seriously delayed due to a number of contributing factors.

Customs' support for AMS-Air has become a very important issue for our members. We have invested millions of dollars in AMS-Air and incur significant daily operational costs. Customs' attempt to introduce a new automated system at this time is very disturbing, more so since Customs has not yet delivered a high quality, cost saving automation program for imports. Quite logically, we fear another wave of start-up investment for ACE and AES, all the while still bearing the costs of an incomplete AMS-Air.

AMS-Air is in its ninth year of operation with a steady growth to over 130 participants and 28 ports nationwide. However, serious flaws remain, some since the October 1989 start-up date. For example:

After nine years of operation, paperless processing is available at only one of 28 ports nationwide;

Only five freight forwarders nationwide participate in AMS-Air and at only three ports;

AMS-Air is not fully endorsed by local Customs and USDA personnel. In fact, USDA refuses to participate at some ports, thereby preventing a truly paperless environment;

Split manifest processing, a common event in air cargo, is bug ridden; and

Programming enhancements and system corrections vital to air carrier operation and freight forwarder participation, such as Project 323 (in-bond enhancements) and others, are over seven years behind schedule.

Again, we want to be clear—the ACS legacy systems are in the twilight of life expectancy, the export process is paper intensive, and it is in dire need of automation. However, the foundation of automation cannot be built on the premise that automating the existing manual process will address our mutual concerns. The ideal system fully re-engineers the flow of data to minimize the cost to the trade and government while maximizing information for compliance, quality of statistics, and information enforcement.

Nonetheless, the cornerstone of Customs' effort to maintain pace with the growth of international trade is eroded by the exceedingly long time it is taking to deliver on the promise of the Modernization Act. In fact, it is acknowledged by many in the trade that the Mod Act needs to be rewritten and ACE redesigned.

Our concern is not that Customs is an unwilling partner in automation development, but is on a collision course with information technology development and its effect on trade practices. We believe that it is imperative that Customs become a part of the transportation process rather than creating a detour for international shipments caused by manifest and commodity data requirements of a closed proprietary system. The flow of legitimate goods is enhanced if Customs becomes a part of the transaction rather than attempting to manage it. The blueprint of future trade practices is based on electronic commerce and the Internet; however, the ACE foundation to date has very little in common.

While we agree that current ACS programs need upgrading and eventual replacement, the Administration's proposal for an automation fee, is unwarranted and unacceptable, as traditional budget request procedures have not been followed. It is nothing more than a tax on top of the $800 million paid annually in Merchandise

Processing Fees (MPF), a portion of which should be used to enhance and maintain Customs automation programs.

Mr. Chairman, until Customs breaks-out development costs by trade functionality and internal Customs requirement, it is unclear what the industry is paying for. Moreover, the development costs have skyrocketed from an initial estimate of $600 million to $1.48 billion without a detailed explanation from Customs.

These investments obviously require careful planning in the context of industry/government partnership and return on investment. With numerous outstanding questions and issues, and the lack of detail on how a user fee would be implemented, it is impossible for our air cargo carriers to agree to an automation enhancement user fee.

Once again, thank you for the opportunity to make our views known. Please let me know if you need any additional information or would like to discuss these issues in detail.

STATEMENT OF THE AMERICAN ELECTRONICS ASSOCIATION

The American Electronics Association (AEA) expresses its appreciation to Chairman Roth, Senator Moynihan and the entire Finance Committee for the opportunity to present our concerns regarding the immensely important topic of the functioning of the U.S. Customs Service. The AEA's 3,200 members represent all sectors of the U.S. high tech industry, the leading sector of the U.S. economy in international trade. As such, the operations of the U.S. Customs Service are of immense importance to us.

Our comments will focus on four areas of concern for us including:

1. Compliance cost burden;
2. Compliance measurement;
3. Audits; and
4. Reasonable Care standard.

AEA CONCERNS WITH THE OPERATIONS OF THE U.S. CUSTOMS SERVICE

1. Compliance cost burden

The U.S. Customs Service has a number of compliance reporting and other requirements that place a heavy cost burden on U.S. firms. These compliance (non tariff) cost burdens seriously undermine the policy of encouraging free trade by reducing tariffs generally (WTO) and reducing tariffs specifically of information technology goods under the Information Technology Agreement (ITA). There is a burdensome disproportionality which must be addressed. Some of these problems require statutory amendment, other derive from Customs interpretation.

Examples of these burdens include:

a. Drawback regulations are complex and difficult to apply. Recordkeeping and automated systems requirements involve significant effort and are frequently inconsistent with normal business accounting procedures. Customs has publicly acknowledged that a very high percent of potential drawback is not claimed. This is largely because the compliance burdens outweigh the cost recoveries available to importers, hence, the choice is often not to participate.

b. Furthermore, many duty preference programs also are not fully utilized because the compliance burdens outweigh the cost recoveries available to importers. For instance, the annual NAFTA eligibility renewal for bulk Exporter Certificates of Origin should be extended from the current 1 year to a 2 year requirement, which would better allow us to focus on expanding eligibility for the NAFTA region companies, rather than recertifying the old.

c. Importers are required to commit significant resources to meet Customs current interpretation of the reasonable care standard. Compliance obligations are often not commensurate with the declining MFN tariff rate revenue generated for the US Government.

d. Customs is shifting its workload to importers. Importers are asked to generate reports, maintain records, and establish accounting systems, which are not appropriate for commercial business operations. Customs does not appreciate the limited resources available to importers to accommodate these requests

1. For example, the Importer Compliance Monitoring Program (ICMP) prototype asks importers to conduct their own internal audits in accordance with standard government accounting requirements. The self-assessment requirements, including the requirement for statistically valid transaction samples, involve a significant commitment of resources from the importer, yet the promised benefits for the importer are tenuous at best.

2. The "certified recordkeeping agent" program does not eliminate any recordkeeping burdens for the importer. The importer is still legally required to produce copies of all records. To relieve this redundant burden, Customs should make the filer responsible for the entry records they have submitted to Customs. This will relieve the importer from the burden of maintaining the same set of documentation that is kept by their broker (for importers that use brokers)

There is not enough benefits to the trade in the recordkeeping certification program. The program only allows one error. After one recordkeeping error, the importer is subject to the same recordkeeping penalties as the rest of the trade even though Customs has certified their recordkeeping processes and procedures. Customs should exempt participants from all penalties.

2. Compliance measurement

While we understand Compliance Measurement exams were instituted in response to the General Accounting Office's assertion that Customs lacked data regarding import compliance, we believe that data gathered and reported from today's CM exams does not result in a valid compliance picture. It is time that Customs reviewed this program, including feedback from importers, so that changes can be made to produce information that the Government and importing community can confidently act upon to improve compliance.

Of particular concern are the following points:

a. There are too many different mathematical tools being used by Customs to measure importer compliance. Notwithstanding many explanations offered by Customs, there is considerable confusion as to (i) how compliance rates are calculated, (ii) how the different calculations are used and (iii) how each measurement affects the importers and their cargo exam rates. Some Rulemaking on the methods, or at least GAO statistical guidance in population definition, sampling, and interpretation of results would be useful.

b. Customs compliance measurement tools don't account for Customs errors. Particularly in the area of HTS classification, local Customs officials are often no better equipped than sophisticated importers to make correct classification decisions. The findings are not made available to importers on a timely basis or ever; when they are made available, importers can readily identify numerous Customs errors. Even when Customs acknowledges the errors, procedures don't allow for timely correction of the importer compliance rates. The importers compliance rate is extracted and calculated based on the sample for the entire industry. This does not paint an accurate picture of the importers compliance rate.

c. Customs' compliance measurement often measures broker and courier errors, rather than importer errors. Importers and consignees, even when diligent in managing the broker/courier process, have limited opportunity to correct these errors. If Customs is serious about increasing the compliance rate, Customs must focus directly on the brokers and couriers, not just the importers and consignees. These errors often account for a majority of an importer/consignee's measured errors.

d. Customs counts as "errors" discrepancies in the initial cargo release documents despite importer correction (using reasonable care) prior to completion of the entry. Importer correction of Automated Manifest System data (manifest errors) results in "discrepancies" against the importer rather than forwarder/carrier. These instances confirm reasonable care has been employed by importers in a systematic way, yet overstates importer non-compliance in CM.

e. Companies have to build in additional transit time to account for compliance exams based on this inaccurate importer CM data. This affects our entire supply chain strategy.

3. Audits

AEA members have been among the early participants in the Compliance Assessment process. Originally intended we believe as "compliance system surveys" they are full depth and breadth transaction audits , extremely costly and burdensome, even for compliant importers.

a. Compliance Assessment audits are time-consuming and intrusive. Even a compliant company is disrupted from its normal business routines when audits extend for long periods. It is not unusual for a Compliance Assessment Team (CAT) audit to take more than two years.

b. Extremely complex requirements make errors an expected event, even for compliant importers exercising reasonable care , forcing an enlargement of the sample or audit. In other cases, when Customs finds no errors in statistical CA samples, more sampling was required to "find errors" because the error free CA statistical sample must have been "too small". The results are the same however, the audit will expand.

c. The statistical model used is based on a confidence interval technique with a Mean Average and upper and lower boundaries. In practice, the CA confidence interval is only applied in a negative manner, i.e. only the lower end of the confidence range is used by the CAT or communicated to the importer. The effect is a one sided understanding of the results, unfavorable to the importer (the upper limit is equally probable) , and requiring potentially unnecessary corrective actions. The CA results analyses are in contrast to the more objectively presented confidence interval reports for CM results submitted to Congress, which notably contain the Statistical Mean, and upper and lower boundaries of the confidence interval.

We think the current one-sided CA technique could benefit from GAO statistical guidance, and public input through rulemaking.

d. The current regulatory scheme allows importers to voluntary disclose errors and tender additional duties. These disclosures often trigger disclosure verification audits. Importers should be encouraged to make disclosures; this should not result in additional audit scrutiny merely because of self audit voluntary disclosures.

e. Headquarters policy guidance is often inappropriately applied by field auditors. There are communication disconnects which result in local implementation without adequate guidance at the national level. This creates in lack of uniformity and less than optimal auditing practices.

4. Reasonable care standard

"Reasonable care" does not impose strict liability on importers, nor does it reduce any of the responsibilities of the Customs Service.

a. As part of the exercise of "reasonable care," importers seek guidance from Customs as to proper classification of goods. Importers do not receive timely, consistent advice, which may be relied on. Rulings are often inconsistent with other rulings, or limited in scope to the specific goods at issue in the request. Importers may wait as long as two years for formal guidance, which is unacceptable in the fast moving electronics sector.

b. As implemented, the standard for measuring "reasonable care" seems to be changing. Identification of an error often leads to the conclusion that the importer must not have exercised "reasonable care;" otherwise, the error would not have occurred. There is no clear guidance as to what distinguishes a systemic versus non-systematic error.

c. The trade continues to operate in an environment of entry by entry processing. This transactional approach increases processing costs for everyone including the Government.

We believe it is time for statutory authority for "Periodic Entry," including provisions for aggregate accounting rather than transaction based accounting which is all but irrelevant, and inconsistent with other Government programs such as IRS, or even relevant antidumping procedures.

CONCLUSION

The AEA Customs Committee recognizes that the Mod Act offers opportunities for improving import processes. Some of the improvements we seek can be implemented in the existing legal framework, while others may require legislative action. We will continue to work with the Customs Service to improve compliance as Customs works with the import community to reduce compliance burdens and facilitate trade.

STATEMENT OF THE AMERICAN IRON AND STEEL INSTITUTE (AISI)

The American Iron and Steel Institute (AISI) submits this testimony on behalf of its U.S. member companies who together account for approximately two-thirds of the raw steel produced annually in the United States.

AISI has maintained a strong working partnership with the U.S. Customs Service since the mid-1960s. AISI's Customs Liaison Subgroup is an especially active unit of our U.S. producers' Trade Committee. We meet regularly with headquarters and field personnel in Customs' Offices of Strategic Trade and Field Operations. We also conduct an ongoing series of seminars for Customs personnel to help officials of the U.S. Customs Service better understand how to properly identify and classify steel mill products. In addition, we provide a network of technical and commercial experts to help answer questions from Customs on an as-needed basis. As a result of these activities, AISI has a thorough understanding of Customs' responsibilities and capabilities in the enforcement, classification, processing and facilitation of steel trade. In this regard, we offer the following comments on budget-related Customs issues for FY 2000 and 2001.

AUTOMATED COMMERCIAL ENVIRONMENT (ACE) MODERNIZATION AT CUSTOMS

There is an urgent need to fund and implement Customs' computer and software capabilities, through the proposed new ACE system, now. The weaknesses and inadequacies of the current Automated Commercial System (ACS) have been well documented. Virtually everyone agrees that the ACS is headed toward near-term failure, possibly within a year or less. AISI therefore strongly supports the immediate and rapid funding and development of a comprehensive, flexible and durable ACE, through the general appropriations process. At the same time, we remain opposed to the enactment of various special fees as a means of funding ACE.

Failure to develop and implement ACE in a timely manner could invite a trade disaster for the United States. Failure of the ACS would probably not cause U.S. imports to slow. Rather, the most likely result of any massive failure of Customs' current computer capability would be to prompt political pressure from importers that could instead result in a relaxation of Customs' vigilance, thus opening the floodgates to imports without any ability to allow proper enforcement to ensure that these imports comply fully with United States' and Customs' rules, regulations and laws.

It is not in the interest of the U.S. economy or U.S. industry to allow the ACS to fail, because the resulting flood of imports would almost certainly include a significant amount of unfairly traded and even fraudulent product that would cause substantial harm to U.S. producer and consumer interests alike. Moreover, any benefit to U.S. importers from such a breakdown in Customs' computer capability would be short-lived, while the injury to competing manufacturers in the United States would be long term.

STEEL IMPORT MONITORING AND NOTIFICATION SYSTEM

Calendar years 1997 and 1998 were the two highest steel import years on record but, in 1998, the United States imported a record 41.5 million net tons (NT), exceeding the previous record tonnage of 1997 by over 10 million NT—or 33 percent. What occurred in the U.S. steel market in 1998 was a supply-driven crisis caused by unprecedented levels of unfairly traded imports. In 1998, the U.S. steel trade deficit was a whopping $11.7 billion—or nearly 7 percent of the total record U.S. trade deficit last year. In 1998, the 8 months April-November were the 8 highest individual monthly totals for steel imports in U.S. history . With our docks and warehouses full to the brim with imports and with U.S. steel inventories at all-time levels, this record surge of steel imports was a cause of serious injury to U.S. steel companies and employees, including layoffs, short work weeks, severe price depression, production cuts and lost orders.

Unfortunately, America's steel trade crisis continues. We believe it's important to put the numbers into proper context. What we've seen are just a couple of months of lower imports overall since November and a modest, halting improvement in market conditions in some steel product lines. The fact is, over three quarters of the reduction in total steel imports since November 1998 has been due to the hot rolled cases filed against 3 countries. Meanwhile, both import and domestic prices remain very depressed. In fact, average import values remain well below the average costs of highly efficient U.S. producers. Unfortunately, in spite of continued record steel demand in the United States.

- only one-fifth of the 10,000 adversely affected U.S. steelworkers have been recalled;
- most U.S. steel companies reported either losses or sharply reduced profits in the first quarter of 1999 compared to the first quarter of last year—the average steelmaker posted a year-over-year decline in earnings in excess of 100 percent;
- U.S. steel shipments declined almost 12 percent in the first quarter of 1999;
- U.S. steel capacity utilization in the first quarter remained under 80 percent; and
- finished steel average unit values in April 1999 were still 15 percent, or $72 per ton, below the values in the first quarter of 1998 when the import surge was just beginning.

Accordingly, it is premature to claim that this crisis is over. It is not over because.

1. the fundamentals that gave rise to the steel crisis have not changed, including world oversupply, closed markets, dumping and depressed foreign economies;
2. steel inventories in the United States remain excessive;
3. the large, open U.S. market continues to be especially vulnerable;
4. America's steel companies and employees continue to suffer injury;
5. they have yet to recover from the serious injury caused by record imports in 1998;

6. imports of products that are temporarily down are down because of trade cases;
7. unfair import prices remain at injurious levels;
8. there is significant import source and product switching;
9. imports of other products not subject to investigation are increasing, and
10. imports overall, at an annual rate thus far in 1999 of 31 million NT, are still very high, while imports from many countries remain at historically high levels.

In sum, the declining total import volume since November 1998 does not mean an end to America's steel trade crisis. First and foremost, there is the problem of continued severely depressed steel import values and the serious injury to U.S. steel companies and employees from dumped and subsidized imports. Once again, it is important to put this issue into perspective. When the press reports that U.S. steel prices in some product lines declined in 1998 by as much as $100-150/ton, and that a "rebound" could now be underway because some steel prices in 1999 are up by, say, $20/ton, this is not a definition for recovery. On the contrary, what it shows is that (1) pervasive unfair trade in the U.S. market is continuing and (2) this unfair trade has long-standing, injurious effects.

At the same time, there is also growing evidence of import source and product switching, and imports of many products from many countries continue to increase. For example:

- imports of hot rolled flat products have risen from China, Indonesia and other countries not covered by unfair trade cases-, imports of cold rolled sheet from Brazil have increased sharply after cases were filed against hot rolled sheet in September 1998;
- imports of hot-dipped galvanized steel products have jumped in recent months,
- imports of rail steel products have increased significantly since November 1998; and
- imports of tin mill products have also surged since the end of 1998.

It is therefore clear that (1) America's steel import problem is not limited to a single product or 2 or 3 offshore suppliers and (2) there must be more forceful action to address the ongoing steel trade crisis in the United States.

On behalf of our U.S. member companies, AISI supports a prompt, effective, comprehensive solution to the steel trade crisis in the United States. As a part of any such solution, it is imperative that the United States government and U.S. steel industry have access to the most up-to-date information possible on potentially disruptive and unfairly traded steel imports. Therefore, AISI continues to support strongly legislation to develop and implement a U.S. steel import monitoring and notification system capable of providing as near as possible "real-time" data on steel imports.

An effective steel import monitoring and notification system would require that an electronic notice of importation accompany each import entry. Steel import notices would be accumulated, updated and published weekly in summary form on an Internet web site. Such data would provide the information needed for the U.S. government and steel industry to assess the steel import situation in near-realtime. This would enable U.S. policy makers to anticipate trade problems before they become crises and enable U.S. steel producers to respond as early as possible to potential disruptive and unfair trade.

America's MAFIA partners Canada and Mexico already employ steel import monitoring and notification programs that provide, as close as possible, real-time data. The U.S. system that is being proposed would be modeled on the Canadian system. In Canada, the steel import monitoring and permit system is administered outside of Customs, and does not appear to present a burden to Canada's Customs Service. Canadian Customs does, however, have a modern automated computer system in place. We therefore recommend including a steel import monitoring and notification program in the development of ACE, to ensure both compatibility and efficiency.

Most importantly, the proposed U.S. steel import monitoring and notification system would not constitute a nontariff barrier to trade. Under the automatic notification system that is being proposed, (1) steel import notice applications could not be refused, (2) any nominal fee would not be an economic burden and (3) import entries would not be delayed. Again, Canada presents a good example. In Canada, record steel imports occurred in 1998 in spite of that country's steel import monitoring and permit program.

AISI is aware that it will take time and money to develop and implement an automated system such as the one that exists in Canada. We also recognize there are concerns that Customs, at present, might not be equipped to handle a computerized steel import monitoring and notification system. AISI would like to work with both Congress and Customs to ensure that such a system does not pose either a budgetary or a human resource burden on the U.S. Customs Service. It is important to

AISI and our U.S. members that Customs resources not be diverted from current enforcement efforts. As in Canada, believe that a small fee for each steel import notice application could substantially fund a similar system in the United States. If, however, the nominal fee imposed on steel import notice applications were to prove inadequate to cover all necessary resources to implement and maintain this program, both within and outside of Customs, we would support additional funding through general appropriations.

The U.S. members of the American Iron and Steel Institute are grateful for this opportunity to express our views on budget authorizations for the U.S. Customs Service and other customs issues.

STATEMENT OF ANDREW M. CAPLAN

I submit the following statement to the Committee based on my concerns, as both an attorney and an American citizen, that the U.S. Customs Service is exercising its statutory authority in a manner which is resulting in the abuse of innocent Americans, and in conduct by individual Customs officers that is marked by racist, anti-Semitic, and other forms of discrimination inconsistent with our Constitution and its command that all persons be accorded equal protection of law.

The first part of this statement recounts an incident to which I was recently a party upon my return to the United States from a trip overseas. The second part examines the relevant Constitutional background to Customs' search and seizure authority and discusses the inconsistency between current Customs' practices and the Constitutional guarantee of equal protection of law. Finally, the third part of this statement draws on my experience as a former military attorney in the U.S. Armed Forces to suggest a potential legislative amendment to Customs' existing statutory authority which, in my view, should correct the current deficiencies in the agency's practices.

During the last two week of October 1998, I visited Sweden, Norway, and the Netherlands. I returned to the United States on October 30, 1998 via Amsterdam, the Netherlands, arriving at the Detroit Metro-Wayne County Airport on Northwest flight 8617 (which is a code-share flight operated by KLM Airlines). My ticket for this flight was purchased with a major credit card, through a travel agent, as part of a travel package (including air tickets and hotel accommodations) sponsored by Northwest World Vacations.

Upon exiting the aircraft, I proceeded through the jetway connecting the airplane with the gate area. While in the jetway, I observed what I recognized to be a drug detection dog. I proceeded past the dog without incident. However, while still in the jetway, I observed the same dog approach a woman standing near me and, in a spirited and zealous fashion, lunge at the individual, requiring a uniformed officer to, in effect, remove the dog from the person. The actions of the dog in relation to the individual were entirely unique and distinct from the dog's actions in relation to all the other passengers in the jetway and, in my view, constituted a possible "alert" on the individual. The individual in question was a pale-complexioned Caucasian woman with light blonde hair who appeared to be approximately 30 years of age.

After clearing the Immigration/Passport Control area and retrieving my checked baggage, I proceeded to the Customs checkpoint area and was approached by a uniformed Customs officer . I was wearing black, wing-tip shoes, charcoal grey wool slacks with cuffs, a black turtleneck shirt, a grey wool sportscoat, and a tan London Fog trench coat. (Due to the fact that northern Europe can be quite cold by the end of October, virtually all of the arriving passengers were wearing bulky outer garments of one sort or another.) My hair was roughly the same length as when I was on active duty as a naval officer, and I was not wearing any facial hair. I was 36 years of age at the time.

The Customs officer asked to see my passport and Customs declaration form. She asked where I had traveled and what was the purpose of my trip. She asked what I do for a living and who is my employer, to which I responded that I am an attorney and work for a federal agency, and I specified the agency. She then asked who was my prior employer, to which I responded that I had previously worked for a different federal agency, and specified the agency. She then asked, again, what type of work I do, and I, again, stated that I am an attorney and work in the General Counsel's office of my agency.

(The views expressed in this statement are strictly my own as a private citizen and are not intended to represent the views or policies of my current agency or former agency. For this reason, I have omitted the names of my current and former agency. I will be happy to supply this information to the Committee upon request.)

Without explanation, I was ordered by the officer to follow her, in full glare of the other passengers (who appeared to be proceeding through the Customs area without any questioning or search at all) to a different room where I was ordered to place my luggage, a 26-inch upright, "pullman" style American Tourister suitcase, as well as a matching carry-on case, onto a large metal examining table.

The space constraints of this statement prevent me from chronicling the full extent of the abusive treatment to which I was then subjected. In all, I was held in custody for almost an hour. During that time, the officer laboriously searched my luggage, going so far as to X-ray a double-sealed bottle of Scotch I had purchased as a gift for my father at the duty-free shop in Amsterdam. This search entailed the Customs officer carefully scrutinizing virtually all of my possessions, including clothing, shoes, toiletries, medicines, vitamins, a book, magazines, a camera—even children's T-shirts I was bringing as gifts for my nieces and nephew.

In addition, I was subjected to what I can only describe as a humiliating interrogation in which I was ordered to chronicle virtually every detail of my vacation. In addition, I was ordered to produce for inspection all my hotel receipts, my airline ticket receipt, and was ordered to recite for the officer the name and address of the travel agent who had booked the vacation. Moreover, the officer inquired whether I had ever been searched before on my prior trips abroad; when I responded that I had not, the officer exhibited an expression of dismay and ordered me to specify what airports I had traveled through in the past. When I responded that my prior trips overseas had been through JFK airport in New York, the officer responded, "Are you sure you've never been searched before?"—to which I responded that I had not been searched before, to which she yet again asked, "Are you sure?"—to which, yet again, I responded that I had not been searched before.

After completing the search of my carry-on bag and finding nothing suspicious, after nearly having completed the search of my checked suitcase and finding nothing suspicious, after conducting the aforementioned interrogation, and even after having been apprised that I was an attorney who worked for a federal agency, the Customs officer informed me in no uncertain terms that I was a suspected drug smuggler. (The officer stated, "Do you know what I'm looking for? Tell me what I'm looking for . . . . I'm looking for drugs. Am I gonna find drugs?")

Finally, I was ordered to produce a business card or some other form of professional identification. I provided the officer with my bar association identification card, which she carefully analyzed. The officer took the ID card and my passport to a telephone in another part of the room and conducted an extended telephone conversation while I remained in custody. After approximately 10–15 minutes, the officer returned, stated that I had been to a "source city," gave no other explanation for the treatment to which I had been subjected, told me I could leave and directed me toward the Northwest terminal. As I exited, I noted that all the other passengers were gone from the luggage arrival/Customs area, and that I had been held in custody for close to an hour. While I was held in custody, I noticed only one other person in the "secondary search area," a bearded, olive-complexioned man who appeared to be approximately 40 years of age. That individual was released after 5–10 minutes. I did not observe in the secondary search area the blonde-haired woman I had previously witnessed being lunged at by the drug detection dog.

The leading judicial decision addressing the Constitutional limitations on Customs' search and seizure authority is *United States* v. *Montoya de Hernandez,* 473 U.S. 531 (1985). That case involved an individual convicted of attempted smuggling of narcotics into the United States through the use of an alimentary canal "balloon" device. However, the case is instructive regarding border searches generally. The *Montoya* decision held that under the Fourth Amendment's search and seizure clause, "routine searches" of persons and effects at border entrances are not subject to any requirement of reasonable suspicion, probable cause, or warrant. However, the decision held that the detention of a traveler at a border beyond the scope of a "routine search" and inspection is justified only if the Customs officer reasonably suspects that the traveler is smuggling contraband. The Court defined "reasonable suspicion" as a "particularized and objective basis for suspecting the particular person" of smuggling. Thus, the Court made clear in *Montoya* that for any search beyond that of a "routine" search, there must be reasonable suspicion—an objective standard requiring particularized, articulable facts; the officer's subjective impressions, or "gut feelings," are insufficient to justify any search beyond that which is "routine."

The majority opinion in *Montoya* did not define the phrase "routine search." Justice Brennan's opinion, while dissenting with respect to other issues in the case, was in concurrence, in effect, with respect to the majority's view that no reasonable suspicion (or greater standard) is required to conduct "routine" searches at international borders. His opinion indicated that routine searches are "typically con-

ducted on *all* incoming travelers" (emphasis added). Moreover, the opinion indicates that reasonable suspicion is required for individual travelers to be "singled out" for further investigation.

In the case of *United States* v. *Martinez-Fuerte,* 428 U.S. 543 (1976), the Court discussed the phrase "routine search" in the context of vehicle searches for illegal aliens near the Mexican border. There, the Court noted that the Fourth Amendment's limitation on search and seizure power is intended to prevent "arbitrary and oppressive" police tactics. The Court upheld the validity of checkpoint vehicle searches based on a "routine search" rationale. In its decision, however, the Court placed great emphasis on the fact that the checkpoint searches were non-discretionary (i.e., *all* vehicles passing through the checkpoint were included) and that all the searches (including those involving secondary search procedures) were extremely brief in nature. The Court noted that another type of vehicle search for illegal aliens, known as "roving-patrols," which, unlike the checkpoint searches, are discretionary in nature, can only be undertaken when the stopping officer is aware of specific, articulable facts, when taken with rational inferences, would reasonably warrant suspicion that the vehicle contained illegal aliens.

Thus, the Court's decisions make clear that a routine border search is characterized by two primary elements: (1) it must be brief in nature; and (2) it must be non-discretionary, i.e., it must be based on procedures to which all similarly-situated persons are subjected (be they all passengers disembarking from an airplane, or all motorists passing the same checkpoint along a highway). Any search that does not meet the definition of a routine search may only be conducted based on reasonable suspicion-a standard requiring that there be objective, articulable facts suggesting the individual may be in violation of law.

Montoya de Hernandez was a Fourth Amendment search and seizure case. The essence of such a case is evidentiary in nature—that is, the court is exploring whether, under the Exclusionary Rule, evidence must be suppressed because law enforcement officials violated the Fourth Amendment's requirement that searches and seizures be conducted in a reasonable manner. A ruling that a particular police practice does not offend the Fourth Amendment means only that, within the context of a criminal proceeding, the government will be permitted to introduce the seized evidence and use it against the accused. The ruling does not necessarily imply that a particular police practice is otherwise legal when viewed in the context of other Constitutional requirements, outside the limited issue of what is admissible in a criminal proceeding. In other words, the fact that a government agency is in compliance with one provision of the Constitution does not give the agency license to violate other provisions of the Constitution.

It is well settled that the Fifth Amendment requires the federal government to accord equal protection of law to all citizens. (As it is frequently conceptualized, the Due Process clause of the Fifth Amendment "incorporates" the equal protection doctrine of the 14th Amendment applicable to the states). Likewise, it is well settled that discriminatory practices based on racial criteria are subject to the most rigid scrutiny and are only allowed when there is a compelling governmental interest and the discriminatory practice is necessary to the accomplishment of a legitimate purpose rationally related to that compelling interest. In addition, the Court has held that while the burden is on the individual alleging unlawful discrimination to demonstrate that the governmental action had a racially discriminatory purpose, such may be demonstrated by showing that the totality of the relevant facts gives rise to an inference of purposeful discrimination, and that under some circumstances, unlawful discrimination may be demonstrated where the discrimination is very difficult to explain on non-racial grounds. In this regard, an individual need not show that other members of the same racial group were similarly treated; a single discriminatory governmental act violates the Constitutional requirement of equal protection. Moreover, once an individual has made the requisite showing of racial discrimination, the burden shifts to the government agency to profer a race-neutral explanation for the complained of actions; general assertions that its officials did not discriminate or that they properly performed their official duties do not satisfy the agency's burden. See *Batson* v. *Kentucky,* 476 U.S. 79 (1986).

In short, the Customs Service, as a federal agency, is required to comply with both the Fourth Amendment and the Fifth Amendment; it may not subject members of the public to unreasonable searches or to treatment that is arbitrary and oppressive and, at the same time, it may not engage in racially discriminatory practices. While the Court in *Montoya* indicated that Customs could perform routine searches without any reasonable suspicion or probable cause, nothing in the Court's decision indicated, either expressly or by implication, that Customs could exercise this authority in a racially discriminatory manner, that the Custom Service, alone among federal agencies, is excused from the Fifth Amendment's requirement of equal pro-

tection, or that individual Customs officers are at liberty to perpetrate racist, anti-Semitic, or other unlawful discrimination.

Following the incident described above concerning my return to the United States from an overseas trip, I reported the incident to the Customs Service, asked for an investigation into the matter, and posed a number of questions with respect to the agency's interpretation of its legal authority, as well as questions concerning the legal obligations of arriving passengers. Among other points of inquiry, I asked whether the Customs Service had determined that federal law permits Customs officers to subject persons entering the country at international airports to discriminatory treatment on account of such person's race, religion, ethnicity, or national origin. Although most people would assume that in the United States, the answer to such a question would be self-evident, the response I received suggests that the Customs Service, as a matter of law, does not consider itself constrained by the Constitutional guarantee of equal protection.

My inquiry was addressed to the Chief Counsel of the Customs Service, who responded, through the Associate Chief Counsel for Enforcement, Steven L. Basha, that his "office does not provide legal opinions to the public." This response is interesting in itself, since legal offices in federal agencies, in fact, routinely provide advisory and interpretative legal opinions to members of the public concerning matters that are under the purview of their agency. Mr. Basha indicated that my inquiries were being forwarded to the office of the Assistant Commissioner for Field Operations, which would respond to me directly. With respect to my inquiries, he indicated only that searches "based upon race or ethnicity are not permitted by Customs *policy*" (emphasis added). Nowhere in the letter did Mr. Basha indicate that such discrimination is against the law, only that it violates Customs "policy."

Several months after sending the agency my inquiry, I received a response from John B. McGowan, Director, Passenger Operations, Office of Field Operations. Of the eight questions I posed in my correspondence, Mr. McGowan's letter was responsive to only one, that is, whether racial/ethnic discrimination is permitted by Customs policy. To this, Mr. McGowan indicated only that a "person's race and ethnic background are not part of the decision process." Again, nothing in the letter states that the Customs Service considers racial/ethnic discrimination to be illegal—only that it violates the agency's "policy."

It is disturbing, to say the least, that in the year 1999, decades after most Americans had assumed it was a long settled matter that it is illegal for employees of a government agency to engage in racial and ethnic discrimination, that two senior officials of a federal agency, when given the opportunity to do so, specifically decline to state that it is a violation of law for employees of their agency to perpetrate such discrimination.

With respect to explaining why I, alone among 400 some-odd passengers on the flight, was held prisoner for almost an hour, subjected to abusive treatment, and informed by a Customs officer in no uncertain terms that I was a suspected drug smuggler, Mr. McGowan offered only that I was selected based "on the fact that [I was] arriving from a source city, Amsterdam." The statement is fascinating more for what is does not say than for what it does say. It does not say I was selected for such treatment because I was arriving from a source city plus some other specified factor; or that I was selected for such treatment because I was arriving from a source city plus some other factor which they decline to specify for law enforcement reasons. Instead, it says only that I was selected for such treatment merely because I was arriving from a source city, period. The letter does not even pretend that there was anything to distinguish me from any other person who got off that airplane—other than my ethnic background.

As the Supreme Court has observed, discrimination may be demonstrated where the discrimination is very difficult to explain on other grounds. In this respect, Mr. McGowan's acknowledgment that the treatment to which I was subjected was based merely on a single factor which applied equally to every person on the plane (i.e., that I was arriving from a source city) constitutes an implicit acknowledgment of discrimination based on ethnicity. I wish this were not so, as I have managed to live for 37 years without ever making such an accusation against anyone, let alone a federal law enforcement officer. Indeed, I would have been vastly relieved if the Customs Service had proffered some explanation—any explanation—that would reasonably suggest that the treatment to which I was subjected was not based on my ethnic background. However, given a full and fair opportunity to do so, the agency has declined to even pretend that there was anything other than my ethnic background that distinguished me from the other passengers on that airplane.

I turn now to what may, perhaps, be the most distressing aspect of this entire affair. I am, of course, referring to the fact that while I—who proceeded past a drug detection dog without incident—was subjected to discriminatory and abusive treat-

ment, a pale-complexioned, "Aryan" person who had been lunged at by a drug detection dog was permitted to proceed through the Customs process without being subjected to even some, much less all, of the humiliating treatment to which I was subjected. Of all the facts of this case, this by itself would be more than adequate to establish not only a case of ethnic discrimination, but a particularly stark and disturbing example of such. (On this point, the response I received from Mr. McGowan stated that the canine enforcement officer in the jetway indicated nothing unusual and had made no record of an alert on a passenger. This statement merely underscores the self-evident proposition that persons engaged in improper conduct generally do not keep written records of such improper conduct, and that law enforcement officers who perpetrate racial, anti-Semitic, or other illegal discrimination are not likely to make an official report of that fact.)

Mr. McGowan's letter also stated that, "You underwent extensive questioning and review of travel and other documents in order to verify that you were law abiding." This statement, perhaps more than any other in the letter, summarizes the problem with the current practices of this agency, and highlights the racial and ethnic bigotry that is being perpetrated. I was required to verify that I was law abiding. White, Gentile persons—even those who are lunged at by drug detection dogs—are not required to verify they are law abiding; they are presumed to be law abiding. Blacks, Jews, Hispanics, and other minority members are accorded no such presumption; we are required to prove that we are worthy of being allowed to re-enter the country, where no such proof is required of White, Gentile persons.

In fact, the current practices of the Customs Service are in violation of both the Fourth and Fifth Amendments of the Constitution. In Montoya de Hernandez, the Supreme Court held that Customs may perform routine searches in the absence of any objective evidentiary standard (e.g., reasonable suspicion or probable cause). Montoya was decided at a time when the routine Customs practice was to engage in brief baggage searches of all returning passengers; indeed, Justice Brennan's opinion in Montoya emphasized that such searches are "typically conducted on *all* incoming travelers" (emphasis added); he went on to note that reasonable suspicion is required for individual travelers to be "singled out" for further investigation. In upholding the authority to engage in routine searches, the Court almost certainly had in mind the routine searches of the time—searches that were brief and non-discretionary—searches that all arriving passengers were required to undergo.

The current practices of the Customs Service are markedly inconsistent with this standard. According to the agency itself, fewer than two percent of airline passengers who pass through Customs are subjected to baggage search. On the flight on which I arrived, the percentage was even lower—just two persons out of approximately 400 on a nearly-full Boeing 747. Under the Court's rulings—indeed, under the very definition of the word—a search is not routine if only two percent of passengers are affected. Searches conducted without reasonable suspicion that involve only two percent of passengers are precisely the type of arbitrary police behavior that the Court has held to be in violation of the Fourth Amendment.

The fact that members of racial and ethnic minority groups are overwhelmingly the victims of such unlawful tactics attests to the fact that Customs—not content with merely violating one provision of the Bill of Rights—is engaged in widespread violation of yet a second Constitutional guarantee—that the government is required to accord all persons equal protection of law. Instead, the Customs Service is permitting its officers to subject citizens of this country to discriminatory treatment based on racist, anti-Semitic, and other forms of bigotry—discriminatory treatment being perpetrated with the imprimatur of the United States government. The draft legislation I have outlined below seeks to remedy this shameful practice.

The proposed legislation which follows is based on my experience as a former military attorney. As a Navy prosecutor, I represented the government in several drug-related cases, and I was responsible for sending to prison individuals who were in violation of federal drug laws. I was very proud to wear the uniform of this country's Armed Forces, and I was very proud of the service I performed in helping rid the Navy of drug offenders. In my experience, the military has by far the most successful anti-drug program in this country. One of the reasons the military's anti-drug program is so successful is that the program is designed to prevent—in practice as well as word—precisely the sort of arbitrary and discriminatory practices that are currently permitted by Customs Service policy. The people who lead our Armed Forces understand something that the Customs Service does not understand: namely, that to successfully wage any war, be it a war against an armed enemy, or a war on drugs, it is of vital importance to maintain not only public support for the war effort, but also the support of the very troops who are waging the war—and that such support will not be forthcoming if the war is perceived as no more than a pretext for perpetrating racist and ethnic discrimination.

Department of Defense policy (see DoD Directive 1010.1) provides for nonconsensual urinalysis testing for drug use under specifically-prescribed circumstances. The first of these is when the testing is part of an inspection program. Such urinalysis inspections fall into two sub-categories: unit sweeps (where all members of a unit, or all members of a defined sub-unit, are required to submit samples) and random samplings (generally derived by randomly drawing a number, and all unit members whose social security number ends in that digit are required to provide a sample). Both forms of inspection share the attribute of being non-discretionary in nature—the decision that a particular person will be required to provide a sample is based either on the draw of numbers, or on the person's membership in a unit or sub-unit. An analogous practice with respect to arriving passengers passing through Customs would be conducting baggage searches of all arriving passengers (or at the very least conducting searches based on a genuinely random selection process).

The second circumstance in which a nonconsensual urinalysis may be conducted is when there has been a search authorization issued based on a finding of probable cause when there is reasonable belief that the sample to be collected contains evidence of illegal drug use. This is an objective standard requiring specific, articulable facts indicating an illegal act has occurred.

These are the only circumstances in which the military uses nonconsensually obtained urine samples in a criminal proceeding to form the prosecution's case in chief; samples obtained in a manner not in conformity with these principles may be used in a criminal proceeding only for impeachment or rebuttal. (Urinalysis results obtained through neither a valid inspection, nor through probable cause, may be used for other non-criminal, administrative purposes—such as safety mishap investigations and fitness for duty determinations—clearly not analogous to Customs searches of arriving passengers.)

With this as background, I propose the following statute:

"Section 1582 of Title 19 of the United States Code is amended to read as follows: (a) The Secretary of the Treasury may prescribe regulations for the search of persons and baggage and is authorized to employ female inspectors for the examination and search of persons of their own sex; and all persons coming into the United States from foreign countries shall be liable to detention and search by authorized officers or agents of the Government under such regulations, subject to the following limitations .

(b)(1) The limitations described in subsections (b)(2) through (b)(4) of this subsection shall apply to persons arriving in the United States by way of any common carrier transportation, including, but not limited to, commercial passenger airline service and maritime passenger vessels.

(b)(2) Except as provided in subsections (b)(3) and (b)(4) of this section, and notwithstanding any other provision of law, the search and detention authority described in subsection (a) of this section shall be exercised only in a non-discretionary manner in which equivalent procedures relating to search, detention, and all other matters pertaining to the processing of persons described in subsection (b)(1) are applied uniformly to all persons arriving in the United States on the same airplane, maritime vessel, or other common carrier.

(b)(3) Disparate procedures of any sort, including, but not limited to, those relating to search, detention, or questioning, may be carried out only if there is reasonable suspicion to believe that an individual passenger is in violation of United States law. For purposes of this section, the phrase "disparate procedures" shall mean any procedures not applied uniformly to all persons arriving in the United States on the same airplane, maritime vessel, or other common carrier. The phrase "reasonable suspicion" shall mean a particularized and objective basis for suspecting the individual passenger of being in violation of United States law.

(b)(4) No person entering the United States may be held in detention in excess of six hours, or be subject to any search, inspection, or viewing, by any means or device, of such person's internal bodily cavities, genitalia, buttocks, rectum, or, in the case of a female passenger, breasts, except when so authorized by court order.

(b)(5) No person entering the United States may be held in detention in excess of two hours without being afforded an opportunity, at Government expense, to make a telephone call to any person chosen by the detained passenger. The Government may monitor such telephone calls, but the substance of such communications will be admissible in any subsequent legal proceeding only as allowed by the Federal Rules of Evidence. A detained passenger shall be afforded an opportunity to make such a telephone call at least once for each additional two-hour increment in which the individual continues to be held in detention."

This statute would, if enacted, require the Customs Service to comply with the Constitution of the United States and the decisions of the Supreme Court. Subsection (b)(2) makes clear that searches may be conducted without any objective

level of suspicion only when conducted under "routine" circumstances, and that such circumstances exist only when based on procedures applied uniformly and in a non-discretionary manner. Subsection (b)(3) makes clear, as the Supreme Court has held, that non-routine search procedures may be utilized only when there is reasonable suspicion that a violation of law has occurred. At present, Customs is performing suspicionless searches on fewer than two percent of arriving air passengers. Search procedures applied to only two percent of passengers are clearly not "routine." Although there do not appear to be published statistics available with respect to baggage searches, Customs' statistics indicate that during 1998, over 43 percent of passengers subject to some form of body search were Black or Hispanic. It is readily assumable that similar statistics are true for passengers subject to suspicionless baggage search and interrogation. When adding in Jews, Asians, Arab-Americans, and other minority groups, it is clear that well over 50 percent of persons subject to disparate procedures based on no objective suspicion are minority members.

The prevalence of such discrimination is not difficult to understand. Customs allows its officers to subject passengers to disparate treatment based on a subjective standard, i.e., one that is based on what the individual officer, in his or her own mind, without reference to any objective criteria, considers to be suspicious. If the officer, in the recesses of his mind, considers Blacks or Jews to be inherently suspicious, the officer is permitted, notwithstanding the stated "policy" to the contrary, to subject the passenger to discriminatory and abusive treatment—when, in fact, there is no objective indication that the particular passenger is any less likely to be a law abiding citizen than any of the White, Gentile passengers.

The study of psychology teaches us that human beings, by nature, tend to be suspicious of people who are different from themselves. If this is true, as there appears to be empirical reason to believe, then allowing the Customs Service to continue to subject people to disparate treatment based on the subjective biases of individual Customs officers is to ensure that this agency, with the imprimatur of the United States government, will continue to abuse and stigmatize citizens of this country based on race, religion, ethnicity, and other minority status. The proposed statute remedies this by requiring that the agency only subject persons to disparate, non-routine treatment when there is reasonable suspicion to believe that a person has done something illegal. In essence, it requires that the Customs Service accord Black people, Jewish people, Hispanic people, and other minority members the same presumption of innocence that is currently accorded White, Gentile people.

The proposed statute is a reasonable balance between legitimate law enforcement objectives and legitimate Constitutional rights of individual passengers. It allows Customs to continue to perform suspicionless searches, provided they are performed in a uniform, non-discriminatory manner. The agency has the flexibility to move resources, as it deems necessary, to perform such suspicionless searches of all passengers arriving from "high risk" areas, and it even has the flexibility to determine which specific plane or ship arrivals should be subject to more rigorous procedures. The only thing the agency will no longer have the flexibility to do is to subject people to racial, religious, and ethnic discrimination. No agency of the United States government should ever have flexibility of that sort.

Moreover, the proposed statute will almost certainly increase the amount of seized narcotics and other contraband. Last year, according to recent testimony by the Commissioner of the Customs Service, of the 1.35 million pounds of narcotics seized by Customs, only 5,000 pounds were seized from air passengers; that represents less than one-half of one percent. The reason for this abysmal record is easy to understand; it is the result of conducting operations based on racial and ethnic bigotry rather than on valid law enforcement methods. In fact, Customs is catching only an infinitesimal amount of the narcotics that are being smuggled into the country by air passengers—the vast majority of which is being smuggled by blonde-haired, blue-eyed people who are well aware of Customs' discriminatory practices. Anyone who was in the Detroit airport on October 30, 1998, as I was, and witnessed such a person being lunged at by a drug detection dog and not being subjected to even the most minimal search procedures, to which minority members are routinely subjected, would have no difficulty understanding the reason for Customs' appalling record. By requiring all non-uniform searches to be based on reasonable suspicion, the proposed statute will force Customs to develop more effective detection and investigative techniques, thus increasing the amount of seized narcotics.

Finally, subsections (b)(4) and (b)(5) seek to remedy the most abusive of Customs' current practices by ensuring that no person is subject to search of their intimate body parts except when so authorized by a detached judicial officer, and by ensuring that most fundamental of American rights—that no person may be held incommunicado for an indefinitie period by the police.

In summary, the proposed statute precludes the Customs Service from subjecting persons to discriminatory treatment based on the subjective impulses of its officers—a system which has led to the current prevalence of racial and ethnic discrimination. Instead, it establishes the principle that non-uniform search procedures may be utilized only when an objective standard of suspicion has been met. The Armed Forces have long operated under such a principle, as discussed above; indeed, the military, which runs by far the most successful anti-drug program in the country, uses a "probable cause" standard for its discretionary drug testing intended for use in the prosecution's case in chief. The proposed statute imposes on Customs a lower objective standard, "reasonable suspicion." If our military leaders can run the Armed Forces of this country using an objective standard for their anti-drug program, there is no legitimate reason why a civilian agency like Customs cannot run its search program using an objective standard that accords to civilians the same rights that members of the military have—to be free of abusive, arbitrary, and discriminatory treatment.

In conclusion, I would like to thank the Chairman, the Ranking Minority Member, and the other Members for holding these very important hearings, and for allowing members of the public the opportunity to express their views. If there are any questions about this statement, I will be happy to provide any additional information or be of any further assistance to the Committee.

STATEMENT OF THE COALITION FOR CUSTOMS MODERNIZATION

[SUBMITTED BY M. BRIAN MAHER, CHAIRMAN, AND STEWART B. HAUSER, PRESIDENT]

The Coalition for Customs Modernization was created in July 1998 by New York and New Jersey industry leaders to raise regional and national awareness of the critical possibility of the U.S. Customs Service computer breaking down and the need for immediate funding for a new system to replace the current system. A collapse of this system would affect every segment of the U.S. economy and jeopardize drug interdiction efforts throughout the country as well as the flow of goods and raw materials in and out of the country.

Presently the Automated Commercial System (ACS) Customs computer system is over 14 years old and requires continued funding to maintain its current operation. In the past 14 years international trade has grown exponentially and ACS is handling over 95 per cent of all Customs transactions and is operating at well beyond its design capacity. As a result, the system is subject to failures such as happened last September 14 costing the Government a $60 million delay in revenue collections. Again, on October 1, the system failed and blocked the flow of $2.2 billion worth of goods into the national economy. It is evident that a new and larger system is an absolute must and that the current system, ACS, must be funded until the new system Automated Commercial Environment (ACE) is in place.

The above financial impact was the result of just a few hours delay. Should there be a system breakdown of a catastrophic nature, the effect on the nation's industrial base would be even more devastating. Almost every industry in this country relies either directly or indirectly on the importing of raw or finished materials or the export of the products it produces. Every segment of the nation's economy would be affected by a Customs computer failure. The most immediate effects would be on the nation's air and seaports. Passengers would be substantially delayed at airports awaiting Customs clearance. Likewise air cargo shipments, by nature high value and very time sensitive, would also be substantially delayed at the airports. Within a week of a computer failure, ocean cargo necessary to our daily lives and long-term production would sit on vessels and even cargo on those vessels able to divert to Canada or Mexico would fare no better as border crossings would not be able to function. The nation's ports would be clogged with export/import cargo with resultant rail and highway congestion beyond belief. Ships arriving from foreign ports would be unable to neither unload their import cargoes nor would they be able to load their export cargo thus delaying shipping worldwide. To avoid the dire consequences of a Customs computer failure, funding must be provided immediately.

Equally important, a system breakdown will severely handicap crucial drug interdiction efforts. Significant progress has been made in this area; however, a system collapse may open the drug trafficking floodgates. Ultimately, a prolonged disruption of the system would affect the economic well-being, safety, and security of every man, woman and child in the country. To date the crucial national significance of this issue has not received the attention it warrants. The endless rhetoric on funding and technology should cease and in its place a unified public/private partnership

should be formed to rapidly address the issue while there is still time to avert this impending crisis.

The $1.2 billion funding to develop and implement the Automated Commercial Environment (ACE) must be appropriated immediately. Each year U.S. industry pays over $22 billion in duties to the United States Customs Service to be deposited in the United States Treasury. Importers have been paying user fees for over 10 years for technology improvements, yet these funds have not been disbursed for use by Customs in its operations. Because of the importance of international trade to the nation's economy, trade, security and public health and safety, averting a major Customs computer collapse by immediately funding a new computer system for Customs should be viewed as a critical national priority.

Clearly, the Federal Government has an obligation to ensure that not only is there an adequate system to collect these funds, but also that an impending system breakdown, with catastrophic consequences to the national economy and drug interdiction efforts, be immediately averted.

We respectfully request that you take immediate action to fund this critically important and necessary function of the Federal Government.

STATEMENT OF THE CITA BOARD OF DIRECTORS

AD HOC COMMITTEE ON THE UNAUTHORIZED PRACTICE OF LAW—LEGAL RESTRICTIONS IN NON-LAWYERS PROVIDING CUSTOMS RELATED SERVICES

Recent years have seen substantial growth in accountants, consultants, and other non-lawyer practitioners providing services to clients regarding customs issues that traditionally have been handled by customs lawyers and, in some cases, customs brokers. Some of this activity has no doubt been spurred by the legislative history to the Custom Modernization Act which intimated that, in some cases, reasonable care in importing operations could be achieved by consultation with customs consultants or public accountants. The Customs Service has similarly indicated its predisposition to sanctioning customs advisory roles for non-lawyers in the issuance of its "Reasonable Care Checklist."

This memorandum seeks to identify what legal restrictions exist on the providing of customs related services by non-lawyers and the extent to which communications with clients regarding such services may or may not be protected by any type of legal privilege. This memorandum does not take an advocacy position on the issues in question.

The memorandum's principal conclusions are as follows:

1. While non-lawyers have taken an active role in providing various legal type services in a number of non-customs areas, these have generally involved the providing and completion of forms with information provided by the client, when incident to the service providers' main businesses. The providing of legal advice by persons who are not lawyers has generally not been allowed. The principal exception to this rule has been in the area of tax where some, but not all, courts have allowed accountants to provide tax planning and related advice, particularly when incident to the providing of accounting services.

2. The Federal Government may displace state control over the unauthorized practice of law and has done so in at least three situations—(i) CPA's can appear before the IRS; (ii) non-lawyer patent specialists can appear before the Patent Office; and (iii) customs brokers can make entries and appear before the Customs Service.

3. Because of the legislative history to the Customs Modernization Act, a recent judicial opinion and various Customs regulations and pronouncements, other than in a few situations, the extent to which non-lawyers can appear before the Customs Service on behalf of clients or advise clients regarding customs issues is not entirely clear.

4. Fee splitting by lawyers with non-lawyers, and by customs brokers with non-licensed individuals, is prohibited in almost all cases.

5. Non-lawyer-client communications are not protected by any federal attorney-client privilege and state and related privileges are limited.

I. THE REGULATION OF THE PROVISION OF LEGAL SERVICES

The providing of legal services is generally regulated by the judiciary in each of the states.

"It is the province of each state to define the practice of law, and to prescribe the qualifications and regulate the conduct of those who may engage in such practice,

either in its own tribunals or outside any tribunal. *De Pass* v. *B. Harris Wool Co.*, 144 S.W.2d 146, 148 (Mo. 1940)."

The authority of the states in this area is well established and is supported by the American Bar Association. *Middlesex County Ethics Comm.* v. *Garden State Bar Ass'n*, 457 U.S. 423 (1982); *Goldfarb* v. *Virginia State Bar*, 421 U.S. 773 (1975); ABA Opinion 198 (1939).

The practice of law and the providing of legal services is generally restricted to attorneys admitted to practice in the state in question, but what constitutes the practice of law is not always easy to define with any type of precision, and may depend on the circumstances of the particular act done. *People ex rel. Chicago Bar Ass'n* v. *Goodman*, 8 N.E.2d 941 (Ill. 1937); *Shortz* v. *Farrell*, 327 Pa. 81, 193 A. 20 (1937). The practice of law is clearly not limited to representing clients before tribunals, but is generally also considered to encompass the rendering of legal advice regarding state or federal law, the preparation of legal documents, the performance of actions which require legal knowledge, training and skill, beyond that possessed by the typical layman, and holding oneself out to be a lawyer. *Arkansas Bar Ass'n* v. *Block*, 230 Ark. 430, 323 S.W.2d 912, *cert. denied*, 361 U.S. 836 (1959); *Spivak* v. *Sachs*, 16 N.Y.2d 165, 166 (1965); *People* v. *Alfani*, 227 N.Y. 334, 125 N.E. 671 (1919). A listing of each state's definition of the practice of law is set forth in Exhibit A.

In those areas such as bankruptcy, real estate brokerage, collection, and tax where laymen have traditionally provided a variety of legal type services, the courts generally look to the character of the act done and the extent to which legal judgment is involved in deciding whether or not a layman has engaged in the unauthorized practice of law. Thus, while completing a bankruptcy claim form with information provided by the claimant or attending creditors' committee meetings will generally not be a problem for a non-lawyer, (*In Re Kincaid*, 146 BR 387 (BC WD Tenn., 1992), advising the claimants as to their claims and preparing bankruptcy petitions and accompanying schedules will likely involve unauthorized practice, *In re Herrera*, 194 BR 178 (BC ND Ill., 1996); *In re Arthur*, 15 BR 541 (BC ED Pa., 1981), 8 BCD 459, 5 CBC 2d 716, CCH Bankr L. Rptr P. 68464.

Similarly, real estate brokers who fill in blanks in printed forms or instruments relating to land, when incidental to the main business of the real estate agent, in many states, may not be engaged in the practice of law. *Merrick* v. *American Security & Title Co.*, 71 App. D.C. 72, 107 F.2d 271 (1939), *cert. denied*, 308 U.S. 625 (1940); *Cowern* v. *Nelson*, 207 Minn. 642, 290 N.W. 795 (1940); *Gardner* v. *Conway*, 234 Minn. 468, 48 N.W.2d 788 (1951); *State Bar of Michigan* v. *Kupris*, 366 Mich. 688, 116 NW2d 341. Similarly, bank employees do not engage in the unauthorized practice of law when they fill in blanks of mortgage instruments when it was incidental and in direct connection to the bank's regular business of making loans. *In re Sadnick*, 65 BR 840 (N.D. Ill. 1986). However, brokers may not prepare forms for persons in transactions in which they are not the broker, *Hulse* v. *Criger*, 363 Mo. 26, 247 S.W. 855 (1952) and non-lawyers may not prepare agreements relating to real property, *Fein* v. *Ellenbogen*, 84 N.Y.S.2d 787 (1948); or deeds, mortgages or other contracts of a legal nature, *Howton* v. *Morrow*, 269 Ky 1, 106 S.W.2d 81 (1937).

Collection agents, likewise, may engage in a number of "legal type" activities such as adjustment of a bill or the peaceful collection of a claim by sending of letters to debtors and related activity, without undertaking the unauthorized practice of law, *see, e.g.*, 15 *Am Jur* 2d Collection and Credit Agencies § 9. However, they may not employ attorneys to prosecute claims and provide various legal services, *State ex rel Seawell* v. *Carolina Motor Club*, 209 N.C. 624, 184 S.E. 540 (1936), nor may they advise or threaten legal proceedings in an effort to collect a claim on behalf of a creditor, *Ala-State, ex rel. Porter* v. *Alabama Ass'n of Credit Executives*, 338 So.2d 812 (1976).

In the area of immigration, the act of recording a client's responses to questions on an INS form would probably not involve the practice of law. However, the act of determining whether the IRS form should be filed at all does require legal skills and if performed by a non-lawyer, would generally involve unauthorized practice. *Unauthorized Practice Committee, State Bar of Texas* v. *Cortez*, 692 S.W.2d 47 (Tex. 1985).

Finally, in the area of tax, laymen can complete tax returns based on information provided by the taxpayer, install bookkeeping and accounting systems, and provide business counsel, but, according to some authorities, cannot render opinions regarding tax liability, construe tax statutes, or tax decisions. *See, e.g., In re Bercu*, 273

App. Div. 524, 78 N.Y.S.2d 209 (1st Dept. 1948), *aff'd*, 299 N.Y. 728, 87 N.E.2d 451 (1949)—accountant restrained from advising on a matter of federal tax law.[1]

However, other authorities hold that supplying information and advice in tax matters, even though not incidental to another service, does not amount to the practice of law. *See* generally, 9 ALR 2d 797. Indeed, one federal court has taken judicial notice that accountants regularly give legal advice in their income tax practice.[2] The willingness of some courts to allow accountants to provide such services is no doubt based on the federal sanction for accountants to appear before the IRS. *See, infra,* Section II.

II. FEDERAL REGULATION OF THE UNAUTHORIZED PRACTICE OF LAW

The prohibition against the unauthorized practice of law also extends to the federal courts. Under 28 U.S.C. § 1654, persons must appear in federal courts either *pro se* or through an attorney admitted to practice before the court. Furthermore, under 5 U.S.C. § 500, an attorney who is a member in good standing of the bar of the highest court of a State may represent a person before an agency on filing with the agency a written declaration that he is currently qualified and is authorized to represent his client.

5 U.S.C. § 500 also permits "[a]n individual who is duly qualified to practice as a certified accountant in a State may represent a person before the Internal Revenue Service ("IRS") of the Treasury Department on filing a written declaration that he is currently qualified . . . and is authorized to represent the particular person in whose behalf he acts."[3] Furthermore, the statute allows non-lawyers to practice before the Patent Office "with respect to patent matters that continue to be covered by chapter 3 (sections 31–33) of title 35."[4] Moreover, the statute's language is not necessarily limited to certified public accountants who wish to practice before the IRS or non-lawyers who wish to practice before the United States Patent Office in that it states that the language is not to be interpreted to "grant or deny to an individual who is not [an attorney licensed by a state] or [a duly qualified certified accountant] the right to appear for or represent a person before an agency or in an agency proceeding."[5]

The impact and scope of the 5 U.S.C. § 500 exemption was extensively considered by the U.S. Supreme Court in *Sperry* v. *State of Florida*, 373 U.S. 379 (1963). There, an individual, not licensed to practice law in the State of Florida attempted to represent clients before a branch of the United States Patent Office in Florida. The Florida Bar Association sued in the Supreme Court of Florida to enjoin the non-lawyer's actions because, as the Florida Bar alleged, such actions constituted the unlawful practice of law within the State of Florida. That Court granted the injunction.

In the petition for a writ of *certiorari*, the non-lawyer petitioner took issue with injunction only to the extent that it prohibited him from engaging in activities covered by his federal license to practice before the United States Patent Office.[6] The Supreme Court held that, although Florida has a substantial interest in regulating the practice of law within the State, "the law of the State, though enacted in the exercise of powers not controverted must yield' when incompatible with federal leg-

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[1] The Wall Street Journal recently reported that the Tax Section of the Texas Bar Association is filing an administrative complaint against the Arthur Andersen accounting firm for providing unauthorized legal services. Wall Street Journal, Sept. 29, 1997 at B5.

[2] "Without judging the merits of the accounting profession's de facto rendition of quasi-legal services, we must take judicial notice of the fact that, in Monroe, Louisiana, as alsewhere, CPA's regularly render opinions and advise their clients on matters of federal and state income tax liability as a routine matter in performance of their proffessional services. As a matter of fact, attorneys-at-law frequently refer such clients to CP's for such advice, which is in a specialized field; and attorneys also also seek such advice directly from CPA's. In writing the policy here sued upon, defendant is bound to have known of this almost universal practice." *Bancroft* v. *Indemnity Ins. Co. of N. America*, 203 F. Supp. 49 (W.D. La. 1962).

[3] 5 U.S.C. § 500(c).

[4] 5 U.S.C. § 500(e).

[5] 5 U.S.C. § 500(d)(1).

[6] The Florida Supreme Court enjoined the following activities until the non-lawyer practitioner became a member of the Florida State Bar: (1) "using the term 'patent attorney' or holding himself out be an attorney at law in this state in any field or phase of the law" (the individual later voluntariiy ceased the use of the word "attorney"); (2) "rendering legal options, including opinions as to patentability or infringement on patent rights"; (3) "preparing, drafting and construing legal documents"; (4) "holding himself out, in [Florida] as qualified to prepare and prosecute applications for letters patent, and amendments thereto"; (5) "preparation and prosecution of applications for letters patent, and amendments thereto, in [Florida]"; and, (6) "otherwise engaging in the practice of law."

islation."[7] However, the Court limited the scope of its ruling stating that although "the State maintains control over the practice of law within its borders," non-lawyers are authorized to practice law only to the "limited extent necessary for the accomplishment of the federal objectives."

In light of the general principles regarding the unauthorized practice of law set forth above and the Supreme Court's holding in *Sperry*, in order to identify what customs related activities performed by a non-lawyer would constitute the unauthorized practice of law, customs related activities need to be specifically identified and the impact of Congressional pronouncements in this area, as well as any administrative regulations validly issued pursuant thereto, must be analyzed.

III. CUSTOMS ACTIVITIES

The scope of customs activities includes such matters as (i) appearing at the Court of International Trade on behalf of a client on any matter, (ii) appearing before the Customs Service on behalf of a client in connection with ruling requests, requests for internal advice, penalty proceedings, domestic industry petitions, protests, filing of import and drawback entries, and the submission of drawback contracts, (iii) providing advice on classification, valuation, marking, special programs and other related matters, and (iv) the completion of customs reports such as computed value cost submissions and APTA diversion reports. In 19 U.S.C. § 1641, a statute dealing with the regulation of customs brokers, Congress has defined the term "customs business" as "those activities involving transactions with the Customs Service concerning the entry and admissibility of merchandise, its classification and valuation, the payment of duties, taxes, or other charges assessed or collected by the Customs Service upon merchandise by reason of its importation, or the refund, rebate, or drawback thereof. It also includes the preparation of documents or forms in any format and the electronic transmission of documents, invoices, bills, or parts thereof, intended to be filed with the Customs Service in furtherance of such activities, whether or not signed or filed by the preparer, or activities relating to such preparation, but does not include the mere electronic transmission of data received for transmission to Customs." 19 U.S.C. § 1641(a)(2). The statute goes on to indicate that "customs business" may only be conducted by persons holding a valid customs broker's license issued by the Secretary of the Treasury. Implementing regulations, 19 C.F.R. § 111.5, state that a broker who represents a client in the importation of merchandise, may represent the client before the Treasury Department on any matter concerning such merchandise, except not in any Customs district in which the broker has not been granted a permit.

While the Customs Service has set forth its understanding of the statutory definition of "customs business,"[8] and has held a meeting to allow members of the public to comment,[9] it has not yet issued formal regulations implementing the changes to the statutory definition made by the Customs Modernization Act. Those 1993 statutory changes involved the addition of the last sentence of the statutory definition set forth above. "It also includes the preparation of documents or forms in any format and the electronic transmission of documents, invoices, bills, or parts thereof, intended to be filed with the Customs Service in furtherance of such activities, whether or not signed or filed by the preparer, or activities relating to such preparation, but does not include the mere electronic transmission of data received for transmission to Customs." The legislative history provides no useful discussion of the meaning of this provision.

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[7] At least one federal court of appeals has indicated that federal preemption of state statutes is most often based on a clear and unambiguous expression of Congressional interest. *Arons* v. *New Jersey State Bd of Ed.*, 842 F.2d 58, 63 (3rd Cir. 1988).

[8] The Customs Service draft of proposed revisions to 19 CFR Part 111 set forth in an October 7, 1996 Customs Bulletin Board Notice provided the following: "*Customs business.* "Customs business" means those activities involving transactions with the Customs Service concerning the entry and admissibility of merchandise, its classification and valuation, the payment of duties, taxes or other charges assessed or collected by the Customs Service upon merchandise by reason of its importation, and the refund, rebate, or drawback *of such duties, taxes, or other charges. "Customs business"* also includes the preparation, *and activities relating to the preparation,* of documents in any format and the electronic transmission of documents and parts thereof intended to be filed with the Customs Service in furtherance of *any other customs business activity,* whether or not signed or filed by the preparer. *However, "customs business"* does not include the mere electronic transmission of data received for transmission to Customs." Italics denote differences from the statutory definition.

[9] 61 Fed. Reg. 67871 (1996).

IV. THE PROVIDING OF CUSTOMS RELATED SERVICES BY LAWYERS AND OTHERS

If one reviews the types of customs services set forth above and tries to identify who can provide such services, based on the above discussion and analysis, there are at least four clear principles which result. First, by virtue of 28 U.S.C. § 1654, no one but a licensed attorney may represent a client at the Court of International Trade. Second, no one but a licensed customs broker may engage in "customs business." For these purposes, at a minimum, this would appear to involve the filing of entries on behalf of an importer. Third, by virtue of their admission to a state bar and 5 U.S.C. § 500, attorneys can provide clients with advice regarding all aspects of customs law, and can appear on behalf of clients before the Customs Service. Fourth, non-lawyers can provide certain customs services to clients within their very specific areas of expertise, e.g., accountants can provide advice as to whether a specific accounting approach that has valuation implications is consistent with generally accepted accounting principles.

Beyond these principles, however, the situation is not clear. Much of the difficulty stems from the legislative history to the Customs Modernization Act which, even though it is not an unambiguous statement of federal intent to preempt state statutes, did indicate that non-lawyers had some role to play in providing customs services. "In meeting the "reasonable care" standard, the Committee believes that an importer should consider utilization of one or more of the following aids to establish evidence of proper compliance: seeking guidance from the Customs Service through the pre-importation or formal ruling program; consulting with a Customs broker, a Customs consultant, or a public accountant or an attorney; using in-house employees such as counsel, a Customs administrator, or if valuation is an issue, a corporate controller, who have experience and knowledge of customs laws, regulations, and procedures; or when appropriate, obtaining analyses from accredited labs and gaugers for determining technical qualities of an imported product." H.R. Rept. No. 103–361, pt. 1 (1993) at 120.

The extent of the role of non-lawyers in this general statement, however, may have been restricted by the illustrative examples following in which accountancy services are implicitly tied to matters within their specific expertise, *i.e.*, how cost elements are booked. "In seeking advice for a valuation question, the Committee expects an importer to consult with an attorney or a public accountant and as appropriate, personnel within the company knowledgeable regarding the importer's accounting system and how cost elements are booked."

Second, recent judicial activity, while initially bringing some clarity to the situation, has now made it even less clear. In *International Customs Associates, Inc.* v. *Bristol-Meyers Squibb Company,* Index No. 16211/92 (Sept. 22, 1995), an individual, who was not licensed to practice law in New York, provided advice on the application of domestic and foreign laws and international agreements and treaties, and on customs laws, tariffs and regulations. This individual sued his client for compensation for his services. The court held against him, ruling that a contract to provide legal service entered into by a person not licensed to practice law in New York, is unenforceable. The advice provided by the plaintiff, in this case, dealt with classic "customs law" issues (*i.e.*, the classification and value of, and the admissibility of, imported merchandise).

However, the summary judgment granted by the court was reversed on appeal and the complaint was reinstated, 233 A.D.2d 161, 649 N.Y.S.2d 789 (App. Div. 1996). The appellate court stated that: "factual triable issues exist regarding, inter alia, whether the services performed by the plaintiff constituted the practice of law in this State as defined by the Judiciary Law § 478 so as to preclude, as a matter of law, plaintiff's claims for compensation pursuant to the parties' contract." When defendant sought leave to reargue the case or appeal to the Court of Appeals, the motion was denied in its entirety. 1997 N.Y. App. Div. LEXIS 2580. According to counsel for the plaintiff, the matter is still in the discovery stage. A tentative trial date of April 27, 1998 has been set in New York State Supreme Court in Manhattan.

The Customs Service itself has issued regulations which appear to allow appearances before the Customs Service by non-lawyers, on behalf of clients, in some matters normally considered to involve the practice of law. For example, 19 C.F.R. § 174.3 states that when a person who is not an attorney or customhouse broker (or an employee of the broker) wishes to file a customs protest, such person must first be authorized to act on behalf of the principal through a power of attorney [10]—there-

[10] 19 CFR § 174.3(a).

by implying that persons other than attorneys and brokers can file protests.[11] Similarly, 19 C.F.R. §175.11 allows domestic interested party petitions requesting the classification, the appraised value, or rate of duty to be filed by "the domestic interested parties themselves, or by duly authorized attorneys or *agents* on their behalf."[12] (emphasis added). Under 19 C.F.R. §174.11, customs brokers can sign petitions on behalf of parties seeking remission or mitigation of fines, penalties and forfeitures. Additionally, although it has no regulatory foundation, the Customs Service regularly entertains ruling requests filed by non-lawyers on behalf of clients. Finally, the Customs Service, apparently considers that customs consultants (other than lawyers and customs brokers) can provide a wide range of legal type services (*e.g.* consultation with importers as to classification, valuation, *etc.*, preparation and prosecution of ruling requests, performance of compliance reviews for importers and consultation with importers regarding the establishment and operation of Customs bonded warehouses, foreign trade zones and container stations) to clients (*See* Exhibit B).

In addition, in at least one pronouncement following enactment of the Customs Modernization Act, the Customs Service has seemingly given an expansive reading to that Act's legislative history on the role played by non-lawyers. In its "Reasonable Care Checklist," T.D. 97–96, 62 Fed. Reg. 64248 (1997), Customs appears to indicate that consultation with a qualified customs "expert" which includes lawyers, brokers, accountants or Customs consultants, can satisfy the statute's reasonable care requirement, not only in the area of valuation, but also with respect to classification and country of origin/marking/quota questions. More directly, Customs clearly states that "to limit the selection of an expert to these individuals [lawyers and licensed brokers] runs contrary to the language of the congressional reports."

In this light, there appear to be several open issues in this area as follows:

1. to what extent can customs brokers advise clients regarding transactions, either by that client or another, with respect to which they have not acted as broker? Even though 19 C.F.R. §111.5 appears to be limited to merchandise entered by the broker, the legislative history to the Customs Modernization Act may allow the providing of such advice, at least regarding all merchandise entered by the client.

2. to what extent can accountants assist clients in completing customs documents such as computed value cost submissions and APTA diversion reports without the involvement of counsel? The legislative history to the Customs Modernization Act and court cases allowing accountants to complete tax returns would appear to protect such activity.

3. to what extent can accountants and other customs consultants provide advice to clients regarding customs transactions? To the extent such advice relates to the person's specific area of expertise, *e.g.* an accountant providing information about GAAP, such advice would be allowed. However, because the statute does not specifically provide for non-lawyers (other than customs brokers) providing customs advice, unless the Customs Modernization Act legislative history is given a broad reading, at least until the *Bristol-Meyers Squibb* case is finally decided, the general principles discussed above regarding the unauthorized practice of law would appear to bar the providing of such advice beyond the provider's specific area of expertise.

4. to what extent can accountants and customs consultants appear before the Customs Service on behalf of clients? Other than as set forth in 19 C.F.R. §§174.3 and 175.11, or as it might be authorized by Customs in its revisions to 19 C.F.R. Part 111, such activities would appear to be problematical. As for the submission of ruling requests, Customs' practice in the area may give non-lawyers a basis for continuing such activities.

5. to what extent can attorneys file import or drawback entries or submit drawback contracts? While 19 U.S.C. §1641 seems to place entry activity within the exclusive purview of customs brokers, 5 U.S.C. §500, on its face, clearly allows attorneys to appear before the Customs Service regarding such matters, and should allow attorneys to submit drawback contracts on behalf of clients.

V. FEE-SPLITTING

Related to the question of non-lawyers providing legal type customs related services is the extent to which lawyers who are either principals or employees of accounting firms or business entities other than law firms may split fees with their non-lawyer colleagues in such entities, and whether customs brokers may split fees

[11] But *see* the informal document prepared by the Customs Service which it distributed at a public meeting on the meaning of the term "customs business" (a copy of which is set forth in Exhibit B) which suggests that non-brokers/non-lawyers cannot prepare and present protests to the Customs Service.

[12] 19 CFR §175.11(b).

with unlicensed persons. As to the first issue, it is clear that, if an attorney who is holding himself out as such to provide legal services, receives fees for the advice he provides, the attorney cannot share the fees with non-lawyers, *e.g.* accountants, or other customs consultants.

22 NYCRR § 1200.17 (Disciplinary Rule 3–102) unequivocally states that, except in certain limited situations, none of which is applicable here, a lawyer or law firm shall not share legal fees with a non-lawyer. Moreover, under 22 NYCRR § 1200.18 (Disciplinary Rule 3–103), lawyers cannot form partnerships with non-lawyers if any of the activities of the partnership consist of the practice of law. These clear New York rules reflect ABA Model Rule 5.4.[13] The rationale for these rules is to protect against possible control by a non-lawyer interested in his own profit, of the professional judgment of a lawyer interested in his client's fate, and to avoid encouraging non-lawyers to engage in the unauthorized practice of law. *Emmons, Williams, Mires & Leech* v. *State Bar,* 6 Cal. App. 565, 573–74, 86 Cal. Rptr. 367, 372 (1970); ABA Formal Opinion 87–355 (1987); ABA Informal Opinion 86–1519 (1986).

Under these rules, if lawyers who practice with members of other professions to offer clients a variety of services related to a problem *e.g.,* a lawyer who works with an accountant to provide tax-related services (New York State Ethics Opinion 557 (1984)), or a lawyer who offers services through a divorce resource center (Nassau County (N.Y.) Ethics Opinion 84–1 (1984)), share their fees with non-lawyers, they violate DR 3–102. Moreover, even if lawyers who are principals or employees in an accounting or other business do not hold themselves out as attorneys, if they work with others in the business who engage in non-authorized legal practice, they may still run afoul of the disciplinary rules.[14] However, based on the plain language of the rule, if an individual admitted to practice law, advises a client in a consulting or other non-legal capacity, provided the services were not those that can only be performed by a lawyer, no violation of the rules would appear to have occurred.

As for the second issue, in several published decisions, the Customs Service has invoked 19 C.F.R. § 111.36(a) to prohibit an unlicensed person from sharing in fees earned by a licensed broker in the course of the broker's rendering of services for a third party. 19 C.F.R. § 111.36(a) provides, in relevant part, as follows: "A broker shall not enter into any agreement with an unlicensed person to transact Customs business for others in such manner that the fees or other benefits resulting from the services rendered for others inure to the benefit of the unlicensed person except as provided in paragraph (b) of this section . . ." Paragraph(b) deals with a limited exception to this prohibition pertaining to broker compensation to a freight forwarder.

In HQ 113715 (Jan. 9, 1997), the Customs Service considered the request of an unlicensed consultant, operating under the name, Export Links Inc., who had been retained by an importer to provide certain management services, including the review of financial and customs records. The consultant requested a ruling on the following scenario: the consultant discovered a drawback opportunity and wanted to engage the services of a licensed customs broker to prepare and present the drawback entries. Under the terms of the engagement, the consultant would contract to pay the broker for the services provided and the importer would sign the required power of attorney authorizing the broker to provided the services. However, the importer would pay all fees directly to the consultant.

Customs ruled that this would violate 19 C.F.R. § 111.36(a) because the consultant would be receiving a monetary benefit from the performance by the broker of customs business for a third party. In a follow-up request, which resulted in the publication of HQ 114045 (Aug. 21, 1997), Export Links varied the facts to include the alternative of hiring a lawyer to engage the customs broker for the same drawback services. Under the revised scenario, the lawyer, working as the agent of Export Links, would retain the broker, who would have the drawback recovery forwarded to Export Links. The broker would bill for services rendered to the lawyer, who, in turn, would invoice Export Links, and payment to the broker would be funneled through the attorney. Customs ruled that the addition of the lawyer would not avoid the prohibition of the regulation since the unlicensed consultant would still be re-

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[13] The one jurisdiction which allows lawyers to enter partnerships with non-lawyers is the District of Columbia. D.C. Bar Rule 5.4(a)(4) and (b) allows lawyers to enter partnerships with non-lawyers only in cases where: (i) the partnership has as its sole purpose the providing of legal services to clients; (ii) all persons having managerial authority or a financial interest in the entity agree to abide by the Rules of Professional Conduct; (iii) the lawyers who have a financial interest or managerial authority in the entity undertake to be responsible for the non-lawyer participants to the same extent as if they were lawyers; and (iv) the above conditions are set forth in writing.

[14] *See, e.g.* 22 NYCRR 1200.16 (DR 3–101) which prohibits a lawyer from aiding a non-lawyer in the unauthorized practice of law.

ceiving a monetary benefit stemming from a contract between the consultant, even if entered into by the lawyer acting as agent for the consultant, and the broker, for the transaction of customs business for the third party.

These decisions relied upon an earlier decision (HQ 221330 (May 20, 1991)) which set forth similar facts. In that decision, as well, Customs concluded that the arrangement, whereby an unlicensed consultant received a monetary benefit as a result of drawback services performed by a licensed broker, violated 19 C.F.R. § 111.36(a).

In sum, the prohibition against fee splitting by customs brokers has received an absolute and unambiguous interpretation by the Customs Service. In the case of employees of consulting or accounting firms who are also individually licensed as customs brokers, the prohibition of 19 C.F.R. § 111.36(a) applies if the services which they provide on behalf of their clients fall within the definition of "customs business," because it is the individual's employer (i.e., the accounting or consulting firm) which is receiving the monetary benefit from the clients and not the licensed individual.

It should also be noted that the representation by these employees of consulting or accounting firms, of clients before the Customs Service may be permitted by the Customs Service simply because they hold a customs broker's license. While there is a question as to whether such representations is proper,[15] it probably does not violate 19 C.F.R. § 111.36(a) because it does not involve the realization of a monetary benefit resulting from the transaction of customs business, e.g., classification and valuation of imports.

VI. ATTORNEY-CLIENT PRIVILEGE ISSUES

Whether or not non-lawyers can provide clients with attorney type services, either privately or before the Customs Service, such activities will not be protected by the attorney-client privilege, and, in fact, may not be protected by any privilege at all, in the event the Customs Service, another governmental agency, or a private party seeks to compel disclosure of communications between the company and the adviser. Under the traditional analysis of attorney-client privilege as applied under federal law, the scope of the privilege is narrow, limited to confidential communications between lawyer and client made in the course of and necessary to the provision of legal advice. It does not extend to communications between accountants and their clients.

However, given the nature and purpose of the privilege (the promotion of effective legal assistance to those in need by fostering an atmosphere of full and frank communication), and in light of evolving case law in patent law and other fields where non-lawyers sometimes practice on an equal level with attorneys, an argument could be made that customs brokers should be extended a limited attorney-client privilege to the extent that their clients seek legal advice concerning customs law matters related to entries which the brokers have made. This issue is not settled and an argument also could be made that the privilege should not be applied to customs brokers, just as it is not afforded to accountants or tax preparers when engaged in providing most accounting services or tax-return-preparation services. As recent case authority illustrates, the focus of this question is on the nature of the relationship between client and professional, that is, whether the advice sought is legal in nature or more like accounting services or tax preparation, as well as the degree to which the advice provider is subject to professional standards, regulation and oversight.

A. Federal rule of evidence 501

The attorney-client privilege, which protects confidential communications between attorney and client, is one of the oldest privileges known under common law. Under federal law, the scope of testimonial privilege is governed by the principles of the common law. Rule 501 of the Federal Rules of Evidence provides: "Except as otherwise required by the Constitution of the United States or provided by Act of Congress or in rules prescribed by the Supreme Court pursuant to statutory authority, the privilege of a witness . . . shall be governed by the principles of the common law as they may be interpreted by the courts of the United States in light of reason and experience. However, in civil actions and proceedings, with respect to an element of a claim or defense as to which State law supplies the rule of decision, the privilege of a witness . . . shall be determined in accordance with State law."

In *In Re Grand Jury,* 103 F.3d 1140 (3rd Cir. 1997), *cert. denied sub nom Robert Roe* v. *United States,* 65 USLW 3795, 3798 (June 2, 1997), the court stated that in

[15] *See* CITBA's February 27, 1997 submission to the U.S. Customs Service on the meaning of the term "customs business."

enacting Rule 501, Congress did not intend to "freeze the law of privilege," but to provide the courts with the flexibility to develop rules of privilege on a case-by-case basis. *Id.* at 1149 (citing *Trammel* v. *United States,* 445 U.S. 40, 47 (1980). Nevertheless, the court noted that: ". . . privileges are generally disfavored; that 'the public . . . has a right to every man's evidence'; and that privileges are tolerable "only to the very limited extent that permitting a refusal to testify or excluding relevant evidence has a public good transcending the normally predominant principle of utilizing all rational means for ascertaining truth." *Id.* at 1149 (citations omitted). Continuing, the court observed that: "In keeping with these principles, the Supreme Court has rarely expanded common law testimonial privileges. Following the Supreme Court's teachings, other federal courts, including this court, have likewise declined to exercise their power under Rule 501 expansively. *Id.* at 1149 (citations omitted).

B. Elements and Scope of Attorney-Client Privilege under federal law

As a privilege known to the common law, the attorney-client privilege is recognized in federal law. The Supreme Court has outlined the purpose and scope of the attorney-client privilege: "The attorney-client privilege is the oldest of the privileges for confidential cmmunications known to the common law. 8 J. Wigmore, *Evidence* § 2290 (McNaughton re 1961). Its purpose is to encourage full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and administration of justice. The privilege recognizes that sound legal advice or advocacy serves public ends and that such advice or advocacy depends upon the lawyer's being fully informed by the client. . . . This rationale for the privilege has long been recognized by the Court . . . ." *Upjohn Co.* v. *United States,* 449 U.S. 383, 389 (1981).

The traditional elements of the attorney-client privilege have been summarized in "Wigmore's famous formulation," as follows: "(1) Where legal advice of any kind is sought (2) from a professional legal adviser in his capacity as such, (3) the communications relating to that purpose, (4) made in confidence (5) by the client, (6) are at his instance permanently protected (7) from disclosure by himself or by the legal adviser, (8) except the protection be waived . . . *United States* v. *Kovel,* 296 F.2d 918, 921 (2d Cir. 1961) (quoting 8 Wigmore, Evidence (McNaughton Rev. 1961), §2292).

Assertion of the attorney-client privilege requires claimants to make four showings: "(1) that he was or sought to be a client of [the attorney]; (2) that [the attorney] in connection with the [document] acted as a lawyer; (3) that the [document] relates to facts communicated for the purpose of securing a legal opinion, legal services or assistance in a legal proceeding; and (4) that the privilege has not been waived. *Pacamor Bearings,* Inc. v. *Minebea Co., Ltd.,* 918 F. Supp. 491, 510 (D.N.H. 1996).

The attorney-client privilege does not apply to all dealings between a lawyer and client. It is limited to communications between the client and the attorney made in the course of professional consultations. *Upjohn,* 449 U.S. at 395, 66 L.Ed.2d at 595 ("The privilege only protects disclosure of communications; it does not protect disclosure of the underlying facts by those who communicated with the attorney . . . "); *United States* v. *Adlman,* 68 F.3d 1495, 1499 (2d Cir. 1995). Thus, "the attorney-client privilege does not protect client communications that relate only to business or technical data." *Pacamor Bearings,* 918 F. Supp. at 510–11.

The attorney-client privilege, however, is not limited only to communications involving litigation, but extends generally to all client communications made in the course of seeking legal advice. "A client is entitled to hire a lawyer, and have his secrets kept, for legal advice regarding the client's business affairs. . . . It is not true, and has not been true since the early nineteenth century, that the confidences of a client are "respected only when given for the purpose of securing aid in *litigation.*" . . . 'The attorney-client privilege protects confidential disclosures made by a client to an attorney in order to obtain legal advice, . . . as well as an attorney's advice in response to such disclosures.' . . . 'The attorney-client privilege applies to communications between lawyers and their clients when the lawyers act in a counseling and planning role, as well as when lawyers represent their clients in litigation.'"*United States* v. *Chen,* 99 F.3d 1495, 1501 (9th Cir. 1996), *cert. denied,* 117 S.Ct. 1429 (1997) (emphasis in original; citations omitted).

The privilege does not attach to all communications made to an attorney. The privilege applies only when the attorney is acting in his capacity as an attorney. "That a person is a lawyer does not, *ipso facto,* make all communications with that person privileged. The privilege applies only when legal advice is sought 'from a professional legal advisor *in his capacity as such.*'" *Chen,* 99 F.3d at 1501 (emphasis in original).

C. No accountant-client privilege exists under federal law

In *Couch* v. *United States,* the Supreme Court stated that: "[N]o confidential accountant-client privilege exists under federal law, and no state-created privilege has been recognized in federal cases . . ." 409 U.S. 322, 335, (1973) (citing cases).

In *United States* v. *Arthur Young & Co.,* 465 U.S. 805, (1984), the IRS sought the tax accrual papers prepared by a CPA for its client. The Second Circuit held that the independent auditor's tax accrual workpapers were entitled to work product immunity. The Supreme Court reversed. Noting that the appellate court's attempt to facilitate communication between independent auditors and their clients more closely resembled a testimonial accountant-client privilege, the Court quoted its statement in *Couch* that "no confidential accountant-client privilege exists under federal law, and no state-created privilege has been recognized in federal cases." *Arthur Young,* 465 U.S. at 817.

The Court further noted the fundamental distinction between the roles of the attorney and the CPA: "Nor do we find persuasive the argument that a work-product immunity for accountants' tax accrual workpapers is a fitting analogue to the attorney work-product doctrine . . . . The *Hickman* work-product doctrine was founded upon the private attorney's role as the client's confidential adviser and advocate, a loyal representative whose duty it is to present the client's case in the most favorable possible light. An independent certified public accountant performs a different role. By certifying the public reports that collectively depict a corporation's financial status, the independent auditor assumes a public responsibility transcending any employment relationship with the client. The independent public accountant performing this special function owes ultimate allegiance to the corporation's creditors and stockholders, as well as to the investing public. This "public watchdog" function demands that the accountant maintain total independence from the client at all times and requires complete fidelity to the public trust. To insulate from disclosure a certified public accountant's interpretations of the client's financial statements would be to ignore the significance of the accountant's role as a disinterested analyst charged with public obligations." *Arthur Young,* 465 U.S. at 817–18. The Court concluded: "Beyond question it is desirable and in the public interest to encourage full disclosures by corporate clients to their independent accountants; if it is necessary to balance competing interests, however, the need of the Government for full disclosure of all information relevant to tax liability must also weigh in that balance. This kind of policy choice is best left to the Legislative Branch." *Arthur Young,* 465 U.S. at 821.

To the extent a federal court recognizes an accountant-client privilege, it is limited to situations where the federal court is applying state law as "the rule of decision" and the particular state law expressly provides for an accountant-client privilege. At present, a number of states have created a statutory accountant-client privilege (for example, Arizona, Colorado, Florida, Georgia, Idaho, Illinois, Indiana, Kansas, Louisiana, Maryland, Michigan, Mississippi, Montana, Nevada, New Mexico, Pennsylvania, and Tennessee). *See Privileged Communications Between Accountant and Client,* 33 ALR4th 539; Wright & Graham, *Federal Practice and Procedure: Evidence* §5427.

Federal courts, however, have consistently rejected creation of an accountant-client privilege or application of a state-created privilege in federal question cases.[16] For example, in *Coastal Fuels of Puerto Rico, Inc.* v. *Caribbean Petroleum Corp.,* 830 F. Supp. 80, 81 (D.P.R. 1993), the court stated: "Various courts have stated that in federal question cases there is no accountant-client privilege, because there is no such privilege under the federal common law. . . . Many courts have agreed with the Supreme Court's position toward the accountant-client privilege in *Couch. In re Subpoena to Testify Before Grand Jury,* 787 F. Supp. 722, 724 (E.D. Mich. 1992); *United States* v. *Mullen & Co.,* 776 F. Supp. 620, 621 (D. Mass. 1991); *United States* v. *Margaritas Mexican Restaurant, Inc.,* 138 F.R.D. 566, 568–69 (W.D. Mo. 1991); *United States* v. *Arthur Young & Co.,* 465 U.S. 805, 817, 104 S.Ct. 1495, 1503, 79 L.Ed.2d 826 (1984)." *See also In Re Grand Jury,* 103 F.3d 1140, 1149 (3rd Cir. 1997)

[16] Proposed legislation which has passed the House of Representatives and is now before the Senate Finance Committee would fundamentally alter existing case law by making privileged communications between taxpayers and non-lawyer professionals who have the right to practice before the IRS, in connection with non-criminal proceedings before the IRS. H.R. 2676, 105th Cong., 1st Sess. (1997), §341. As explained in the House Committee Report on the proposed legislation, H.R. Rep't. No. 105–364, Pt. 1, 105th Cong., 1st Sess. (1997) at 66, the provision would allow taxpayers to consult with other qualified tax advisors in the same manner they currently may consult with tax advisors that are licensed to practice law (except with respect to criminal proceedings). However, the proposed legislation extends only to IRS proceedings, not court litigation. The provision also does not extend the privilege of confidentiality to communications that would not be eligible for the privilege if prepared by an attorney.

("[T]he Supreme Court has rarely expanded common-law testimonial privileges. Following the Supreme Court's teachings, other federal courts, including this court, have likewise declined to exercise their power under Rule 501 expansively.")

In *Wm. T. Thompson Co.* v. *General Nutrition Corp.*, 671 F.2d 100, 103 (3rd Cir. 1982), in the context of a civil action in federal district court in California, Thompson sought to depose Touche Ross in Pittsburgh, Pennsylvania and obtained a subpoena *duces tecum* directing Touche Ross to appear and produce documents. Touche Ross and General asserted that the requested materials were protected under Pennsylvania's statutory accountant-client privilege. The district court rejected this contention. On appeal, the Third Circuit stated that this issue's "starting point" was not the Pennsylvania statute but Federal Rule of Evidence 501. The court stated: "Under this rule, in federal question cases the federal common law of privileges applies. [citation omitted] Where state law provides the rule of decision, however, state privilege law will govern. [citation omitted] Under the federal common law there is no confidential accountant-client privilege. *Couch* v. *United States*, 409 U.S. 322, 335, 93 S.Ct. 611, 619, 34 L.Ed.2d 548 (1973)." 671 F.2d at 103–104.

The *Thompson* court also noted that in cases where both federal law claims and state law claims were presented, the federal law's privilege rule would prevail. The court stated that, although the federal courts could resort to state law analogies for the development of a federal common law of privileges where the federal law was unsettled, "the governing federal rule with respect to accountant privilege is settled by *Couch* v. *United States.*" 671 F.2d at 104; *accord Coastal Fuels of Puerto Rico, supra*, 830 F. Supp. at 81.

In cases that involve federal and state law claims, the courts have held that where fundamental federal interests are implicated, the federal law of privilege should apply. Thus, in *Matter of International Horizons, Inc.* v. *Committee of Unsecured Creditors*, 689 F.2d 996 (11th Cir. 1982), a bankruptcy proceeding in which the committee of unsecured creditors sought access to documents possessed by the debtor's accounting firm, the court first rejected an accountant-client privilege under federal law and then declined to apply the forum state's (Georgia) accountant-client privilege because: ". . . recognition of the accountant-client privilege in bankruptcy proceedings would substantially thwart an important *federal* interest. . . . [It would] completely undermine the important federal interest in providing bankruptcy courts and creditors with complete and accurate information regarding a debtor's financial condition." *Id.* at 1005–1006.

Similarly, in *Enforce Administrative Subpoenas of the Securities and Exchange Commission* v. *Coopers & Lybrand*, 98 F.R.D. 414 (S.D. Fla. 1982), the court declined to apply the forum state's accountant-client privilege in a subpoena enforcement proceeding brought by the SEC. The court held that, as the case before it was "fundamentally a federal matter involving the enforcement of an investigatory subpoena relating to alleged securities laws violations . . . there is no confidential accountant-client privilege under federal law, and that in a fundamentally federal proceeding such as this, the court may not recognize a state-created privilege." 98 F.R.D. at 415; *see also Lewis* v. *Capital Mortgage Investments*, 78 F.R.D. 295, 312–13 (D.Md. 1977) (holding that in an action involving section 10(b) of the Securities Exchange Act and SEC rule 10b–5, the applicability of the Maryland accountant-client privilege was unwarranted).

In light of the fact that the customs laws are "fundamentally a federal matter," it is unlikely, based on the relevant caselaw, that a federal court would recognize the existence of an accountant-client privilege in a proceeding involving the customs laws of the United States.

D. The protections of the attorney-client privilege have been extended to accountants where they are employed by and act on behalf of a lawyer hired by the client for legal advice

In certain instances, the protection of confidential communications afforded to the attorney-client privilege has been extended to accountants. These cases, however, demonstrate that the privilege does not apply to an accountant in his own capacity, but only where the accountant is acting on behalf of the attorney in connection with the lawyer's provision of legal advice to the client.

In *United States* v. *Kovel*, 296 F.2d 918 (2d Cir. 1961), Kovel, a former IRS agent with accounting skills, was employed by a law firm. When Kovel was subpoenaed in the course of a grand jury investigation of a law firm client, the law firm asserted that the attorney-client privilege prevented Kovel from disclosing any communications from the client under investigation. The court agreed that, under the circumstances presented, the privilege applied to Kovel. "Nothing in the policy of the privilege suggests that attorneys, simply by placing accountants, scientists or investigators on their payrolls and maintaining them in their offices, should be able to

invest all communications by clients to such persons with a privilege the law has not seen fit to extend when the latter are operating under their own steam. On the other hand, . . . the complexities of modern existence prevent attorneys from effectively handling clients' affairs without the help of others . . . [T]he presence of an accountant, whether hired by the lawyer or by the client, while the client is relating a complicated tax story to the lawyer, ought not destroy the privilege, . . . the presence of the accountant is necessary, or at least highly useful, for the effective consultation between the client and the lawyer which the privilege is designed to permit. By the same token, if the lawyer has directed the client, either in the specific case or generally, to tell his story in the first instance to an accountant engaged by the lawyer, who is then to interpret it so that the lawyer may better give legal advice, communications by the client reasonably related to that purpose ought fall within the privilege; . . . . What is vital to the privilege is that the communication be made *in confidence* for the purpose of obtaining *legal* advice *from the lawyer.* If what is sought is not legal advice but only accounting service, . . . , or if the advice sought is the accountant's rather than the lawyer's, no privilege exists." *Kovel,* 296 F.2d at 921–22 (emphasis in original).

In *United States* v. *Adlman,* 68 F.3d 1495 (2d Cir. 1995), the IRS sought from Adlman, a corporation's in-house counsel, a memorandum prepared by the corporation's auditors at the counsel's request. The district court held that the attorney-client privilege did not apply to the memorandum. The appellate court affirmed, holding that, under the facts, the district court did not abuse its discretion in finding that the attorney-client privilege did not apply given that the evidence was subject to competing interpretations. Although acknowledging that, under *Kovel,* "the privilege for communication with attorneys can extend to shield communications to others when the purpose of the communication is to assist the attorney in rendering advice to the client," 68 F.3d at 1499, the court found that the privilege did not apply in this particular case because: "In many respects, the evidence supports the conclusion that Sequa consulted an accounting firm for tax advice, rather than that Adlman, as Sequa's counsel, consulted AA [Arthur Andersen] to help him reach the understanding he needed to furnish legal advice. Adlman himself serves not only as counsel to Sequa but also as one of its officers. AA, furthermore, is regularly employed by Sequa to furnish auditing, accounting, and advisory services." 68 F.3d at 1500. The court concluded that if Sequa furnished information to AA in order to seek tax advice, no privilege would apply.

In one case involving a customshouse broker and an accountant, the focus was not on the attorney-client privilege per se but the work-product doctrine. In *In Re Grand Jury Proceedings,* 601 F.2d 162 (5th Cir. 1979), a customshouse broker (McCoy) was the target of a grand jury investigation which sought a wide range of documents relating to his business. Also at that time, McCoy was engaged in divorce proceedings. McCoy and his divorce attorney consulted a criminal lawyer, who suggested that the divorce attorney prepare an analysis of McCoy's financial transactions. The divorce attorney employed an accountant (Sussman), who prepared the financial analysis based on documents from McCoy and McCoy's regular accountant. Sussman was served with a subpoena seeking documents related to McCoy's brokerage business, with which he refused to comply. In reversing Sussman's contempt conviction, the appellate court held that the documents sought were protected by the work product doctrine. "This doctrine is distinct from and broader than the attorney-client privilege, . . . it protects materials prepared by the attorney, whether or not disclosed to the client, and it protects material prepared by agents for the attorney. . . . It was merely a circumstance that Sussman, as an accountant, was employed to prepare financial analyses to assist the lawyer in assessing McCoy's potential criminal liability. . . . The information sought was evidently material to McCoy's defense. Under these circumstances, the financial analyses prepared by Sussman were protected by the attorney-work-product doctrine." *Id.,* 601 F.2d at 171.

E. The attorney-client privilege has been applied to communications made to attorneys employed by accounting firms when the client seeks legal advice from the accountant-attorneys in their capacity as attorneys

In situations where an attorney is employed by an accounting firm, courts have determined that the attorney-client privilege may be afforded to communications made to such attorneys, but only to the extent that the client sought legal advice from the accounting firm, as opposed to business advice or accounting services, and the communications concerned legal matters. In *United States* v. *Mullen & Co.,* 776 F. Supp. 620 (D.Mass. 1991), the National Credit Union Administration sought to enforce an administrative subpoena against Mullen, an accounting firm. The targets of the agency investigation asserted attorney-client privilege regarding certain documents related to the work Mullen provided them, claiming that two of the three ac-

countants who worked on their matters were attorneys who provided "legal financial" advice. *Id.* The court found that the oft-cited *Kovel* [*see supra*] analysis properly applies the attorney-client privilege to communications pertaining to legal advice sought from the accountant in the accountant's capacity as an attorney. *Id.* at 621 (citing cases). However, because the particular facts before the court were insufficient to allow the court to determine if the *Kovel* analysis applied, the court outlined a series of questions that it viewed as relevant to determining whether the attorney-client privilege applied in that case to communications with the attorneys employed by the accounting firm.

The following questions, of course, would also be relevant to analyzing whether the attorney-client privilege applied to an attorney employed by an accounting firm to provide customs law advice. "Recognizing that the nature of the service is not determinative, but rather the nature of the professional relationship, . . . , what legal advice were the target individuals seeking? Were they, or any of them, then represented by counsel? What was the relationship of outside counsel to the accounting firm? Which Mullen employee worked on which document? Was the non-lawyer accountant subordinate to the two lawyer-accountants? If so, did they or either of them select the non-lawyer accountant to aid in the provision of legal services? If the target individuals claim to have relied upon Mullen employees as lawyers for legal advice, how reasonable was that reliance? What facts demonstrate that the lawyer-accountants in any way held themselves out as affording legal advice? Does Mullen or either of these two individuals carry legal malpractice insurance? Are the lawyers, in fact, authorized to practice law in any jurisdiction? Do they practice law on the side? Since it is suggested that the provision of legal services runs counter to the lawyer-accountant's ethical duties as accountants, what approvals were garnered from their superiors at Mullen? Does anyone at Mullen recognize that its employees were purporting to render legal services? If so, have they been disciplined? What steps has Mullen taken to insure that its clients recognize they are not being afforded legal services?" *Mullen,* 776 F. Supp. at 622.

This, of course, is a single case and does not establish a universally accepted rule. However, it does reflect judicial thinking in some quarters.

F. In certain specialized fields of law, the attorney-client privilege has been applied to non-attorney practitioners subject to registration and regulation

In general, while the attorney-client privilege has historically not been extended to non-lawyers who undertake legal work, some courts have recognized exceptions to the general rule in certain specialized fields of law where non-lawyers have been expressly permitted by statute to practice. Three examples where the issue has arisen are discussed below. These examples illustrate that the attorney-client privilege has been extended to non-lawyers in very limited situations where the non-lawyers are subject to registration and regulation, and are required to comply with professional standards.

1. Patent law: patent agents registered to practice before the U.S. Patent Office

The status of patent agents vis-a-vis the attorney-client privilege has evolved over time. In the past, "the common law did not permit patent solicitors to claim attorney-client privilege." Wright and Graham, Federal Practice and Procedure: Evidence § 5478. Patent agents were not accorded the attorney-client privilege even when the patent agent was an attorney on the ground that patent attorneys were not performing legal services because most patent work involved business and technical considerations rather than legal analysis. *See, e.g., Zenith Radio Corp.* v. *Radio Corp. of America,* 121 F. Supp. 792 (D.Del. 1954); *Georgia-Pacific Plywood Co.* v. *United States Plywood Corp.,* 18 F.R.D. 463 (S.D.N.Y. 1956).

After the Supreme Court's decision in *Sperry,* courts began to depart "from the common law consensus that patent work is not 'professional legal services'" and began to "look to the individual communication and apply the privilege to those that are legal in nature while denying it to those that are primarily business or technical." Wright and Graham, Federal Practice and Procedure: Evidence § 5478.

The leading case in this new approach was *In Re Ampicillin Antitrust Litigation,* 81 F.R.D. 377 (D.D.C. 1978). In that case, the court reviewed the case law concerning the application of the attorney-client privilege to patent agents and noted a split in the case law. *Id.* at 392. The court, however, found the *Sperry* decision significant in deciding whether to apply the attorney-client privilege to registered patent agents:

"While the denial of the attorney-client privilege to patent agent communications is different from the refusal to allow a patent agent to engage in any patent activities at all, imposing such a limitation on patent agent communications would result in significantly unequal treatment of patent agents and patent attorneys. Congress,

in creating the Patent Office, has expressly permitted both patent attorneys and patent agents to practice before that office. The registered patent agent is required to have a full and working knowledge of the law of patents and is even regulated by the same standards, including the Code of Professional Responsibility, as are applied to attorneys in all courts. Thus, in appearance and fact, the registered patent agent stands on the same footing as an attorney in proceedings before the Patent Office."

"Therefore, under the congressional scheme, a client may freely choose between a patent attorney and a registered patent agent for representation in those proceedings. That freedom of selection, protected by the Supreme Court in *Sperry,* would, however, be substantially impaired if as basic a protection as the attorney-client privilege were afforded to communications involving patent attorneys but not to those involving patent agents. As a result, in order not to frustrate this congressional scheme, the attorney-client privilege must be available to communications of registered patent agents."

In Re Ampicillin, 81 F.R.D. at 393. Thus, in summary, the court held that:

"[W]here a client, in confidence, seeks legal advice from a registered patent agent who is authorized to represent that client in an adversary process that will substantially affect the legal rights of the client, which thereby necessitates a full and free disclosure from the client to the legal representative so that the representation may be effective, the privilege will be available."

Id. at 394.

Some federal courts have subsequently applied the reasoning of *In Re Ampicillin* in affording attorney-client privilege to registered patent agents. *See, e.g., Foseco International, Ltd.* v. *Fireline, Inc.,* 546 F. Supp. 22, 25 (N.D. Ohio 1982); *Advanced Cardiovascular Systems* v. *C.R. Bard, Inc.,* 144 F.R.D. 372, 375 (N.D.Cal. 1992); *Stryker Corp.* v. *Intermedics Orthopedics, Inc.,* 145 F.R.D. 298, 304 (E.D.N.Y. 1992); *Glaxo, Inc.* v. *Novopharm Ltd.,* 148 F.R.D. 535 (E.D.N.C. 1993); *John Labatt Ltd.* v. *Molson Breweries,* 898 F. Supp. 471 (E.D.Mich. 1995). Other courts have declined to extend the privilege to non-lawyer patent agents. *See, e.g., Status Time Corp.* v. *Sharp Electronics Corp.,* 95 F.R.D. 27, 33 (S.D.N.Y. 1982) ("These cases do not persuade me to deviate from the fundamental principle that only communications between an attorney or an agent of the attorney and his client are covered by the privilege.").

In *John Labatt, supra,* a patent and trademark infringement case, Molson sought access to documents which Labatt asserted were protected by the attorney-client privilege. The documents in question involved one member of Labatt's legal department, a non-lawyer but a registered patent agent, who served as the company's intellectual property officer. The court first reviewed and adopted the reasoning of *In Re Ampicillin* in determining that the attorney-client privilege applied to registered patent agents. 898 F. Supp. at 474. The court then addressed Labatt's assertion that the privilege applied to its registered patent agent-intellectual property officer whenever he gave advice relating to intellectual property law. The court disagreed, finding that the privilege, as applied to patent agents, was a limited privilege:

"In their assertions . . . Labatt has expanded the scope of the privilege between patent agent and clients beyond what case authority or sound policy support. The farthest a privilege for a non-lawyer patent agent has been extended is to advice sought in confidence from a patent agent authorized to represent the client in an adversary process that will substantially effect the legal rights of the client—i.e. in the patent application process. *In re Ampicillin Antitrust Litigation,* 81 F.R.D. 377, 394 (D.D.C. 1978). No case provides blanket attorney-client privilege between a USPTO recognized non-lawyer patent agent and his client over *all* intellectual property matters, as Labatt seeks. [Citations omitted.]"

"The Labatt assertions also understate the requirements for the creation of an attorney-client privilege for a non-lawyer. A patent agent's claim to attorney-client privilege has its foundation in the USPTO's limited authorization to non-lawyer patent agents to practice law. [Citing *Sperry, In re Ampicillin,* and 35 U.S.C. §§31–33 (1994)] Essentially, the authorization provides the individual with the status of an attorney but only for a limited purpose, i.e. the purpose for which the USPTO registered the non-attorney as an agent to practice before it. *See* 37 C.F.R. §10.6(c) . . . . Thus, by definition, communications between a patent agent and a client beyond that "limited purpose" are not privileged. Therefore, a patent agent's discussions with a client after the patent issued concerning the patent having been infringed or its legal validity if challenged in court are not privileged communications. USPTO registered patent agents cannot defend or enforce patent rights in federal courts."

898 F. Supp. at 475.

The court also addressed whether the attorney-client privilege applied to non-lawyers' practice before the USPTO in the field of trademarks. The court concluded that, under the same rationale that extended the privilege to patent agents, a limited privilege should be extended to trademark practitioners on a case-by-case basis:

"There is a separate regulation for USPTO recognition of a non-attorney as a trademark agent from the procedure for registering as a patent agent. 37 C.F.R. § 10.14. In trademark matters, the recognition of foreign agents exists only for a specific application. . . . There is no USPTO permanent registry for trademark agents as there is for patent agents. In effect the scope of the USPTO recognition defines the scope of the attorney-client privilege. Since the USPTO only recognizes trademark agents for a particular case, an attorney-client privilege will exist only for that particular trademark application."

898 F. Supp. at 475.

Finally, the *Labatt* court offered the following general guideline to determining whether to extend the protection of the attorney-client privilege to non-lawyers practitioners:

"[W]here Congress allows non-attorneys to practice law before federal agencies, a commensurate attorney-client privilege arises over communications with clients necessary to practice in the areas authorized."

898 F. Supp. at 476.

2. Tax law: Taxpayer representatives practicing before the IRS

By statute, the Treasury Department may regulate the practice of representatives of persons in proceedings before the Department. 31 U.S.C. § 330. The Department may require representatives to demonstrate "good character," "good reputation," and "necessary qualifications," and may suspend or disbar representatives from practice. *Id.*

In *Falsone* v. *United States,* 205 F.2d 734 (5th Cir.), *cert. denied,* 346 U.S. 864 (1953), the IRS sought from a CPA documents relating to the tax returns of the CPA's client. The CPA, who was not an attorney, asserted that the attorney-client privilege protected the documents sought from disclosure. The court found that the privilege did not apply. The court noted that, by statute, taxpayers are required to keep certain tax records and that the Commissioner is authorized to examine the books and records of taxpayers. *Id.* at 739. Thus, the court concluded that "even if we should consider the relation between a taxpayer and his certified public accountant as confidential as that between client and attorney, the accountant would, nevertheless, be required to produce the books and records of the taxpayer." *Id.*

The CPA also asserted that "the attorney-client privilege extends to certified public accountants who, like appellant, are enrolled before the Treasury Department." *Id.* In addressing this claim, the court acknowledged

"The Treasury Department has promulgated . . . certain Rules and Regulations governing recognition of attorneys and agents representing persons before the Treasury Department. . . . [which] grant to enrolled agents the same "rights, powers, and privileges * * * as an enrolled attorney" in order to provide for the effective discharge of the duties of such agents."

Id. at 740–41. However, the court observed that:

"There is no provision that a client's communications to an enrolled agent are privileged, ... If, however, the rules and regulations could be construed as so providing, then, it seems to us that they would be in conflict with the statute, 26 U.S.C.A. § 3614(a) . . . and that the statute must prevail."

Id. at 741. Thus, the court denied application of the attorney-client privilege. (This case predates *Sperry* and the line of cases following *In Re Ampicillin* applying the attorney-client privilege to patent agents registered to practice before the Patent Office. We have not found any case authority, however, that applies the rationale espoused in the patent agent privilege cases to non-lawyer practitioners before the Treasury Department or the IRS.)

With respect to communications between tax preparers and their clients, courts have generally denied claims of attorney-client privilege. In *In Re Grand Jury Investigation,* 842 F.2d 1223, 1224–25 (11th Cir. 1987), the court stated:

"Courts generally have held that the preparation of tax returns does not constitute legal advice within the scope of that privilege. [Citations omitted.] We agree with the majority rule. Admittedly, the preparation of a tax return requires some knowledge of the law, and the manner in which a tax return is prepared can be viewed as an implicit interpretation of that law. Nevertheless, the preparation of a tax return should not be viewed as legal advice."

The court distinguished between preparation of a tax return and the provision of legal advice on unrelated tax matters, which would fall within the scope of the privilege. *In Re Grand Jury Investigation,* 842 F.2d at 1225. *See also United States* v.

Bornstein, 977 F.2d 112, 116 (4th Cir. 1992) ("Preparation of tax returns is primarily an accounting service, not a legal one, and accounting services are ordinarily not privileged.").

Another basis cited by courts for denying the attorney-client privilege to tax preparers is that federal statutes require taxpayers to keep tax records and authorizes the IRS to examine such records in connection with a taxpayer's return. *See, e.g., Lustman* v. *Commissioner*, 322 F.2d 253, 259 (3rd Cir. 1963) ("[W]here records relating to tax liability are the subject matter of inquiry, the Internal Revenue Code [26 U.S.C. § 7602] negates any privilege which might otherwise exist."); *United States* v. *Braswell*, 436 F. Supp. 669, 675 (E.D.N.C. 1977) ("[A] claim of privilege by a taxpayer in the face of a proper IRS documentary summons will be unavailing since, by virtue of their character and the rules of law applicable to them, the books and papers are held subject to examination by the demanding authority.'").

3. Lay advocate in special education administrative proceedings

In *Woods on Behalf of T.W.* v. *New Jersey Department of Education*, 858 F. Supp. 51 (D.N.J. 1993), the parents of a handicapped child filed an action against various New Jersey state agencies under the Individuals with Disabilities Education Act (IDEA). Defendants sought to depose the lay advocate (Arons) who had represented the parents in proceedings before the New Jersey Office of Administrative Law (OAL). New Jersey Court Rules authorize non-lawyers to represent parents of children in special education proceedings. The court addressed whether the attorney-client privilege should extend to a lay advocate representing parents in a special education dispute with the New Jersey OAL. The court found that as the action was based on the IDEA, a federal statute, federal common law governed the question of privilege. The court reviewed the status of privilege as applied to non-lawyers and acknowledged that courts had reached conflicting results. After analyzing the purposes of the attorney-client privilege and the particular circumstances of the case before it, the court concluded that it was appropriate to afford attorney-client privilege to the lay advocate.

"The rationale supporting a lay advocate privilege is premised upon the substance of the function, rather than the label. . . . In determining whether the privilege is warranted, courts have considered whether the law expressly authorizes lay advocates to provide the same representation provided by licensed attorneys, whether lay advocates are subject to an extensive system of regulation requiring individual application, proof of expertise, compliance with ethical standards, and direct control by the adjudicative tribunal, and whether the purposes of the privilege are fully applicable to this kind of representation.

"The countervailing policy, adopted by courts declining to extend the attorney-client privilege to lay advocates, appears to be that the need for disclosure requires the attorney-client privilege to be "strictly confined with the narrowest possible limits consistent with the logic of its principle." 8 Wigmore at § 2291."

"This court finds both polices support recognition of a lay advocate privilege in the present case. "Congress manifested an affirmative intention not to freeze the law of privilege. . . . Several factors warrant the existence of a lay advocate privilege in this instance. First, New Jersey Court Rule 1:1–21(e)(8) specifically authorizes lay advocacy before the OAL to represent parents or children in special education proceedings. Similarly, the Administrative Code provides that an application must be made, the OAL has control over the lay advocate and the lay advocate must follow the Rules of Professional Conduct ("RPC"). See N.J.A.C. 1:1–5.4 and 1:1–5.5.

"Certainly, the purpose of the attorney-client privilege is applicable to Arons' representation of the plaintiffs. The purpose of the privilege is to encourage uninhibited discourse between the client and attorney and thereby to enhance the quality of legal service rendered, *Upjohn Co.* v. *United States*, 449 U.S. 383, 389, . . . (1981). The substance of this relationship is one of attorney and client. The necessity of full and frank communications between Arons and the plaintiffs is no less compelling solely because Arons is not a licensed attorney."

"Therefore, the court concludes that the communications between Arons and the plaintiffs while Arons represented the plaintiffs as a lay advocate are privileged to the extent allowed under the attorney-client privilege."

Woods, 858 F. Supp. at 54–55.

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
AL	Code §34-3-1 State bar, County Prosecutor	practice or assume to act or hold himself out to the public as a person qualified to practice or carry on the calling of a lawyer	90-85: Lawyer may not split fees with collection agency
AK	Application of Babcock, 387 P.2d 694 (AK 1963) State bar	Not limited to appearing in court, or advising and assisting in the conduct of litigation, but embracing the preparation of pleadings, and other papers incident to actions and special proceedings, conveyancing, the preparation of legal instruments of all kinds and the giving of legal advise....It embraces all advice to clients and all actions taken for them in matters connected with the law.	None found.
AZ	State Bar of Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 366 P.2d 1 (1961) County Prosecutor	those acts, whether performed in court or in the law office, which lawyers customarily have carried on from day to day through the centuries	

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
AR	Arkansas Bar Assn. v. Block, 230 Ark 430,436, 323 S.W.2d 912, cert denied, 361 U.S. 836, 80 S.Ct. 87 (1959) Supreme Ct	the practice of law is not limited to the conduct of cases in court....[I]t embraces the preparation of pleadings and other papers incident to actions and proceedings on behalf of clients before judges and courts...the preparation of legal instruments of all kinds, and, in general, all advice to clients and all action taken for them in matters connected with law.	None found.
CA	People v. Merchants Protective Corp, 189 Cal. 531, 535, 209 P. 363, 365 (1922) County Prosecutor	the practice of law is the doing and performing of services in a court of justice in any manner depending therein throughout its various stages and in conformity with the adopted rules of procedure. But in a larger sense it includes legal advice and counsel and the preparation of legal instruments and contracts by which legal rights are secured although such matter may or may not be depending in a court.	Most relate to continued practice while under suspension.
CO	Denver Bar Ass'n v. Public Utilities Comm., 154 Colo. 273, 279, 391 P.2d 467, 471 (1964) Supreme Ct	one who acts in a representative capacity in protecting, enforcing, or defending the legal rights and duties of another and in counseling, advising and assisting him in connection with these rights and duties is engaged in the practice of law.	None found.

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
CT	State Bar Assn of CT v. CT Bank & Trust Co., 145 Conn. 222, 140 A.2d 863 (1958) State bar, State Atty, Bar Member	The practice of law consists in no small part of work performed outside of any court and having no immediate relation to proceedings in court. It embraces the giving of legal advice on a large variety of subjects and the preparation of legal instruments covering an extensive field. Although such transactions may have no direct connection with court proceedings, they are always subject to subsequent involvement in litigation. They require in many aspects a high degree of legal skill and great capacity for adaption to difficult and complex situations. No valid distinction can be drawn between the part of the work of the lawyer which involves appearance in court and the part which involves advice and the drafting of instruments.	None found.
DE	Supreme Ct	Delaware Supreme Court created the Board of UPL	UPL 91-16: Paralegals representing clients at administrative hearings before DE Dep't Health & Soc Svcs pursuant to Fed Regs not UPL

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
DC	DC Court Appeals Rule 49(b)(2) Court	"Practice of Law" means the provision of professional legal advice where there is a client relationship of trust or reliance. One is presumed to be practicing law when engaging in any of the following conduct on behalf of another: (A) Preparing any legal document, including any deed, mortgages, assignments, discharges, leases, trust instruments or any other instruments affecting interests in real or personal property, wills, codicils, instruments affecting the disposition of property of decedents' estates, other instruments intended to affect or secure legal rights, and contracts except routine agreements incidental to a regular course of business; (B) Preparing or expressing legal opinions; (C) Appearing or acting as an attorney in any tribunal; (D) Preparing any claims, demands or pleadings of any kind, or any written documents containing legal arguments or interpretation of the law, for filing in any court or administrative tribunal; (E) Providing advice or counsel as to how any of the activities described in subparagraph (A) through (D) might be done, or whether they were done, in accordance with applicable law; (F) Furnishing an attorney or attorneys, or other persons, to render the services described in subparagraphs (a) through (c) above.	See DC Bar Rule 5.5 and Comment.

St	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
FL	State bar, Supreme Ct, State Atty		72-21: Lawyer providing "prototype trust instruments" to nonlawyer mutual fund agents is aiding UPL 95-1: Lawyer may not split fees with a nonlawyer for representation of claimants in soc sec disability cases
GA	Huber v. State, 234 Ga. 357, 216 S.E.2d 73 (1975) County Prosecutor	the practice of law...is not confined to practice in front of the courts of this state, but is of larger scope, including the preparation of pleadings and other papers incident to any action or special proceeding in any court or other judicial body, conveyancing, the preparation of legal instruments of all kinds whereby a legal right is secure, the rendering of opinions as to the validity or invalidity of the title to real or personal property, the giving of any legal advice, and any action taken for others in any matter connected with the law.	21: Lawyers not admitted in GA may not practice in local branch of multi-state firm 23: Lawyer may not delegate responsibility for a real estate closing to a nonlawyer
HI	Oahu Plumbing and Sheet Metal, Ltd. v. Kona Construction, Inc., 60 Haw. 372, 590 P.2d 570 (1979) Atty Gen	the practice of law...consists, among other things, of...the rendition of any service to a third party, affecting the legal rights (whether concerning persons or property) of such party, where such...rendition of service requires the use of any degree of legal knowledge, skill or advocacy.	None found.
ID	State bar		

St	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
IL	Supreme Ct, County Prosecutor		93-15: Employer representation by non-attorney at Il Dep't Employment termination hearings - UPL 94-1: Atty aids in UPL when resolution of problems at closing left to broker 94-2: Solicitation of representation by one not admitted in Il - UPL 94-5: Representation in arbitration by one not admitted in Il - UPL 95-7: Assistance or advice by nonlawyer in completing state corporation forms - UPL
IN	State bar, Supreme Ct, Atty Gen, County Prosecutor, Local bar		None found.
IA	Supreme Ct		
KS	State v. Schumacher, 214 Kan 1, 519 P.2d 1116 (1974) Atty Gen	the practice of law...is the doing or performing of services in a court of justice, in any matter depending therein throughout its various stages, and in conformity to the adopted rules of procedure. But in a larger sense it includes legal advice and counsel, and the preparation of legal instruments and contracts by which legal rights are secured, although such matter may, or may not be depending in a court.	83-5, 85-13: Lawyer may not split fees with collection agency

ST	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
KY	Supreme Court Rule 3.020 State bar, Supreme Ct, County Prosecutor	The practice of law is any service rendered involving legal knowledge or legal advice, whether of representation, counsel or advocacy in or out of court, rendered in respect to rights, duties, obligations, liabilities, or business relations of one requiring the services.	Atty Gen. 77-665: Administrative agencies may prohibit representation by nonlawyers before agency

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
LA	Title 37, § 212 County Prosecutor	The practice of law means and includes: (1) In a representative capacity, the appearance as an advocate, or in the drawing of papers, pleadings or documents, or the performance of any act in connection with pleading or prospective proceedings before any court of record in this state; or (2) For a consideration, reward, or pecuniary benefit, present or anticipated, direct or indirect; (a) The advising or counseling of another as to secular law; (b) In behalf of another, the drawing or procuring, or the assisting in the drawing or procuring of a paper, document, or instrument affecting or relating to secular rights; (c) The doing of any act, in behalf of another, tending to obtain or secure for the other the prevention or the redress of a wrong or the enforcement or establishment of a right; or (d) Certifying or giving opinions as to title of immovable property or any interest therein as to the rank or priority or validity of a lien, privilege or mortgage as well as the preparation of acts of sale, mortgages, credit sales or any acts or other documents passing titles to or encumbering immovable property.	Atty Gen. 91-539: Givis'g legal advice & preparing & recording legal documents = UPL
ME	Atty Gen		None found.

St	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
MD	Business Occupations & Professions Code § 10-101(h) Atty Gen	(1) "Practice law" means to engage in any of the following activities: (i) giving legal advice; (ii) representing another person before a unit of the State government or of a political subdivision; or (iii) performing any other service that the Court of Appeals defines as practicing law. (2) "Practice law" includes: (i) advising in the administration of probate of estate of decedents in an orphans' court of the State; (ii) preparing an instrument that affects title to real estate; (iii) preparing or helping in the preparation of any form or document that is filed in a court or affects a case that is or may be filed in a court; or (iv) giving advice about a case that is or may be filed in a court.	65 Atty Gen. 20 (1980): Nonlawyer may fill out forms before UCC agency, but may not give legal advice, interpret legal docs, or apply legal principles to problems of complexity for client
MA	Atty Gen, DA, 3 Bar Members		
MI	State bar		Atty Gen. 5456 (1979): Not every representation by a nonlawyer before an administrative agency - UPL
MN	Atty Gen, County Prosecutor		

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
MS	Darby v. Mississippi State Board of Bar Admissions, 185 So.2d 684, 688 (Miss. 1966) State bar	The practice of law includes the drafting or selection of documents, the giving of advice in regard to them, and the using of an informed or trained discretion in the drafting of documents to meet the needs of the person being served. So any exercise of intelligent choice in advising another of his legal rights and duties brings the activity within the practice of the legal profession.	25: Lawyer providing client with form collection letters - aiding UPL 209: Law firm may not share legal fees with nonlawyer referral service
MO	Missouri Revised Statutes §484.010	The "practice of the law" is hereby defined to be and is the appearance as an advocate in a representative capacity or in the drawing of papers, pleadings, or documents or the performance of any act in such capacity in connection with proceedings pending or prospective before any court of record, commissioner, referee or any body, board, committee or commission constituted by law or having authority to settle controversies.	None found.
MT	Code §37-61-201	Any person who shall hold himself out or advertise as an attorney or counselor at law or who shall appear in any court or record or before any judicial body, referee, commissioner or other officer appointed to determine any question of law or fact by a court or who shall engage in the business and duties and perform such acts, matters, and things as are usually done or performed by an attorney at law in the practice of his profession...shall be deemed practicing law.	

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
NE	Atty Gen, County Prosecutor		None found.
NV	State bar		Atty Gen. 14 (1983): Representation before appeals officer in WCC by nonlawyer prohibited
NH	Bilodeau v. Antal, 123 N.H. 39, 435 A.2d 1037 (1983) Code 311.1 & Comment 2a State bar, Atty Gen, County Prosecutor	the practice of law is to be determined on a case by case basis A party in any cause or proceeding may appear, plead, prosecute or defend in his proper person or by any citizen of good character 2a. Frequency of lay-representation Although the occasional representation of a party by a lay-person is permitted, the frequent appearance of a nonlawyer in a legal capacity is not permitted	None found.
NJ	Cape May County Bar Ass'n v. Ludlam, 45 NJ. 21, 211 A.2d 780 (1965) Supreme Ct	The exercise of judgment in the proper drafting of legal instruments, or even the selecting of the proper form of instrument, necessarily affects important legal rights. The reasonable protection of those rights, as well as the property of those served, requires that the persons providing such services be licensed members of the legal profession.	None found.

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
NM	State ex. rel. Norvell v. Credit Bureau of Albuquerque, Inc., 85 N.M. 521, 514 P.2d 40 (1973)	indicia of the practice of law, insofar as court proceedings are concerned, include the following: (1) representation of parties before judicial or administrative bodies, (2) preparation of pleadings and other papers incident to actions and special proceedings, (3) management of such action and proceeding, and non-court related activities such as (4) giving legal advice and counsel, (5) rendering a service that required the use of legal knowledge or skill, (6) preparing instruments and contracts by which legal rights are secured.	
NY	Atty Gen		677: Delegation of closing to paralegal not UPL if tasks merely ministerial 679: Lawyer may not compensate client for investigatory services based upon percent of court-awarded legal fees See also, Canon 3: A Lawyer Should Assist in Preventing UPL

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
NC	General Stat. §84-2.1 State bar, County Prosecutor	The phrase "practice law" as used in this Chapter is defined to be performing any legal services for any other person, firm, or corporation, with or without compensation, specifically including the preparation or aiding in the preparation of deeds, mortgages, wills, trust instruments, inventories, accounts or reports of guardians, trustees, administrators or executors, or preparing or aiding in the preparation of any petitions or orders in any probate or court proceeding; abstracting or passing upon titles, the preparation and filing of petitions for use in any court, or assisting by advice, counsel, or otherwise in any such legal work; and to advise or give opinion upon the legal rights of any person, firm or corporation: Provided, that the above reference to particular acts which are specifically included within the definition of the phrase "practice of law" shall not be construed to limit the foregoing general definition of such term, but shall be construed to include the foregoing particular acts, as well as all other acts within said general definition.	None found.
ND	State bar		

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
OH	Land Title Abstract & Trust Co. v. Dworken, 129 Ohio St. 23, 193 N.E. 650 (1934) Supreme Ct	The practice of law is not limited to the conduct of cases in Court. It embraces the preparation of pleadings and other papers incident to actions and special proceedings and the management of such actions and proceedings on behalf of clients before judges and courts, and in addition conveyancing, the preparation of legal instruments of all kinds, and in general all advice to clients and all action taken for them in matters connected with the law.	
OK	E. J. Edwards, Inc. v. Hart, 504 P.2d 407 (Okla. 1973) State bar, Office Gen Counsel	the rendition of services requiring the knowledge and application of legal principles and technique to serve the interests of another with his consent	
OR	State bar		None found.
PA	State bar, Supreme Ct, County Prosecutor		

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
RI	Gen. Laws § 11-27-2 Supreme Ct, Atty Gen	The term "practice of law" as used in this chapter shall be deemed to mean the doing of any act for another person usually done by attorneys at law in the course of their profession, and, without limiting the generality of the foregoing, shall be deemed to include the following: (1) The appearance of acting as the attorney, solicitor, or representative of another person before any court, referee, master, auditor, division, department, commission, board, judicial person or body authorized or constituted by law to determine any question of law or fact or to exercise any judicial power, or the preparation of pleadings or other legal papers incident to any action or other proceeding of any kind before or to be brought before the same; (2) The giving or tendering to another person for consideration, direct or indirect, of any advice or counsel pertaining to a law question or a court action or judicial proceeding brought or to be brought; (3) The undertaking or acting as a representative or on behalf of another person to commence, settle, compromise, adjust, or dispose of any civil or criminal case or cause of action; (4) The preparation or drafting for another person of a will, codicil, corporation organization, amendment or qualification papers, or any instrument which requires legal knowledge and capacity and is usually prepared by attorneys at law.	None found.

St	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
SC	Atty Gen, County Prosecutor		84-03: Corporation owned by lawyer and five nonlawyers that drafts deeds, mortgages, etc. = UPL Atty Gen.: Representation before administrative agencies by nonlawyers held = UPL in 87-57 (Alcohol Bev Cntrl Comm); and 78-207 (Publ Svc Comm)
SD	State bar, Atty Gen, County Prosecutor, Any citizen		None found.
TN	Code §23-3-101 County Prosecutor, Local bar	"Practice of law" means the appearance as an advocate in a representative capacity or the drawing of papers, pleadings or documents or the performance of any act in such capacity in connection with proceedings pending or prospective before any court, commissioner, referee or any body, board, committee or commission constituted by law or having authority to settle controversies.	Atty Gen.: Representation before administrative agencies by nonlawyers held = UPL in 87-58 (Equalization Bd); and 89-95 (Guardian ad litem); Representation not UPL in 88-3 (Dep't Employment Security Appeals)

St	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
TX	Code Section 81.101 Supreme Ct	"practice of law" means the preparation of a pleading or other document incident to an action or special proceeding or the management of the action or proceeding on behalf of a client before a judge in court as well as a service rendered out of court, including the giving of advice or the rendering of any service requiring the use of legal skill or knowledge, such as preparing a will, contract, or other instrument, the legal effect of which under the facts and conclusions involved must be carefully determined.	Atty Gen. M-974 (1977): Representation by nonlawyer before state Insurance Bd Not UPL if authorized by agency
UT	UPL committee		None found.
VT	In re Welch, 123 Vt. 180, 185 A. 2d 458 (1962) Atty Gen, County Prosecutor	one is deemed to be practicing law whenever he furnishes to another advice or service under circumstances which imply the possession and use of legal knowledge and skill. The practice of law includes all advice to clients, and all actions taken for them in matters connected with the law.	None found.

St	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
VA	Rules Part 6, §I State bar, Atty Gen, County Prosecutor	Specifically, the relation of attorney and client exists, and one is deemed to be practicing law whenever --- (1) one undertakes for compensation, direct or indirect, to give another, not his regular employer, in any matter involving the application of legal principles to facts or purposes or desires; (2) one, other than as a regular employee acting for his employer, undertakes, with or without compensation, to prepare for another legal instruments of any character, other than notices or contracts incident to the regular course of conducting a licensed business; and (3) one undertakes, with or without compensation, to represent the interest of another before any tribunal --- judicial, administrative, or executive --- otherwise than in the presentation of facts, figures, or factual conclusions, as distinguished from legal conclusions, by an employee regularly and bona fide employed on a salary basis, or by one specially employed as an expert in respect to such facts and figures when such representation by such employee or expert does not involve the examination of witnesses or preparation of pleadings.	UPL 183: Nonlawyer conducting real estate closing = UPL

St.	Reference & Enforcement Mechanism	Definition of Practice of Law	State Bar Ethics Opinion Examples
WA	In re Droker, 59 Wash. 2d 707, 370 P.2d 242 (1962) Wash. State Bar Ass'n v. Great W. Union Fed. Sav. & Loan Ass'n., 91 Wash. 2d 48, 586 P.2d 870 (1978) Atty Gen, County Prosecutor	The term "practice of law" includes not only the doing or performing of services in a court of justice, in any matter depending therein, throughout its various stages, and in conformity with the adopted rules of procedure, but in a larger sense includes legal advice and counsel, and the preparation of legal instruments and contracts by which legal rights are secured. The selection and completion of legal documents, or the drafting of such documents, including deeds, mortgages, deeds of trust, promissory notes and agreements modifying those documents constitutes the practice of law.	None found.
WV	Code §51-1-4a State bar		None found.
WI	Atty Gen, District Prosecutors		
WY	Supreme Ct		

EXHIBIT B

ATTACHMENT A

DRAFT

TRANSACTION/ACTIVITY	BROKERS	NON-BROKERS	LAW
1. Consult with importer regarding classification, value, origin, of goods, and drawback of duties	Yes	Yes	Yes
2. Prepare ruling request to be submitted by importer to USCS	Yes	Yes	Yes
3. As above, but submitted to USCS by preparer under P.O.A.	Yes	Yes	Yes
4. Meet with USCS on behalf of importer re ruling request	Yes	Yes	Yes
5. As above, with importer present At meeting with Customs	Yes	Yes	Yes
6. Prepare protest or petition pursuant to 19 USC 1514 or 1520 to be submitted by importer to USCS	Yes	No	Yes
7. As above, but submitted to USCS by preparer under P.O.A.	Yes	No	Yes
8. Meet with USCS on behalf of importer re protest or petition	Yes	No	yes
9. As above, with importer present at meeting	Yes	No	Yes
10. Accept employment by importer/ exporter/or other to design operating procedures, systems, and/or computer software to extract and order data from accounting/financial system that will be used for Customs related	Yes	~~Yes~~	Yes

DRAFT

	Broker	Non-Broker	Law
activities. Examples: (a) program that identifies and chronologically lists imports and exports that can be used to obtain drawbacks from USCS: (b) program that identifies products on the basis of mfg. costs incurred; that qualify for preference programs such as NAFTA, CBI, etc.	(a) Yes (b) Yes	Yes Yes	Yes Yes
✓ 11. As above, but computer system produces as finished product documentation which is intended for transmission/submission to USCS without intermediate preparation or manipulation by client or other parties.	Yes	No	No
12. Perform compliance reviews for importer	Yes	Yes	Yes
✓ 13. Meet with USCS on behalf of importer during audit conference or other activity initiated by USCS (i.e., as opposed to Nos. 4 and 8 above).	Yes	No	Yes
14. As above, with importer present	Yes	No	Yes
15. Consult with importer concerning establishment and operation of Customs bonded warehouses, foreign trade zones, Container Stations, etc.	Yes	Yes	Yes
16. Prepare documentation (applications, blueprints, etc.) for importer's use to effect establishment of facilities listed in No. 15	Yes	Yes	Yes
17. Meet with USCS representing importer re establishment of those facilities	Yes	Yes	Yes
18. As above, with importer present	Yes	Yes	Yes

ATTACHMENT A **DRAFT** Page 3 of 4

		Broker	Non Broker	---
19.	Same as Nos. 15 through 18 but client is not and will not be an importer or exporter (e.g.; operator of General Order Warehouse or FTZ operator)	Yes	Yes	Yes
20.	Provide contract services to operate facilities listed in No. 15, in whole or in part	Yes	Yes	Yes
21.	Represent operator of established facilities listed in No. 15 before USCS in regard to any Customs controversy, audit discrepancies, inventories, modifications of boundaries, etc.	Yes	No	Yes
22.	Set up manufacturer/importer/ exporter's drawback program (procedural manuals, ADP system, forms, etc.)	Yes	Yes	Yes
23.	Prepare drawback documentation to support submission of claims to USCS by client	Yes	No	ND
24.	As above, but also prepare claims for submission to USCS	Yes	No	ND
25.	As above, but submit claims on behalf of client to USCS under P.O.A.	Yes	No	ND

ATTACHMENT A

DRAFT

Possible Issues for "Customs Business" Meeting

1. When does "preparation" of an entry begin? Does it include:

a. advice as to what specific information is to be placed in particular box on an entry, without actually writing in the information; NO

b. providing an importer with computer software enabling it to complete and transmit an entry? NO

2. Does the authority contained in proposed section 111.2(a)(2)(b) authorizing a broker to file drawback entries in districts in which it is not permitted also allow the broker to prepare the entry at a location in which it is not permitted? yes

3. Do the provisions of section 111.5 prohibit a broker from representing an importer in connection with an entry for which it was not the filer? NO May a "consultant" represent the importer in connection with an entry? NO

4. May "consultants" file requests for rulings or otherwise represent importers before the Customs Service, if they are neither a broker nor an attorney, if such activity is deemed to be in contravention of State statutes prohibiting the unauthorized practice of law? yes

5. May a carrier or other unlicensed individual file entry or obtain release of merchandise on behalf of an importer? NO

DRAFT

STATEMENT OF CATHY HARRIS

My name is Cathy Harris. My home address is 7593 Watson Bay Court, Stone Mountain, GA 30087. I have been employed with the U.S. Customs Service for 13 years but I am an over 20 year federal employee. I am currently a Senior Customs Inspector, GS–11, assigned to the Atlanta Airport. I have also worked for U.S. Customs in Miami, FL, El Paso, TX and Houston, TX.

I am submitting this written testimony on behalf of an organization called "Customs Employees Against Discrimination Association" (C.E.A.D.A.). I am one of the founders of this organization and the current secretary. I will acknowledge disturbing facts in which I have witnessed first hand and other disturbing facts and concerns that members of the organization have shared with the organization.

I am using the Port of Atlanta as an example of illegal acts by Management nationwide in many Customs Service Ports. The illegal events in Atlanta is going on in many Customs Offices Nationwide. Internal Affairs have refused to investigate many illegal acts even if you report these illegal acts orally or in writing. Internal affairs motto should be "Ignore the Bad and Punish the Good" because this is what this office have been doing for many, many, years. Custom Managers Nationwide are "above the laws" and intentionally and purposely inflicts Mismanagement, Abuses of Authority, Prohibited Personnel Practices, Corruption, Nepotism, Cronyism, Favoritism, etc. Customs Rules, Laws and Regulations and the Union National Agreement Nationwide is not read and followed. Union representatives are also intimidated by Management Nationwide and constantly uses their positions as union representatives to harass union paying employees for management.

Nationwide many employees have reported these managers to Internal Affairs but these managers will turn around and accuse us, the Customs Employees of making false allegations and then management will have Internal Affairs falsely investigate us. Black Customs employees, especially black females Nationwide in the Customs Service are constantly threatened orally and in writing and falsely disciplined by Managers over and over again for: insubordination, failure to carry out a work order, negligent performance of our duties, etc. These same managers physically are striking at us especially if we don't allow them to sexually touch us.

Management Officials from CMC Directors, SES, to GS–15, 14, 13, and 12s are committing perjury during EEO investigations and Administrative Hearings. Many Customs Employees Nationwide have reported these and many illegal acts through the Chain of Command over and over again, to the office of the Attorney General, the Department of the Treasury (orally and in writing), the U.S. Office of Special Counsel, many Internal Affairs offices Nationwide but our cries for help have been totally ignored over many, many years.

Here is my story of how Internal Affairs allowed Managers to run completely and totally "Out of Control" ruining many, many lives along the way:

I did not have much experience with Internal Affairs until I transferred from Miami, FL to Atlanta, Georgia as a Senior Customs Inspector in July 1994. My second day after arriving here, I was pursued sexually by a male Supervisory Customs Inspector, Dale O'Connor, GS–12. As a matter of fact a year before I transferred to the Port of Atlanta, I had came by this Port for an interview with the Port Director. While waiting on a friend in the breakroom, this same Supervisor, Dale O'Connor, GS–12, whom longevity have now reached 18 years in the Port of Atlanta, backed me into a corner so that I could not move. He asked me who I was and I showed him my credentials, and explained that I had just came up for an interview with the Port Director and I was waiting on a friend in which I knew from Miami to arrive to work. This Supervisor asked me all kinds of personal questions, such as how long are you going to be here? Do I have time to go out with him? Then he said maybe he could put in a good word for me? He asked me several intimate questions in which I felt uncomfortable with because he was a Supervisor, GS–12 and I was a GS–11, Senior Customs Inspector. Finally someone came to get me to tell me my friend had arrived to work. I was so relieved to get away from this Supervisor.

On my second day in Atlanta, this same Supervisor, Dale O'Connor, GS–12, spotted me and made a beeline in my direction. He said he remembered me from a year ago when I came out for the interview, and he still wanted a date with me. Again I was uncomfortable and gradually moved away from this supervisor. But over the next, at least 6 weeks, I avoided any area that this supervisor was in because he made me so feel uncomfortable. During this time he even rubbed his body up against mine sexually and kept making remarks to me such as "I like soft women, women who wear makeup." When I worked a position inside the office where only me and this supervisor worked for about 5 hours, I knew I had a problem. This supervisor constantly walked close to me trying to rub up against me. When he was

sitting in the other room at his desk. He stared at me the whole evening. He even made the comment that I should come in an sit on his lap. I tried to stay out of eyeview of this supervisor and avoided him as much as I could that evening and at other times. When I saw him coming toward me, I would even go the other way. Finally he realized after about 6 weeks, that he was not getting anywhere with me, so he started embarrassing me and demeaning me in front of my co-workers, another federal agency employee (Dept. of Agriculture), airline employees and the traveling public. When I worked the roving position where I walked amongst the passengers with my weapon, he followed me all over the airport. Everytime I worked this position and turn around, he would be 10 feet behind me. When I made it a point to move to another area, again he would be 10 feet behind me. No matter where I went while on duty, he would be right there stalking me. Even when I went to the bathroom with unlock doors, I feared that he was going to bust in this room and do something to me. Even though I am a tall female, about 5'8," this Supervisor was well over 6'1 or 6'2. He not only intimidated me with his height, but he intimidated me because he was one of the supervisors in a "position of authority" who would be signing my yearly appraisals.

Finally after the constant stalking, giving me intimidating stares, his demeaning and degrading manner in which I was singled out and treated while my co-workers laughed at me and made jokes, I reported this individual to management for sexually harassing me, creating a hostile work environment against me and illegally putting me in for a Proposed 10 Day Suspension for "Failure to Carry Out a Work Order" and "Insubordination." On January 19, 1995, I filed my initial EEO Complaint along with a Sexual Harassment Complaint. Once I filed the complaints the harassment increased 110% daily. This Supervisor even had my co-workers spread malicious and vicious rumors about me to my co-workers, other federal agencies (Dept. of Agriculture, etc.) and airline employees. These rumors was so vicious and intimidating that everyone all my co-workers was afraid to be seen talking to me. Because of the longevity and seniority of this Supervisor in the Port of Atlanta (18 years now), he answered to noone, not even the Port Director or District Director or now not even the Customs Management Center (CMC) Director. This Supervisor was totally and completely "out of control" and clearly felt he was totally above the law. Everytime the employees saw this individual come out of the office or come from the back they would run away from me. Everyone, my co-workers, airline employees and employees from the Department of Agriculture, told me that this Supervisor had told them stay away from me because they were going to terminate me and discipline them if they were caught talking to me. After Internal Affairs in Miami, the office that oversee the Atlanta Airport for corruption, was notified about the Sexual Harassment, someone made a decision to only do an "Administrative Inquiry" instead of having their office investigate. A management official from Miami, Patricia Goldman, GS–14, called me and told me that she was coming up to Atlanta to investigate the Sexual Harassment Complaint. But because Patricia Goldman took 45 days to come to the Port of Atlanta to investigate the Sexual Harassment Complaint, this Supervisor and the Port Director had called everyone whom they were going to use to write statements against me into the Port Director's office to groom them for their testimony. The other persons who probably would have spoken out on my behalf said this Supervisor, had threatened and intimidated them and told them that if they tell lies about him, he would sue them in court. Many employees had witnessed over the years many acts of Sexual Harassment from this Supervisor to female Airline travelers, female Airline workers and female Customs Employees. But because of the tactic in which this Supervisor had of intimidating and verbally threatening people, many was afraid to come forward. It is my belief that still this female member of management Patricia Goldman, found that this Supervisor indeed sexually harassed females but covered up her findings by telling Internal Affairs and the Port Director that I had lied in my written statements. Excerpts from the Sexual Harassment is attached and more employees stated that this Supervisor Sexually Harasses females than the ones that said he did not harass females (Attachment #1).

After this Sexual Harassment and EEO Complaint came at least 6 more retaliations that followed these complaints. Even though retaliation is illegal, management have continuously for 5 years now and even up until two weeks ago, retaliate against me because I filed the initial EEO Complaint and Sexual Harassment Complaint.

Other Acts of Retaliations during my tenure in Atlanta:

1. February 15, 1995—The NTEU attorney, located in Atlanta, Steve Flig, tried to coerce me into dropping the initial EEO Complaint and Sexual Harassment Complaint by telling me the District Director would only give me a "Letter of Reprimand." But because I knew that with three (3) "Letters of Reprimands," you can

be terminated in the federal government and the fact that I had did nothing wrong, I refused to sign this illegal document.

2. April 14, 1995—Management, Supervisor Dale O'Connor, had an Airline Employee, a Supervisor with the airlines, write a 3 page complaint letter against me. (This was the first and only complaint that I ever received while working this position for two years).

3. April 17, 1995—The ten day suspension was mitigate down to 5 days in which I served while the whole port laughed at me. (I was the only Customs employee suspended in the Port of Atlanta from 1995 to 1998 (3 years).

4. April 24, 1995—Management, Supervisor Dale O'Connor, tried to write me up again when I went to the other Customs Office.

5. May 8, 1995—Management assisted a "Department of Agriculture" (federal government) employee, write a letter containing false statements about me and this employee sent copies to the Port Director and an supervisor. This employee also told other federal agencies, airline workers and my co-workers not to talk to me because U.S. Customs was getting ready to fire me.

6. July 5, 1995—My government weapon was taken away from me for 3 months while the whole port laughed at me. The Range Officer, who had my weapon headed up a pool of employees, who were making bets that I would not get my weapon back.

7. July 28, 1995—I was ordered in writing to go to a physician on August 3, 1995, to undergo a "fitness for duty exam" to get my weapon returned to me.

8. August 4, 11, and 25, 1995—I visited the government doctor on four different occasions. I also took blood screenings, hormone tests, two drug screenings and a pap smear. (I am the only person in the port of Atlanta that have been ordered by management to undergo these types of tests to have my weapon returned to me).

9. August 22, 1995—I was called by the medical nurse and told to report to a psychiatrist office in two days on August 24, 1995. (I was given only two days to report to a psychiatrist even before I received a copy of any of my medical test results).

10. August 23, 1995—I was told by management, Supervisor John Frydrych, that I did not have to go to the psychiatrist office.

11. September 5, 1995—I signed for a letter dated September 1, 1995, from District Director stating that I had to report for a psychiatrist exam on September 18, 1995 or I probably would be terminated.

12. September 18, 1995—I went to a psychologist exam. (I am the only person in the Port of Atlanta that have been ordered by management to undergo this type of exam).

13. October 13, 1995—My weapon was returned back to me after going to a psychologist not psychiatrist. (Meanwhile during this period my name and reputation was further defamed by management, Supervisor Dale O'Connor).

14. April 1996—I was moved from the Atlanta Airport to the Cargo Office because of "Constant Harassment" from management, Supervisor Dale O'Connor and Supervisor John Frydrych (I am the only customs inspector that have had to change offices because of constant harassment from management).

15. September 19, 1996—While working in the only other office that I could work in, management, Supervisor Hugo Rex, not only harassed me weekly, he had a member of the brokerage community write a complaint letter against me.

16. October 1996—I underwent my first "Administrative Hearing" which included 5 different EEO Complaints.

17. January 7, 1997—I wrote a "Hostile Work Environment" letter to management, Process Owner Joanne Fogg, requesting help with harassment from my co-workers, who were not only embarrassing me in front of the public but making statements such as "someone should blow my face off" and calling me a "bitch" when we were alone.

18. March 4, 1997—Another male co-worker, telephonically harassed me, sabotaged my desk and family pictures but management refused to assist me. (This male Customs Inspector served a week suspension during the week of May 30, 1999—July 6, 1999 for illegally tape-recording Employees and Supervisors. This same employee is the reason that I filed my last EEO Complaint in April 1997. This same employee caused another black female to have a nervous breakdown by constantly stalking her in the government vehicle and starting verbal fights with her).

19. March 18, 1997—I wrote a letter to management requesting help from harassment from yet another male co-worker. He constantly made sexual remarks about my body parts while joining in with other males in my office to harass me. In 1996, this male had pulled his government weapon in the parking lot at the bowling alley against his ex-wife boyfriend and went to jail overnight. Because management, Supervisor Dale O'Connor, like this male Customs Inspector, he never was turned into Internal Affairs for being jailed and he was only given so kind of in-house suspension in order to keep the matter from other co-workers. (Two Internal Affairs offi-

cers came out to the Port of Atlanta to investigate the sexual actions of this employee, but like always Internal Affairs would take a report from me, a report from this employee and a report from the Port Director telling them that I constantly made false allegations against employees. So nothing would ever become of any investigations.

20. March 20, 1997—Member of upper management, (CMC Director, GS–15, Port Director, GS–14, Process Owner, GS–13, Chief Inspector, GS–13 and two GS–12 Supervisors), embarrassed me in front of these same co-workers who I had reported to them by orchestrating a "personal attack" against me in a meeting. After this attack which lasted for about 45 minutes, I was severely damaged and is afraid to work in this office again for fear of other personal attacks and threats. (In all my 20 years of federal government, I had never seen such an abnormal and "out of control" display of unprofessionalism by a group of managers especially upper management).

21. June 1997—After I assisted Management with an Internal Affairs investigation by telling the truth about a Pat-Down Investigation and backing up a black female traveler story against a white female co-worker, management and the Union President, a white female, assisted my co-workers with writing a "Petition" against me. Thirty-six (36) out of Forty-six (46) of my co-workers signed a petition stating that they did not want to be assigned any duties with me. The union president, Julia Palermo and a union representative, also signed this petition. (I was severely hurt when I found this petition in my EEO Investigative File when I received it in June 1997).

22. November 14, 1997—I was put in for a s-e-c-o-n-d "Proposed Ten (10) Day Suspension by Supervisor Dale O'Connor. (I am the only employee in the Port of Atlanta that have received two proposed suspensions).

23. January 26, 1998—My new Supervisor, Heidi Nassauer, officially counseled me in writing regarding my excessive leave usage. (In October 1996, the Port of Atlanta hired their first female supervisor, a white female). Other employees especially the union president walked in 20 to 30 minutes late every day but they were never counseled.

24. February 10, 1998—I underwent my s-e-c-o-n-d Administrative Hearing. (I am the only employee in the Port of Atlanta that have undergone t-w-o "administrative hearings" and who have filed a total of 7 EEO complaints.

25. March 23, 1998—Management, my present Supervisor Heidi Nassauer deleted updated security files from my computer. Supervisor Dale O'Connor stole a Customs seal, a Control Accountable Item, from my security office while ransacking the office at least 3 days a week. Internal Affairs was never called even though I reported this theft to Chief Inspector John Young, GS–13. (The black female who worked that position before me, said Supervisor Dale O'Connor often ransacked her desk and bags also).

26. May 18, 1998—I was orally counseled and it was confirmed in writing for entering an office (Supervisor's Office) that all the employees in the Port of Atlanta could enter except me. Management, Chief Inspector John Young, 7B my personnel file. (I was the only employee in the Port of Atlanta that could not enter and exit this office like my co-workers even though I was the security officer for the airport and my door was located only 7 feet from this office).

27. August 3, 1998—I received another (MY THIRD) Proposed Suspension. This one was for five (5) Calendar days for:

Charge 1: Failure to Promptly Report an Alleged Improper Search to Management or to Internal Affairs (Management in the Port of Atlanta knew these abuses had been going on for a very long time. The Supervisor over this team was Supervisor Dale O'Connor).

Charge 2: Providing Conflicting Information to Management and Internal Affairs regarding a Personal Search. (Management did not miss a chance to lie in an Internal Affairs or EEO investigation and during an administrative hearings).

28. September 14, 1998—I wrote a Letter of Intent to file an "Unfair Labor Practice/EEO" because management allowed the union representatives to abolish the positions that I would have selected during the rotation even though I had the seniority to get these positions.

29. October 1998—I was given yet another Supervisor, George Robinson, GS–12. Each Supervisor tried to break me just a little bit harder than the one before. The first day that George Robinson took over as my supervisor, he called me in his office and used profanity against me and told me to stop filing EEO Complaints and that he was going to suspend me or terminate me if I did not get any seizures. I went to get a union representative but could not find one and then brought a friend in his office with me while he brought another supervisor in the office with him. Still he continued to demean and degraded me in front of these two persons.

30. November 9, 1998—I responded to two demeaning cc-mail messages from Supervisor George Robinson, which I felt where only written to harass me.

31. November 18, 1998—I received a response from Chief Inspector John Young for a transfer to the cargo office. He responded negatively.

32. December 1, 1998 —I was suspended for 1 day for failure to report an Abusive Patdown and providing conflicting information to management. On this day, I arrived for work on the 1:00 pm—9:00 pm shift. When I arrived at 1:00 pm, Supervisor George Robinson approached me in front of all my co-workers (about 20 employees), threw a letter on my desk and yelled at me to leave, that I was on suspension. "You are not suppose to be here!" he yelled at me. Then he said, go now! Then he said I am ordering you to go home or we will discipline you again. I said let me call my children first. He then said NO! Use the phone on the street! Go home now! But I had never received or reviewed a Suspension Letter for a 1 day suspension before that day.

33. January 11, 1999—I requested copies of a letter for another Proposed Suspension for 14 Calendar days (fourth (4TH suspension), which was dated January 8, 1999. This suspension letter came from Supervisor George Robinson.

Charge 1. Disrespectful Behavior

Change 2. Failure to Follow a Direct Order

34. February 1, 1999—Port Director John Deegan and Supervisor Steve Babbie embarrassed me in front of about 20 of my co-workers by trying to give me a disciplinary letter in front of them. I asked the Port Director if I could get a union representative and go into a room, but he replied no. I walk away to find a union representative. The next day when I arrived for work for Overtime in the morning a Suspension Letter for 2 weeks for me was posted on 3 different bulletins boards where all the Customs Inspector desks are located. After taking the suspension letter down and faxing it to the union attorney, the union attorney told me that management was setting me up for termination. I told the union attorney to do something about it. And he said he could not and then he hung the phone up on me. I called his office over the weekend and left a message, telling him if he even let management suspend me for 1 day, I would "Go to the Media."

35. February 1, 1999—I filed an Alternate Dispute Resolution (ADR) (Grievance) with the local NTEU because Supervisor George Robinson had wrongfully embarrassed me in front of my co-workers and illegally docked my pay for two hours of overtime.

36. February 1, 1999—Because I filed an Alternate Dispute Resolution (ADR)/ Grievance with the local union, I received a letter from Chief Inspector John Young stating that the suspension for the 14 days would begin on February 24, 1999.

37. February 9, 1999—I received a letter from local union attorney saying that he was going to invoke arbitration on the proposed 14 days suspension so they could not suspend me at that time. I have not heard another word from union attorney Steve Flig.

38. April 1999—I was told by several of my co-workers that Julia Palermo was taking another petition around the port and soliciting my co-workers to sign it. Forty-four (44) of my co-workers signed this petition against me and copies where sent to the Commissioner of Customs, Congressman John Lewis, Congressional Cynthia McKinney and Rainbow Coalition, Southern Regional Manager Joe Bishop.

39. April 9, 1999—I wrote another memo requesting that I be assigned another immediate supervisor other than Supervisor George Robinson because he had been taunting me almost daily since October 1998, that he was going to get me suspended and terminated.

40. May 1999—The entire port attended a Customs Management Center (CMC) roundtable. CMC Director, Mamie Pollock, held several roundtables meetings with all the employees in the Port. Before my Roundtable Meeting on May 10, 1999, Monday, SEVERAL, of my co-workers had told me that the CMC Director, Mamie Pollock, SES, was passing around a report with my name in it. Then they told me that my name was the only employee name in this entire report. When I attended the meeting on May 10, 1999, I asked the CMC Director why was she passing around a report with only my name in it, telling all my co-workers even the new people who did not know it that I had been disciplined. Her response was, that the report came from Linda Batts, Special Assistant to the Commissioner of Customs. (Even if she did not make the report up, she did not have the right to pass it around to the entire port once again in an effort to create a "Hostile Work Environment."

41. May 23, 1999—Because I was an hour late for overtime on Sunday, management, Supervisor Hugo Rex sent me home and would not allow me to work even after another Inspector had explained that the same situation happened to him and he was allowed to work.

42. May 27, 1999—I wrote a letter to management trying to keep from filing an Alternate Dispute Resolution (ADR)/Grievance in order to get paid overtime for this day on Sunday, May 23, 1999. I never received a reply back.

Everytime I was put under a new supervisor, Supervisor Dale O'Connor would constantly coach them on how to write me up. He has went around the port for five years threatening me orally that he would have my current supervisor write me up. He still is harassing me and a few months ago, he again rubbed up against my backside. Since the Sexual Harassment investigation, this supervisor have been suspended twice and it was proven that his team at the Atlanta Airport was harassing black travelers. But yet this male is still allowed to work and harass me and others in the Port of Atlanta. I told Internal Affairs of instances when I had female witnesses names, black and white who this male had gotten terminated from their jobs around the airport because they would not allow him to flirt with them but Internal Affairs never responded to me. All the employees in the port have witnessed years and years of this supervisor "sexual carousing and the mannerisms of a "sexual predator", but Internal Affairs have refused to "hold these managers accountable for their illegal actions. My co-workers and I reported orally and in writing many incidents to Internal Affairs in Washington and Miami that should have been investigated but they simply would not even return our calls or told us that the matter had been investigated. All this office of Internal Affairs ever did is to say they were to take a report and leave but never assisted me with any form of harassment from any of these managers. Everytime I got a new supervisor, Supervisor Dale O'Connor would coach and intimidate them on ways in which to write me up. My co-workers in Atlanta and I reported a single female supervisor, GS–12, who was dating a married Senior Customs Inspector, GS–11 to Internal Affairs in both of these offices, Washington and Miami, because they were upsetting the whole part because of their affair. What this female supervisor was doing was cheating on the overtime by leaving this male on overtime when my co-workers and I should have been on overtime. I, myself, turned her into the Chief Inspector, GS–13, John Young, her superior, about 5 times for apparently and purposely leaving me off the overtime and putting this male on so they could ride to and from work together. This manner in which this female was cheating on the overtime, lasted over two years and we had no one to report her illegal acts too because Internal Affairs did not care. This Supervisor would ride to and from work with this male and be in her office behind closed doors with this male with blankets and pillows and would not allow us to have a break. This male was only her boyfriend but he sat around the Supervisor's office as if he was a supervisor and did not do any work. But meanwhile, me and others who her boyfriend did not like was constantly harassed by this female Supervisor. This affair caused so much animosity amongst the Customs Inspectors and it is still going on today. When we called Internal Affairs to see if they had come out to Atlanta to investigate the apparent, illegal, manner in which she was giving this male overtime, they said they did investigate by only making a call to the port director, John Deegan, and he told them that these illegal acts where not going on. This is the manner in Atlanta and nationwide that Internal Affairs conduct investigations. Supervisors get every other weekend off in Atlanta but they made the Customs Inspectors work 10, 11, 12, 13 days straight and then they might draft us to work on our day off. Management never tired to revamp the system so the Customs Inspectors could get a "good quality of life" because they simply and only cared about themselves. Ex-Port Director, made many illegal promotions which generated many, many EEO Complaints in the Port of Atlanta. One female who went to school with the Port Director's daughter was given 3 different jobs in one year. Another female who went to school with his daughter was promoted quickly. Many employees where promoted over much more qualified Customs Employees. The Port Director allowed the Supervisors to vote to promote an employee if they like these employees not on their background, education or experience which again is illegal. Double standards and Sexism occurred quite often, when only females weapons was taken away. Many Customs employees who had apparently committed criminal acts was only given slaps on the wrist. But other innocent employees, had to file many, many EEO Complaints just to be able to hang onto their jobs. Many Customs Employees future in the Customs Service.

Attachment: Excerpts from Sexual Harassment Investigation in 1995.

EXCERPTS FROM U.S. CUSTOMS ADMINISTRATIVE INQUIRY

The following comments were taken from written statements made by Customs employees and other airport employees interviewed during the Internal Affairs in-

vestigation into the sexual harassment/hostile work environment complaint initiated by Cathy Harris:

As it relates to Mr. O'Connor, I have found him to be a good supervisor and feel he is always fair. I have never seen him do anything to anyone that I would consider sexual harassment. I have noticed that the stewardesses and Mr. O'Connor flirt in a friendly way. MLB

I have been under the supervision of Dale O'Connor for eight years. In my opinion, Dale is the best supervisor in the Port of Atlanta. I have never seen Dale touch a female employee in any sexual manner. He does FLIRT with the airline employees, including flight attendants. He knows a lot of flight-attendants and is married to one. Sometimes the flight attendants come up to him and hug him in greeting. He has never sexually harassed anyone. CM

Mr. O'Connor was my supervisor when I was assigned to the Customs Mail facility in Atlanta. During the year he supervised me I filed an EEO complaint against him that was settled during the counseling stage. The complaint was not sexual harassment.

She asked if it was true that I had filed a sexual harassment complaint against Mr. O'Connor. I said that I hadn't. She asked me what the circumstances were. I told her Mr. O'Connor had made a comment about my hair that contained a reference to a SEXUAL AREA. I emphasized the comment had occurred over 4 years ago and that there was no repeat of any further comments. When I was around him I never saw him not performing his job. I never saw him touch anyone. LR

On several occasions I saw Mr. Dale O'Connor standing in front of the escalator, looking at every flight attendant that would come down. On a few occasions, I saw him pat the flight attendants on the behind as they walked past. I assumed he knew them well, he seemed to be very comfortable doing that. KDR

Since his arrival in the Port of Atlanta, Supervisor Dale O'Connor has portrayed himself as a ladies man. Almost immediately, he was observed maneuvering his way into strategic positions which would allow him the opportunity to better view pretty girls arriving on flights. He always made it a point to be out of his office and in position whenever those flights from the Caribbean countries and any area where very little clothing is worn, would arrive. Often he would follow closely behind females skimpily clad, as they made their way to the exit gawking at them and if smiling at them as it to suggest a desire to become more intimate. He never failed to position himself at a secondary counter whenever a pretty female was being examined. Because on secondary, females wearing little clothing, often inadvertently display parts of their bodies. Often this ploy is used to distract the Customs Inspector from his task of inspection. Supervisor O'Connor never missed the chance to watch. Passengers often asked, innocently, after he left, "why was he staring at me?" O'Connor would often come back by and comment "Not Bad!"

Inspectors quickly learned that flight attendants were protected by O'Connor and placed on earth for his pleasure. In the old terminal he wouldn't allow any inspectors to inspect or process them as they waited in line. He would be observed signing their declarations and expediting the pretty ones out of Customs. Flight attendants would ask for him by name whenever they needed to avoid the long lines. O'Connor used his authority and the protection offered by his position to obtain dates from the female attendants. His carousing cost him 2 marriages. He is presently married to an international flight attendant.

When the law was changed as to the exemptions allowed flight attendants (from $25 to $200) O'Connor argued and enforced an improper application of the law until it was brought to the attention of the Chief Inspector, John Young, who corrected him. It is my belief that he only wanted to protect those attendants so that he might get favors from them.

O'Connor's womanizing is well-known and observed by many. His lack of professionalism as displayed by his weakness for short skirts and low-cut blouses directly impacts on the entire workforce. GR

I have indeed witnessed O'Connor hugging females as they came off a flight but this was not always solicited by him. Often female flight attendants hug O'Connor as a gesture of friendship. JS

I have worked with Dale O'Connor from the time he arrived in Atlanta until May 1994. He has never personally sexually harassed me, but his actions to other females is questionable. It is a known fact and known by management that he has an eye for females. Many times during the day while cleaning aircraft he is known for expediting and actually signing off the declaration for the female crew while making the male crew stand in line. Whenever an attractive female enters the room he would follow them with his eyes from the time she entered till she would leave. He would look her up and down as if undressing her. One time the Dallas Cheerleaders came in and he personally cleared all of them himself. (Supervisors are not

suppose to act as an inspector and clear anyone, they are only suppose to supervise) but he would clear whom he pleased.

One clerk had to quit her job because she could not work with Dale O'Connor any more. She wrote a 4 page letter to management but they failed to take action. She personally told me she could not work with him. He made comments to her that she needed a MAN and he had the right EQUIPMENT or words to that effect, to handle her problems. I believe he thinks as a supervisor he is untouchable, and will get back at you. CBW

I witnessed on many occasions, Dale O'Connor relentlessly pursue and stalk flight attendants of every airline that operated on T Concourse and E Concourse, in Hartsfield Atlanta International Airport since approximately January 1993. Regardless of his title or rank, I constantly observed him apply special attention to the need of any female flight attendant and fall short of his duties as a U.S. Customs Inspector. In my experience as a Customer Service Agent for Delta Air Lines, it is conceived that his actions are that of a person who walks the gray line of flirting and sexually harassing someone. I have a mother, numerous aunt's and a wife. His actions are not needed in the work place! DJ (Delta AA EMPL)

I, on various occasions during my tenure in Atlanta, have witnessed Supervisor Dale O'Connor flirting unprofessionally with the women who work at the airport and the airline stewardess who travel through the airport. He makes uncalled-for jokes which are inappropriate as a Supervisor for Customs. This kind of unprofessional conduct has been going on for a long time. RM

I have observed Dale O'Connor for eleven years and have not seen him grab or fondle any woman. He does spend time talking to flight attendants, airline employees and Customs Women employees and appears to enjoy their company greatly. O'Connor makes every effort to meet any new female visiting the Customs work area. JZ

I have witnessed Supervisor Dale O'Connor from the Customs Service on several occasions staring at the backside of women, tilting his head back and forth in an unprofessional manner as they walked up the stairs. Dale O'Connor would also stare at the females in a sexual suggestive manner and pat stewardess on their behinds as they walked past him. He seemed to be very comfortable with his behavior. YW (DEPT AGRI)

STATEMENT OF THE JOINT INDUSTRY GROUP

INTRODUCTION

On behalf of the Joint Industry Group (JIG), these comments are submitted to the United States Senate Finance Committee in response to the May 13, 1999, US Customs Service oversight hearing. JIG is a coalition of more than one hundred and fifty members representing Fortune 500 companies, brokers, importers, exporters, trade associations, and law firms actively involved in international trade. JIG membership represents over $350 billion in annual trade. The JIG enjoys a close and cooperative relationship with the US Customs Service and frequently engages Customs on trade-related issues that affect the growth and strength of American imports and exports.

These comments address the position of the Joint Industry Group regarding the Customs Service's dual mission of effective border enforcement and trade facilitation promotion. This statement also comments on Customs' efforts to modernize its aging automated processing systems with a modern, efficient system which is vital to the continued strength and stability of the US economy.

We commend the US Customs Service for its continued efforts in satisfying its two main missions of border enforcement and the facilitation of international trade. The success of Customs' enforcement programs such as Operation Brass Ring demonstrate Customs' capabilities in preventing the movement of illegal drugs and contraband into the United States without causing costly delays in time and money to the vast majority of importers and exporters who comply with Customs regulations.

JIG also continues to support Customs successful work to ensure that its computerized systems are Year 2000 compliant. Although small, localized problems resulting from the changeover to the Year 2000 are likely to occur, we are confident that the Customs Service is sufficiently prepared to address and quickly solve any difficulties that arise.

CUSTOMS MODERNIZATION ACT

For several years since passage of the Customs Modernization Act (Mod Act), JIG has worked closely with the Customs Service as it has developed new programs and

initiatives to fully implement Mod Act legislation. Passed in 1993, the Mod Act placed added compliance responsibility on industry. This included industry accepting the responsibility for classifying goods, exercising reasonable care, developing corporate account-based systems, assigning merchandise value, determining the country of origin, and identifying duty rates of imported products. The Administration, through the Customs Service, agreed to provide methods to facilitate the process by enhancing automation systems to accommodate the new requirements. This added new meaning to the term "trade facilitation." It was not a term that indicated a regress of Customs enforcement policies, rather it alluded to the Customs side of the agreement. While industry has fulfilled its side of the Mod Act, at a cost of tremendous additional resources and expenditures, the Customs Service has been unable to provide the most important component of its side of the agreement—automation. At this point, industry can only continue to hope that the Automated Commercial System will last long enough for Customs to develop its successor.

AUTOMATED COMMERCIAL SYSTEM (ACS)

JIG membership continues to be concerned about the aging Automated Commercial System (ACS). ACS is more than 16 years old and is experiencing brownouts, delays, and declining service with increased frequency. A major blackout or "crash" of the system will have devastating effects on companies, the environment, and the economy.

For many of our member companies, a one-day shut down of ACS will cause disruptions. A prolonged ACS blackout of more than a day or two would halt production lines and cause serious delays in shipping needed goods to customers. An inactive assembly line is a scenario that will face many of JIG's manufacturing company members. General Motors, DaimlerChrysler, and Ford Motor Company will be forced to shut down production lines at a much earlier date than most companies because of their high volume just-in-time-delivery procedures. In fact, miles of trucks backed-up across the Texas, California, New York, and Michigan borders is certain to occur during a major shut down of ACS. Imagine the potential impact to the US economy and US workers if production comes to a halt in our major US manufacturing companies.

THE AUTOMATED COMMERCIAL ENVIRONMENT (ACE)

The system intended to replace ACS, the Automated Commercial Environment (ACE) has been scrutinized for years. JIG members have taken an active role in ACE development and funding since the passage of the Mod Act. Our organization has participated in the Customs Service's Trade Support Network Conferences (TSN's) that have given industry an opportunity to ensure that each sector's automation needs are addressed. Industry advised Customs to adopt a modular approach to the ACE design, and Customs has done so. We suggested that Customs outsource the construction of ACE to an information technology firm specializing in automated systems. Customs has concurred and is preparing a request for proposal with the help of a Federally Funded Research and Development Contractor (FFRDC). Overall, we have been pleased with the Customs approach to this point.

CUSTOMS SERVICE FY 2000 BUDGET

The President's proposed FY2000 budget for Customs Service automation systems is a misguided attempt to further tax US business. The proposed new tax, termed a "user fee" by the Administration, is illegal under the NAFTA agreement with Canada and Mexico. It conflicts with the Treasury Department's own mission of reducing the amount of data required for imports under the International Trade Data System (ITDS). ITDS seeks to reduce the amount of data required, while the proposed budget taxes the amount of data sent. The two objectives are contradictory.

The tax would place an additional burden on an industry that has already contributed $800 million a year for the last ten years in Merchandise Processing Fees (MPF). A portion of the MPF should have been used to build and implement Customs' automated systems. Furthermore, the President's budget proposes to fund automation at a level that is less than half of the amount genuinely needed. We are disappointed in the Administration's inability to assume a leadership role in the development of mission critical Customs systems.

JIG is pleased with the recent passage in the House of Representatives of HR 1883, the Trade Agency Authorizations, Drug Free Borders, and Prevention of On-Line Child Pornography Act of 1999, which authorizes $150 million in both FY2000 and FY2001 for ACE development. While this is only an authorization for a portion of the required funds, it is movement in the right direction.

This bill will now come to the Senate and this Committee where funding must also be authorized. We are confident that the Senate Finance Committee agrees with this authorization, but it is also our hope that the Senate can be persuaded to double the authorization to $300 million annually. Customs estimates that ACE development will cost $1.2 billion over the next four years. To satisfy funding requirements, $300 million needs to be authorized and appropriated for FY2000 and continued annually through FY2003.

While funding ACE is of utmost importance, funding should be authorized by this Committee to ensure that ACS remains operational until ACE is fully developed. Current funding for needed ACS maintenance and upgrades is not sufficient. In FY2000, a minimum of $79 million is necessary just to maintain ACS. The President's budget proposed $35 million with an additional $32 million in base funds. This represents a deficit of $12 million. We urge the Committee to authorize these funds in addition to the money needed for ACE development.

CONCLUSION

In FY1998 the Customs Service processed over 20 million shipments of import merchandise with a value of nearly $1 trillion. From these imports, the government has collected over $800 million annually through the Merchandise Processing Fee. Industry has already paid many times over for an automated processing system, provided for in the Mod Act, that should already be built and operational.

With the amount of trade volume expected to double by 2005, time is short to develop funding solutions sufficient to bring ACE fully operational. Processing the increased volume of trade efficiently while at the same time enforcing US border regulations can only occur if funding for needed automation systems begins now. We are confident that ACE is the long-term solution to this problem, but will only become a reality if Congress and the Administration can fully fund its development in a four-year timeframe.

The Joint Industry Group and its membership thank the Senate Finance Committee for the opportunity to submit these comments.

STATEMENT OF THE NATIONAL ASSOCIATION OF FOREIGN-TRADE ZONES

Mr. Chairman and Members of the Committee:

On behalf of the National Association of Foreign-Trade Zones (NAFTZ), thank you for the opportunity to present this statement to this Committee hearing on U.S. Customs Service issues. My name is Karen Sager. I am the President of the NAFTZ.

The NAFTZ is a nonprofit trade association representing over 700 members, including grantees, operators, users and service providers of U.S. foreign-trade zones. Today there are more than 200 approved zone projects located in all 50 states and Puerto Rico. The total value of merchandise received at foreign-trade zones annually is approximately $180 billion. The total value of merchandise exported from foreign-trade zones is approximately $17 billion. Over 2,900 firms utilize foreign-trade zones and employment at facilities operating under FTZ status exceeds 367,000 jobs. The NAFTZ provides education and leadership in the use of the FTZ program to generate U.S.based economic activity by enhancing global competitiveness.

The growth in the number of zone projects throughout the United States and the increased use of those projects by U.S. based companies is a strong indication of how important participation in the international marketplace has become to the U.S. economy. A key to the success of those endeavors is the ability to move merchandise quickly and cost effectively with a reasonable degree of predictability. Critical to that movement is the processing of merchandise by the U.S. Customs Service.

The Customs Modernization and Informed Compliance Act, commonly referred to as the "Mod Act," was passed in November 1993 to give the U.S. Customs Service the tools that it needed to streamline and automate its commercial operations. There were two major elements to Customs' "modernization" efforts—the revision of the regulations themselves to eliminate obsolete or unnecessary procedures and requirements, and the development and implementation of the systems needed to support the revised regulations that now govern the movement of merchandise across U.S. borders.

Customs has made significant progress in rewriting and revising its regulations to incorporate the changes envisioned in the Mod Act. To their credit, Customs has involved the trade community in their efforts in order to develop regulations that address both the needs of Customs to ensure compliance and the needs of the trade community to be able to move their merchandise smoothly, efficiently and predictably. Trade has responded with increased compliance and by developing their systems and procedures to address Customs' requirements.

Within the foreign-trade zone program, the NAFTZ has worked with Customs on the development and testing of a procedure that embodies all of the principles envisioned in the Customs Modernization Act. In 1991, a proposal was made to Customs to extend weekly entry processing to non-manufacturing zones, a procedure available to manufacturing zones since 1986. With the passage of the Mod Act, Customs initiated a pilot program to test the viability of such a procedure. Included in the proposed regulations was a requirement that in order for a zone to be approved for this procedure, the zone must provide Customs in advance with information related to the merchandise processed through the zone under this procedure. This pre-information allows Customs to evaluate the compliance level of merchandise moving through the zone in an orderly, structured environment rather than randomly as shipments occur. Additionally, zones approved for this procedure were required to file all entries electronically and to make duty payments through Customs' Automated Clearing House System. The agreed upon objective of the procedure was "to reduce the number of entries from zones as well as automate and expedite the processing of such entries." At the conclusion of the three year pilot, the weekly entry procedure for non-manufacturing zones was deemed an operational success by Customs.

However, Customs headquarters initially delayed the final implementation of this procedure for two years and has recently withdrawn the proposed final regulations for implementing this procedure. Customs cites as its justification for withdrawing these regulations its perception that processing fewer entries from non-manufacturing zones would have a significant impact on its collection of merchandise processing fees (MPF) since fewer entries would be processed. The NAFTZ believes that reducing the frequency of entries processed for the same merchandise from one per shipment to one per week in conjunction with increased automation provides Customs with opportunities to improve its operational efficiency thus decreasing its cost of operation. Because Customs has no cost accounting system in place for its commercial operations, it has not been able to assess the true financial impact of implementing a weekly entry procedure. Therefore, Customs has chosen to forego the demonstrated operational efficiencies afforded by weekly entry simply because retaining individual entries may generate more MPF than a weekly entry. This basis for decision making appears to be contrary to the Customs environment envisioned when the Mod Act was passed in 1993. The NAFTZ believes that Customs must focus its efforts on creating an effective, efficient Customs Service that carries out its dual mission of protection of our borders and the facilitation of trade that is vital to our country's economy. We believe that it is the role of Congress to provide the funding required to support this mission.

The second critical element of the Mod Act was its mandate to improve the automation of the Customs Service operations enabling them to meet the demands of the increasing volume of trade in the most cost effective manner. It is now time for Congress to authorize and appropriate the resources to the Customs Service to enable them to develop and implement the systems necessary to realize the full benefits envisioned in the Mod Act.

Customs' current system, the Automated Commercial System (ACS), is a 15 year old system that is now operating at 90%+ of its capacity. There have been several instances of system "brownouts" and failures that have impacted the movement of critically needed merchandise to U.S. based production faciilities causing production slowdowns with a potential loss of employee earnings. It is only a matter of time before ACS experiences a prolonged shutdown with the potential for a severe negative impact on the U.S. economy.

The U.S. Customs Service has been working with the trade community to develop a replacement system for ACS. Their efforts to date have come under a great deal of criticism principally for a lack of cost accountability and a lack of written plans for development, evaluation, implementation and ongoing monitoring for their proposal. While the NAFTZ agrees that these weaknesses must be addressed, the international trade community cannot afford to wait much longer for the unveiling of a "perfect" system. Customs' proposed system, the Automated Commercial Environment (ACE), in conjunction with the International Trade Data System (ITDS), successfully addresses many of the processes and procedures needed to implement the full benefits of the Mod Act. The NAFTZ therefore urges Congress to support the step by step authorization, appropriation and release of the funding required to address the identified weaknesses in ACE so that a new Customs automation system can be designed, evaluated, developed and implemented within the next four years. Oversight by Congress, with continued input from the trade community, should be a condition of the authorization, appropriation and release of these funds.

In the President's proposed FY2000 budget, there is a request for a new user fee to fund Customs' automation. This user fee has been proposed *in addition to* the

current merchandise processing fee (MPF) which was established to offset the cost of commercial operations. We object to this proposal for two reasons. First, the NAFTZ believes that the amount of money currently being collected from the importing community through the MPF should be more than adequate to cover Customs' cost of automation. More importantly, the underlying structure for this proposed user fee shares the same problems inherent in the current merchandise processing fee assessment.

The current MPF is assessed on an entry by entry basis. Simply put, if Customs processes more entries, more MPF is collected. Customs defines what constitutes an entry. Therefore, if Customs wants to collect more revenue, it can cause more entries to be processed. This becomes a disincentive to the implementation of modernization measures designed to increase productivity and maximize efficiency. It is exactly this type of logic that led to Customs' failure to move forward on the implementation of the weekly entry procedure for non-manufacturing zones.

In addition, the MPF lacks accountability. The MPF collected is directed to the General Fund rather than being dedicated to the cost of Customs' commercial processing. Further, there is no cost-basis accounting system to ensure that there is a correlation between the actual cost of the service and the fee collected. This type of approach to assessing user fees is subject to challenge by members of the World Trade Organization (WTO). Under WTO guidelines, user fees assessed on international goods must be justified by the cost of the services provided for that fee. Since there is no cost accounting system in place, Customs is not only unable to justify any additional user fees, it cannot cost justify the fee that is currently being assessed on importers today. Furthermore, there is nothing to substantiate Customs' claim that the MPF is a user fee dictated by costs rather than a tax placed on imports.

In summary, the National Association of Foreign-Trade Zones asks Congress to direct the U.S. Customs Service to continue to move forward with procedures and regulations that will improve the efficiency and effectiveness of its operations such as weekly entry procedures for non-manufacturing zones. The NAFTZ also urges the Congress to authorize and appropriate adequate funding to allow the U.S. Customs Service to correct the weaknesses identified in the proposed Automated Commercial Environment (ACE) and to move forward with the final design, evaluation, development and implementation of this new system in conjunction with ITDS. We believe that automation is an integral part of Customs' commercial operations and, as such, the merchandise processing fee currently being collected from importers should be used to fund it. The NAFTZ also believes that the time has come for Congress to reexamine and restructure the basis for the assessment of the merchandise processing fee so that the MPF collected is not dependent upon the number of entries processed by Customs. Instead, it must be based on what Customs needs to effectively fulfill its dual missions of trade facilitation and enforcement within its commercial operations. Until this cost justification is in place, no new fees or taxes should be approved.

Thank you for the opportunity to comment on these important issues.

STATEMENT OF THE NATIONAL CUSTOMS BROKERS AND FORWARDERS ASSOCIATION OF AMERICA, INC.

[SUBMITTED BY PETER H. POWELL, SR., C.H. POWELL COMPANY]

Mr. Chairman, I am Peter H. Powell Sr., of the C. H. Powell Company, a logistics company whose services include customs brokerage. I am also President of the National Customs Brokers and Forwarders Association of America (NCBFAA).

As you well know, Mr. Chairman, from our many years of working together, a customs broker acts on behalf of an importer in its obligations to the Customs Service: filing information, paying duties and ensuring compliance with the laws of the United States. This role has led to a very close relationship between a customs broker and a customs official, and between the NCBFAA and the U.S. Customs Service. We are "force multipliers," handling 95% of all commercial entries. A professional, customs broker, by virtue of his acting as the link to Customs for hundreds of importers, greatly simplifies the task for Customs of handling, this year, 21 million entries and provides the best possible assurance that information is complete, accurate and timely.

We have long known that Customs automation is essential to these processes. While we heard "automate or perish" long ago, brokers quickly understood the criticality of this tool and worked in harmony with Customs to develop ACS—the Automated Commercial System. Jointly, Customs and the broker community were re-

sponsible for its early development and then its evolution over almost two decades. Recently, however, it has become clear to our community that ACS is in trouble—and we who are on the front lines became aware of this first. The most obvious sign of ACS' inability to keep up with rapidly increasing volumes (entries will double between 1994 and 2001 and nearly triple by 2005) has been the brownouts and outages experienced in this past year. Yet, ACS has other limitations caused by aging technology coupled with expanding demands for better and more sophisticated performance. In many respects, ACS' successor system, the Automated Commercial Environment (ACE), sounds like something different. In fact, it's merely modernization of what is—frankly—antiquated. Yes, there needs to be new hardware and software; however, the customs process itself remains functionally the same, albeit more efficient and improved to cope with work loads that increase at an alarming pace. ACE can increase productivity through faster processing of information. ACE increases flexibility by permitting resort to other tools for processing information—such as the Internet, for example. ACE improves interfaces with the private sector and with 104 other federal agencies. And, ACE helps implement those processes that this committee has mandated through laws such as the Customs Modernization Act.

Let's assess the cost of inaction. We customs brokers can tell you that trade will come to a crashing halt if ACS collapses under the weight it must now bear. This extends not only to imports but also to exports. This affects not just foreign, but American businesses. It involves domestic manufacturers dependent on imported parts or foreign markets. It will be catastrophic to American retailers, now reliant on "just-in-time-inventory," who will find their warehouses empty while their goods pile up at America's docks and airports.

Unfortunately, we seem headed down that road. This year's funding outlook is bleak. To maintain ACS on "life support," Customs estimates that it will need $12 million this year—however $8.5 million is unfunded. To continue life support in FY2000, the Administration proposes $35 million, which we understand to be $32 million short. But, stop for one moment. Even were Congress to find the money to fund ACE—whether over 4 or over 7 years—do we want our lifeline to international trade merely sustained on life support? I would venture that we need a robust, functioning automation system in the interim that can meet the demands of trade over the next 4 to 7 years. To put processing in limbo, without improving the present system to meet intervening contingencies, is equally neglectful on all our parts. NCBFAA has proposed EEEP—Enhanced Electronic Entry Processing—a means by which ACS can accommodate remote entry filing until ACE is on its feet. How can we stand by and wait another 4 to 7 years to enjoy benefits conceived by this Committee over 5 years ago?

As for ACE, the funding outlook is equally poor. Treasury continues to dole out funds sparingly, with $3.4 million in FY99 funds awaiting a "Cost Benefit Analysis." This committee has authorized some funds in a bill now awaiting action on the Senate floor; however, the Administration has requested no funds—I repeat, zero funds—for FY2000. And, it has proposed an untenable user fee concept, which we oppose, to permit a mere $150 million in FY2001. To adequately fund ACE, we project that Congress must appropriate at least $300 million over 4 years. Instead, we have only the Administration's proposal, which is, at best, misguided and, at worst, woefully inadequate.

NCBFAA believes that ACE must be constructed forthwith. We acknowledge that a $1.2 to $1.4 billion price tag demands great caution and the necessary diligence on the part of those authorizing, appropriating and overseeing the spending of these funds. NCBFAA in no way implies that the Congress should simply throw money at this problem. In fact, we too have our reservations. That is why we intend to participate at every level, over every issue coming before Customs' Trade Support Network (TSN). We believe that the fielding of ACE must be, to a great degree, evolutionary and collaborative. Just as we worked with Customs to field a system, ACS, that has proven monumentally successful over 15 years, we intend to insist on that same level of partnership now. After all, our livelihood is at stake. So too must Congress insist on meaningful oversight and Treasury guarantee that it can meet your terms.

Nonetheless, the days of armchair quarterbacking must draw to a close. We must reduce the demands on Customs planners and implementers so that they can realistically move forward, focussed on achieving the result demanded by Congress rather than merely constructing an elegant, risk adverse process. We have confidence that Customs, under your oversight, can produce a successful Automated Commercial Environment. NCBFAA, urges you to support ACE with the necessary authorizations.

Thank you, Mr. Chairman.

STATEMENT OF REXAM DSI

[SUBMITTED BY KENNETH WERTH]

Rexam DSI is a manufacturer of decorative papers that are used for book binding and fancy packaging. We have 5 manufacturing sites, one each in Johnston, RI, West Springfield, MA, Brownville, NY, Lowville, NY, and Reading, PA. We employ 590 people at Rexam DSI, producing saturated papers or coating and converting those papers for specific applications.

Most of our business is declining, but one growth market is packaging for high end luxury goods (pens, watches, jewelry, etc.). Unfortunately recent actions (or inactions) by U.S. Custom Services are threatening our future. For many years our customers have covered their boxes with our product, Skivertex®, and exported the boxes to the U.S.A. These were imported to the United States under classification 4202.99.1000 and carried a duty of 3.4% in 1999. Now, apparently a mistaken ruling was made and certain customers are being charged a higher duty of 18.8% based on HTSUS 4202.92.9060—a jewelry box with an outer surface of sheeting of plastic.

Rexam DSI has worked with Fortunoff and Kalencom, a jewelry box distributor, to get this ruling corrected. We have tried every channel open to us, but Custom Service has decided to place the request on hold because of a pending court case involving vinyl materials and hand bags—the "Sarne" case.

While this delay may seem reasonable to Customs Service, it will have a terrible effect on Rexam DSI. Most of our customers and their customers are small to medium size, private companies. They can not afford to pay the extra duty and wait for the correct ruling and a refund. They will switch to a totally different material, probably cheaper, probably manufactured in Asia and Rexam DSI will be the loser.

Ironically, we cannot take Customs Services to court. We are not directly damaged by their actions. However, once we are truly damaged, no relief will help. Styles would have changed and we could not change them back.

We would like the opportunity to testify at the Finance Committee Oversight Hearing of U.S. Customs Service on May 25th to further explain how the U.S. Custom Service is adversely affecting a U.S. based manufactured.

Thank you for your interest in our concerns.

STATEMENT OF THE SHARP MANUFACTURING COMPANY OF AMERICA

Sharp Manufacturing Company of America ("SMCA") submits these comments to highlight a structural problem in the handling of NAFTA-related rules of origin issues. SMCA believes that the current U.S. procedures for addressing NAFTA rules of origin problems are not working. A mechanism to better address such problems should be put in place.

SMCA manufactures microwave ovens, color televisions, LCD projection systems and copier toner in Memphis, Tennessee. It employs 1,400 people. SMCA is a division of Sharp Electronics Corporation ("SEC"). Established in 1962 and headquartered in Mahwah, New Jersey, SEC has annual sales of more than $3 billion and employs more than 3,100 people in the United States (most of them in facilities in New Jersey, Tennessee and Washington State).

THE DISPUTE REGARDING THE MEXICAN RULE OF ORIGIN DECISION

SMCA's concern stems from a NAFTA origin dispute with the Mexican Government. In February 1995 officials from the International Audit Division of the Mexican Department of Revenue Policy and International Tax Matters, Secretariat of Finance and Public Credit ("Hacienda") conducted a NAFTA origin verification of microwave ovens at SMCA's Memphis plant. In late July of 1995 the Audit Division denied the NAFTA origin of four Sharp microwave oven models manufactured by SMCA in Memphis and imported into Mexico between January 1 and August 31, 1994.

The basis for the decision was that: (a) certain boards containing the central processing unit ("CPU boards") were non-NAFTA-originating goods produced in Thailand; (b) the boards should be classified as "parts of microwave ovens" under item 8516.90.45 of the Harmonized Tariff Schedule ("HTS"); and, (c) as a consequence, the change of tariff classification required by NAFTA Annex 401 for microwave ovens (HTS subheading 8516.50) had not been fulfilled.

Pursuant to this NAFTA provision, a good is considered to be a NAFTA-originating microwave oven (HTS subheading 8516.50) if the non-originating materials used in the production of the oven undergo a change in tariff classification from any other HTS subheading except from tariff item 8516.90.35 or 8516.90.45. According

to a U.S. Customs Service Headquarters Ruling issued on October 3, 1995 (HQ 957727), the CPU boards imported from Thailand were properly classified as a control panel under HTS item 8537.10.90. (See Attachment 1.) Therefore, the requisite change of tariff classification occurred and the SMCA microwave ovens were NAFTA origin ovens. This conclusion was supported by a 15 May 1996 opinion from the World Customs Organization (No. 96.N.722–Fo/N). (See Attachment 2.)

Despite the U.S. Customs ruling (which was consistent with seven prior Customs rulings and the EC's classification of similar CPU boards), Hacienda denied SMCA's administrative appeal in March 1996. In late January 1998 the Mexican Tax Court, an administrative tribunal within Mexico's executive branch, denied SMCA's appeal. It did so even though the United States, the importing country of the subject CPU boards, and the World Customs Organization had rejected the basis upon which Hacienda concluded that SMCA's microwave ovens were not NAFTA originating.

THE PRESENT PROCESS

NAFTA supposedly provides a mechanism for raising concerns about Mexican (or Canadian) rule of origin decisions.[1] However, the mechanism did not work in the microwave oven dispute. Before continuing, SMCA wants to make clear that it is not condemning the actions of U.S. Customs officials involved in this matter. Indeed, SMCA greatly appreciated the efforts made by the officials of the Customs' International Agreements Staff Section headed by Myles Harmon, who were instrumental in the issuance of the Customs ruling and obtaining the World Customs Organization opinion.

What concerns SMCA is that current Treasury/Customs policy appears to preclude any prospect of a satisfactory outcome in NAFTA rules of origin disputes. The only means of seeking to avoid assessment of duties and penalties by the Mexican authorities was to pursue the administrative and judicial review procedures provided by Mexican law. However, the Treasury/Customs position was that it was inappropriate to press the issue in NAFTA forums while Mexico was conducting its domestic review.[2] As a result, there was no possibility of using the NAFTA dispute resolution procedures to convince the Mexican authorities not to misclassify the CPU boards and thus erroneously deny NAFTA origin to SMCA's microwave ovens.

THE NEED FOR A NEW MECHANISM

Facilitation of the flow of internationally traded goods and services is central to the commercial operations aspect of Customs' mission. This is not limited to import-related activities. Increasingly, particularly under NAFTA, the U.S. Customs Service is responsible for promoting and protecting the interests of American exporters. Areas such as vigilant assurance of consistent and proper classification and rules of origin decisions by our NAFTA partners should be given greater attention. U.S. policy should be structured so that the NAFTA mechanisms actually have the potential to resolve disputes rather than merely to discuss NAFTA-inconsistent actions that already have been taken.

Consistent and proper tariff classification among NAFTA partners is essential to the proper functioning of NAFTA. This critical goal cannot be achieved if the U.S. Government remains of the view that nothing substantive can be done until after the importer confronted with an erroneous rule of origin decision by the Mexican (or Canadian) authorities exhausts all domestic remedies under Mexican (or Canadian) law.

While SMCA has not compiled anecdotal evidence from other American companies, it believes that its experience is not a rare, isolated occurrence. Rather, many companies and a wide range of products have been—and in the future could be—subject to arbitrary classification and rule of origin decisions by the Mexican au-

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[1] Pursuant to Article 513, the NAFTA Parties established a Working Group on Rules of Origin. It is supposed to meet at least four times a year and can meet upon the request of any Party. The Treasury Department is the lead agency for this Group, with Deputy Assistant Secretary John Simpson as the lead person. Much of the staff work is coordinated by Joyce Metzger in Customs, who is head of the NAFTA Customs Subgroup.

If the Working Group fails to resolve the matter within 30 days, the complaining party may request a meeting of the NAFTA Commission under Article 2007. The Commission is directed to convene within 10 days of receipt of a request and to endeavor to resolve the dispute promptly. If it has not done so within 30 days, the complaining party is entitled to request establishment of a NAFTA Chapter 20 arbitral panel.

[2] The matter was raised in the NAFTA Working Group on Rules of Origin, but SMCA understands that the U.S. representative did little more than express U.S. concern and hope that Mexico would make the proper rule of origin decision. There was no concerted effort to secure a resolution favorable to SMCA.

thorities. It should be noted that because Mexico, as a matter of law, assesses additional internal taxes, surcharges, interest and mandatory fines upon underpayment of import duties, the amount of duties owed as a result of the denial of the NAFTA preferential tariffs multiplies very quickly. Moreover, unlike U.S. Customs law, an importer is not permitted to deposit the potential underpayment of duties in Mexico while it challenges the underlying determination through review procedures. Thus, at a certain point in the process of seeking remedies under Mexican law, it becomes prohibitively expensive for an American company confronted with an adverse NAFTA origin determination to challenge such determination. The company can be forced to pay the additional duties, rather than continue to challenge erroneous conclusion reached by Mexico. This is, in fact, what happened to SMCA.

Treasury/Customs policy should be changed. A mechanism should be created so that once it becomes apparent that Mexican (or Canadian) authorities are likely to issue an erroneous rule of origin decision, the United States should demand that the NAFTA Working Group on Rules of Origin meet expeditiously to consider the problem. At that meeting the U.S. delegate should treat the issue as a dispute requiring resolution rather than as a mere expression of concern. Evidence of the erroneousness of the proposed decision should be presented and the Mexican (or Canadian) delegation should be pressed to ensure that the final decision would be in accordance with the NAFTA origin rules.

If this effort was not successful within the 30-day period provided by NAFTA Article 513, the United States should press for an immediate meeting of the NAFTA Commission, in which, once again, the emphasis should be on dispute resolution rather than merely expression of concern. SMCA recognizes that this would be a major departure from current NAFTA procedure. To date very few special meetings of the Commission have been called and even fewer have aggressively sought to achieve dispute resolution. However, unless this is done the NAFTA mechanism will continue to be useless to prevent the issuance of erroneous rule of origin decisions.

Finally, if after 30 days conciliation by the NAFTA Commission is unsuccessful, the U.S. Government should immediately thereafter request a Chapter 20 arbitral panel. Unless the United States pursues such a vigorous, expeditious procedure, the NAFTA procedure will remain of little value. Companies like SMCA will become disillusioned about NAFTA and they may be discouraged from building or expanding manufacturing facilities in the United States to serve the North American market. Also, companies might be forced to consider using Mexican manufacturing facilities rather than their U.S. plants to serve the North American market as a means to avoid potential arbitrary NAFTA origin determinations by Mexico. This would not be in the national economic interest.

Attachments.

ATTACHMENT 1

DEPARTMENT OF THE TREASURY
U.S. CUSTOMS SERVICE

OCT - 3 1995

HQ 957727

CLA-2 R:I 957727 ch

CATEGORY: Classification

TARIFF NO.: 8537.10.9060

Peter J. Gartland
Donovan, Leisure, Newton & Irvine
30 Rockefeller Plaza
New York, New York 10112

Re: Tariff classification of a CPU board for a microwave oven.

Dear Mr. Gartland:

This is in response to your letter, dated March 15, 1995, requesting the tariff classification under the Harmonized Tariff Schedule of the United States (HTSUS) of a Central Processing Unit (CPU) board for a microwave oven.

FACTS:

The CPU board (Part No. DPWBFB244WRU0) consists of a printed circuit board on which are assembled diodes, capacitors, transistors, integrated circuits, relays, electrical connectors, a varistor which functions as a surge suppressor, and other components. After importation, the CPU board is attached to a flexible plastic panel with circuits, numbered pads and a ribbon connector. The completed unit controls the cooking time and power level of a microwave oven (Model No. R-5A86) with a voltage not exceeding 1,000 volts.

ISSUE:

What is the proper tariff classification for the CPU board?

LAW AND ANALYSIS:

The competing provisions are subheading 8537.10, which provides in part for boards, panels (including numerical control panels) and other bases, equipped with two or more apparatus of heading 8535 or 8536, for electric control or the distribution of electricity, for a voltage not exceeding 1,000 volts; subheading 8538.10, which

provides for certain parts suitable for use solely or principally with the apparatus of heading 8537; and subheading 8516.90, encompassing parts for microwave ovens.

By its terms, heading 8537 captures, with exceptions not relevant here:

1. Boards, panels and other bases;

2. Equipped with two or more apparatus of heading 8535 or 8536;

3. For electric control or the distribution of electricity.

The instant CPU board contains apparatus which are mounted on a board or a base. It has been equipped with relays, connectors, resistances and the varistor, which are apparatus provided for in heading 8536. See Explanatory Note to heading 8536 of the Harmonized System at page 1390. The unit is clearly designed for electric control as it regulates the cooking time and power level of a microwave oven. However, it is not capable of performing these functions as it is imported without the numbered touch pads and the ribbon connector

General Rule of Interpretation 2(a) states in pertinent part that:

Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as entered, the incomplete or unfinished article has the essential character of the complete or finished article.

In this instance, the unit is comprised of a base equipped with several apparatus of heading 8536 and is identifiable as a board performing the functions identified in heading 8537. As a result, it possesses the essential characteristics of a finished control board. Therefore, we conclude that the CPU board is classifiable in heading 8537.

Section XVI, Note 2, states in pertinent part that:

[P]arts of machines (not being parts of the articles of heading 8484, 8544, 8545, 8546 or 8547) are to be classified according to the following rules:

(a) Parts which are goods included in any of the headings of chapters 84 and 85 (other than headings 8485 and 8548) are in all cases to be classified in their respective headings;

(b) Other parts, if suitable for use solely or principally with a particular kind of machine, or with a number of machines of the same heading (including a machine of heading 8479 or 8543) are to be classified with the machines

> of that kind. However parts which are equally suitable for use principally with the goods of headings 8517 and 8525 to 8528 are to be classified in heading 8517.

Thus, goods which are described by any of the headings of chapters 84 and 85 (other than headings 8485 and 8548), whether finished or unfinished, are classified in their respective headings and are not classified with the goods for which they are intended. As the CPU board is classifiable in heading 8537, as a matter of law it cannot be classified in subheading 8516.90 as a part of a microwave oven.

You have asked us to address the relevance of certain provisions of Annex 401 of the North American Free Trade Agreement (NAFTA) and its legal notes to the classification of these goods under the Harmonized Tariff Schedule of the United States. Specifically, in the Annex 401 rules of origin the NAFTA parties created tariff item 8516.90.45 which provides for printed circuit assemblies for microwave ovens. Chapter 85, Note 1, Annex 401, defines the expression "printed circuit assemblies." In addition, other provisions for printed circuit assemblies have been added to Chapter 85, HTSUS.

Pursuant to Public Law 100-413, the United States acceded to the Harmonized system convention. As a contracting party to the convention the United States has agreed to apply without change the text of the headings, subheadings, legal notes and General Rules of Interpretation. Contracting Parties may create further subdivisions for tariff and other purposes. Annex 401 of the NAFTA represents an instance in which the NAFTA Parties created a number of tariff provisions for the purpose of applying NAFTA rules of origin to goods imported into the NAFTA territories.

For tariff classification purposes, however, classification is governed by the General Rules of Interpretation to the Harmonized System which requires a strict adherence to the hierarchical structure of the HS. Accordingly, the scope of the four and six digit provisions must be decided as a matter of law. Only thereafter may the terms of an eight digit provision be considered. Stated differently, a subdivision of the international nomenclature cannot expand or contract the scope of a four-digit heading or six-digit subheading.

In addition, the legal notes to Annex 401 of the NAFTA are extrinsic to the classification of merchandise. Their relevance is to illuminate the provisions of the Annex 401 rules. The provisions of Annex 401 have no bearing on the classification of goods. As stated above, in this instance the merchandise is excluded from heading 8516 as a matter of law. Accordingly, there is no basis upon which to consider the terms of item 8516.90.45.

HOLDING:

The subject merchandise is classifiable under subheading 8537.10.9060, HTSUS, which provides for boards, panels (including numerical control panels), consoles, desks, cabinets and other bases, equipped with two or more apparatus of heading 8535 or 8536, for electric control of the distribution of electricity, including those incorporating instruments or apparatus of chapter 90, other than switching apparatus of heading 8517: for a voltage not exceeding 1,000 V: other, other: programmable controllers. The applicable rate of duty is 4.8 percent ad valorem

Sincerely,

John Durant, Director
Commercial Rulings Division

22316 [illegible]
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ATTACHMENT 2

WORLD CUSTOMS ORGANIZATION
ORGANISATION MONDIALE DES DOUANES

NOMENCLATURE AND CLASSIFICATION
DIRECTORATE

FAX : 32 2 508 4239

Mr G. WEISE,
Commissioner of Customs,
U.S. Customs Service,
1301, Constitution Avenue, N.W.
WASHINGTON, D.C. 20229 - Etats-Unis.

96.N.722 - Fo/N.

Brussels, 15 May 1996.

Reference : Your fax of
17 April 1996.

Dear Mr. Weise,

SUBJECT : Classification in the Harmonized System (HS) of a "CPU board for a control panel".

Thank you for your fax requesting an opinion on the HS classification of the above-mentioned product.

A. Description and use

According to the information and the sample you provided, it appears that the article at issue is a printed circuit board equipped with a metal oxide varistor, transistors, a liquid crystal display, an output transducer (beeper), two relays, an integrated circuit, capacitors, resistors, a transformer, diodes and two connectors. The integrated circuit is a micro controller which has software (e.g., cooking times, heating power level) burned into its memory. After importation, the product is attached to a flexible plastic panel with printed circuits, numbered pads and a ribbon connector. The circuitry in the numbered touch pad is interconnected and allows for the selection of cooking times and power levels from the integrated circuit. The completed unit will ultimately be assembled with other parts into a microwave oven with a voltage not exceeding 1,000 volts.

B. Classification

According to the above description, it appears that the printed circuit board and the flexible plastic panel when assembled constitute a control panel for a microwave oven. The printed circuit board constitutes thus a part of a microwave oven. As the printed circuit board is, however, a base "equipped with two or more apparatus" of heading 85.36 (two relays and two connectors; for the sake of clarity the Secretariat would like to point out that resistors and

varistors are classifiable in heading 85.33 - cf. your letter, page 2, third paragraph from the bottom), the Secretariat feels that the article at issue answers to the description set out in heading 85.37 and is therefore classifiable in that heading, in conformity with Note 2 (a) to Section XVI, and more specifically in subheading 8537.10 by application of General Interpretative Rules 1 and 6. That would preclude the possibility of classification in headings 85.16 or 85.38 in this particular case.

Should you not share my view on this classification matter, the Secretariat would be willing to submit this question to the Harmonized System Committee. If you agree with this submission, the Secretariat would appreciate an early confirmation.

Yours sincerely,

I. Kusahara

I. Kusahara,
Director.

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