

March 1988

# AIR CARGO IMPORTS

## Customs Needs to Overcome Concerns to Benefit From Centralizing Examinations



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**General Government Division**

B-230524

March 31, 1988

The Honorable Lloyd Bentsen  
Chairman, Committee on Finance  
United States Senate

The Honorable John C. Stennis  
Chairman, Committee on Appropriations  
United States Senate

The Honorable Dan Rostenkowski  
Chairman, Committee on Ways and Means  
House of Representatives

As required by the Omnibus Budget Reconciliation Act of 1987, signed December 22, 1987, we are reporting on our review of the Customs Service's Centralized Examination Stations (CES) program, which is aimed at streamlining the process of clearing imported merchandise. Customs' implementation of the CES program raised concerns among members of the importing community primarily because it changed the traditional way Customs operated and put additional burden on the importing community. Congress directed Customs to suspend all airport CES operations and required it to provide written justification for any new CESS.

The act requires that our report be addressed to the Senate Committee on Finance and House Committee on Ways and Means. We have also addressed the report to the Senate Committee on Appropriations because it had requested an analysis of the CES program before passage of the act. As agreed with the committees, we have limited our work to airport CESS.

**Results in Brief**

At the airports we visited (New York, New York; Newark, New Jersey; Philadelphia, Pennsylvania; and Chicago, Illinois) where CESS served as centralized locations for clearing merchandise, we found that Customs district officials had not resolved many of the concerns raised by the importing community before allowing CESS to begin operations. In spite of their concerns, however, the importing community seemed generally satisfied with the CESS after they had begun operations, primarily because Customs' services to the importing community had been enhanced by quicker examinations of cargo and release of merchandise. An exception was the CES at the John F. Kennedy International Airport (JFK) in New York where many problems unique to that facility worked

against a successful CES program. Therefore, we have no basis for recommending against restarting the CES program at the locations we visited except at JFK, where problems persist.

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## Background

Historically, Customs examined imported merchandise as it arrived in the United States. Increases in the volume of trade over the years, however, along with increases in the use of containerized shipments and other innovations in transporting merchandise, have placed heavy demands on Customs inspectors. How quickly and efficiently Customs physically inspects and processes cargo through ports of entry is a continuing concern for Congress and the importing community. As used in this report, the importing community generally includes importers, customs brokers, container freight station operators, air carriers, and bonded warehouse operators. A more thorough description of the members of the importing community can be found in the glossary to this report.

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## The CES Concept

CESS are privately operated facilities that make imported merchandise available to Customs inspectors for physical examination. CESS have the equipment and personnel necessary to unload cargo from containers for Customs' examination and to reload the containers for shipment. CESS are primarily intended to be used for merchandise handled by container freight stations; bonded warehouses; truck, rail, and air terminals; and other facilities receiving transferred bonded merchandise. (Before CESS, Customs examinations were done at locations which were geographically separate from one another and which required inspectors to travel to them.) In most instances, cargo designated for Customs examination must be transferred at the importer's expense to a CES for inspection. CESS provide working space for Customs inspectors who examine and release merchandise brought to them.

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## The Evolution of CESS

From 1842 to the early 1980s, Customs' policy was to examine a portion of every importer's shipment. In 1978, we examined the inspection process and reported<sup>1</sup> that Customs' cargo inspections did not ensure compliance with the laws and regulations governing imports because the inspections were usually cursory. We recommended that fewer but more intensive examinations be performed. In 1981, the Department of the

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<sup>1</sup>Customs Cargo Processing - Fewer But More Intensive Inspections Are in Order (GGD-78-79, Sept. 7, 1978).

Treasury amended Customs' regulation relating to the examination of imported merchandise. The amended regulation allows Customs to establish systems whereby only high-risk shipments are physically examined by inspectors. Other shipments may be released without physical exam.

The centralization of cargo examinations evolved over the last 4 years through two nationwide Customs programs. In December 1984, Customs issued Directive 3270-01, which reduced the number of cargo examinations at importers' premises and established centralized locations for examining containerized cargo. According to Customs, this initiative resulted from many operational problems, including (1) examinations not being cost effective, (2) extensive inspector travel time and associated costs, (3) inadequate facilities for conducting examinations, and (4) noncooperative laborers at the importers' premises.

On January 5, 1987, Customs Directive 3270-03 was issued to provide national guidelines for the establishment and operation of CESS. Customs' goal for the CES program was to go one step beyond centralizing the examination of containerized cargo by centralizing all cargo examinations previously done at scattered facilities throughout the ports. Through the CES program, Customs hoped to greatly reduce nonproductive travel time of inspectors while improving service to the importing community.

According to the January 5, 1987, directive, all regional and district managers were to coordinate the selection of CESS with as wide a cross section of the importing community as possible. The final designation of the CES, however, was to be the responsibility of the district director. Issues regarding labor unions and the costs for moving merchandise from carriers' warehouse facilities to the CESS were to be addressed by the importing community, not Customs.

As of December 22, 1987, Customs had established a total of 117 CESS, 10 of which were for examining air cargo. Additional CESS were scheduled for start-up in 1988.

## Objectives, Scope and Methodology

The Omnibus Budget Reconciliation Act of 1987, signed into law on December 22, 1987, said

"The Comptroller General of the United States shall conduct a comprehensive analysis, including a cost-benefit study, of the centralized cargo examination station

(CES) concept from the perspective of both the United States Customs Service and business community users. The analysis shall be submitted on the same day to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate (hereinafter in this subsection referred to as the 'Committees') not later than March 30, 1988, and shall include recommendations as to how best to implement cargo inspection procedures."

The act required that Customs suspend operations at each airport CES and that the CESS remain closed for 90 days after the date of the act. It also prohibited Customs from establishing any new CESS unless it provided at least 90 days advance notice in writing.

Before passage of the act, we had initiated a review of the CES program at the request of the Senate Committee on Appropriations based on language contained in Senate Report 100-160 dated September 17, 1987. We met with the Senate Committee on Finance and the House Committee on Ways and Means on January 26, 1988, to discuss the feasibility of completing a cost/effectiveness analysis of the CES program by March 30, 1988. We were told that the Committees' primary interest was in the CES program at airports, particularly JFK in New York, where importers, customs brokers, container freight station operators, and some Customs inspectors had made numerous complaints.

We met again on February 22, 1988, to discuss our observations from our visit to JFK and the Newark airport. At that time it was agreed that our work would be limited to (1) identifying those factors of the CES program that affect Customs and the importing community and (2) comparing the importing community's acceptance of the CES program at four airport locations where Customs had implemented the CES program. It was agreed that we would not analyze CESS established at seaports or at land border crossing points and that we would not evaluate the soundness of the cargo examination process under the CES program. The decision as to whether additional work by us at the seaports and other CES facilities is warranted was deferred until after March 30, 1988.

To identify those factors of the CES program that affect Customs and the importing community, we reviewed Customs' documents relating to the implementation of the CES program, including directives, the legislative history, and letters received by the congressional committees both criticizing and praising CESS at various locations. In focusing on those factors that affect Customs, we spoke with Customs officials at Customs Headquarters in Washington, D.C., and at district offices and ports in New York, New York; Newark, New Jersey; Philadelphia, Pennsylvania; and

Chicago, Illinois. We also spoke with Customs officials concerning proposed CESS at the Los Angeles, California, airport. We spoke with Customs inspectors at the airports we visited and reviewed a Customs' Office of Internal Affairs report on the CES program (87-NC-9, dated August 10, 1987). To identify those factors that affect the importing community, we spoke with a total of 18 customs brokers, 20 airline officials, and 6 container freight station operators at the airports we visited. We also spoke with representatives of the National Customs Brokers and Forwarders Association of America Inc., the National Bonded Warehouse Association, and the National Treasury Employees Union.

To compare the acceptance of the CES program at airports, we toured CES sites at JFK, Newark, Philadelphia, and Chicago airports and talked to their operators, members of the importing community, and Customs officials and inspectors. We also toured one of several proposed CES sites at the Los Angeles airport. Our visits at each location lasted 2 or 3 days and, to the extent possible, we obtained statistical information from Customs and the importing community. Because of time constraints, however, we were unable to verify or conduct reliability checks on the data.

Our audit work was conducted from January to March 1988, except at the Los Angeles District Office where we began our work for the Senate Committee on Appropriations in December 1987. We did our work in accordance with generally accepted government auditing standards except as noted above.

## Factors Affecting the Acceptance of the CES Program

Discussions with members of the importing community, CES operators, and Customs officials and inspectors revealed several factors that positively affected the acceptance of the program, the most notable being improved Customs services. The discussions also revealed several other factors that adversely affected the acceptance of the CES program. These factors include: the method Customs used to select CES operators; the CES operators' liability for lost, stolen, or damaged merchandise; the additional costs for CES operations; CES operators' access to importing documentation; and the quality of cargo examinations.

The CESS we visited differed in terms of fees charged by the CES operators, operating hours, number of Customs inspectors assigned, and the level of centralization. (The appendix provides details of the conditions we found at each location we visited.) With the exception of JFK, Customs and the importing community were able to overcome many of the

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objections raised during the implementation of the program at each location. At JFK, objections remain unresolved.

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**Factors Contributing to Acceptance of CES**

Except at JFK, discussions with members of the importing community and Customs officials and some inspectors revealed the following factors that contributed to the acceptance of the CES program:

- Merchandise could be examined by Customs inspectors and released quicker because the CES operators made several pickups each day and they offered 24-hour service for claiming merchandise that had been released by Customs.
- Customs inspectors were available at least 8 hours a day at CESS to examine cargo as opposed to 1 or 2 hours a day at the air carriers or container freight stations.
- CESS were conveniently located and easily accessible to the importing community.
- Inspectors could make more efficient use of their time. For example, we were told that merchandise was not readily available for inspection at some carriers and inspectors were required to wait or come back later.
- Inspectors' working conditions were improved.

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**Factors Adversely Affecting Acceptance of CES Program**

Discussions with members of the importing community and Customs officials and inspectors revealed five factors that initially affected the CES program's acceptance. The first factor that several members of the importing community mentioned to us was the selection of CES operators. At each airport we visited, Customs solicited bids for a CES operator to handle and open all air shipments subject to Customs' examination. The Customs district directors selected the CES operators with only general guidance from Customs headquarters on how to establish a CES.

In its August 1987 report on the CES program, Customs' Office of Internal Affairs was concerned that because of the lack of specific guidelines in the selection process, Customs could be vulnerable to possible (1) improper manipulation of the selection process by third parties, (2) legal actions from qualified bidders not selected, and (3) selection of CES operators who are not the most advantageous to Customs. We did not have sufficient time to verify their assessment. According to Customs' Assistant Commissioner for Inspection and Control, action is being taken on the recommendations contained in the report, and he expects that by June 1, 1988, Customs will have specific guidance for establishing CESS.



A second factor involved the lack of written agreements between Customs and the CES operators on the CES operators' liability for lost, stolen, or damaged merchandise. According to Customs officials, importers are responsible for presenting merchandise to Customs for examination and Customs is not responsible for the merchandise. In meetings with the importing community, we were told that because Customs is designating CES operators to handle merchandise, Customs may be liable for lost, stolen, or damaged merchandise. Although we did not verify this during our review, we were told that CES operators have not provided documentation relating to their liability for any lost, stolen, or damaged merchandise. Members of the importing community said the community needs to be assured that its cargo is protected.

According to the audit report by Customs' Office of Internal Affairs, which also addressed this issue, the possible results of the absence of agreements covering liability could be that Customs may be subject to legal action brought about due to defaults, irregularities, or negligence on the part of the CES operators. Customs' Assistant Commissioner, Inspection and Control, said that along with the guidance to district offices for establishing CESS, the district directors will be authorized to enter into written agreements with the CES operators covering such areas as merchandise liability.

A third factor is the costs the CES program imposes on the importing community. Customs has provided no guidance on how fees should be established and has no procedures for assessing the reasonableness of CES operators' fees. Under the program, CES operators at JFK, Newark, and Philadelphia airports had been assessing charges based on house airway bills (see glossary) whether the merchandise was examined at the CES or not. These charges ranged from \$1.49 per house airway bill at JFK in 1986 to \$7.00 per house airway bill at Philadelphia in 1987. It should be noted that the level of service that the importing community received from the fees paid varied. In New York, the container freight station operators were required to bring merchandise to the CES for examination. In Philadelphia, the CES operator picked up the merchandise from the carriers or container freight stations and maintained control of it until Customs examined and released it to the importers. In Chicago, charges were assessed only on merchandise that was handled by the CES operator. (About 80 percent of the merchandise is released without Customs' physical examination. Consequently, the CES operators only needed to handle the remaining 20 percent of the merchandise.)

Several members of the importing community suggested to us that Customs pay the CES operators' fees from the user fees it began collecting in 1986 to offset the cost of Customs' commercial operations. Customs collected about \$539 million in FY 1987. Customs believes that user fees should not pay the costs associated with presenting cargo for examination and that such costs should be borne by the importing community. We did not have sufficient time to adequately evaluate whether Customs user fees could offset the costs associated with CES operations.

A fourth factor expressed to us by some members of the importing community related to CES operators having access to import documentation. Customs permits the CES operators, who may be in direct competition with carriers, container freight stations, or others, to have access to documentation on cargo shipments. For example, at the Philadelphia airport, the CES operator stationed employees in Customs' offices so they could have quick access to those shipments needing physical examination at the CES. The employees also had access to all airway bills so that the CES operator could assess charges. Members of the importing community believe that knowing how much carriers or others charge for services gives CES operators an unfair competitive advantage. We did not verify whether such an advantage existed.

A final factor involved the cargo examination process, which some Customs inspectors believe is not sound under the CES program because they do not visit carrier facilities and container freight stations as they used to do. According to these inspectors, this prevents them from identifying irregularities with cargo that had not otherwise been designated for inspection. For example, the union leader representing inspectors at JFK told us that before establishment of the CES program, inspectors visited one or more container freight stations each day but they were required to examine only about 10 to 20 percent of the merchandise. Nevertheless, the inspectors gave a cursory examination of other imported merchandise at the container freight stations and only did detailed examinations on any that appeared suspect. The inspectors said that under the CES program, they did not visit the facilities so cargo not selected for examination did not receive even a cursory examination.

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## Conclusion

At the airports we visited where CESS served as centralized locations for clearing merchandise (New York, New York; Newark, New Jersey; Philadelphia, Pennsylvania; and Chicago, Illinois), we found that Customs district officials had not resolved many of the concerns raised by the importing community before allowing CESS to begin operations. In spite

of their concerns, however, the importing community seemed generally satisfied with CESS after they began operating, primarily because Customs' services to the importing community were enhanced by quicker examinations of cargo and release of merchandise. An exception to this was the CES at JFK in New York, where many problems unique to the facility worked against a successful CES program. Therefore, we have no basis for recommending against restarting the CES program at the locations we visited except at JFK, where obstacles remain to be resolved.

As requested by the Committees, we did not obtain official agency comments, though we did discuss the results of our work with Customs headquarters officials and they generally agreed with our assessment. The Assistant Commissioner, Inspection and Control, told us that Customs would establish CESS only at those airports where the importing community is satisfied that the CES program enhances overall operations. He said that Customs would not seek to restart the CES program at JFK until major concerns are overcome.

As arranged with the Committees, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days after the report date. At that time, we will send copies to interested parties and make copies available to others upon request.



Arnold P. Jones  
Senior Associate Director

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## Abbreviations

CES	Centralized Examination Stations
GAO	General Accounting Office
JFK	John F. Kennedy International Airport



# GAO's Observations of CES Facilities at Various Airports

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## Newark International Airport

The CES at Newark International Airport was established in April 1987. Until this CES was closed by congressional legislation 8 months later, Customs inspectors physically examined about 20 shipments per day at the CES between the hours of 8:00 a.m. and 5:00 p.m.

The CES operator said that air carriers at Newark airport handled about 40,000 house airway bills per year and that the CES operator charged \$5.80 per house airway bill to operate the CES. According to the CES operator, the charge was based on the cost of facility modification, the purchase of new equipment, operating costs, and a profit.

Although some members of the importing community had initial reservations about the CES, they now fully support its operation. With the CES, the importing community gained increased access to Customs, i.e., they could receive service 8 hours a day rather than the previous 1- to 2-hour slots Customs allocated to a particular facility. Importing community representatives said the CES operated at a higher level of service than did the previous Customs system, resulting in faster cargo processing time. Additionally, the CES site was particularly attractive because it was centrally located with convenient access. Customs, airport officials, and the importing community would like to see the facility reopened as soon as possible to retain possession of this desirable site. Importing community officials sent letters to Customs and their congressional representatives supporting the continuation of Newark's CES.

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## Philadelphia International Airport

In September 1987, Customs' Philadelphia District Office announced plans to establish a CES at the Philadelphia International Airport. In October 1987, a CES operator was selected and on November 16, 1987, the CES began operation. During the approximately 4 to 6 weeks the program was operational, about 30 shipments per day were picked up by the CES operator and taken to the CES, where Customs inspectors examined and released the merchandise. Customs officials said the air carriers at the Philadelphia airport handled about 200 house airway bills each day and that the CES operator charged \$7.00 per house airway bill.

Although the Philadelphia importing community was unhappy that it was not more involved in designing the local CES program, most of the members we talked with were impressed with the service they received during the time the CES was operational. They said Philadelphia's CES offered the importing community several pickups per day, Customs

examination hours from 8:00 a.m. to 5:00 p.m., quick release of merchandise, and a 24-hour-per-day operation so that importers could obtain their merchandise. At the time the CES was closed, some concerns by the importing community, such as liability for the merchandise, were being worked out. Customs and the importing community were generally in favor of reopening the CES in Philadelphia.

## Chicago O'Hare Airport

The CES operations at Chicago O'Hare Airport differed from those at Newark and Philadelphia airports in three ways. First, Customs did not have a CES facility at Chicago that handled only air cargo. Instead, four CESS were established at the Port of Chicago, two of which were in close proximity to O'Hare Airport to handle air cargo in addition to rail, truck, and ocean vessel cargo. These facilities began operations in January 1986 as part of Customs effort to centralize examinations of containerized cargo and were operational at the time of our visit on February 29, 1988. The second difference was that at the Chicago airport, Customs inspectors continued to examine air cargo at air carriers' premises on the airport grounds. Only cargo being handled at off-airport locations was taken to the CESS for examination. The third difference was that the CES operators for the Chicago airport did not assess a per house airway bill charge. Rather, CES examination costs were included with other cargo-related charges and could not be broken out.

According to members of the Chicago importing community, handling low volume off-airport air cargo at CESS was an acceptable method of operation. The community believed the CES program provided better access to Customs inspectors. The two airport CESS operated 24 hours per day and Customs inspectors were available from 8:00 a.m. to 5:00 p.m. to make examinations.

When Congress closed down airport CESS, Customs offered the Chicago importing community the option of having examinations done at the CESS or at individual facilities. Although only a few carriers requested that Customs examine cargo at their facilities, Customs believes there are potential problems if the number of locations it has to visit to make examinations increases and they become more geographically dispersed because it will need more inspectors.

In addition to the current CESS, Chicago district officials have been considering the centralization of all air cargo at the airport. The importing community is opposed to this idea and expressed concerns about costs, the inefficiency of moving large quantities of merchandise off the air

carriers' premises for inspection, and the liability for loss or damage. Customs officials said that these centralization plans have not been finalized.

## New York JFK International Airport

The CES at JFK was established in December 1986. Although Customs held planning sessions with a CES committee comprised of Customs inspectors and members of the importing community, major opposition to the program existed before and during operations.

The CES was similar to the two located near Chicago's airport in that air carriers operating on the airport grounds were not required to have their cargo examined at the CES. When operating, the CES at JFK serviced about 34 container freight stations, requiring the freight station operators to move cargo designated for examination to the CES. Customs officials estimated that inspectors were examining about 14 percent, or about 56,000, of these shipments per year. Customs made examinations from 8:00 a.m. to 5:00 p.m., Monday through Friday, and permitted freight station operators to bring cargo to the CES by appointment twice a day.

JFK handles about 50 percent of the air cargo traffic in the United States. Customs officials at JFK said that container freight stations at the airport handle about 400,000 house airway bills per year. The CES operator initially charged \$1.49 per house airway bill, though these fees were raised several times and were \$3.60 per house airway bill when the facility was closed in December 1987.

The importing community and some Customs inspectors were opposed to the program. They said the CES location presented problems to some members of the importing community because their facilities were located some distance from the airport, making transportation of their merchandise to the CES difficult, expensive, and time consuming. Storage costs were also increasing, as were processing delays.

According to Customs officials, other factors at JFK complicating the CES program's acceptance were large-scale Customs changes occurring when the CES was starting up. For example, centralizing paper entries required those brokers who were not automated to deal with Customs' new automated processes or automate themselves. They were resisting the expense. Another change involved pulling 40 Customs inspectors from their regular assignments to participate in a textile inspection program.



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## Los Angeles International Airport

Customs officials in Los Angeles planned to begin phasing in a CES at the airport in 1988. Initially, Customs planned to consolidate the existing 34 inspection sites into 1 CES on the airport grounds and to examine nearly 390 shipments per day. Customs solicited proposals on the CES operation and received seven proposals. Four of the seven suggested that charges be on a per entry basis with costs to the importing community ranging from \$2.85 to \$3.85 per entry. The other three suggested a charge per examination. According to Customs officials, the facility Customs found most acceptable received strong objections from the importing community because of physical location, inaccessibility, and traffic congestion.

Customs responded by asking for a traffic study. The study is currently in progress and results are expected by the end of March 1988. Customs is continuing to work with the importing community as it evaluates the CES proposals and is considering establishing more than one CES at the Los Angeles airport. Customs is also contemplating a CES at Los Angeles to handle the cargo of container freight stations only. Air carriers would continue to receive on-site inspections by Customs.

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# Glossary

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<b>Air Carrier</b>	Transporter of merchandise using aircraft.
<b>Bonded Warehouse Operator</b>	Owner or operator of warehouses used for the storage of imported merchandise not released from Customs' custody.
<b>Centralized Examination Stations (CES)</b>	Privately operated facilities designated by Customs to receive cargo for examination that was traditionally examined in geographically separated locations.
<b>Container</b>	A unit of transport equipment that can be 20 to 40 feet in length and is specifically designed to facilitate the movement of goods by one or more modes of transport without rehandling or reloading individual pieces of merchandise.
<b>Container Freight Stations Operator</b>	A person engaged in the business of receiving containerized cargo; unloading it from containers; and, after proper Customs release occurs, delivering it to consignees.
<b>Customs Broker</b>	Person or firm licensed by Customs to transact business with Customs on behalf of importers.
<b>Entry</b>	A document filed with Customs as a record of importation, description, value, and disposition of a given lot of imported merchandise by an importer, broker, or bonded carrier.
<b>Examination</b>	A review of the documentation that lists, for example, the items contained in the shipment, country of origin, or manufacturer. It may also include a physical examination of all or some of the merchandise.
<b>House Airway Bill</b>	A line item on an airway bill. An airway bill is a contract between the shipper and the carrier for the carriage of goods.
<b>Importer</b>	One who imports goods.

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**Inspector**

A Customs employee who scrutinizes baggage, effects, and cargo at the time of entry into the United States to determine the presence of dutiable merchandise and compliance with U.S. trade laws and regulations.

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**Port of Entry**

Any place designated by an act of Congress, executive order of the President, or order of the Secretary of the Treasury at which a Customs officer is assigned with authority to accept entries of merchandise, collect duties, and enforce the various provisions of the Customs laws.

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**Release of Merchandise**

The transfer, with Customs' permission, of merchandise from carrier or warehouse proprietor to importer.



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