

# DECLARE YOUR MISTAKES TO CUSTOMS CORRECTLY

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An importer can make a prior disclosure when he discovers that he violated the Customs laws before Customs finds out. Until recently, most prior disclosures involved either mundane errors made at the time of entry such as the wrong price on the invoice or, far less frequently, discovery that a substantial violation of the law had occurred and it was in the interest of the importer to report it.

However, prior disclosures are occurring more often and under very different circumstances today. Customs compliance audits now routinely begin with the announcement that errors disclosed to Customs, prior to a certain point in time will be considered prior disclosures of violations of the law. If an importer discovers an error while preparing for an audit, his natural inclination is to make a prior disclosure. Sometimes this is not necessary and sometimes the prior disclosure can create a host of problems.

According to the Informed Compliance Publication, prior disclosure:

*"provides reduced penalties to parties who advise Customs of noncompliance with import laws and regulations . . . In some cases the penalty may be reduced to zero!"*

A cheery thought, but it misses a basic point. Prior disclosure means you are admitting you broke the law. So importers should have a good idea of what they are getting into when they consider making a prior disclosure.

## **BEFORE YOU DO ANYTHING, READ THE PUBLICATION**

If you think you may need to make a prior disclosure, we urge you to read the *Informed Compliance Publication*, but we think you should also know the following:

\* Before you make a prior disclosure, talk to an attorney. In the forward to the Informed Compliance Publication, Customs suggests conferring with a customhouse broker, consultant or attorney. While speaking with an adviser is sound advice, this is one area where it really is in the interest of an importer to discuss the matter with a knowledgeable attorney. Attorney maintains privilege. A Customhouse broker does not.

By making a prior disclosure you are giving up some very important legal rights. Such as the right to contest the amount of the duties and penalties Customs may want you to pay. You also are putting yourself in a position to incur significant liabilities, such as liquidated damages assessed against your bond and potential criminal charges.

You want to make sure that the prior disclosure is necessary and is done correctly so that it complies with the requirements of the program. (Of course, situations involving small one-time errors may not require an attorney.)

Prior disclosures cover just violations of Title 19 United States Code, Section 1591. An importer should understand that admitting to violating Section 1592 (the civil penalty statute) and obtaining a reduction of a penalty does not preclude Customs from charging it with violating some other law.

The most extreme situation is a criminal prosecution, in which case you minimize a civil penalty by making a prior disclosure but find yourself charged with a crime (and facing jail time). The Informed Compliance Publication notes this is a possibility and states correctly that criminal prosecutions are quite infrequent. However, they do occur. And the reasons for government prosecution of a violation are not always related to the amount of money or number of Customs entries involved. More often, other laws can apply.

### **FIRST CUSTOMS, THEN THE INTERNAL REVENUE SERVICE**

Suppose you admit to Customs that the prices listed on invoices from your related foreign supplier were too high, and you actually paid far less. You paid more duty than was required, which is not a large concern to Customs. But it may be of concern to the Internal Revenue Service. The IRS is trying to calculate the cost of goods sold and to determine your taxable income. Reduce the cost of goods and you end up having more taxable income as well as potential income taxes and penalties.

Likewise, if you disclose to Customs that the garment you imported was classified incorrectly, Customs may take your check for any additional duties and then issue a Notice of Redelivery demanding the return of the goods because of an improper visa. Can't bring the garments back? You will be subject to a liquidated damage claim assessed against your bond.

*Make the Disclosure in Writing.* One common error of importers is to make a prior oral disclosure. Customs Regulations permit oral disclosures, but you must also establish that the disclosure was made before a Customs investigation had been started. Making the disclosure in writing unequivocally establishes when it was made. Sometimes oral disclosures are made during the course of a discussion with a Customs official. It is always important to "memorialize" the disclosure with a follow-up letter noting when you were speaking to the official and what was disclosed. In fact, Custom regulations *require* you to file a written follow-up within 10 days of an oral disclosure.

*Make sure you violated a law before you go to Customs.* Just because you think Customs disagrees about the tariff classification of a product or its country of origin, it does not mean you violated Section 1592 and made a false statement.

For instance, suppose you import a new product that you research and determine is a widget for Customs purposes. After a year of entries claiming the product is a widget, your customer tells you that Customs told him the product is a sprocket which has a higher rate of duty. Time for a prior disclosure? Probably not. Assuming you used reasonable care to reach your conclusions and prepare your Customs entry, Customs is stuck with the widget rate for all entries liquidated for more than 90 days.

*Prior disclosures mean the money is gone!* But (continuing with our parable), you are a good citizen and don't want to shortchange the government of sprocket duties, anger Customs or incur the cost of a law. Of course none of these are good reasons, but you make a prior disclosure and pay the duties to Customs anyway. There is no penalty assessed. But one month later, Customs issues a ruling for another good citizen that the product is indeed a widget.

Despite the fact you were right all along, you probably can't get your money back. When Customs issued the new prior disclosure regulations it stated that it may give the money back if it is later determined to be wrong.

### **NO GUARANTEE THAT CUSTOMS WILL REFUND**

The problem is, there is no guarantee that Customs will issue a refund. It is not in the regulations, but simply "policy", for Customs to decide whether they should refund money. Customs doesn't have to tell you it is considering whether this "error" was a violation of the law when you made the disclosure. Even if the Court of International Trade issues a decision classifying the goods as widgets, it is unlikely that Customs will invoke its policy as a gracious loser.

*When you make a voluntary disclosure you must tender any duties that you think are due, at least according to the regulations, but this is one area where there is some flexibility.*

If you are disclosing a one-time mistake, then cut a check and send it with the letter. However, in many situations, your ship may have been off course for a while. Many entries have been made and it will take some time to determine the outstanding duty liability. Often, Customs may need to make some findings to determine the correct duty rate or value.

The regulations allow an importer to make the prior disclosure and to then have Customs determine how much duty is due. Thirty days after Customs informs the importer of the loss of revenue, not after the disclosure, he must pay. Having Customs determine the duties due may not seem like a good idea, but in reality it is usually a joint exercise. Customs ordinarily needs information from the importer to revise the entries if it calculates the duties. If the importer calculates the duties, Customs will review the importer's calculations.

Customs regulations do require the importer to make a complete disclosure. Thus, even if you don't know how much money you owe (or what other corrective steps may have to be taken) you must submit a reasonably complete list of all the shipments.

*Make sure you make a full confession.* The benefits of prior disclosures are limited to the matters contained in the disclosure. If you disclose royalty payments that are dutiable but don't disclose the fact that the goods were misclassified, you can still be penalized for those errors.

So before you make a prior disclosure, have someone do a brief analysis of your Customs entries to make sure there aren't any other undisclosed problems. Which brings up a last point, Customs investigates prior disclosures in all but the most mundane situations. Your "thank-you" for the prior disclosure is usually a visit by a Customs agent. Thus, instead of avoiding or limiting scrutiny by Customs, the prior disclosure actually increases Customs' review of your import transactions.

Most often making a prior disclosure is to your benefit. But prior disclosure is not a simple filing and it is not an unconditional "Get Out of Jail Free" card. It is an admission that you violated the law. In your eagerness to avoid a problem, don't cause a larger one by making an incorrect or even unnecessary prior disclosure.