CANADIAN ASSOCIATION OF IMPORTERS AND EXPORTERS INC.

WITH

CANADIAN SOCIETY OF CUSTOMS BROKERS

AMPS COUNTDOWN Conferences

Toronto September 5, 2002
Windsor - September 12, 2002
London - September 13, 2002

LEGAL ISSUES FOR AMPS:
Compliance Review, Reason to Believe, Voluntary Disclosures, Appeals, Penalty Reduction Agreements

[Updated to 15/10/02]

Shane B. Brown and Jesse I. Goldman

Gottlieb & Pearson
Toronto, Ontario
Tel: (416) 250-1550
Fax: (416) 250-7889

ADMINISTRATIVE MONETARY PENALTY SYSTEM "AMPS"

Why Do We Have Administrative Monetary Penalty System (AMPS)?

- CCRA has initiated various programs over the last few years to stem rising non-compliance levels.
- CCRA is going to send a big wake-up message, including utilizing computer based auditors
- CCRA is going to make traders deal with their customs related activities in the same manner that they deal with corporate tax related matters.
- One doesn't rely on a "lick and a prayer" when dealing with corporate tax. One outsources income tax compliance related resources and expertise if not available in house.
- AMPS will require the brokerage and importing/exporting communities to be more knowledgeable and diligent than ever.
- AMPS gives CCRA the means to compel importers to reconsider compliance obligations or face added cost to their businesses.

Why Should the Trade Community Take Heed?

- In addition to monetary penalties, non-compliance will have a negative effect on performance records, possibly resulting in the withdrawal of special service option privileges and increased targeting for examinations and audits, in turn increasing the risk of civil penalties.
- Financial exposure resulting from reassessment and/or penalties on goods already sold.
- Exposure to foreign audits and lawsuits by foreign customers for non-qualifying goods imported under NAFTA.
- Take steps to prepare for the AMPS being implemented by the CCRA.

GOTTLIEB & PEARSON
International Trade and Customs Lawyers

Key Elements of the 2002 AMPS Initiative

- AMPS is a civil penalty system designed, through the application of monetary penalties, to encourage importers, exporters, carriers, and their agents to comply with Customs legislation.

- Administrative Monetary Penalties existed prior to the introduction of AMPS 2002. Most were introduced in 1992. For example, penalties between $1,000.00 and $25,000.00 applied to:
    - failures to comply with bonded or sufferance warehouse, or duty free shop, license terms and conditions, and
    - failure of importers, customs brokers, warehouse operators, etc. to keep prescribed records. (Customs Act (C.A.), former s.109.1. Superceded 29/11/01 by AMPS 2002 penalties waived until 7/10/02)

- AMPS 2002 applies to contraventions of Customs and international trade Statutes and related Regulations, CCRA program requirements, undertakings (e.g. Customs Self Assessment Program), etc. There are approximately three hundred and fifty AMPS penalties grouped within twenty-one specific categories. Even procedural, revenue neutral errors will attract penalties !

- Notices of Penalty Assessment (NPA) will be issued pursuant to C.A., s. 109.3 for contraventions enumerated in C.A., s. 109.1 and 109.2.

- Section 109.1 refers to failures to comply with any provision of certain designated Acts and Regulations. The Designated Provisions (Customs) Regulations, will designate approximately 50 Customs Act provisions, 7 Customs Tariff provisions and 58 Regulatory provisions. There will be frequent opportunities for CCRA to issue multiple AMPS penalties where the importer, etc. committed only one improper act.

- AMPS will impose monetary penalties in proportion to the type and frequency of the infraction. Most penalties are graduated and take into consideration the compliance history of the client.

- Typical penalties applicable to importers and exporters start at 5% of value for duty ($100 to $1,000 minimum penalty), and escalate to 20% of value for duty ($400 to $3,000 minimum). The maximum AMPS penalty is $25,000 per violation. A mistake repeated on 20 importations would constitute 20 violations !

- AMPS Notices of Penalty Assessment (NPA) will be issued without consideration of fault, intent, diligence or reasonable care.

- All information held by the government may be examined by the party to whom it refers. Such request would be made To the District manager of Customs or the Regional Manager of Compliance Verification, and may be made by the client or an

authorized representative, such as a customs broker. This should be done where an client believes there are inaccuracies or insufficient information in such files.

- Contraventions of Customs Act provisions remain punishable by Criminal charges seeking a fine and/or imprisonment. Such Criminal fines can now be at least $25,000 for all contraventions. Previously, fines were limited to $2,000 for contraventions of provisions not enumerated in section 160. Criminal charges are normally laid only in cases of perceived fraud.

Reviewing and Managing Your Compliance Status

- Proactive traders can significantly reduce penalty exposure. It is CCRA policy not to apply a penalty in cases where traders voluntarily reveal their non-compliance. An importer must be careful not to voluntarily reveal without a detailed review and guidance by its customs counsel.

- A review would include:
    - a detailed examination of
    - customs–related systems, processes and documentation,
    - valuation, classification and origin programs, and
    - an assessment of one's] level of compliance.

- A Report on the review's findings would serve as a platform to develop and build a Compliance Plan to ensure that all import/export related activities and communications with the CCRA are conducted with a very high degree of accuracy to avoid assessment of AMPS penalties.

- Outsourced AMPS compliance reviews/audits could be self funding in whole or part by way of:
    - Penalties avoided
        - by being compliant
        - by Voluntary Disclosure of non-compliance
    - Penalties reduced by way of a Penalty Reduction Agreement.

- The CCRA can compel disclosure of Reports issued by consultants, brokers, accountants, etc. These Reports can lead CCRA auditors directly to instances of non-compliance if the importer has not had enough time or the opportunity to rectify the situation, resulting in issuance of AMPS penalties. Reports prepared by legal counsel are privileged and cannot be so disclosed without express permission from the client. CCRA's powers to enter premises and to compel production of documentation were significantly enhanced by Bill S-23 (S.C. 2001, c.25).

- When contemplating an AMPS compliance review, a prudent importer, etc. should consider the fact that section 43 of the Customs Act provides the Minister with broad powers to obtain any documents from any person if those documents relate to the administration or enforcement of the Customs Act. Any person not complying with the

Minister's demand commits an offence punishable under Section 160 of the Customs Act by fine and/or imprisonment, unless the documents are privileged.

- Most communications between a lawyer and client, and an agent of either the lawyer or the client for the purpose of assisting and obtaining legal advice for the client, (collectively, "qualified persons") are subject to solicitor-and-client privilege. Documents created in anticipation of a definite prospect of litigation ("litigation documents") are also privileged documents. The law entitles certain people to deny officials access to oral or documentary privileged communications.

- Accountants, customs brokers, etc. have no right to refuse to disclose communications that would otherwise be subject to solicitor-and-client privilege, unless they are a "qualified person".

- Subsection 43(3) specifically protects a lawyer or a lawyer's agent claiming solicitor-and-client privilege on behalf of the client. The lawyer's client and qualified agents of the client claim solicitor-and-client privilege pursuant to common law principles.

- Voluntary disclosure to any third party by the client, or by any person entitled to claim privilege on the client's behalf, may extinguish solicitor-and-client privilege as against all third parties, including CCRA officials, because confidentiality has been breached. For example, a lawyer's client who provides a copy of a legal opinion to his customs broker, the broker not being an agent in respect of obtaining the legal advice, may render all copies of the opinion no longer subject to privilege, wherever they may be located.

- Where circumstances require an importer, etc. to have someone other than a lawyer involved in the development of legal advice, or in possession of documents that should be privileged, that information will be better protected by having such other advisors be the agent of a lawyer.

- An AMPS compliance review should particularly look for instances where the importer, etc. has 'reason to believe' that past practices are not compliant.

'Reason to Believe' and CCRA's Reassessment Policy

- 'Reason to believe' is addressed in the May 31, 2001 draft D11-6-6 Self-Adjustments to Declarations of Origin, Tariff Classification, [etc]. It is the most current draft. An amendment is expected.

- A detailed enumeration of CCRA's Reassessment Policy (i.e. when Detailed Adjustment Statements will be issued) is going to be added to D11-6-6. Such Policy is not currently published for public consumption. The current draft of such policy has been distributed to Regional Directors.

- Where there is published advice, including Trade Tribunal Decisions, Canada Gazette Notices, Customs Memoranda, Customs Notices and similar guidelines, it is considered to be in the public domain and freely available. Declarations made contrary to this advice constitutes the situation where the client should have had reason to believe an error occurred and would be subject to an AMPS penalty.

- The CCRA has therefore provided administrative guidance respecting "reason to believe". A frequent issue and one that is foreseeable in the context of the AMPS is where one draws the dividing line between a reason to believe and a reason to legitimately doubt the correctness of customs policy or regulation, e.g. tariff classification. Although the CCRA recommends obtaining an advance ruling where policy is in doubt, we know that this is not always practical.

- So what does one do when one feels there was no reason to believe? First, if there is clear published policy, follow it and appeal – both the original declaration through a request for re-determination, and, if necessary, the AMPS penalty. An AMPS penalty for failing to amend for reason to believe when there is clearly applicable published CCRA policy will not be successful – even if one eventually wins the substantive non-AMPS argument on re-determination. This is because, at the time of declaration, one will be seen to have had reason to believe that one's declaration was not correct. It is arguable that a re-determination in one's favour should also result in a cancellation of the AMPS penalty. We understand that the CCRA may be presently fine-tuning this important piece of policy, but until it is more clear than it is today, try to avoid an AMPS penalty for failing to amend where there is reason to believe.

- Where one believes that published policy is either not applicable to one's fact situation, or is ambiguous, it is arguable that one had no reason to believe and thus did not commit and "AMPable" contravention. Evidence of due diligence, such as a legal opinion, will be helpful in establishing that the CCRA may be incorrect and that one did not have reason to believe, or had reason to believe otherwise. This may be particularly true in complex cases of legislative interpretation often arising from, but not limited to, customs valuation issues, origin issues, tariff classification issues, and SIMA issues.

- Our best advice is to stay onside of AMPS and try to deal with these substantive disputes through the re-determination process. In doing so one may be able to double one's benefit by resolving the substantial dispute in one's favour and avoiding an AMPS penalty that has very limited opportunity for reversal on appeal.

- Additional duties payable as a result of a re-determination or further re-determination are payable immediately rather than within thirty days as was previously the case. (C.A., s.59(4)).

Voluntary Disclosure of Non-Compliance

- CCRA offers a program encouraging disclosure of deficiencies in accounting and payment of duties and taxes under the Customs Act, Customs Tariff, Income Tax Act and Excise Tax Act. This is known as the "Voluntary Disclosures Program" (VDP). AMPS penalties may be waived under the VDP.

- Under VDP, disclosures must be voluntary, complete and involve a potential monetary penalty. VDP permits relief from penalties, but any taxes or duties owing, plus interest, are payable.

- VDP may also be denied in situations of repetitive VDP requests for the same infraction and the importer has been unwilling to take corrective action.

Appeal and Other Redress Provisions

Bill S-23, now S.C., 2001,c.25, introduced a package of amendments to the Customs Act and other legislation , including new AMPS related redress provisions discussed below:

- **Termination or Correction Prior to NPA Issuance -** During the penalty assessment process, the importer, etc. may request that the supervisor of the officer involved review the enforcement action. If satisfied that enforcement action is not warranted, or that the officer has erred, the supervisor may terminate or correct the assessment process.

- **Withdrawal or Correction After NPA Issued -** After an NPA is issued, the Minister or designated officers may within 30 days cancel the NPA or reduce the penalty if satisfied there was no contravention or that the amount assessed was excessive (C.A., s. 127.1). Written application should be made to the NPA issuing office.

- A defense of "due diligence", or other mitigating circumstances, which may absolve the contravention or reduce the penalty, will only be considered by the Adjudications Division in a request for the Minister's decision ("appeal").

- **Appeal of an NPA to the Minister-** An NPA may be appealed to the Minister under s. 131 within 90 days (C.A., s. 129(1)). Up to 1 year after the expiry of the 90 days, the importer, etc. may apply to the Minister, through the Adjudications Division, Appeals Branch, for an extension of time in which to file the appeal. The application must show that the applicant was unable to file an appeal or that the applicant had a bona fide intention to appeal, and that it would be just and equitable to grant the application (C.A., s. 129.1). If the Minister refuses to grant the extension, that refusal can be appealed within 90 days to the Federal Court (C.A., s.129.2).

- A request for the Minister's decision should not be filed without considering the possibility that the Minister may demand additional penalty, in cases where the maximum penalty was not assessed in the first instance (C.A., s.133(1.1)).

- **Appeal of Minister's Appeal Decision to the Federal Court -** The Minister's decision on the appeal may be appealed under s. 135, within 90 days, to the Federal Court, Trial Division.

- **Extended Re-determination Appeal Time Limits -** Bill S-23 also introduced provisions allowing an importer to apply for an extension of the time limit for requesting a further re-determination of origin, classification, value for duty or marking by the Commissioner for requesting a further re-determination. The same grounds must be demonstrated as in the case of an application to extend the NPA appeal time limit. Such an application for an extended deadline for requesting further re-determination must be filed with the Commissioner within one year after the expiry of the normal 90 day period. **I**f the Commissioner refuses to grant the extension, that refusal can be appealed within 90 days to the Canadian International Trade Tribunal (CITT) (C.A., s.60.1 and 60.2). Similar provisions apply concerning appeals of the Commissioner's re-determinations to the CITT (C.A., s. 67.1)

Penalty Reduction Agreements

- Penalty Reduction Agreements (PRA's) are contracts between the client and CCRA outlining specific actions that must be undertaken or internal systems that must be instituted in order to ensure future compliance.

- CCRA's present policy allows for PRAs only where the Customs Information System (CIS) used by the importer, etc. is clearly the cause of non-compliance. A CIS is the system employed to record import and export activities for the purpose of complying with the reporting provisions of the Customs Act. A CIS may be manual and/or computerized.

- Corrective actions may include actions such as systems and equipment improvements, changes to reporting and accounting techniques, better record keeping and the training of staff.

- PRA's are really a new vehicle for the Minister of National Revenue to exercise her discretion pursuant to subsection 3.3(1) and (1.1) of the *Customs Act*. This is a long-standing provision which since 1996 has formed the basis of the CCRA's fairness initiative.

- A PRA is only available where a CCRA client has contravened the Customs Act, Customs Tariff or related regulations in a way that has resulted in an AMPS contravention and one or more Notices of Penalty Assessment totaling $5,000.00 or more. Depending on the amounts involved the PRA may be used to reduce or

eliminate the penalty amount assessed. The CCRA requires that costs related to PRA correction be at least equal to penalties reduced or eliminated.

- Importers and exporters should note that the PRA is a contract between the CCRA and the client. It is a contract that commits the client to certain remedial measures revolving around Customs Information Systems elements and requires regular reporting to the CCRA and the completion of remedial measures according to established time frames. The contract also requires the client to incur specified costs associated with the amount available for penalty reduction pursuant to the Penalty Reduction Agreement.

- Although the CCRA states that the purpose of the PRA is to facilitate the client's ability to comply with Customs legislation through a partnership to correct a Customs Information System problem, all of the burden and obligation is on the client. Failure of a client to fully comply with a PRA as to substance and timeframes will result in the cancellation of the PRA and the application of penalties and interest (that may have otherwise been reduced or eliminated had one complied with the PRA) as well as additional Notices of Penalty Assessment for ongoing contraventions not corrected during the life of the PRA.

- Thus, although new NPAs are not issued for the specific contravention addressed by a PRA during the life of the original PRA, failure to comply will incorporate these contraventions and result in additional AMPS penalties, and interest if penalties are not paid within 30 days.

- It is also very important to note that a requirement for a PRA coming in to effect is that redress under section 127.1 (corrective measures) or an appeal under section 129 (request for Minister's decision) can not remain applicable and available concerning NPAs covered by the PRA Put another way: Part of the PRA agreement is an agreement to either waive or allow to expire one's NPA correction and appeal rights.

- It is questionable whether one is better served by dealing with compliance issues on a case by case basis (i.e. where an appeal is merited, having the issue resolved through adjudication) or employing a PRA to deal with systems related non-compliance. Although the two approaches are not interchangeable, there is some overlap in strategy that will become clearer over time.

- As a legally binding contract that commits the client to opening its processes, books and records, and other information to the CCRA on a regular basis, we strongly recommend that legal advice be sought before a PRA is agreed to.

- Because the PRA is Customs Information System based, we feel that the only clients that should consider a PRA should be those capable of facilitating a change in their Customs Information Systems in a way that is not overly burdensome or time consuming. It must be realistic and add value from a customs compliance

standpoint. Clients with completely manual Customs Information Systems may find that a cost benefit analysis indicates that the requirements of a PRA are not worthwhile.

- It is also noteworthy that the costs of obtaining legal or other advice and assistance in negotiating the terms of a PRA and Customs Information Systems changes are the type of costs contemplated in a PRA arrangement with CCRA.

- Given that a PRA serves to reduce or eliminate AMPS penalties on a one to two basis to costs incurred, clients desirous of a PRA should be aware that they will be required to spend an amount to negotiate and maintain the PRA and to negotiate extensions or variations on the PRA as circumstances arise. These costs should be incurred only after obtaining professional advice concerning the panoply of issues and commitments arising from a PRA.