



# THE ROLE OF CUSTOMS IN MITIGATING ILLICIT TRADE

## The Americas Edition

### *Background paper*

*This paper has been specifically prepared by TRACIT to provide background information to support discussions in the “Combating Illicit Trade Summit of Customs Directors-General of the Americas”, Panama City, 26-27 March 2024.*

*This document is designed to guide dialogues while addressing the complexities and challenges of curbing illicit trade in the region and promote unified actions among Customs leaders in the Americas region.*

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## 1. ILLICIT TRADE AND THE ROLE OF CUSTOMS

Illicit trade is increasingly recognized as a major threat posing extensive policy, regulatory and enforcement challenge worldwide. It encompasses a wide spectrum of illegal conduct - both offline and online - with detrimental impacts on several industries: pharmaceuticals, consumer goods, tobacco, alcohol, petroleum products, fishing, forestry, agri-foods, precious metals, pesticides and thousands of products vulnerable to trademark counterfeiting and copyright piracy.

The adverse knock-on effects of illicit trade are multifold. Depending on its manifestation, it may expose consumers to sub-standard, unhealthy products; deprive governments of critical tax revenues; multiply burdens on border control; and create serious environmental degradation. Individual trafficking schemes can be highly complex, involving a plurality of jurisdictions and intermediaries operating in a web of connected illegal practices. Far from being a victimless crime, illicit trade feeds organized crime, relies on forced labor, and generates significant proceeds connected to money laundering operations.

### 1.2 The role of Customs administrations

Customs agencies worldwide have a key role to play in combating illicit trade by conducting inspections, detecting and identifying illicit goods and carrying out seizures. In doing this, they have a difficult balance to achieve: on the one hand, they are expected to facilitate trade flows by quickly processing high volumes of merchandise; on the other hand, they need to ensure that these “quick-and-easy-processing” imperatives do not obviate actions that are necessary to control illicit trade.

Whether at borders or other ports of entry, these agencies need to focus limited human and technical resources on detecting the “needle in a haystack”, effectively prevent illegal goods from entering, exiting or transiting through their countries. As tracing goods once they enter the domestic market is an even more difficult task, it is not surprising that most seizures occur at national borders.

Customs’ expertise in screening cross-border movements has long made them an essential first line of defense against illicit trade. Ensuring a strong Customs environment is thus essential in combating cross-border illicit trade. Improving transparency and accountability within Customs is crucial not only for streamlining trade across borders but also for effectively intercepting illicit goods. The World Customs Organization (WCO) notes that Customs are particularly susceptible to corruption since there can be low levels of supervision and accountability over their control and discretion across border transactions; and this situation is exacerbated by the sheer volume and complexity of regulatory frameworks.<sup>1</sup> Integrity in Customs and a robust anti-corruption framework is therefore of critical importance, and promoting a strong and robust Customs environment through enhanced public-private dialogue in cross-border processes can create significant benefits for society.

## 2. CUSTOMS' CHALLENGES, VULNERABILITIES AND SOLUTIONS

Governing global trade flows requires overcoming a variety of challenges posed by the staggering volumes of goods crossing international borders, whether via road/air/maritime containers or small parcels delivered by couriers and postal systems.

The intricate and often fragmented nature of global supply chains presents significant opportunities for traffickers to exploit these systems. Each layer of complexity or vulnerability within the supply chain offers a chance for illegal diversion of goods or concealment of their illicit origins or nature. The fragmentation of the process creates severe challenges for law enforcement authorities – including Customs agencies - in monitoring product origin and tracking its route up to the final destination.

*The following section provides background information to the Roundtable Summit with Customs Directors-General. Each section is designed to steer the conversations toward devising strategies that enhance their capabilities to fight illicit trade.*

### 2.1 Mitigating illicit trade in small parcels

*Background information to support Dialogue Session 1 (Day 1): Discussants will address the rapid growth of illicit trade in small parcels, especially air cargo, along with the need to improve targeting a range of illicit goods especially counterfeits, pharmaceuticals, narcotics and wildlife and increase the quality and frequency of electronic advance data exchange.*

Trafficking of illicit goods in small parcels (both through mail and express carriers) is growing in significant volumes and is increasingly becoming a complex problem for law enforcement to tackle. The rise of e-commerce and increased use of small parcels has made Customs' work even more challenging. Criminals use diversification of consignments through smaller and multiple parcels via online sales to reduce the chances of detection and to minimize losses from interdiction. This growing trend of high volumes of small parcels shipments strains the already limited law enforcement capacities, as agencies are traditionally more equipped to screen larger bulk shipments than to manage the screening of thousands of smaller packages. Data analyzed in the context of the WCO 2022 Illicit Trade Report confirms the dilemma of allocating Customs resources between small but frequent seizures in mail and less frequent but huge vessels seizure.<sup>2</sup>

In 2018, the OECD reported that about 63% of Customs seizures of counterfeit goods were in the form of small parcels.<sup>3</sup> Four years later, the WCO reported this number to be closer to 78%. The WCO also reports that the most used method for trafficking medicines and for concealing fauna and flora was by packing them into small parcels, which accounted for 64% and 43% respectively of all seizures.<sup>4</sup> Particularly, air cargo is the dominant conveyance method for small parcels of illegal wildlife especially live animals.

Another critical challenge for law enforcement is the increasing conveyance of narcotics through small parcels. According to the US Customs and Border Protection (CBP), the primary

mode of shipment for such drugs from international sources is via postal and express carriers, and often in quantities that are less than 1 kilogram in order to evade detection.<sup>5</sup>

### The opioid crisis and the role of small parcels<sup>6</sup>

Fentanyl, an opioid far more potent than heroin—up to 50 times, is relatively affordable when illicitly imported and mixed with other drugs like heroin or cocaine or made into fake medications. Fentanyl can be easily distributed through mail or courier services in compact parcels and envelopes. Individuals can easily purchase it online or its delivery may be organized by trafficking networks linked to international criminal organizations. Just a small package can contain thousands of doses, raising substantial risks for officers inspecting these shipments. The potential for airborne particles to cause deadly overdoses through accidental inhalation upon opening a package has heightened the danger. For this reason, US Customs officials are equipped with specialized handling tools and overdose prevention kits.

Electronic advance data (EAD) is vital for efficient risk profiling and assessment, and underpins trade facilitation, security and safety. Currently, the provision of EAD for small parcels is inconsistent and contains several gaps.<sup>7</sup> EAD is frequently absent for national posts as they lack appropriate infrastructure to fully digitize shipments; and consequently, present higher vulnerabilities to illicit trade.<sup>8</sup> This leads to cumbersome manual review processes, creating numerous opportunities for the entry of fraudulent packages into postal systems. In comparison, express carriers have better systems that can provide EAD and effectively track and trace to remove suspicious packages. However, Customs still face challenges in obtaining precise data from these carriers, and some may hesitate to share information for fear of their shipments being mistakenly intercepted and delayed.

### Policy and operational solutions

1. **Integrate Customs screening and examination process** into postal processing chains. This will enable prompt inspection upon arrival to facilitate diverting packages for automated scanning of parcels.
2. **Encourage better collection and relay of EAD** to leverage the data supplied by the exporting mail carriers to facilitate advanced Customs decisions and more efficient processes. This allows inbound Customs administrations to target items of interest in advance, while ensuring continuous flow of legitimate postal traffic. It is recommended that mail carriers collect clear, accurate and complete data in prescribed (by the Universal Postal Union) formats for harmonized collection and transmission to Customs. Furthermore, mail carriers and Customs administrations should develop or maintain IT systems that can effectively communicate with each other. The joint UPU-WCO guidelines on the exchange of EAD can be a useful guidance tool for this process.
3. **Establish cooperation with e-commerce platforms** as they possess large amounts of data on the goods, value, vendors involved, consumers and histories of parties using the platforms. This information is critically useful for risk assessment.

## 2.2 Expanding collaborations to strengthen border control

*Background information to support Dialogue Session 2 (Day 1): Discussants will address the value of expanding collaboration among Customs authorities across borders and with other enforcement agencies, international organizations, and the private sector; and the value of Customs Attachés and automated data sharing.*

The World Customs Organization (WCO) emphasizes the importance of Customs cooperation across borders to facilitate trade, enhance security, and combat illicit trade. The transnational nature of illicit trade in goods ranging from counterfeits to wildlife to narcotics and beyond, requires vigilant and coordinated efforts across the region for an effective response against the problem.

The WCO's Revised Kyoto Convention (RKC) and the WCO SAFE Framework of Standards (FoS) encourage Customs to cooperate and establish Customs-to-Customs network arrangements with the aim of promoting seamless movement of goods through secure international supply chains.

Beyond this crucial cooperation, it is equally important that Customs engage with other law enforcement bodies, as well as with regulators who can assist in determining the legality of goods. This multi-agency collaboration is crucial to drive data sharing and real-time information exchange on suspected consignments and importers/exporters. In addition, Customs Attachés also serve as vital links for intelligence sharing and facilitating the exchange of best practices between their host and home countries.

Additionally, cooperation with IP rights holders is also critical for better detection of illicit goods, especially counterfeits. Right holders possess extensive knowledge about their products, supply chain routes, authorized operators, importers, exporters and high-risk countries or transit points. This information is invaluable for developing and refining risk management systems, enabling Customs to more effectively identify and intercept counterfeit goods.

Customs can also make use of existing institutional mechanisms that facilitate multi-stakeholder cooperation. For example,

- WCO's Regional Intelligence Liaison Offices (RILO) provides a platform for sharing intelligence and operational information among Member Countries.
- WCO and INTERPOL have also instated mechanism to enhance cooperation between Customs and the police. One such effort is the Customs-Police Cooperation Handbook which provides guidance on the complementary roles of each institution and on the opportunities for collaboration.
- WCO has also set up the Private Sector Consultative Group as a platform to enhance dialogues between Customs agencies globally and the private sector.
- The WCO also hosts regular regional events to enhance cooperation among law enforcement. For example, the Regional Conference of Customs Directors General of the

Americas and the Caribbean Region acts as platform to share experiences and best practices for Customs cooperation and for decision-making in the digital age.<sup>9</sup>

## Policy and operational solutions

- 1. Increase domestic coordination and operational data-sharing** to establish strong working patterns based on systematic exchange-of-information. To acquire a full picture of illicit networks and dynamics, information stemming from several agency-specific datasets needs to be leveraged, shared and cross-checked.
- 2. Partner with regulatory/inspection authorities** to actively promote synergies with regulatory and inspection authorities by leveraging their expertise in the detection of illicit goods, threat assessment, market dynamics monitoring, etc. Regulatory/inspection authorities can also contribute to border control activities for imported, exported and transiting products, participate in investigations as well as provide access to testing laboratories and screening technologies.
- 3. Strengthen Customs to Customs information exchange.** As prescribed by the WCO Revised Kyoto Convention, it is crucial to co-operate with other Customs administrations and seek to conclude mutual administrative assistance agreements to enhance controls. Furthermore, implement guidelines and tools elaborated by the WCO to facilitate the establishment of effective and harmonized cooperation regimes between Customs authorities of different countries. Notably, the WCO Model Bilateral Agreement on Mutual Administrative Assistance in Customs Matters contains provisions on information-exchange, establishes an enforcement and investigative framework addressing hot pursuit, cross-border surveillance, covert investigations, and joint control and investigation teams. In addition, apply the concept of mutual recognition for Authorized Economic Operators (AEO) through the conclusion of Mutual Recognition Agreements between two or more Customs agencies that recognize each other's audits, controls and authorizations as equivalent.
- 4. Share accurate data at the international level** through better and accurate information-sharing mechanisms, coordination of joint, intelligence-driven operations such as sea patrols, and the establishment of inter-agency protocols and arrangements to optimize and share law enforcement resources and tools. This includes making systematic use of available operational platforms with a global reach such as Interpol's I-24/7 and WCO Customs Enforcement Network (CEN) as a central depository for enforcement-related information including seizures data and communication mechanisms.

## 2.3 Controlling illicit trade in Free Trade Zones (FTZs)

*Background information to support Dialogue Session 3 (Day 1): Discussants will address the challenge of balancing controls and measures to improve controls in FTZs and the tools available to increase transparency and reduce illicit activities in these zones.*

While FTZs serve to boost legitimate trade and attract foreign investment - including by eliminating tariffs and minimizing bureaucratic procedures - they are also vulnerable to manipulation by illicit trade perpetrators. Lack of transparency and oversight in many FTZs is prone to abuse by criminal groups who tend to exploit the many vulnerabilities, in particular:

- **Misuse of transshipment points** in cargo routings through FTZs represents a significant challenge to combating illicit trade. In practice, illicit operations in FTZs can include assembly, manufacturing, processing, warehousing, re-packaging, and relabelling to deliberately bypass sanctions, disguise identities or the country of origin. After these manipulations, goods may be imported directly into the hosting state or re-exported to another country or FTZ, potentially repeating the process.
- **Lack of clarity in the scope of regulations** presents significant challenges. In some instances, it is not explicitly stated that national Customs have the power to enforce regulations within FTZs. This lack of clarity, combined with a general “hands-off” attitude from law enforcement authorities, offers an attractive playground for unscrupulous actors to engage in illicit trade for a variety of goods.
- **Lack of resources.** Given the extremely high volumes of shipments often processed in FTZs, one serious vulnerability is inefficient cargo inspection, often due to shortages of human and technological resources. For example, WWF highlights with respect to illegal wildlife trade passing through FTZs that “the focus on the economic gains from lighter regulation and reduced Customs presence in such zones has meant that guidance on countering illicit and corrupt practices has often been overlooked in their operations”, and that “they have become particularly prone to corrupt practices that facilitate a wide range of criminal activities, including wildlife trafficking.”<sup>10</sup>

The 2020 WCO Practical Guidance on Free Zones<sup>11</sup> emphasizes the importance of maintaining a balance between promoting trade and ensuring that FTZs are not exploited for illicit activities including money laundering, tax evasion and trade in counterfeit goods or other illicit goods, such as drugs, weapons, and fake medicines. It notes that a lack of oversight over FTZs impacts not only the country where it is located, but also that country’s trading partners, thus providing a strong argument for international cooperation. The Guidance suggests expanding the Authorized Economic Operator (AEO) concept to FTZ stakeholders and strengthening partnerships with them. It also prescribes best practices for Customs to manage and monitor operations in FTZs.

Notably, the Guidance recommends that businesses engage with FTZs that are “clean”, i.e. that are legally compliant, and that governments meet the criteria outlined in OECD Code of Conduct for Clean Free Trade Zones,<sup>12</sup> such as:



- Provide unconditional access to Customs into FTZs to carry out ex-officio on-site checks in support of investigations into illegal activities;
- Ensure that operating entities are physically located within the FTZ, and that they communicate to Customs the identity of the tenants and clients in their operations;
- Prohibit those entities that do not comply with applicable Customs procedures to operate in these zones; and
- Ensure operating entities maintain digital records of all goods entering, leaving, produced or stored in the FTZ, and submit such information to Customs.

Furthermore, the OECD prescribes as a voluntary Certification Scheme,<sup>13</sup> a public private partnership between the OECD, Free Trade Zones and the TIC (Testing, Inspection, and Certification Council) Industry. It requires an independent assessment and monitoring compliance of FTZs with the provisions of the OECD Code of Conduct, which is open to non-OECD members as well.<sup>14</sup> For FTZs, implementing the Certification Scheme would signal transparency and the commitment to be clean, in turn increasing their potential to access international markets, financing, and new customer opportunities.

## Policy and operational solutions

1. **Implement strong operational measures to protect FTZs from illicit trade activity.** Notably, conduct risk profiling of suspect shipments and ex-officio checks in FTZs. Extend Customs supervision to the FTZ perimeter as well as entry and exit points. Require that FTZs maintain and report on statistical data on goods entering and leaving their territory based on their tariff classification and information that identifies the owner of goods.
2. **Adopt and implement Annex D of the WCO's Revised Kyoto Convention<sup>15</sup>** and comply with the guidelines addressed therein on explicit Customs jurisdiction over FTZs, rules on origin of goods, Customs transit and transshipment procedures.
3. **Implement WCO's Practical Guidance on Free Zones** to enhance Customs procedures/control in FTZs that will curb illicit activities, while effectively supporting the healthy development and competitiveness of FTZs.
4. **Adhere to the OECD Recommendation on Countering Illicit Trade** to support transparency in FTZs. Encourage FTZs to adopt and implement the voluntary Code of Conduct for Clean Free Trade Zones set out in the Annex to the Recommendation. Moreover, FTZs are also encouraged to get certified per the independent third-party Certification Scheme.

## 2.4 Addressing structural vulnerabilities to illicit trade

*Background information to support Dialogue Session 4 (Day 1): Discussants will address remedies and best practices to reduce Customs' vulnerability to illicit trade stemming from complex and fragmented regulatory frameworks.*

Customs face the daunting task of inspecting goods according to multiple normative frameworks encompassing multiple products and pertaining to safety/health standards, intellectual property rights (IPRs), environmental protection, and more. In the last few years, Customs in the Americas region have made advancements in improving IT infrastructure, advanced data sharing capabilities and cross-border collaboration. However, this progress cannot be fully realized until structural and regulatory vulnerabilities are addressed.

- The diverse rules and regulations across jurisdictions hinder effective regional cooperation and information sharing. Customs may not necessarily possess the technical knowledge or the expertise required to effectively enforce a very diverse spectrum of legal frameworks. The lack of harmonization of laws across the region provides opportunities for exploitation in the weaker regimes, permitting loopholes that criminals can exploit to trade in illicit goods across the borders. The diversity of trade compliance measures across countries in the region adds to this complexity, making costs for businesses high. This includes differences in import or export licenses, Customs declarations, product and safety standards to name a few. This can encourage the circumvention of legal routes, as illicit traders may seek to avoid the costs and delays associated with compliance.
- Import duties in the region can range from 0 – 40% depending on the product's value and how it is categorized in Customs.<sup>16</sup> The significant variability across countries and for different categories of goods complicates the regulatory landscape. Criminals exploit this through tariff misclassification and undervaluation of goods to pay lower duties. By misclassifying a high-tariff item as a lower-tariff item, criminals can significantly reduce the costs associated with importing goods, increasing their profit margins on illicit goods.
- Limited manpower, inadequate infrastructure, and insufficient technologies hinder comprehensive examinations of the vast number of shipments entering ports daily. The overwhelming influx of shipments and the broad cross-sectoral mandate of Customs stretch their capacity to detect illicit trade. It is estimated that even the most technologically advanced ports can inspect a maximum of only 5% of goods passing through Customs, with about 1% stopped for random inspection.<sup>17</sup> In low-income countries, Customs may lack basic means to detect illicit goods, including equipment like X-rays, canine support, rifles, communication devices or vehicles. Moreover, in many countries, Customs still have limited capacity and technological tools for effective risk assessment and profiling, often conducting checks on shipping documents manually, which results in low detection rates of illicit shipments.

## Policy and operational solutions

1. **Create mechanisms for allocating more resources**, especially in developing countries, to help authorities in complying with international standards, including for the setting up and functioning of data collection and information sharing mechanisms. It is essential for governments to provide Customs with adequate resources (equipment, human, know-how) leading to the development of more accurate “red flags” about suspected illicit trade practices and streamlining detection and inspection procedures.
  2. **Invest in cutting-edge technology** to upgrade IT infrastructure for Customs. Reliance on state-of-the-art technological solutions is crucial to support screening the myriad goods that are traded across borders each day and efficiently process and analyze the enormous amounts of information available to them. While it is impossible to physically monitor, control and secure borders through manpower alone, the use of advanced technologies, such as unmanned aerial vehicles (UAV), embedded sensor, next generation surveillance cameras, X-ray imaging systems and other non-intrusive inspection techniques are increasingly proving to be more effective than physical inspection.
  3. **Empower Customs by enhancing their knowledge** and proficiency in operating equipment essential for intercepting illicit goods, fostering a skilled and adept workforce capable of leveraging advanced tools.
  4. **Improve regional harmonization and legal cooperation.** Review existing regulations at a regional level to identify gaps that allow for exploitation. This includes reviewing conflicting regulations, penalties for violations, duties and taxes and checking whether current regulations are keeping pace with the evolving tactics of illicit traders.
  5. **Develop regulations and processes at a regional level** to address the fragmented nature of regulations across the Americas. This could be achieved through the development of common standards for safety, health, environmental protection, and IPRs. Establishing a unified legal framework would facilitate more straightforward enforcement across borders, reduce opportunities for exploitation by criminals, and lower compliance costs for businesses.
- **Increase collaboration between Customs and rights holders** to enhance detection capabilities of IPR infringing goods including through the exchange of data that can be fed into risk management systems. Furthermore, grant Customs ex-officio power to suspend the release of suspected IPR infringement goods, covering items in transit, transshipment, FTZs, and those undergoing import or export procedures, with or without notification from rights holders. In addition, authorize Customs to destroy counterfeit goods, as requested by right holders, without the necessity of initiating court proceedings, provided that the declarant or holder of the shipment does not oppose such destruction.

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