

Season 3- Episode 1

Olga Torres: Hi and welcome to Torres Talks Trade Podcast. I'm delighted to welcome Don Pearce, who is a retired special agent from the U.S. Department of Commerce's Bureau of Industry and Security, who is an experienced investigator and subject matter expert in strategic trade control policy, transnational criminal investigations, and export control systems. We're also joined by Tony Saranchak, former U.S. Customs and Border Protection auditor with experience in Customs audits, risk analysis, internal control evaluation and preparing companies for internal and external audits. He held positions at CBP's Reg Audit as an assistant field director, a Big 4 accounting firm, as well as a large importer company. Welcome guys. I'm delighted to have you join us for the first podcast where we're going to be covering Trade Wars 2.0 with a big emphasis on enforcement, export controls and the America First era. A lot has happened since the first Trump administration and the focus of the podcast is going to be on the new push for enforcement on the increased cooperation that we're seeing from a lot of these agencies that are regulating not just trade but also national security. We'll explain some of what I mean by trade and national security, and give you very practical guidance, like what we're hearing from our clients, what we're hearing from their experience as former government, being with the government, and having that in-house intelligence from the government perspective. With that, we know we've had just pretty much a new world in terms of tariffs in the United States. We had Liberation Day. We have Liberation Day 2.0 as well. Pretty much every country in the world is getting some kind of tariffs, some of them higher than others. We've had a number of Section 232 actions as well. We're expecting more in a variety of industries, from pharmaceuticals to furniture, copper, steel, and aluminum. A lot of action there, in addition to former Section 301 tariffs on China, and also adding more Section 301 investigations. I think the last one was Nicaragua; we've had the Brazil Section 301 as well. A lot is happening on their various statutes. On the tariff side, we're also seeing a push for criminal enforcement. We saw the DOJ Criminal Division memorandum in May where the focus one of the top enforcement priorities is going to be tariff evasion and customs violations. That criminal push is something that I feel like it's going to be more trendy, that we haven't seen as much in other administrations. I had already seen more FCA actions under the Biden administration that a lot of them had to do with the first Trump administration, either ADD anti-dumping duties or Section 301 on China that we were enforcing under the Biden administration under False

Claims Act. We kind of already had some civil DOJ, kind of perspective there or we were seeing some actions. But we're expecting now more on the criminal side and having more DOJ involvement possibly.

We're also expecting more coordination between the agencies. We saw that trend under the Biden administration where agencies will be sharing more information and sharing trade alerts, working on cases together, but we're just expecting that to continue. We saw the announcement - was it August, I believe? - the trade task force where it's going to be coordinated with DOJ and Customs and HSI and various other agencies. We're seeing the expansion of the whistleblower program under the DOJ to specifically cover customs violations or tariff evasion. A lot is changing, a lot of emphasis on enforcement. I think it has to do, obviously, with the fact that we can have all these regulations, but if people don't follow them, then what's the point of having them? Especially when there's as much revenue impact as we're seeing now.

With that said, and with this new enforcement era, I think a lot of the challenges that I'm seeing on the ground is companies telling me, "I know that I need to be changing the way I've been conducting business. I'm trying to absorb like let's say new tariffs," and we'll talk about the export control side and then the sanction side as well.

But on, at least on the tariff side, it's a lot of uncertainty. And a lot of uncertainty because we've had cases for example, people were saying, hey, I'm going to move my supply chain away from China. Maybe I'll go to Vietnam or another Asian country or other nations. And now all of a sudden everybody has tariffs, right? It kind of changes your theory of I need to be moving out of China, maybe still highest duties, but it's sort of a lot of uncertainty. We don't know how the Supreme Court, I guess we will know next week, how they're going to rule the IEEPA tariffs. There is uncertainty and when there is uncertainty, I feel like when you're affected by it, it is almost nature by humans to say I want to wait, why am I having to pay while the government is figuring it out?

Tony, from your perspective as a former government or Customs auditor, what were the main schemes that you were used to seeing back then to evade duties or tariffs? And are you expecting any difference today? Like are you expecting companies to be doing anything different from what it was before? And how do you expect the government to kind of acclimate to the new situation.

Anthony Saranchak: As far as the type of methods for undervaluation or non-compliance, the most intentional one and willful was double invoicing because you could hide a lot within

that. If you go another level down, first you see that there's two invoices, different dollar amounts, but then if you dig further, there could be many reasons for that and why they're trying to do that. And that's why Customs does two different tests. They look at the invoice with the entry package and then they trace it to what was paid, the actual price paid or payable and that's how they find it. A lot of people don't think of that at first when they're going to be subject to an audit or an inquiry.

Olga Torres: That's really funny that you say that. Or not funny, but interesting. In the past few weeks we've had, I should say months, but there was a call that we got a few weeks ago and we're doing a lot of consults, right, like a lot of importers trying to figure out and one of the calls that we had and it didn't lead to landing a client unfortunately for us, but it was something to the extent of, well, we're doing such and such and it was not double invoicing. It was something related to the value of the product, et cetera. And it's like, well, how does Customs find out if we're saying something on an invoice, like how do they even know what we're doing internally? And I mentioned well, proof of payment, right? Like that's one of it. But how? And I'm like, there are auditors that would do that. And the next questions are like, well, how often do they audit? What's the percentage of audits that happen each year? What's the risk that I have? And those are kind of like stats that are not, as far as I know, are not necessarily published if you're not like one of the largest importers. What would you tell someone that is asking, well, why should I? What is really my risk here? What will be your advice there? Like, yes, we can audit you, but. . . .

Anthony Saranchak: But it goes beyond just being audited because an import specialist can bring up a CF-28 and all they have to do is check off one little box and you have like 50 value questions to answer. One of them is to submit the price paid or payable a check, wire transfer, et cetera. It could be a lot of different things and sometimes that's just a general question they're asking. Sometimes they might know if you have a transaction that goes through with a lower invoice than what was actually paid, it could be found. Customs computes and compares like average unit prices and compares them and that may be a way that could come up also. Or there's many different ways an import specialist could say part of my task today is I have to look at some transactions and they happen to look at two for a certain importer and hey, these values for are really different and there goes a CF-28 sent out.

Olga Torres: Yeah. And we're seeing a lot more CF-28s now and we're also seeing Customs

really good about detecting changes and that kind of brings me to another topic. I want to stay in valuation because you mentioned it, but we are seeing a lot more CF-28 where sometimes it can start with classification, but they'll just select everything else which would include you to figure out valuation. When people say well how will they figure out what I am doing on the value side? It could be as simple as you could have other issues like classification and they have the form CF-28 and they can just select all of the above and then you have to provide more information that you weren't expecting. And it's not a full blown audit, but that's a way for the government to get information.

Anthony Saranchak: Correct.

Olga Torres: Another scheme that I've seen, which I suppose you could say, more sophisticated scheme where they try. And a lot of the times I think it's people really trying to figure out is this legal? Is this not legal? But this idea that you can take certain things out of the price, right? Like, oh, I'm sending some equipment and that will lead the producer to lower the price, is that OK? Or a lot of the times we get the question of can I take off inspection costs or labor what are your thoughts on that? And obviously explaining that that we can't do that, but do you see that? Are you expecting that to continue?

Anthony Saranchak: That's like the second example I was going to list of common errors and intentional non-compliance is additions to the price payer payable. Intentionally if you're going to do something, it's a way to hide things and make it harder to find. Not that it can't be found now but [it's] harder. Now unintentionally, also, it can get so complex. Some of these categories of expenses, it's hard to know. You have to do your research. And so sometimes an importer think they're doing the right thing and they did enough research, but they haven't and they're excluding something that really should be included.

Olga Torres: Yeah. One of the things that I've been dealing with a lot is you get the call and they give you some scenarios and all of them are like, no, can't do that or no that shouldn't be done. Oh, and also what you have been doing in the past.

And that's our worst case scenario because we want to be able to help, right? We want to be able to save you money and come up with a legal strategy to mitigate potential duties. But in many of the cases we get the call and it's like, no, we can't. All of these avenues, no, you cannot take that out from the price paid or payable. But then as we're doing that analysis,

we're also finding out they had issues in the past and that gets us into a situation of the risk of not disclosing or do you want to disclose now that you have knowledge? Like, what are your thoughts on that, especially now that CBP has better data analysis? If you can also give us your input into what kind of automation is CBP having, how can they more manually I suppose or more automatically, I guess not manually but more automatically detect these kinds of schemes or valuation or even other issues?

Anthony Saranchak: With the double invoicing that only takes a small amount of people to maybe be involved and coordinate to do that. Sometimes inadvertently where it gets complex within a company is that there's so many departments involved and that flow of the assist that machine or that part you're purchasing and sending overseas would be totally different than the PO flow and the invoice for the merchandise itself. It gets complicated and you have to have the right amount of communication between all the departments to have the knowledge and awareness that these are going on and occurring on the automation side. We saw Customs kind of ramped it up with the de minimis tariffs. And when they said that, OK, you can't do this anymore or we're going to be tracking it more. It's come out now that's where they were first using AI more and that's why they were catching more importers that were splitting an order, sending it to the same customer through two different brokers. Well, if you analyze enough data, you can catch that and it may take time, it may not be detected right away. That's where it started I think with Customs. And then they realized I think how successful it was and now it's expanding into a lot of stuff with the entry side of it. I was just looking at all the different programs and things that they're using it for. It's more a detection of improper merchandise and illegal things right now, but it's so wide in scope it's going to keep going further and be more applied to the documents upon entry. It's just a matter of time.

Olga Torres: Yeah. And it's really interesting because when we're talking about . . . I mentioned sometimes you end up discovering violations, right? And we are seeing Customs being more on top of things. Just this year alone, every time we would say we don't recommend you do that or let's wait until we get such and such guidance, et cetera and if sometimes people don't listen to us and within weeks really we will either see a CF-28 flying. We even started seeing that trend where Customs was sending the investigation letters, the Section 232 investigation letters. And we're seeing Customs using other tools that are kind of quicker like the CF-28, not a full blown audit, but it sort of forces a company to come in and

have to figure out what to say, one, and two, if at that point in the analysis they could discover based on what they're reviewing that they have issues.

Do you think that the current penalty structures will be enough to deter violations? Like are you predicting more, for example, more referrals to DOJ if there's a potential . . . like how will Customs, what are they going to be looking at to do a referral to DOJ? Because I've had pretty scary cases in the past where you could be like I'm a little worried that Customs could say this is more on the fraud side and more like knowledge and potentially more criminal. But we historically didn't really see those referrals and if they happened they were not common. And one of the concerns that I have now with the new DOJ memorandum and sort of that criminal enforcement focus and specifically naming trade and specifically within trade customs and tariff evasion, are you expecting Customs to be more prone to do referrals to DOJ?

Anthony Saranchak: I think they will be because, first of all, with the general enforcement, there's a lot of different factors. They're looking at the type of violation. How big is the importer? Is it high visibility importer? What's the nature of it? How many transactions? Is it a politically sensitive issue or a trade area Customs has as a priority area. You have all that and now you throw in everything's sensitive with these tariffs and it's competitive among the different industries, too. It's really just cutthroat at times because you hear sometimes when you talk to companies that well you know if you find a violation or something you start digging back further. When did you start using this? Well, what did you do? How did you assess that? You even thought you qualified. And sometimes what you hear is, well we were under pressure just to start using it because we found out our competitor was using it and if they qualify then we should qualify and we were going to figure that out later. And never did. It gets complicated. I think the interesting part is that as far as I don't know if anybody knows what the right point is for what amount of penalties is effective because it's a balance between hitting those with a good hammer that are really intentionally doing the wrong thing. But also trying to facilitate Customs' job is also to facilitate trade and make sure that everything's applied evenly among the importers. And that gets harder sometimes when you have these sensitive issues of the tariffs, all these extra tariffs now. I mean, it's like unprecedented and everybody's, all these companies are looking for ways to be more cost competitive, stay cost competitive at a time they're still dealing with post COVID issues. And now they have all this. It puts a lot of pressure on people to try and guess what their competitors are really

doing. And is this what I have to do temporarily just to survive and it's not maybe something intentional that they wanted to do forever, but it happens. It happens.

Olga Torres: It's a really interesting time because we've always seen this, but I think it is exponential now where we see situations where importers want to, let's say, do a disclosure, right? They find out that they have an issue, whether it's valuation, classification, you name it. And I think the struggle that we're seeing just based on the current climate and the duties that just skyrocketed quickly like sometimes they can't pay the duties. The duties are so much, and there's like that misunderstanding that if I do a prior disclosure, oh, the duties may go away. It's sort of explaining, well, no, if we do a prior disclosure, yes, it gets your mitigation - hopefully we're not seeing some kind of DOJ referral, etc. - you still have to pay the duties, right? Like Customs is not going to let go on those duties. What we're getting you with the prior disclosure is you're likely not going to get penalties. And I see that that's a big issue right now because you want to clean up, but you have to pay the old duties.

And it can be the past five years, although in most cases the problem is like in the past few months, right? Because that's when it skyrocketed.

This is a really tough question: What will be your recommendation for an importer that is struggling to pay duties but wants to clean up? What are ways that you think that it can be done like a prior disclosure and doing a clean-up where you're also kind of facing a duty situation that you may not be able to afford?

Anthony Saranchak: If you're just trying to do the right thing currently, first you have to, I think you have to make sure you have a good broker that you can talk to because they're going to have eyes not just on your company, but other importers and more within your industry probably and though they can't give you specifics about cost add or value or anything, they can kind of give you on a high level maybe what they think. So have a good broker, have a good expert and have regular communication with your general counsel. And appropriate external expertise, an attorney probably if you're talking about something that's sensitive that you might have a disclosure. This just comes down to the tone of the company, the risk, and their culture. You have to be able to say we're just not going to do what we think everyone else is doing just to stay competitive. And that's hard, that's pressure, but that's what it takes. You can't just listen to what you hear is not always what other companies are doing. And first sale I think is the biggest example of this, not on a fraud level, but two executives have lunches together, "oh, we're claiming all this first sale, isn't it great? We're saving all

this duty.” This executive comes back and calls his customs manager to get on this. “We need to claim first sale now.” Okay, none of them have talked about what are the requirements. How long is it going to take that we first have to assess if we can meet the requirements?

Olga Torres: Yeah, we're seeing that on USMCA, right? Just declare USMCA and it's like, have you done the analysis? Like there's a really in-depth complex analysis that goes into it. I always say if it sounds too good to be true, it probably is. So just assume that until you do the analysis.

Anthony Saranchak: The difference I've seen from being at Customs and being a consultant now, you can pick up on some of these issues. When I was an AFD, assistant field director, with Customs, I didn't have to worry about, this is how you have to find a way to do this. This is what you're going to do. These are going to be the recommendations in the audit report that you have to figure out. But on the consultant side, you see that sometimes you have a manager that has someone difficult above or the person above them doesn't fully understand the whole scope of the issue, so then you have to help that person educate the other.

Olga Torres: Yeah, I know that's so true. I've also seen a lot of pressure on brokers and attorneys, and I'll get to that. But brokers specifically, a lot of, “hey, my broker told me,” and it's typically something like really good, like quick fix. And “my broker is wrong because I relied on my broker that told me that there was an exclusion.”

Anthony Saranchak: Yes.

Olga Torres: And now, “should I sue my broker?” Believe it or not, we're getting those questions. I also started seeing, I recently got contacted to be an expert witness and I ended up not taking the case, but against a customs attorney. And sometimes like they're not 100% customs attorneys. There could be, like, more litigation attorneys or transaction attorneys that are like, “oh, I can figure out the tariff situation. I can read the EO's and you know, figure out what applies to what,” and they don't really understand the nuances of customs compliance and sort of dealing with the agency. I think there's a lot of like even risk for attorneys, for customs brokers. If you're not up to speed on everything, if you're not, that's not really your practice area, but there's a lot of push on you to kind of like figure it out because everybody's asking you. I do think people . . .there's a lot of pressure, right? There's a lot of pressure on

importers. I've had situations where we're almost kind of like the bad guys when we're delivering the message. And I'm just a messenger. I'm not saying I agree with the rules or I don't. I'm just telling you what the rules are.

And I think part of that, and I and I'll move to you, Don, because we're seeing it on the export side as well. It's that, like, flurry of things that are happening, right? And it's just a lot of the methods are somewhat unconventional. Like I know when Mexico, for example, got a pause on trade, we were finding out from social media posts there was nothing 100% official. It's just sort of hard to keep track of what's going on. And then at least on the import side, you're owing more money all of a sudden that you can't really collect from anybody else. You can't really raise your prices right away and stay competitive anyway. And you were told, some people tell me, "Well, this is a pro-business administration. This doesn't sound pro-business to me." And there's this sort of hesitation to change, disbelief, like sort of like there's stages. We're calling it the stages of grief, right? "Is this really happening? That can't really be happening to me. This is crazy, I'm going to go out of business. I have to figure something else in the meantime." Not understanding the government has a statute of limitations, they can look back. And the more that you. . .if you don't take that pain of figuring out the right way of doing it, I think it's going to backfire eventually.