

## Customs in the Cayman Islands





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# EXECUTIVE SUMMARY

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Customs is often the first official organisation encountered by people when entering a country and by traders importing and exporting goods. Over the last 15 to 20 years, Customs organisations worldwide have been modernising the way they operate in response to both the growth in world trade and the rise in international terrorism. Customs organisations need to be able to facilitate trade as effectively as possible, while maximising the value of revenues collected through taxes, duties and fees; and preventing illegal goods from entering the country.

Customs makes a significant contribution to the Cayman Islands economy, through collecting duties on behalf of the Cayman Islands Government and helping to protect the borders by restricting the entry of contraband goods.

In 2016, the Cayman Islands Government requested support from the UK Government to carry out reviews of immigration and customs functions and search and rescue (SAR) capability in the Cayman Islands. In December 2016, the UK Border Force Intelligence Directorate and UK Maritime and Coastguard Agency (MCA) carried out separate reviews and prepared reports setting out a number of observations and recommendations to strengthen border security and SAR capabilities. In August 2017, the Premier announced that, as part of the 2018 Strategic Policy Statement, the law enforcement units in the Immigration and Customs Departments would be combined to make a single border protection agency; and additional funding would be provided to create a new Coast Guard unit.<sup>1</sup> Both of these bodies are expected to significantly improve border security. Cayman Islands Customs and Border Control was established on 1 February 2019, and the Cayman Islands Coast Guard is expected to begin operations in the last quarter of 2019.

The objective of our audit was to determine how efficient and effective Cayman Islands Customs is at collecting revenue and protecting the border. Specifically, we attempted to answer the following audit questions:

- Are Customs' operations supported by sound legislation and strategic direction?
- How efficient and effective is Customs at collecting revenue and facilitating trade?
- How efficient and effective is Customs at protecting the border?
- How well does Customs plan and manage its workforce to achieve its strategic direction?

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<sup>1</sup> Statement by Premier Hon. Alden McLaughlin, MBE, JP, MLA, 2018 Strategic Policy Statement, 23 August 2017.

Our audit covered the revenue collection and border security operations of Cayman Islands Customs, including the Department of Customs in the Ministry of Finance and Economic Development (MFED) and Customs functions within District Administration in the Ministry of District Administration, Tourism and Transport (MDATT). The audit did not look at border protection issues outside the responsibility of Cayman Islands Customs.

Our audit was carried out in 2018, and at that time the Customs senior management team had been in place for just over a year.<sup>2</sup> Plans were also being developed to merge the Customs Department and elements of the Immigration Department into the new Cayman Islands Customs and Border Control (CBC); and to create the Cayman Islands Coast Guard. Our audit findings refer to operations of the Customs Department that were in place during 2018. Customs and Border Control (CBC) was established subsequent to our audit, and our recommendations are therefore directed to CBC (and the relevant ministries).<sup>3</sup>

## KEY MESSAGES

Customs is responsible for collecting revenue, facilitating trade and protecting the borders. However, it did not have a strategic plan to provide vision and clarity of organisational objectives and priorities. Nor did it use performance information effectively to help demonstrate its efficiency and effectiveness or to identify areas for improvement. At the end of December 2018, the Customs Department had around 157 staff but did not have a workforce plan or corporate training plan to help plan and manage staff effectively. Customs had started a project in January 2017 to modernise its IT systems. However, we found that the first phase of the project was not well managed, resulting in delays and cost overruns.

Customs collects around \$165 million a year in duties, fees and fines on behalf of the Government. This amounts to around 20 to 25 per cent of annual government revenues and revenue collected from duties, fees and fines is consistently higher than budgeted. We found that the process for projecting revenues could be improved. It is also unclear whether the Government is collecting all of the revenue that it should as there continues to be significant weaknesses in the approach to awarding and managing revenue concessions.

Customs has played a significant role in protecting the borders, together with the Department of Immigration, Royal Cayman Islands Police Service and the Department of Agriculture. The Government is

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<sup>2</sup> The Collector of Customs took up post in August 2015, after a period of three and a half years during which four Acting Collectors had been in place. Two Acting Deputy Collectors were appointed in July 2016, after the previous incumbents retired, and were appointed permanently in January 2017.

<sup>3</sup> Prior to Customs and Border Control (CBC) being created, the Customs Department was part of the Ministry of Finance and Economic Development (MFED). As of 1 February 2019, CBC is a department within the Ministry of Human Resources and Immigration (MHRI). MHRI is changing its name to the Ministry of Employment and Border Control. MFED remains responsible for preparing budgets and overseeing revenue concessions for the Cayman Islands Government.

changing its approach to border protection. On 1 February 2019, Customs was merged with parts of the Immigration Department to create Customs and Border Control (CBC). This is only the first step in improving border protection; much more needs to be done. Customs has already started moving to a more risk-based and intelligence-led approach. This means that the collection, analysis and use of information and intelligence will need to improve significantly. CBC will also need to ensure that it has the right resources in place, including staff with the right skills targeted at the right areas; and that it has user-friendly IT systems in place.

# GLOSSARY OF ACRONYMS

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|         |  |
|---------|--|
| ACI     | Advance Cargo Information  |
| API     | Advance Passenger Information  |
| ASYCUDA | Automated System for Customs Data  |
| CBC     | Customs and Border Control   |
| CFED    | Customs Fraud Enforcement Division   |
| CIG     | Cayman Islands Government  |
| CIMS    | Customs Information Management System  |
| CIU     | Customs Intelligence Unit  |
| CMC     | Change Management Committee (for the IT modernisation project)                                 |
| CNET    | Customs Narcotics Enforcement Team   |
| COLS    | Customs Online System  |
| CPIU    | Container Processing Inspection Unit   |
| CSD     | Computer Services Department   |
| DOA     | Department of Agriculture  |
| IRIS    | Integrated Resource Information System (CIG financial information system)                      |
| JMU     | Joint Marine Unit  |
| MCA     | UK Maritime and Coastguard Agency  |
| MDATT   | Ministry of District Administration, Tourism and Transport                                     |
| MFED    | Ministry of Finance and Economic Development   |
| MHRI    | Ministry of Human Resources and Immigration<br>(now Ministry of Employment and Border Control) |
| MOU     | Memorandum of Understanding  |
| NIM     | National Intelligence Model  |
| PNR     | Passenger Name Record  |
| RCIPS   | Royal Cayman Islands Police Service  |
| SAR     | Search and Rescue  |
| SOP     | Standard Operating Procedure   |
| TRACES  | Trader Registration and Access to Customs e-Services System                                    |
| TRIPS   | Total Revenue Integrated Processing System   |
| WCO     | World Customs Organization   |
| WTO     | World Trade Organization   |



# INTRODUCTION

## CUSTOMS PLAYS AN ESSENTIAL ROLE IN BOTH COLLECTING REVENUE AND PROTECTING THE BORDER

1. Customs is one of the first agencies of government that residents and visitors encounter when they enter a country. Customs operations in the Cayman Islands are now regulated by the *Customs and Border Control Law, 2018*, which came into effect on 1 February 2019. The legislation established the new Cayman Islands Customs and Border Control (CBC) from two predecessor bodies – the Customs Department and those elements of the Immigration Department related to border control. CBC plays a vital role in supporting the economy and security of the Cayman Islands as it is responsible for collecting revenue from duties on imported goods; and controlling the entry of goods, including those prohibited or restricted by law such as firearms and drugs.
2. Prior to 1 February 2019, Customs activities were regulated by the *Customs Law (2018 Revision)*. Our audit focused on the operations and activities that were in place during 2018, before CBC became operational on 1 February 2019.
3. In addition to the *Customs and Border Control Law, 2018*, Customs and Border Control has wide-ranging powers, usually in conjunction with other public entities, under a large number of other laws as outlined in Exhibit 1.

**Exhibit 1 – Cayman Islands laws that relate to Customs and Border Control**

| Customs & Trade Facilitation               | Agriculture Related   | Crimes & Drugs                              | Immigration, Law & Order        |
|--|---|---|---------------------------------|
| Customs & Border Control Law, 2018         | Animals Law (2015 Revision)                                     | Dangerous Substances Law (2017 Revision)    | Immigration Law (2018 Revision) |
| Customs Tariff Law                         | Endangered Species Protection & Propagation Law (1999 Revision) | Misuse of Drugs Law (2017 Revision)         | Penal Code (2018 Revision)      |
| Advance Passenger Information Law, 2018    | Endangered Species (Trade & Transport) Law (2017 Revision)      | Evidence Law (2018 Revision)                | Bail Law (2015 Revision)        |
| Export Duty Law (1998 Revision)            | National Conservation Law, 2013 (partly in force)               | Proceeds of Crime Law (2018 Revision)       | Traffic Law, 2011               |
| Special Economic Zones Law (2017 Revision) | Plants (Importation & Exportation) Law (1997 Revision)          | Anti-Money Laundering Regulations           |                                 |
| Trade Marks Law, 2016                      |   | Trafficking in Persons Law (2015 Revision)* |                                 |
|  |   | Firearms Law (2008 Revision)                |                                 |

Source: OAG analysis of legislation

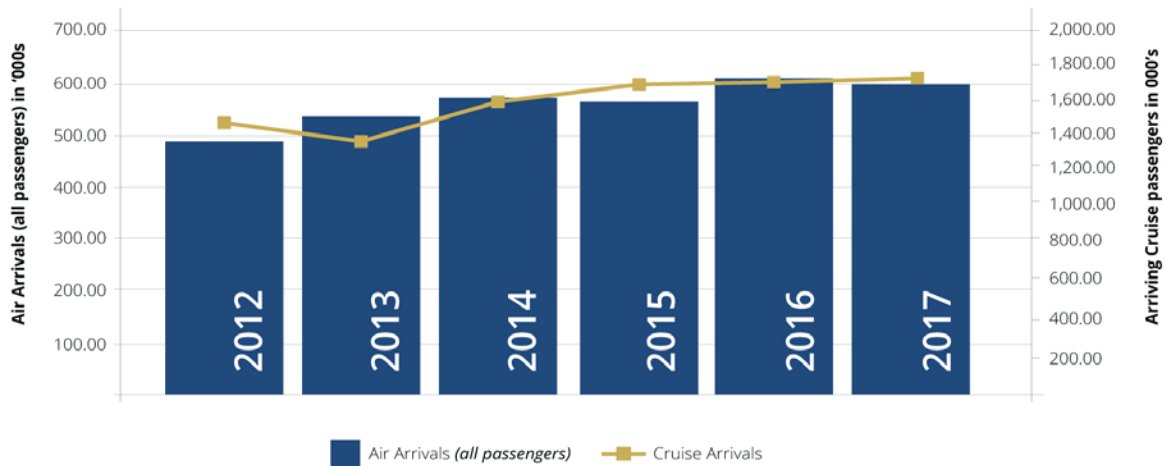
4. Customs Officers are law enforcement agents of the Cayman Islands Government (the Government or CIG) and have distinct roles and responsibilities under different Cayman Islands laws. Customs Officers are also responsible for stopping or deterring the entry of any prohibited items including drugs and firearms and intercepting prohibited goods that could harm the local agriculture.
5. Prior to 1 February 2019, Customs activities operated across two government ministries: the Customs Department in Grand Cayman, under the Ministry of Finance and Development (MFED); and Customs in Cayman Brac and Little Cayman, which was part of District Administration within the Ministry of District Administration, Tourism and Transport (MDATT). The Customs Department was headed by the Collector of Customs and employed around 157 staff as at December 2018.<sup>4</sup> Customs within District Administration, employed a further 13 staff reporting to the District Commissioner. The Customs Department operated in three sections: Administration, Revenue Collection, and Border Protection, each headed up by a Deputy Collector. The Finance Unit was headed up by the Finance Manager and reported directly to the Collector of Customs. The three sections covered the following:
  - Administration provided corporate services such as human resources, information technology, training and statistics.
  - Revenue Collection was responsible for the collection of duties and fees at the airport, warehouses, and courier shipments; and for fraud investigation.
  - Border Protection was responsible for inspections at the seaport and airport, and for the Container Processing Inspection Unit, Customs Intelligence Unit, and the Customs Narcotics Enforcement Team.
6. Customs also worked with other border protection agencies such as the Department of Immigration; the Department of Agriculture (supporting the regulation and importation of plants, animals and food products to protect the health of people and the ecology of the islands); and the Joint Marine Unit led by the Royal Cayman Islands Police Service (RCIPS) to carry out coastal patrols.
7. Changes in the economy have a direct impact on Customs activity. Between 2012 and 2016 the population of the Cayman Islands increased by around 7.5 per cent, from 56,732 to 61,361; and the value of imports increased by around 11 per cent, from \$758.8 million to \$854.2 million. Exhibit 2 shows that the number of passengers arriving through the airports increased year-on-year in the six years from 2012 to 2017, with an overall increase of 21 per cent. It also shows that passengers arriving on cruise ships increased by around 15 per cent over same period. Together these factors increase the volume of people and transactions that Customs needs to manage. Current forecasts

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<sup>4</sup> OAG analysis of Employee Listing of Customs Department as of 31 December 2018

show that the population is likely to grow a further 11 per cent by 2020. This growth in the population is likely to further impact Customs activities in the future.

**Exhibit 2 – Air and cruise ship arrivals in the Cayman Islands, 2012 – 2017**



Source: Economics and Statistics Office, Tourism Statistics

8. All travellers and goods entering the country present risks. For example, importers or visitors may attempt to evade paying duties or to import dangerous or prohibited goods. In 2016-17 Customs made 58 arrests for drug offences and 11 arrests for firearms offences as well as seizing drugs and ammunition. Customs also participated in 29 joint operations with RCIPS and Immigration, which resulted in 19 arrests and seizures of drugs and firearms.<sup>5,6</sup>
  
9. Customs collects a significant amount of government income – in calendar year 2017, a total of \$167.6 million, made up of \$161.9 million in duties and \$5.7 million in environmental fees.<sup>7</sup> This was around 24 per cent of \$705 million total government coercive revenue (revenue collected for which no direct service is provided).<sup>8</sup>

<sup>5</sup> 2016-17 covered the 18-month period from 1 July 2016 to 31 December 2017.

<sup>6</sup> Ministry of Finance and Economic Development Annual Report 2016-17.

<sup>7</sup> 2017 Annual Economic Report, Economic and Statistics Office (ESO), Cayman Islands Government

<sup>8</sup> Note that the revenue numbers here differ from those in paragraphs 67-68 of this report due to the fact that the numbers used in the ESO report are based on a calendar year (Jan – Dec) while the numbers used in the paragraphs 67-68 are based on a fiscal year (July – June).

## THERE IS A GLOBAL EFFORT TO MODERNISE CUSTOMS OPERATIONS

10. Since 1990, world trade has expanded by 3.0 to 4.7 per cent annually. Experience has shown that countries that integrate successfully into the world economy have the highest growth rates.<sup>9</sup> Successful integration includes, for example, improving allocation of resources, intensifying competition, raising productivity, and accessing new technologies, designs and products. One of the most important functions to support world trade is an effective Customs service that provides traders with transparent, predictable and speedy clearance of goods, and provides travellers with quick passage through border entry points.
11. The rise of international terrorism and the spread of international criminal networks mean that national security has become an increasing concern for many countries. To improve border security, Customs departments need to become less dependent on importers' declarations and better able to independently assess the risk of shipments and travellers before they arrive. They therefore need to use information and intelligence more effectively to identify risks and issues in advance and target their efforts accordingly. Customs departments are also becoming increasingly dependent on information technology (IT), sophisticated analysis, and the ability to communicate information quickly to front-line officers.
12. The World Customs Organization (WCO) promotes and supports the global modernisation of Customs functions. The WCO includes 182 member states that together account for 98 per cent of world trade. The WCO Council adopted the revised Kyoto Convention in June 1999 as the blueprint for modern and efficient Customs procedures in the 21st century; it sets out a number of key principles for Customs administration. The Cayman Islands is associated with the WCO through the United Kingdom, but it is not a member in its own right. However, Cayman Islands Customs does recognise the WCO model of modernisation and plans to move toward it.

## CHANGES IN CAYMAN ISLANDS BORDER PROTECTION

13. In 2016, the Cayman Islands Government requested support from the UK Government to carry out reviews of immigration and customs functions and search and rescue (SAR) capability in the Cayman Islands. In December 2016, the UK Border Force Intelligence Directorate and UK Maritime and Coastguard Agency (MCA) carried out separate reviews and prepared reports setting out a number of observations and recommendations to strengthen border security and SAR capabilities.
14. As part of the 2018 Strategic Policy Statement, the Premier announced in August 2017 that the law enforcement units in the Immigration and Customs Departments would be combined to make a

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<sup>9</sup> *Customs Modernization Handbook*, World Bank, 2005

single border protection agency and that additional funding would be provided to create a new Coast Guard unit.<sup>10</sup> Both of these bodies are expected to significantly improve border security.

15. The Cayman Islands Customs and Border Control Service (CBC) started operating on 1 February 2019. The Cayman Islands Coast Guard is expected to begin operations in the last quarter of 2019; in the meantime, the Joint Marine Unit will continue to deliver operational responses to concerns at sea.

## ABOUT THE AUDIT

16. We carried out this audit to determine how efficient and effective Cayman Islands Customs is at collecting revenue and protecting the border. The audit sought to answer the following questions:

- Are Customs' operations supported by sound legislation and strategic direction?
- How efficient and effective is Customs at collecting revenue and facilitating trade?
- How efficient and effective is Customs at protecting the border?
- How well does Customs plan and manage its workforce to achieve its strategic direction?

17. The audit was carried out during 2018, as plans were being developed to merge the Customs Department and elements of the Immigration Department into a new body – Cayman Islands Customs and Border Control (CBC) - and to create the Cayman Islands Coast Guard. Our report refers to operations that were in place during 2018 in the previous Customs Department. Since our audit, the Customs and Border Control (CBC) has been established and our recommendations are therefore directed to CBC and the relevant ministries.

18. Our audit covered the revenue collection and border security operations of Cayman Islands Customs, including the Department of Customs in the Ministry of Finance and Economic Development (MFED), and Customs within District Administration in the Ministry of District Administration, Tourism and Transport (MDATT). We reviewed how Customs worked with partner agencies such as the Royal Cayman Island Police Service (RCIPS), including the Joint Marine Unit and the Joint Intelligence Unit, the Department of Immigration, and the Department of Agriculture. The audit did not look at border protection issues outside the responsibility of Cayman Islands Customs.

19. In carrying out our audit we conducted interviews with senior officials in Customs and its partner agencies and met with Customs' customers including shippers, importers, brokers and courier services. We reviewed documents including legislation, government studies on border security

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<sup>10</sup> Statement by Premier Hon. Alden McLaughlin, MBE, JP, MLA, 2018 Strategic Policy Statement, 23 August 2017.

reform, corporate plans, project reports, financial data and intelligence data and reports. We analysed financial, performance and human resource data. We discussed preliminary findings with Customs and other agencies and revised our analysis as required. More information about the audit, including audit criteria, approach and methodology can be found at Appendix 1 of this report.

20. The report is divided into three sections:

- Strategic and business planning
- Revenue collection
- Border protection

21. The assistance and cooperation we received from Customs and Cayman Islands Government officials in all phases of the audit is gratefully acknowledged. Without their help, the audit could not have been completed.

## STRATEGIC AND BUSINESS PLANNING

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22. As part of our audit we reviewed the legislative framework that supports Customs' activities; Customs' strategic planning; the use of performance information to manage the business; workforce planning and management; and the project to improve the use of information technology (IT).

### NEW ARRANGEMENTS ARE IN PLACE FOR CUSTOMS OPERATIONS IN THE SISTER ISLANDS

23. Customs activities must be supported by fit-for-purpose legislation that allows them to function as effectively as possible. The *Customs Law (2018 Revision)* provided an adequate basis for Customs operations and provided for most of the changes that were needed to modernise Customs. The *Customs and Border Control Law, 2018*, which came into effect on 1 February 2019, transferred to Customs and Border Control (CBC) the roles and responsibilities of Customs that were set out in the 2018 law.
24. We found that prior to the establishment of CBC, the way Customs was operating in Cayman Brac and Little Cayman was not in line with legislation. The *Customs Law* stated that the Collector of Customs was responsible for the management, supervision and control of Customs; empowered to collect revenue; and authorised to appoint Customs Officers. However, Customs in the Sister Islands has historically operated under District Administration within MDATT. This meant that the District Commissioner rather than the Collector of Customs appointed and directed Customs Officers that worked in the Sister Islands. This approach posed risks as customers could challenge the authority under which revenues were being collected and any arrests or seizures made could be disputed. In addition, the separation of Customs into two departments led to some operational difficulties, including access to training and equipment. At the time of our audit only six Customs Officers in Cayman Brac had received "use of force" training, and none of this training was current; only two officers had received "profiling" training. Customs staff in Cayman Brac did not have access to appropriate safety and enforcement equipment such as batons and vests.
25. This issue has been resolved with the enforcement of the new legislation, which clearly sets out that the Director of CBC is accountable for CBC's strategic, operational and tactical functions across all three islands. CBC (and MHRI) and District Administration (and MDATT) have agreed a Memorandum of Understanding (MOU) for administrative support services "back-office functions" for CBC operations in the Sister Islands. The MOU states that there will be a Deputy Director of CBC with responsibility for managing operations in the Sister Islands and the CBC Director may delegate responsibilities to a CBC Officer in Little Cayman for day-to-day operations on the island.

## A STRATEGIC PLAN IS NEEDED TO PROVIDE DIRECTION AND CLARITY

26. To help achieve their objectives Customs departments, like any other organisation, need to have strategic plans to help direct their activities and set clear goals, objectives and priorities. We therefore expected Customs to have a long-term strategy that:

- sets out its vision, goals and objectives;
- identifies relevant changes in its environment and details how it will respond to them;
- has clear baselines describing its current state of affairs;
- identifies success measures, including outcomes; and
- is linked to financial plans to demonstrate affordability and to workforce plans to guide human resources decisions.

27. The European Commission's Directorate General for Taxation and Customs Union published *Customs Blueprints* in 2015, which details how gaps and needs analysis can be used to develop plans for meeting Customs strategic goals.<sup>11</sup> Our review of Customs services across the world identified some good-practice examples of strategic plans. For example, the *Canada Border Services Agency 2017-18 Departmental Plan* includes all of the elements that a good strategic plan should include.<sup>12</sup> The New Zealand Customs Service also has a strategic framework and reports progress against this in its annual reports.

28. We found that Cayman Islands Customs did not have a comprehensive strategic plan covering all of the elements that we would expect. The Collector of Customs told us that he had intended to develop a strategic plan for the Customs Department but this was put on hold after the Premier's announcement about the creation of Customs and Border Control.

29. Although Customs did not have a strategic plan it did have some of the building blocks in place. In 2017 it developed a Business Process Document (Customs Modernisation), which set out Customs' vision as transforming itself from a "gatekeeper" to an intelligence-led, risk-managed service conforming to the World Customs Organization (WCO) model of Customs modernisation. It also set goals and objectives for changing its business processes to achieve the vision. However, the Business Process Document does not contain any of the other components of a strategic plan. For example, it does not present a comprehensive survey of environmental factors affecting Customs; establish clear cost and performance baselines for its current operations; identify what performance levels it aims to achieve through modernisation; or provide a clear link to financial or workforce plans.

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<sup>11</sup> *Customs Blueprints: Pathways to better customs*, European Commission, 2015.

<sup>12</sup> *Canada Border Services Agency 2017-18 Departmental Plan*, Canada Border Services Agency, 2017.



30. To determine how well Customs was achieving its overarching vision, we compared its processes at the time of our audit to the WCO principles. Exhibit 3 summarises our analysis.

**Exhibit 3 – Cayman Islands Customs Department operations compared to World Customs Organization’s (WCO) key principles**

| WCO Key Principles for Customs Administration  | Cayman Islands Customs’ Operations & Processes (December 2018)   |
|--|--|
| <b>1</b> Transparency & predictability of Customs controls                                     | Limited public information about policies and procedures affecting individuals and companies.  |
| <b>2</b> Standardisation and simplification of goods declaration & supporting documents        | Customs has been working to simplify tariff codes. However, there are no guidelines on goods declaration or supporting documents.                                |
| <b>3</b> Simplified procedures for authorised persons  | Green (nothing to declare) line at airport was introduced in July 2018. However, this does not always operate as intended. Preferred traders programme in place. |
| <b>4</b> Maximum use of information technology   | Use of IT is limited. The COLS project is intended to improve this.  |
| <b>5</b> Minimum necessary Customs controls to ensure compliance with regulations              | Customs procedures manuals are in place and implemented by officers when determining compliance.   |
| <b>6</b> Use of risk management & audit based controls   | No progress.   |
| <b>7</b> Coordinating intervention with other border agencies such as immigration & the police | Customs works with other border agencies such as Immigration and RCIPS, including the Joint Marine Unit.   |
| <b>8</b> Partnership with trade  | There is limited focus on facilitating trade although there was some consultation during the COLS project.   |

*Source: Progress of the Cayman Islands Customs is based on OAG analysis against the WCO key principles for Customs Administration as part of the General Annex of the Revised Kyoto Convention from the United Nations Trade Facilitation Implementation Guide.*

31. Our analysis of Customs operations against the WCO key principles determined that there is limited or no progress against half of the key principles, namely transparency and predictability, information technology, risk management and audit, and partnership with trade. Customs has made considerable progress in applying the remaining principles, but almost all require further development to improve service quality. For example, while harmonised tariff codes have been simplified and forms are easier to complete, there are no detailed guidelines to help importers fill out their declarations.
32. An overarching strategic plan is important for communicating the vision and priorities of an organisation. We found that Customs officials had different perceptions of the priorities for border protection, which included fraud prevention, anti-cybercrime and anti-terrorism.
33. As previously outlined, our audit was carried out while the merger of the Customs and Immigration departments was underway. It is important that the new organisation – Customs and Border Control - develop a strategic plan as soon as possible to provide the strategic direction and leadership that will be needed for staff and to measure the organisation’s success in the future. This will need to reflect the new strategic priorities for the organisation and it is important that it reflects both Customs and Immigration activities so that is seen as a merger rather than a take-over.

**Recommendation 1: Customs and Border Control should develop a strategic plan as soon as possible. The plan could build on the Customs Department’s Business Process Document and should ensure that it captures all of the relevant activities of both predecessor organisations.**

#### **BETTER PERFORMANCE INFORMATION IS NEEDED TO MANAGE THE BUSINESS EFFECTIVELY**

34. Organisations need good quality performance information to measure whether they are achieving their strategic goals. This should include a range of performance indicators covering all activities and functions that are able to measure productivity and efficiency and demonstrate the achievement of outputs and outcomes. Management should use this performance information to inform decisions that will help them manage their business more effectively.
35. Our review of other Customs services across the world found that they had a range of performance measures linked to their strategic objectives. For example, the New Zealand Customs Service:
  - monitors the trend in its rate of profiling arriving passengers using Passenger Name Data as an indication of its ability to implement its modernisation and risk management programmes;
  - estimates the “level of harm” avoided by its interception of contraband;
  - is attempting to develop a measure of the “strike rate” of interceptions based on intelligence and the overall rate of compliance;
  - measures clearance times for passengers based on a 45-minute standard;

- measures the trend in unit costs for processing travel and trade; and
- measures the level of public trust in Customs.

36. As part of the budgeting process, the Ministry of Finance and Economic Development (MFED) sets a range of outputs for Customs in its *Annual Plans and Estimates* that include quantity, quality and timeliness objectives. Our review of these identified a number of weaknesses in the established performance measures, including the following:

- Most of the performance measures are activity based rather than based on outcomes - for example, the number of passengers to be processed. Some of these activity-based measures may lead to perverse behaviours - for example, processing airline passengers in Cayman Brac within five minutes may not be possible if any problems are encountered but Customs Officers believe they should process passengers quickly simply to meet the target.
- Many of the performance measures are subjective. For example, in the processing of passengers and inspection of aircraft, vessels and cargo, inspecting officers are to be highly trained but there is no definition of “highly trained”.
- Some performance indicators may be difficult to measure. For example, the quality goal for investigation of Customs offences requires that all investigations be conducted in accordance with law. Verifying compliance with this measure would require inspections or audits (integral elements of customs administrations’ internal controls procedures), which are not carried out.
- Some measures require 100 per cent achievement - for example, 100 per cent of cruise ships and commercial vessels processed within 15 to 30 minutes of arrival. This may be difficult to achieve as the time to process cruise ships will depend on the number of passengers disembarking and any potential problems that are encountered.

37. Customs does not collect information to measure performance against the outputs specified in the *Annual Plans and Estimates*. There is therefore no mechanism in place to report performance against the measures set. Neither does Customs have comprehensive performance information or a performance management system in place to support effective decision making and help manage the business.

38. We were told that Customs had started to develop a performance measurement system in 2016 but this was never implemented because it was hard to allocate time and costs against particular objectives, which made the development of performance measures difficult. The system was also limited because the proposed measures were for border protection only and did not include revenue collection, trade facilitation or corporate functions.

39. Customs does measure its performance in relation to the collection of revenue, and it reports this information monthly to MFED (to monitor whether the government’s budget and forecasts are on track). However, this performance information is limited to outputs - the value of revenue collected

by type of duty, fee or fine. It does not include any efficiency or effectiveness measures such as the cost per dollar of revenue collected.

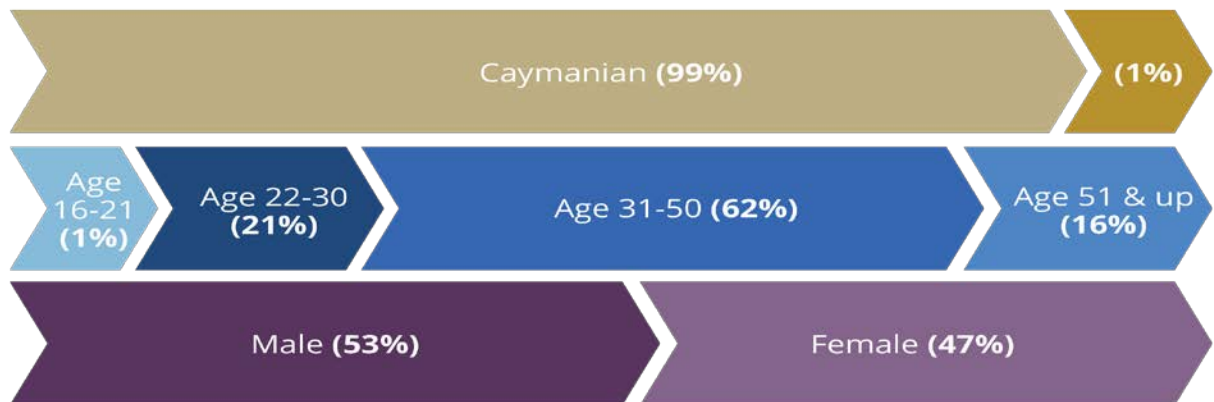
- 40. Later in this report we discuss potential performance indicators that could be developed to help measure and monitor the efficiency and effectiveness of Customs and Border Control’s operations.

**Recommendation 2: Customs and Border Control should develop and implement a range of performance measures that cover inputs, outputs and outcomes and that allow it to determine whether strategic goals are being met.**

**CUSTOMS NEEDS TO BETTER PLAN AND MANAGE ITS WORKFORCE**

- 41. As at December 2018 Customs employed 157 staff. About one half were Customs Officers and the other half provided administrative support such as human resource management, training, financial management and information technology. Exhibit 4 provides a summary of the Customs workforce as at 31 December 2018. It shows that the Customs workforce is reasonably balanced between men and women and most staff are under 50 years old.

**Exhibit 4 – Customs workforce demographics as at December 2018**



Source: OAG analysis of IRIS listing of Customs Department’s employees at 31 December 2018

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CUSTOMS DOES NOT HAVE A WORKFORCE PLAN SETTING OUT WHAT STAFFING IT NEEDS TO DELIVER ITS OBJECTIVES AND GOALS

42. According to the World Customs Organization, “Good management of human resources is probably the single most important issue that affects the efficiency and effectiveness of customs, irrespective of its organisational structure.” In order to ensure the good operation of an organisation and to ensure that its future needs can be met, the organisation requires plans that assess the current workforce, that anticipate changes in demand and in the environment, that identify the number and skills of staff required now and in the future, and that identify gaps and state how these are going to be addressed.
43. In April 2018, the OAG published *Workforce Planning and Management in the Cayman Islands Government*. It found that few government departments had workforce plans to ensure that they had the right people with the right skills in the right place at the right time.<sup>13</sup>
44. Customs does not have a strategic workforce plan that sets out what it needs now or in the future to enable it to meet goals and objectives and manage the business effectively. We were told that staff, in terms of who and how many, are currently allocated to various sections on an historic basis or where demand for additional resources are identified as a result of intelligence. There have been no work studies or analyses of the staffing levels currently needed to deliver the business effectively, or the impact of new or different ways of doing business in the future.
45. Customs does not currently have the tools it needs to inform workforce planning. It does not have a comprehensive human resources (HR) database that consolidates all of the HR information for each staff member. This makes it difficult to pull together and analyse HR data for effective planning and reporting.

**Recommendation 3: Customs and Border Control should develop a workforce plan that aligns with its strategic priorities and demonstrates how it will address existing pressures on the workforce and anticipate future needs.**

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<sup>13</sup> *Workforce planning and management in the Cayman Islands Government*, Office of the Auditor General of the Cayman Islands, April 2018

46. In May 2017 the CIG Internal Audit Service published the results of its HR audit that assessed compliance with the *Public Service Management Law* within the Customs Department. The report concluded that 65 per cent of staff were satisfied with a range of HR-related areas. However, it also found non-compliance with a range of HR issues including, management of sick leave, annual leave and compensatory time off. The management response stated that high annual leave, compensatory time and overtime balances were due to staff shortages and business needs.
47. These findings are consistent with the observations from our audit. We found the following:
- As at June 2018, 10 posts were vacant (7 per cent); a decrease from 15 vacant posts as of June 2016.
  - Use of sick leave is high. In 2017, 45 employees used all of their sick leave and 11 more had a balance of a day or less. Fifteen staff had negative sick leave balances, some as high as 630 hours. The annual sick leave used averaged almost 10 days per staff member, ranging from 0 to 94 days.
  - Overtime payments were high. Customs paid a total of \$738,368 in overtime in 2018 - a significant increase in overtime payments since 2017. Some of this increase may be because of preparations for the merger into CBC. Customs paid overtime costs of \$438,839 in 2017, with the Airport unit accounting for 36 per cent of this (\$172,941). Some of these overtime payments may also be attributable to flight delays. Customs recovered almost \$800,000 from airlines for flight delays in each of the financial years 2016-17 and 2018.
  - Staff were not using their annual leave allowances and were building up compensatory time balances. In 2018, staff carried forward average annual leave balances of 4.8 days; balances at the year end ranged from 0 to 38 days. This is an improvement on 2017. The May 2017 Internal Audit Service reported that the average compensatory time owing to employees was 22 hours (almost 3 days). Compensatory time charged by employees in 2017 ranged from 0 to 336.5 hours.
48. Together, these issues raise a number of concerns about the management of the Customs workforce. Staff had been building up significant annual leave and compensatory time balances and overtime appears high. This may indicate that the service has been or is struggling to manage the workload.
49. The Civil Service Engagement Survey 2018 shows that Customs Department staff had an overall engagement score of 71 per cent (with a response rate of 64 per cent). The survey results cover a range of drivers of staff engagement including: my work, organisational objectives and purpose, my

manager, my team, learning and development, inclusion and fair treatment, resources and workload, pay and benefits, and leadership and managing change. Customs survey results range from 27 per cent of staff being satisfied with their pay and benefits to 92 per cent being clear about the organisational objectives and purpose.<sup>14</sup>

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CUSTOMS DOES NOT HAVE A CORPORATE TRAINING PLAN AND THERE IS SCOPE TO IMPROVE STAFF SKILLS IN SOME AREAS

50. Customs operates on both domestic and international levels. Customs Officers therefore need to know domestic laws, policies and priorities and they must also be knowledgeable about the global trade and transportation businesses and the international agreements that govern them. They must maintain contact with domestic agencies such as the police and also with foreign Customs services and international trade organisations. To enable them to carry out these roles effectively, Customs Officers need training that may not be available from external sources - for example, training in legislation and internal policies and procedures.
51. We found that Customs does not have a corporate training plan that pulls together all of the training needs of its staff and how the needed training will be delivered. It has a document entitled Strategic Training Plan, but this sets out the process for preparing a training plan and is not a plan in itself. Training and development is managed on the basis of individual employees, not against an overall corporate requirement. The lack of an HR database means that there is no comprehensive list of certifications and skills, although these will be retained in individual staff members' personnel files.
52. All new Customs Officers recruited must take the Customs Basic Course, which is a 16-week course that covers all aspects of Customs activity and relevant law. However, our audit identified some areas where there is scope to strengthen some training:
  - Front-line supervisors told us that new staff required more training in "profiling" and in interacting with customers. Specialised law enforcement skills, such as profiling, are necessary for Customs Officers to be effective at protecting the border and detecting contraband. All Customs Officers receive around two days of profiling training as part of the basic course and some receive more advanced training.
  - We were told by importers that they experienced inconsistency in how Customs Officers treated files and made determinations of duty; and that many officers were not focused on customer service. Since January 2018, Customs has been collecting information on customer satisfaction at various locations, including the airport, cargo depot, airport post office and counter services. By

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<sup>14</sup> Customs Department, Civil Service Engagement Survey results 2018

December 2018, customer satisfaction levels had increased across all locations and particularly at counter services (increasing from 43 per cent to 79 per cent) and the airport post office (increasing from 61 per cent to 78 per cent).<sup>15</sup> This is a significant improvement. In addition, one of the priorities in the CIG's five-year strategic vision to be a world-class civil service is to improve customer service. The civil service will provide customer service training as part of this strategy, and Customs staff will be able to take advantage of courses when they become available.

- Effective implementation of the IT modernisation project means that staff will need to be trained in data analysis (skills not currently present in Customs) and in post-clearance audit.<sup>16</sup>

**Recommendation 4: Customs and Border Control should develop a HR database to ensure that it has easy access to comprehensive data on staff qualifications and training needs.**

**Recommendation 5: Customs and Border Control should review its training and development needs and ensure that staff are sufficiently trained in profiling, customer service, data analysis and post-clearance audit.**

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CUSTOMS MANAGES THE INTEGRITY OF ITS STAFF WELL BUT THERE IS SCOPE TO IMPROVE THIS

53. Customs is vulnerable to corruption because the nature of its work places staff in situations where they have sole discretion and responsibility and where they are authorised to make important decisions on the levels of duty owed or the admissibility of imports and exports. Since the Government depends on Customs to collect about 25 per cent of its total annual revenue and to prevent illegal goods from entering the country, the integrity of Customs staff is essential.
54. The 2018 Civil Service Engagement Survey found that a large majority of Customs staff were aware of the ethical standards of the service. The survey results show that 54 per cent of Customs staff stated that senior management actively modelled appropriate leadership behaviour; 64 per cent reported that their immediate manager modelled the behaviour and values expected in the civil service. The results also state that 58 per cent of staff thought if they raised a concern it would be promptly investigated. The shippers, importers and couriers we interviewed and officials of other government departments also expressed confidence in the ethics of Customs officials.
55. A key element in maintaining integrity is a well-structured and clear code of conduct for officers. Customs has Workplace Rules to guide its staff. We compared these to WCO best-practice guidance

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<sup>15</sup> Customer satisfaction reports for Customs Department for the periods 8 January to 28 February 2018; and 1 to 31 December 2018

<sup>16</sup> Post-clearance audit (PCA) or audit-based controls are defined by the Revised Kyoto Convention as measures by which Customs satisfy themselves as to the accuracy and authenticity of declarations through the examination of the relevant books, records, business systems and commercial data held by persons concerned. PCA is a critical control methodology for Customs as it enables them to apply a multi-layered risk-based control approach rather than a transaction-based control environment.



on codes of conduct and found that they met 10 of 11 WCO criteria, the only exception being that the Workplace Rules do not provide any direction on staff purchase of government property, especially seized or forfeited goods.

56. We found two areas where activities to support ethical conduct could be improved when comparing Customs operations to WCO guidance.<sup>17</sup> The rotation of staff and the vetting of employees could be improved further as follows:

- Rotating staff is important in preventing corruption, as it helps maintain the independence of officials and prevent the development of personal relationships with importers and exporters. Customs has a rotation policy that aims to rotate or transfer employees once a year, although “specialist jobs” such as intelligence, investigation and X-ray scanning are to be rotated between three years and five years. The policy states that each year, Assistant Collectors should propose rotations to senior management for decisions. However, we could not find any evidence of these proposals being documented. Since 2016, Customs has rotated between 15 and 25.6 per cent of Customs Officers each year. However, Customs could not tell us how often employees had actually been rotated or how long incumbents had been in their jobs.
- The Customs Intelligence Unit vets each employee annually for both criminal convictions and criminal associations using both police and open source data. It also monitors crime and court reports on a continuing basis. However, Customs officials are not vetted for indebtedness or financial difficulties. This is a significant gap in the vetting process, as such checks could help identify any staff that may be more susceptible to corruption. Other border protection agencies carry out these types of checks. For example, the Immigration Department does these types of checks as part of its recruitment process; and Canada Border Service’s security clearance includes credit checks.

**Recommendation 6: Customs and Border Control should strengthen its integrity management by ensuring Workplace Rules include direction on staff purchase of government property, especially seized or forfeited goods; there is effective and regular rotation of staff; and by adding financial stability of CBC Officers to its annual vetting process.**

#### THE FIRST PHASE OF THE PROJECT TO IMPROVE IT SYSTEMS WAS NOT WELL MANAGED

57. Customs’ operations rely on two main Information Technology (IT) systems. The Total Revenue Integrated Processing System (TRIPS) was introduced in 2014 to record Customs revenue collection and support the implementation of the new Harmonized Tariff Codes. The Trader Registration and

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<sup>17</sup> Customs Modernization Handbook, World Customs Organization

Access to Customs e-Services System (TRACES) provided business traders with a self-service portal to submit their Customs declarations to the TRIPS system for immediate processing and revenue collection.

58. Over the past few years, Customs experienced problems with its two IT systems. TRIPS had issues relating to incompleteness and non-compliance; as well, the system lacked adequate technical support. In 2016, Customs determined that TRIPS was at risk of complete failure, which would mean reverting to manually processing declarations. An IT audit in 2015 found that TRACES was unsecured and raised serious security issues for traders. These security issues resulted in the refusal of some traders to use TRACES.
59. In January 2017, Customs developed a business case to urgently replace TRIPS and TRACES with a new IT system to improve security and its operations. The business case stated that the new system would accommodate the current Harmonized Tariff Codes as per the *Customs Tariff Law*; ensure compliance with various other legislative requirements and the integrity of revenue; transition clients and business traders to a new self-service portal where they could make cargo declarations (Customs Online System – COLS); and provide a border protection service portal that would provide greater security of data and help implement risk management strategies across Customs. The business case did not present any options other than to internally develop a new IT system. Nor did the business case present a risk analysis. Although not a statutory requirement at that time including options appraisal and risk assessment in business cases are generally considered to be good practice. Cabinet approved the business case, with \$225,534 supplemental funding, on 28 March 2017.
60. The IT modernisation project is intended to deliver a fully functional and autonomous Customs Information Management System (CIMS) that has a comprehensive suite of revenue collection, enforcement and administration modules; provides the public with a high-quality service; reduces costs; and advances global trade. The business case indicated that the project would be delivered over four years from early 2017 to mid-2021 and estimated the total costs for all five phases at \$277,512. Any additional costs would be borne by Customs. Exhibit 5 provides an overview of the five phases of the project. Phase 1 of the project included the development of a Customs Tariff Support System (CTSS) to replace TRIPS, and Customs Online System (COLS) to replace TRACES.

## Exhibit 5 – Five phases of the Customs IT modernisation project

| Phase | Purpose   | Timescale            | Cost             |
|-------|---|----------------------|------------------|
| 1     | <b>Customs Tariff Support System (CTSS)</b><br>Develop CTSS as direct replacement for TRIPS with a limited number of enhancements. Develop Customs Online (COLS) to replace Trader Portal (TRACES).   | Q1 2017 –<br>Q1 2018 | <b>\$119,067</b> |
| 2     | <b>Customs Information Management System (CIMS)</b><br>Transition from CTSS to CIMS. CIMS to include courier, bonded warehousing, parcel post and Cayman Brac and integrate with other public entities including Port Authority and Department of Agriculture. Further development of COLS.   | Q2 2018 –<br>Q2 2019 | <b>\$106,467</b> |
| 3     | <b>CIMS Administrative and Enforcement Efficiencies</b><br>Expand and improve financial, administrative and enforcement processes. To include border protection modules; administration modules, such as HR and duty concessions reporting; and financial reporting of key performance indicators and revenue financial projections. Should be able to provide real-time information. TRIPS to be fully phased out. | Q3 2018 –<br>Q2 2019 | <b>\$51,978</b>  |
| 4     | <b>CIMS Non-Trader Efficiencies &amp; Mobile Device Driven efficiencies</b><br>Introduction of mobile apps for customers and Customs staff to enable remote working, receive alerts and share intelligence.   | Q3 2019 –<br>Q2 2020 |                  |
| 5     | <b>CIMS Communications</b><br>Improving communications within Customs and with customers.   | Q3 2020 –<br>Q2 2021 |                  |

Source: HM Customs transition from TRIPS to enhanced CTSS system and Business Case to replace TRIPS system

61. In April 2017, Customs established a Change Management Committee (CMC) to oversee the project and work with the relevant Customs sections, including IT, to develop the new Customs Tariff Support System (CTSS) with minimal disruption to current operations. The membership of the CMC included a number of middle managers but had no executive authority. Although the CMC Terms of Reference stated that it was “responsible for leading the new 2017 Customs Strategic Vision,” it did not do this in practice. In May 2017, the CMC prepared a report that stated that there was “a lack of clarity with some aspects of the vision and mission statements” including what was to be done, when it was to be done and how to measure achievement. The CMC also reported that there was pressure to design and implement an IT solution before user and customer requirements were fully defined and that communication between the CMC, business analysts and information system developers was poor. We understand from our other audit work that there were concerns in the

early stages of Phase 1 that CIG's Computer Services Department, which was developing the project, was doing this with limited input from Customs. These issues were later resolved. Customs terminated the CMC at the end of Phase 1. A new Steering Committee was set up in March 2018 to oversee the introduction of COLS, headed by the Deputy Collector for Revenue Collection, who is part of the Customs' senior management team.

62. Phase 1 was launched in early November 2017 – three months later than planned. By the end of 2017, Customs had spent around \$335,000 on the project, which is significantly more than the total budget for the entire project. Phase 1 was not fully completed until July 2018 as Customs carried out a lessons learned review to help inform future phases of the project. Phase 2 commenced in August 2018. The business case for the project, including revised cost estimates and timescales, had not been updated at the time of our audit. By December 2018, Customs had spent \$662,000 on the project.
63. Customs consulted with its key partners and customers when developing COLS. However, there are mixed views on how effective this was. The project was approved in March 2017 and stakeholder engagement started in May 2017. However, Department of Agriculture (DOA) staff told us that they were not contacted until late in the process, and then not to build the DOA process into the system but simply to provide information on how to use the system. Customs consulted with some business partners about issues with the old system and asked for their views on what worked and did not work. We were told by business partners that the introduction of COLS had initially resulted in the need for additional hours to operate the system (as supporting documents had to be scanned) but these hours reduced over time.
64. The IT modernisation project was planned to continue until mid-2021, and now needs to be picked up by CBC (from 1 February 2019). It is important that the remainder of the project takes into account the IT needs of the whole organisation, particularly in relation to border protection enhancements planned for Phase 3.

**Recommendation 7: Customs and Border Control should ensure that effective project management is put in place for the remainder of the IT modernisation project. This should include an updated plan that meets the needs of the new organisation; training and human resource requirements; monitoring of costs and timescales against budget; and adequate stakeholder involvement to ensure that user needs are built into the IT system.**

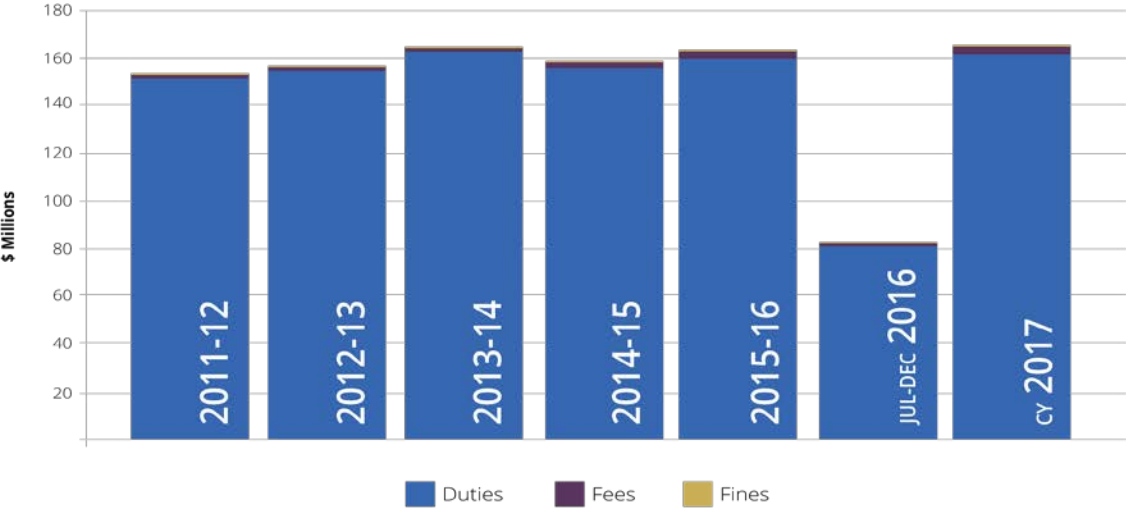
# REVENUE COLLECTION

- 65. Customs collects a significant proportion of the Government’s total annual revenue. That means the achievement of the Government’s strategic policies, goals and objectives depends on how effective and efficient Customs is at achieving the revenue target set for it in the annual budget statement.
- 66. As part of our audit we examined the revenues collected by Customs and the costs incurred to collect the revenue generated by the Customs Department; the process for setting Customs’ revenue budget; the extent of the “tax gap”, i.e. the potential revenue lost through non-tracking of concessions and evasion of import duties; and Customs’ approach to facilitating trade.

**CUSTOMS COLLECTS AROUND \$165 MILLION A YEAR IN DUTIES, FEES AND FINES**

67. Over the six (financial) years from 2011-12 to 2016-17, the total revenue collected by Customs has ranged from \$153 million to \$165 million a year. Exhibit 6 provides a summary of total Customs revenues collected in the Cayman Islands over the six years.

**Exhibit 6 – Revenues collected by Customs, 2011-12 to 2016-17**

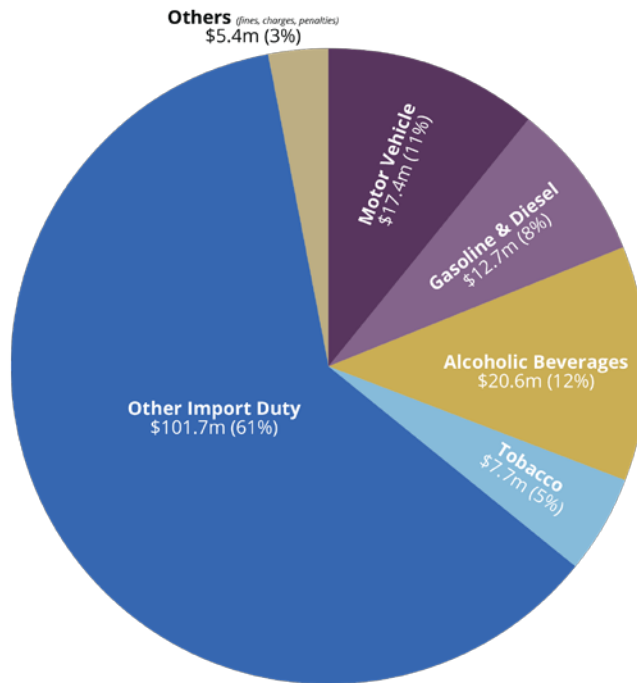


*Source: OAG analysis of Grand Cayman and Cayman Brac financial data*

68. For the 12-month period ending 30 June 2017, Customs collected total revenues of \$166 million in Grand Cayman and the Sister Islands. Exhibit 7 shows that revenue collected is made up of a range of duties, taxes, charges and fines. Customs collected around \$102 million in other import duties, which represented the largest source of Customs revenue (61 per cent), followed by alcohol

beverages duty (12 per cent), with the lowest being in fines, tax, charges and penalties and representing 3 per cent of total revenue collected. The Government increased the duty free allowance from \$350 to \$500 for all airline passengers, effective from 1 November 2018. According to CIG, this increase in allowance could cost the Government around \$1 million in lost revenue.<sup>18</sup>

**Exhibit 7 – Total Customs revenue collected by type, 12-months ending 30 June 2017**



Source: Treasury Department, MFED & Department of District Administration, MDATT.

REVENUE COLLECTED FROM DIFFERENT DUTIES HAS VARIED SIGNIFICANTLY OVER THE FIVE YEARS TO 2017

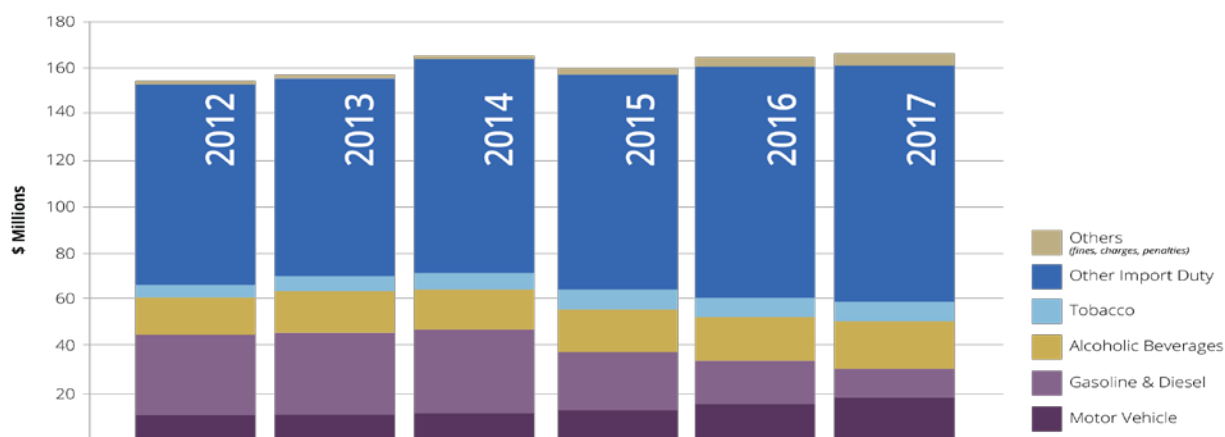
69. We further analysed revenue collected for each of the types of duty for the six years from 2011-2012 to 2016-2017 (Exhibit 8) and noted some significant variations in some types of duty.<sup>19</sup> These include the following:

<sup>18</sup> Ministry of Finance estimated that the lost revenue from this change would be between \$0.4 million and \$1.1 million.

<sup>19</sup> The 2016/17 financial year covered an 18-month period from 1 July 2016 to 31 December 2017. Our analysis includes the revenue in 2016-17 for the 12 months to 30 June 2017

- Other Import Duty. This is consistently the largest element of revenues earned and is driven by the volume and prices of goods imported. Over the six years to 2017, the value of “other import duty” collected increased by 18 per cent.
- Alcoholic Beverages Duty increased by around 26 per cent between 2012 and 2017. The Customs Department told us that this increase was due to economic growth and an increase in tourism activities.
- Motor Vehicle Duty increased by around 79 per cent over the same period; it is driven by the volume and value of vehicles imported. The Customs Department told us that the increase was due a significant increase in the number of vehicles imported.
- Gasoline and Diesel Duty decreased by around 64 per cent over the six-year period. It decreased significantly in 2015 and 2017. The Customs department told us that this was a result of the concession given to the Caribbean Utilities Company, Ltd. (CUC) on the duty rate paid for diesel; and a reallocation of \$8 million each year to the National Road Authority’s road development fund.
- Tobacco Products Duty increased by around 69 per cent over the period. This duty is consumer driven and therefore subject to fluctuation depending on the level of consumption.
- Other – Fines, charges, tax, and penalties. The majority of this revenue relates to environmental tax and package charges. We noticed that environmental fees increased by 1,047 per cent over the six-year period. The trend correlates with the increasing trend of the motor vehicle duty.

**Exhibit 8 – Revenue collected by type, 2011-12 to 2016-17**



Source: Treasury Department, Ministry of Finance and Economic Development

Note: Financial years ending 30 June. 2016-17 was an 18-month financial year, data shown relates to the 12-month period to 30 June 2017.

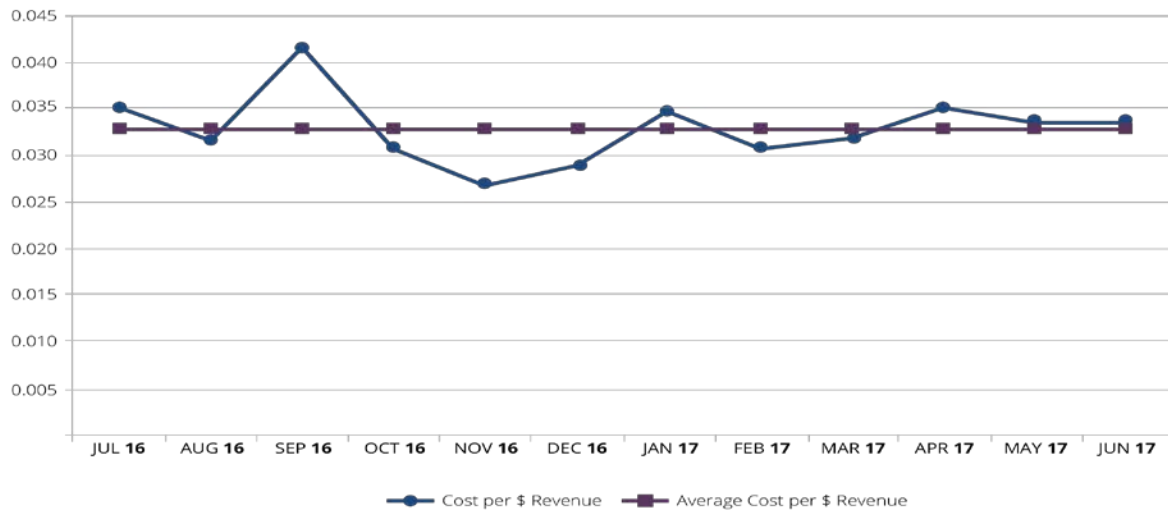
70. Customs spends around \$14 million to \$15 million a year carrying out its activities (as specified in the annual budget statement).<sup>20</sup> As previously reported, Customs does not collect performance information on the efficiency of its operations – for example, unit costs of its activities or the cost for every dollar of revenue collected.
71. As part of our audit, we obtained information on the amount of revenue collected and time charged specifically to the various Customs revenue codes. We used this to estimate the unit cost of each dollar of revenue collected. We estimate that for the 12-month period from July 2016 to June 2017, on average, it cost Customs \$0.033 for every dollar collected. Exhibit 9 shows the trend of the unit cost per dollar revenue collected during the 12-month period. This shows that the unit cost increased in September and decreased during November and December. This is as a result of relatively less revenue collected with a similar number of hours charged in September, while more revenue was collected with fewer hours charged in November 2016. This seems reasonable as we would expect the unit costs for November and December to be lower as they are traditionally busier periods with more items being imported in the run up to Christmas. We were not able to find any published international comparisons on unit costs of revenue collection.
72. We recommended earlier (Recommendation 2) that CBC develop and implement a range of performance measures that would allow it to measure the efficiency and effectiveness of its operations and identify where any improvement may be needed. This is an example of an efficiency measure that CBC may find useful.

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<sup>20</sup> The costs of \$14-\$15 million are for both the Customs Department in MFED and Customs operations within District Administration in MDATT.



**Exhibit 9 – Customs unit cost per dollar of revenue collected for 12-month period (July 2016 – June 2017)**



Source: Treasury Department, Ministry of Finance and Economic Development and hours charged to Customs revenue code in TRS.

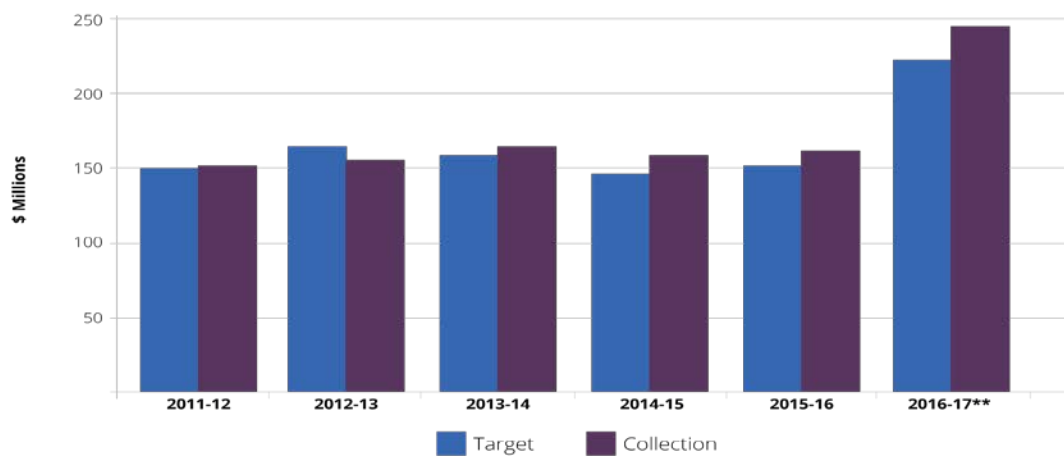
Note: The unit cost per revenue dollar collected is calculated as the total monthly revenue collected divided by estimated cost (direct labour hours charged to respective revenue code plus allocated overheads).

**BUDGET SETTING NEEDS TO IMPROVE**

73. Given the significance of revenues collected by Customs to the total annual government revenue, we expected a robust budget setting process to be in place. We would have expected this to include realistic revenue targets based on the strategic plans and policies of government; and assumptions of expected changes in economic activities, such as changes in population, tourist arrivals, work permit activity, planning approvals and building permit approval.
74. The Revenue Unit within the Treasury Department of MFED is responsible for preparing the annual revenue budget of the Customs Department (in Grand Cayman). The Revenue Unit informed us that it used both dynamic regression and modelling to estimate revenues, depending on the type of duty. It told us this approach provided robust forecasts, which it then adjusted to reflect any changes in the *Customs Law*, government policy or changes in the economy that may impact government’s revenue. We selected two financial periods (financial years ended June 2015 and June 2016) and requested evidence to support the budget setting process. For example, we requested forecasts for selected revenue categories and the adjustments made based on changes in the *Customs Law* and changes in the economy where applicable. However, the Revenue Unit could not provide us with any evidence of the initial, adjustments for economic factors, or the key assumptions used. Nor did we find any evidence of management discussions, analysis of the draft budget or consultations with the management of the Customs Department.

75. Customs does not have a significant input to the budget setting process. It makes a submission of its departmental revenue forecast to MFED to inform the process carried out by the Revenue Unit but has limited input after that. Although the budget setting process suggests that MFED and departments should engage throughout to agree on final budgets we could find no evidence of Customs being further involved in setting its revenue budgets. We would expect the input of the Customs Department into the budget process to be continuous and include discussion of key assumptions used and, qualitative factors considered; and we would expect Customs to take ownership of the final forecasted amounts that it will be held accountable for.
76. Our analysis of actual revenue collected by Customs shows it to be consistently higher than the budgeted amount (as set by MFED), with the exception of 2012-13. Since 2014-15 actual revenues collected have been 7 – 10 per cent more than forecast, yielding between \$10.4 million and \$22.7 million more than estimated. The reasons for this are not entirely clear but could be because external economic factors, such as numbers of tourists, were higher than forecast; but it could also indicate that budgeting needs to improve. Exhibit 10 shows the budgeted versus actual revenue for the six-year period 2011-12 to 2016-17.

**Exhibit 10 – Customs revenue budget versus actual, 2011-12 to 2016-17**



*Source: Treasury Department, Ministry of Finance and Economic Development. Note: \*\* 2016/17 revenue is an 18-month period from 1 July 2016 to December 2017.*

**Recommendation 8: The Ministry of Finance and Economic Development’s Revenue Unit should ensure that its process for preparing the revenue budget includes reasonable forecast and assumptions and that these are documented to provide an adequate audit trail for changes, review, discussions (including with Customs and Border Control) and approval.**

## IMPORT DUTY CONCESSIONS ARE NOT PROPERLY MANAGED OR MONITORED

77. The Government provides concessions and waivers for organisations and individuals with specific development projects to promote economic development. Concession requests are approved by Cabinet but some (less than \$20,000) are able to be approved by the Minister of Finance. Customs is responsible for processing approved concessions by applying the approved waiver amount when goods are imported.
78. In our September 2015 report, *Collecting Government Revenues* we reported that revenue waivers were poorly managed. We recommended that the Government formalise policies and procedures for all parts of the revenue waiver process, including a set of decision criteria on which to assess revenue waiver applications and a formalised records management process. This has not yet been done. Our current audit identified similar weaknesses in revenue concessions similar to those found in 2015, which means that the Government could be losing a significant amount of potential revenue through the mismanagement of concessions.
79. The Government does not have a formal concession policy setting out the criteria for the review and approval of concession requests. This means there is a lack of transparency in the process for approving concessions. It can also lead to inconsistent assessment and approval of concessions and waivers. The Ministry of Finance reported in August 2018 that a draft concession policy was scheduled to be submitted to the Caucus on 31 August 2018.<sup>21</sup> However, at the time of this report the draft policy had not yet been submitted to the Caucus for its review and consideration.
80. Although MFED oversees most requests for concessions, some are submitted and agreed through other ministries. MFED does not have a complete record of all concessions approved, which may lead to inconsistency in the review and approval process. MFED was unable to provide us with a full list of approved concessions or the value of goods imported under approved concessions.
81. The approval letters for concessions do not have all of the information necessary to monitor them effectively. We found that:
- Approval letters do not disclose the identity of any secondary beneficiaries or agents of the approved concessions, such as sub-contractors who may import goods under the approved concession awarded to a main contractor. There is a risk that beneficiaries may import items duty-free when they should have paid duties.

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<sup>21</sup> *Follow-up on past PAC recommendations*, Office of the Auditor General, October 2018

- Approval letters do not always specify the total amount of the concession to be granted; the percentage of the total import duties; the types of goods to be imported duty-free; or expiration dates. This means that individuals and companies with approved concessions could exceed the approved limit (of waived import duties), continue to import goods duty-free forever or import unqualified goods without paying duties when they should have.

82. Some concessions are awarded with related conditions such as the creation of jobs. However, these are not monitored. The Government therefore does not know whether businesses are delivering the conditions that were specified as a requirement of concessions being granted.

83. The Ministry of Finance does not carry out any formal assessments to ensure that companies or individuals approved for deferred duties payments have sound financial standing to pay the duties in the future.<sup>22</sup>

84. Customs has no means of tracking concessions. That is, there is no readily available information on how much of a concession has been processed at any point in time and how much is left to be used. We could not obtain any evidence showing the amount of concession processed for the sample we selected and reviewed. We noted that to be able to respond to a parliamentary question, the Collector of Customs had to request specific reports on the amount of concession processed for certain companies. Customs could include a module, with built in controls, within its IT modernisation project that has capability to do the following:

- Verify the validity and completeness of the concessions submitted for processing.
- Track the level and percentage for each concession entered in the system to ensure that import duties waived do not exceed the approved limit.
- Flag any inconsistencies or non-compliance with the terms of the approved concessions.
- Provide reports for management review of significant concessions.

**Recommendation 9: The Ministry of Finance and Economic Development should develop a formal, comprehensive concession policy and procedures that sets out consistent roles, responsibilities and accountabilities and includes criteria for the assessment of concession requests.**

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<sup>22</sup> **Deferred duty payment** refers to the **payment of duties** for goods declared over a specified period, after the release of the goods.

**Recommendation 10: The Ministry of Finance and Economic Development should ensure that approval letters awarding concessions clearly specify the total value of concession awarded, types of goods covered by the concession, expiration date, any secondary beneficiaries to be covered by the concession, and any related conditions.**

**Recommendation 11: The Ministry of Finance and Economic Development should ensure that approved concessions are validated, monitored and reported upon, including the cumulative value of imported goods against the total value of the concession awarded, site visits for concession applications to validate the assertions in the request and to enhance compliance, and any conditions attached to approved concessions.**

**Recommendation 12: Customs and Border Control should develop an approach to ensure that it can monitor concessions effectively.**

#### **CUSTOMS RELIES TOO HEAVILY ON IMPORTER DECLARATIONS**

85. Customs revenue is collected within a voluntary compliance framework that encourages importers to declare in full, accurately, and in good faith the goods they import. The revenue due depends on the value of declared goods and the related tariff code selected by the importer. If importers under-declare the goods imported or use a tariff code that results in lower duty fees, the total revenue collected by Customs will be less than it should be. Appendix 2 includes examples of duty-free goods in the Cayman Islands.

86. We expected Customs' processes and procedures for collecting revenue to be in line with the WCO Voluntary Compliance Framework.<sup>23</sup> Our review of the processes and procedures highlighted that Customs appears to place too much reliance on the self-declaration by importers. We found the following during our audit:

- Customs does not do regular post-clearance checks of processed declarations for compliance to ensure that the appropriate revenue amount was collected.
- We were informed that the Customs Fraud Enforcement Division is significantly understaffed and therefore does not have the capacity to proactively perform risk assessments of importers. The unit generally responds when called upon after an offence has been committed.
- There is no evidence of formal risk management that informs management about the risk of non-compliance and assists in management decisions on high-risk importers, staffing, etc. Customs Officers rely on their local knowledge and experience to identify high risk imports and place more

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<sup>23</sup> *Voluntary Compliance Framework*, World Customs Organization

emphasis on some areas, for example alcohol, tobacco and fuel imports as they pose a greater risk to lost revenue.

87. Customs is alert to the risk of under-valuation of imported goods, and it performs independent valuation of items, such as vehicles, when the price declared by the importer does not seem reasonable or has no valid supporting documents (such as an invoice).

88. Customs launched its new online declaration submission platform, Customs Online System (COLS), in early November 2017. In addition to the built-in controls, declarations submitted through COLS are reviewed to ensure the accuracy and completeness of the declarations before they are processed.

#### THE EXTENT OF THE “TAX GAP” IS UNCLEAR

89. Most jurisdictions, for example the United Kingdom, USA, Sweden and New Zealand, calculate the tax gap estimate on a regular basis. The tax gap refers to the difference between the total amounts of taxes owed to the government compared to the actual amount received. It is a way to gauge taxpayers’ compliance with their tax obligations. The Cayman Islands is a tax-free jurisdiction, that is, residents do not pay income taxes or taxes on their purchases. However, the Cayman Islands Government does impose duties and fees on imported goods. Neither Customs nor MFED calculates the extent of the tax gap, so they do not know how much revenue is potentially lost to the Government.

90. As part of our audit, we therefore attempted to calculate the extent of the tax gap; defining the tax gap as including the following:

- import duties wrongly applied;
- non-declaration of good imported; and
- concessions or waivers on duties.

91. However, we could not obtain sufficient evidence to quantify the value of potential revenue lost to the Government because of the weaknesses in processes and arrangements identified above. There is a risk that the Government is foregoing significant amounts of revenue each year.

92. We have previously reported concerns in relation to the management of concessions. In *National Land Development and Government Real Property* in June 2015 we highlighted issues with the following two significant concessions that had been agreed by government:

- The Government’s agreement with Dart Realty (Company) Ltd. (DRCL) from 2010 for development to stimulate the Cayman Islands economy and provide public infrastructure resulted in extensive tax and duty concessions without approval from the Legislative Assembly. As part of this deal the Government agreed to provide development permissions and tax and duty concessions in return

for various developments and commitments by DRCL. The actual value of the concession is not known or monitored. However, most building materials are subject to 15 per cent duty, which means that the government will have foregone millions of dollars in revenue.

- The Government provided Heath City with numerous inducements, including US\$800 million in customs duty concessions for medical equipment and supplies, for a period of 50 years. Although the concessions will not be evenly spread throughout the period, this equates to an average of \$16 million a year in foregone revenues.

93. We noted earlier, that MFED could not provide us with a comprehensive list of approved concessions or the value of goods imported under these concessions. In our report *Fighting Corruption in the Cayman Islands* we noted that the value of planning permissions granted in the Cayman Islands had increased from \$285 million in 2013 to \$800 million in 2017.<sup>24</sup> With duty on construction materials at 15 per cent, the potential revenue to be collected from developments is significant. It is not known how many of the approved developments in 2017 may have requested and received concessions. However, for illustrative purposes, if 10 per cent were awarded a concession the Government could have waived \$6 million in revenues.<sup>25</sup>

**Recommendation 13: The Ministry of Finance and Economic Development should determine the level of the “tax gap”, and should take appropriate actions to close any such gap.**

#### **CUSTOMS DOES NOT HAVE A FORMAL PROCESS TO ASSESS THE IMPACT OF ITS ACTIVITIES ON TRADE FACILITATION**

94. The World Trade Organization defines trade facilitation as “the simplification, modernization and harmonisation of export and import processes”. In simple terms, trade facilitation is about ensuring the movement and clearance of goods across borders at minimum cost. According to the WCO “Customs plays a critical role not only in providing expedited clearing processes but also in implementing effective controls that secure revenue, ensure compliance with national laws, and ensure security and protection of society. The efficiency and effectiveness of Customs procedures has a significant influence on the economic competitiveness of nations.....”<sup>26</sup>

95. We found that Customs has no formal process to track or determine how its activities and procedures affect trade facilitation. Customs 2015-16 annual report states that the Department’s activities “increased trade facilitation by 50%”. However, Customs was unable to provide us with

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<sup>24</sup> *Fighting Corruption in the Cayman Islands*, Office of the Auditor General, November 2018

<sup>25</sup> Calculation assumes 50 per cent of planning permission value relates to construction building materials at 15 per cent duty rates

<sup>26</sup> Procedures and Facilitation Overview, WCO website

any evidence to support this statement. We found that that there are no processes in place to track the following:

- The time it takes to complete each significant step of the clearing process, from submission of declaration through payment of duties to the release of imported goods to traders.
- How the activities of the Port Authority, Department of Agriculture and the other related agencies contribute to the efficient and effective clearance of imported and exported goods.
- How coordination (or lack thereof) among the various law enforcement agencies affects the efficient and effective clearance of imported/exported goods.
- The extent to which the shortage of staff and the unavailability of the mobile scanner impact the examination of imported and exported goods.
- The extent to which errors and incorrect submissions by importers contribute to delays in clearance of imported and exported goods.
- The extent to which errors and internal processing activities of Customs contribute to delays in clearance of imported and exported goods – for example, the time taken for a Customs officer to process one declaration in CTSS 2.0.

96. As previously reported Customs does not have performance information to assess the efficiency and effectiveness of its operations and identify areas for improvement. All of the issues identified above could be developed into performance indicators for Customs and Border Control's activities that would measure and monitor:

- costs related to preparation, submission and approval of documents;
- cost of clearance and transportation of goods;
- average transaction time; and
- cost of moving imported goods from the Port to the place of business or use.



## BORDER PROTECTION

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97. The Cayman Islands has a significant volume of people and goods flowing through its borders. The country relies heavily on imported goods for its consumers and industries, and its economy is based on tourism (including cruise ship tourism) and financial services, all contributing to border activity. As with many other countries across the world, the Cayman Islands Government is becoming increasingly concerned about the entry of weapons, narcotics, and illegal immigrants and threats from serious and organised crime.
98. Customs played a major role in preventing the entry of contraband goods through all ports of entry, that is, sea cruise port, ocean cargo centre and airports. Since 1 February 2019, Customs and Border Control (CBC) has responsibility for border protection in terms of contraband goods and people (previously the responsibility of the Department of Immigration).
99. As part of our audit we examined Customs role and approach to protecting the borders, and progress made in the creation of Customs and Border Control.

### **CUSTOMS PLAYS A SIGNIFICANT ROLE IN BORDER PROTECTION**

100. Customs plays an integral role in border security by intercepting regulated, restricted and prohibited goods at airports, seaports and mail centres. It does this by processing and inspecting travellers, goods and packages entering the country. Customs Officers are also empowered to conduct inspections, make arrests and use other law enforcement powers in order to guard the border.
101. The increasing number of travellers through the airport and cruise ship arrivals (as was shown in Exhibit 2) has increased the demand for Customs Officers to be present and visible at the ports of entry. Customs Officers assess whether passengers entering through the airport have any duties to pay or are carrying contraband goods. Prior to July 2018, all passengers made declarations on Customs forms, which were submitted to officers at the airport who made a judgment as to whether to accept the declaration or examine the passenger's baggage. In July 2018, Customs introduced the green line (nothing to declare) at the airport, which put the onus on passengers to select which line they use to enter. However, this does not always operate as intended. Passengers are still being requested to complete Customs forms and Customs Officers are usually checking and collecting these forms at the entry to the green line, resulting in delays in entry. In April 2018, Customs started pre-clearing some flights from Miami to the Cayman Islands. Cruise passengers are generally subject to random searches as they disembark from their tender boats.

102. Customs processes cargo entering the Cayman Islands (by air and sea) to ensure that relevant duties are paid and there are no contraband goods. The level of air cargo has increased by 147 per cent and sea cargo by 21 per cent between 2012 and 2017. Customs processes air cargo through its courier section; and sea cargo is subject to X-ray and manual inspections by the Container Processing Inspection Unit (CPIU) at the Cargo Distribution Centre.<sup>27</sup> A large number of goods also enter through the postal system as residents purchase and receive goods from overseas.
103. Customs has a number of specific units that contribute to border protection through detection and investigation of potential contraband goods. These include the Customs Fraud Enforcement Division (CFED); Customs Narcotics Enforcement Team (CNET); K9; Intelligence Unit; and the Joint Marine Unit (JMU).
104. Although there have been no specific objectives for Customs in relation to protecting the border, the Budget Statements do set out what Customs is expected to achieve each year and the outputs to be delivered. As Exhibit 11 shows the 2016-17 Budget Statements set out a range of outputs for Customs to deliver in relation to passengers and cargo, and to detection, interdiction and prosecution of Customs offences.

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<sup>27</sup> The Cargo Distribution Centre is a facility owned by the Port Authority of the Cayman Islands for temporary storage of sea freight containers.

**Exhibit 11 – Customs performance targets for processing passengers and cargo and for detection, interdiction and prosecution (1 January to 31 December 2017)**

| Passengers   |                       | Cargo   |                 | Detection, interdiction & prosecution in relation to Customs offences  |               |
|--|-----------------------|---|-----------------|--|---------------|
| Measure  | Target                | Measure   | Target          | Measure  | Target        |
| <i>Number of passenger aircrafts inspected</i>           | 16,380 – 17,200       | <i>CPIU: Number of inspections of imported/exported cargo</i>                             | 4,715 – 5,520   | <i>CFED: Number of post-audit checks</i>                               | 27 - 29       |
| <i>Number of passengers processed by air</i>             | 785,000 – 864,150     | <i>Freight Security Initiative Unit: Number of inspections of imported/exported cargo</i> | 6,615 – 7,665   | <i>CFED: Number of investigations</i>                                  | 62 - 65       |
| <i>Number of marine crafts processed &amp; inspected</i> | 1,312 – 1,433         | <i>Courier: Number of Customs entries processed</i>                                       | 83,989 – 88,400 | <i>CNET: Number of investigations</i>                                  | 153 - 162     |
| <i>Number of passengers processed by sea</i>             | 1,680,000 – 1,785,000 | <i>Collections: Number of Customs entries processed</i>                                   | 45,885 – 48,300 | <i>CNET: Number of searches</i>  | 57 - 60       |
|  |                       | <i>Inbond: Number of Customs entries processed</i>  | 472 – 493       | <i>K9: Number of searches</i>  | 574 - 604     |
|  |                       |   |                 | <i>K9: Number of anti-smuggling demonstrations &amp; presentations</i> | 8 - 12        |
|  |                       |   |                 | <i>Intelligence Unit: Number of investigations</i>                     | 1,117 - 1,176 |
|  |                       |   |                 | <i>JMU: Number of marine related activities</i>                        | 1,013 - 1,067 |

Source: 2016-17 Budget Statements

105. However, as specified earlier, Customs does not measure actual performance against these targets and we have reported that Customs does not routinely use some of these measures, such as post-clearance audits.

106. We have been able to determine performance against some of these targets from other sources. For example, tourism statistics show that 418,000 air passengers and 1,728,400 cruise ship passengers arrived during 2017.<sup>28</sup> The number of cruise ship passengers is in line with the performance target of 1,680,000 to 1,785,000 set out in the Budget Statement.

107. Customs has been successful in intercepting some contraband and in making arrests that contribute to protecting the border. In 2017, it made 58 arrests for drugs offences and 11 arrests for firearms offences and seized:

- 51.08 lbs of ganja
- 2.12 lbs of cocaine
- 3 firearms
- 22 rounds of ammunition.

108. In addition, Customs contributed to 29 joint operations with RCIPS and Immigration that resulted in 19 arrests and the seizure of 630 pounds of ganja, 5.77 pounds of cocaine and one firearm.<sup>29</sup> We noted that Customs and RCIPS report different figures for detections and interceptions. This suggests that there may be inconsistent recording of information and crime and there is a need to develop a better process for consolidating reported crime.

#### **THE APPROACH TO PROTECTING THE BORDERS IS CHANGING**

109. The Government's Strategic Policy Statement for 2016-17 identifies border protection as a priority. In 2016, the Cayman Islands Government asked the UK Border Force to conduct a review of the capabilities of Customs and Immigration. UK Border Force provided its report to the Government in December 2016 containing the findings of its review and making recommendations for improvement.

110. Customs in the Cayman Islands has historically adopted a "gatekeeper" role, but as a result of the UK Border Force review and other international developments in modernising Customs, has been moving to a more intelligence-led and risk-based approach. A risk-managed approach has obvious advantages to both the Customs service and to customers. The majority of goods and passengers entering the country will be low-risk and therefore require limited or no inspection, reducing costs to both sides and improving the efficiency and effectiveness of operations. This approach will allow Customs to focus its attention on high-risk shipments and people and subject them to greater

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<sup>28</sup> ESO Statistical Compendium 2017

<sup>29</sup> Annual Report 2016-17, Ministry of Finance and Economic Development.

scrutiny, and will likely achieve higher rates of intercepting contraband and act as a greater deterrent. However, this change in approach will require a significant change in the way Customs collects, analyses and uses intelligence.

111. Many Customs operations across the world are modernising their approaches, systems, procedures and methodologies. These generally include the following:

- Shifting from physical control over consignments at the time of importation to post-release verification using audit-based controls.
- Relying on a single agency to take responsibility for the entire border management process.
- Ensuring effective coordination between various government agencies responsible for regulating cross-border trade and achieving meaningful rationalisation of regulatory requirements.
- Using modern information technology (IT) to provide seamless transition of data to all interested parties. This includes reliance on electronic transmission of manifests before cargo arrival, direct trader input of import and export declarations, and electronic payment of duties.
- Harmonising and simplifying Customs procedures in line with international best practice standards, including making best use of regional groups.<sup>30</sup>
- Identifying of importers and travellers who do not comply with regulations.

#### **BETTER USE OF INTELLIGENCE IS NEEDED TO INFORM RISK MANAGEMENT**

112. The WCO states that intelligence is “a vital weapon for Customs Administrations in the fight [against] commercial fraud and illicit drugs trafficking which are becoming increasingly international in character”.<sup>31</sup>

113. A modern Customs department requires a strong intelligence function and the use of information technology to exploit traveller and shipment data before arrival to identify risks and alert front-line inspectors, including:

- Advance Passenger Information/Passenger Name Record (API/PNR)
- Advance Cargo Information (ACI)
- Foreign and criminal intelligence
- Internal intelligence arising from Customs own operations.

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<sup>30</sup> *Customs Modernization Handbook*, World Customs Organization

<sup>31</sup> *Resolution of the Customs Co-operation Council concerning the importance of intelligence in supporting Customs enforcement activity*, World Customs Organization, June 1992

114. Customs approved Risk Management Standard Operating Procedures (SOP) in 2011 and revised them in 2017. However, they have never been implemented. The SOP state that a Head of Risk Management should be in place but one has never been appointed.
115. As previously reported, Customs is building a platform that is capable of managing data for risk management and intelligence sharing in Phase 3 of its IT modernisation project. However, the project is behind schedule. Phase 3 was initially scheduled to start in the third quarter of 2018 and be complete by the second quarter of 2019. However, Phase 2 started later than planned due to the delays in Phase 1 of the project. Customs could not provide us with revised start and completion dates for Phase 3.
116. Customs will also need to build a gateway for both passenger and cargo information in its new IT system to provide a bridge to ASYCUDA, which is used by the Joint Regional Communication Centre and most Caribbean customs services.<sup>32</sup>
117. At the time of our audit, Customs had not assessed the technology and human resources implications of implementing data analytics as part of its intelligence and risk management processes.

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SOME INTELLIGENCE IS PROVIDED FOR CUSTOMS OPERATIONS BUT THIS NEEDS TO IMPROVE

118. At the time of our audit, the Customs Intelligence Unit (CIU) was responsible for coordinating with local and regional law enforcement agencies, creating intelligence products for the Customs Department and vetting incoming and existing officers. Under the new CBC, the remit of the CIU has been expanded to include intelligence on passengers.
119. The CIU received information from a range of sources, including RCIPS, Department of Immigration, Joint Regional Communications Centre of the Caribbean Community for Crime and Security (JRCC), Interpol, and foreign customs and criminal intelligence agencies. CIU used this information and intelligence to assess threats to the Cayman Islands and issues advice to front-line officers alerting them to specific individual shipments or travellers; and it provided more general warnings on the characteristics of non-compliant people or goods.
120. Under the *Customs Law* all inbound airlines and ships are required to provide advance electronic information to Customs on passengers, crew and cargo at least 48 hours in advance of their arrival in the Cayman Islands. However, we were told that although most airlines had been submitting this

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<sup>32</sup> ASYCUDA is an automated system designed by the United Nations Conference on Trade and Development to administer a country's customs. It is used by over 90 countries, including most countries in the Caribbean.

information in relation to passengers to the Department of Immigration since 2013, not all airlines were doing so.

121. The advance passenger information required from airlines has been increased for CBC under the new *Advance Passenger Information Law, 2018*, which was passed by the Legislative Assembly in June 2018. At the time of writing this report, the new law had not yet been brought into force but we understand that this it expected to happen during 2019.

122. The UK Border Force has agreed to provide additional assistance to help Customs improve its intelligence and risk analysis in order to develop a strategic border assessment. UK officials envisage a Cayman intelligence unit linked to the UK, which would produce an annual strategic review.

**Recommendation 14: Customs and Border Control should ensure that it has appropriate systems and processes in place to capture, analyse and use intelligence effectively.**

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#### KEY BORDER SECURITY AREAS NEED TO BE BETTER RESOURCED

123. Customs has personnel in various border protection posts in the airport, cruise port and cargo centre. However, it is not clear how it aligns its workforce needs with high-risk activities. Customs senior managers told us they believe overall resourcing to be sufficient and they have agreed that better deployment of staff is needed. This could be addressed through effective risk management, use of intelligence and workforce planning.

124. We also identified that the Container Processing Inspection Unit's X-ray scanner was not in use between August 2015 and October 2017 (27 months). The X-ray scanner is capable of scanning 100 per cent of the containers arriving in George Town, about 60 to 80 containers a day. However, when it is not in operation Customs staff carry out physical inspections of containers instead. There is a risk that contraband goods may have entered the country undetected through containers that were not properly inspected.

**Recommendation 15: Customs and Border Control should reallocate staffing to ensure that high-risk areas are sufficiently resourced.**

#### NEW BODIES HAVE BEEN CREATED TO IMPROVE BORDER PROTECTION

125. As outlined earlier, the Government has identified border security as a major priority and, while we were undertaking our audit, was in the process of merging Customs with parts of the Department of Immigration to create a new Customs and Border Control (CBC) and creating a new Cayman Islands Coast Guard.

126. To support the development of the new CBC, the Ministry employed a consultant from UK Border Force to provide advice and support. The consultant started in January 2018 and finished on 31 August 2018. CBC was originally intended to be operational from 1 January 2019. However this was delayed until 1 February 2019.

127. The creation of the CBC is a significant change in the border protection approach of the country and its vision is “to be a world-class border protection service”. The Director of Customs and Border Control was recruited in August 2018 and started on 1 February 2019. The new structure of the CBC includes the Director, the Senior Deputy Director and five other Deputy Directors with the following remits: <sup>33</sup>

- Senior Deputy Director in charge of intelligence.
- Deputy Director for Enforcement including asylum, anti-fraud, anti-narcotics, Joint Marine Unit and K9.
- Deputy Director for Trade and Revenue including cargo clearances, bonded warehousing, parcel post and courier clearance.
- Deputy Director for Ports including all airports and seaports, visas and freight security (x-ray inspection).
- Deputy Director for Administration including human resources, finance, training, IT and statistics.
- Deputy Director for Sister Islands Operations.

128. The *Customs and Border Control Law, 2018*, was passed by the Legislative Assembly in November 2018, and the law came into force on 1 February 2019.<sup>34</sup> The Customs and Border Control (Entry and Landing) Regulations, 2019 also came into effect on the same date. These regulations provide CBC with jurisdiction over all border control matters.

129. CBC became operational on 1 February 2019. However, it is important that senior management of the organisation and the Ministry continue to plan beyond the start date of CBC, to ensure that

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<sup>33</sup> <http://cbc.gov.ky/index.php/about-us/management-team>

<sup>34</sup> The *Immigration (Transition) Law, 2018* that governs the other new agency, Work Opportunities and Residency Cayman (WORC) also came into force at the same time. Combined these two laws split the work of the previous Immigration Department into two new entities.



business as usual continues and to plan for subsequent organisational development that is sufficient, effective and focused on delivering improvements.

130. The Cayman Islands Coast Guard will operate as a separate entity, under the direction and control of Royal Cayman Islands Police Service (RCIPS). It will have a wide range of maritime-related functions including border security in territorial waters, search and rescue, and criminal interdiction in territorial waters. It will also have an enforcement role for domestic marine legislation and will assist CBC as required.
131. To support the development of the Cayman Islands Coast Guard, the Ministry seconded a consultant from the UK Maritime and Coastguard Agency to provide advice and support between January 2018 and March 2019. The Cayman Islands Coast Guard will be headed up by a Commander who will report directly to the Commissioner of Police and all Coast Guard staff will have the status and powers of police officers. The Commander and Deputy Commander of the Coast Guard were appointed in August 2018. The Cayman Islands Coast Guard is expected to begin operations in the last quarter of 2019; in the meantime, the Joint Marine Unit will continue to deliver operation responses to concerns at sea.
132. The intention is for the Cayman Islands Coast Guard to have a separate “ring-fenced” budget that cannot be used for any other purposes. However, this may be difficult to achieve in practice. Although the *Public Management and Finance Law* allows for ring-fenced budgets, it has no provisions to protect such budgets.

## CONCLUSION

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133. Customs makes a significant contribution to the Cayman Islands economy by collecting duties on imported and exported goods and plays a significant role in protecting the borders. Despite this important role Customs did not have a clear strategic plan setting out its vision, direction and objectives. Although it did have a Business Process Document that provided some vision for the future this had not been developed any further. Nor did Customs have any of the other essential elements we might expect to support the effective management of the business, such as a workforce plan or performance management framework. Customs has started to develop a new IT system to improve its business processes. However, the project was not well managed in the early phases and by the end of December 2018 Customs had spent almost three times more than the original estimated budget.
134. My Office published *Collecting Government Revenues* in September 2015, which covered the revenues collected by Customs along with other departments. That report found that although revenues were being collected in accordance with legislation there were no policies and procedures in place for processing revenue waivers or concessions and they were not granted in a consistent and transparent manner. It is disappointing that there has been very little progress in this area. In this report we have found that import duty concessions are still not properly managed or monitored and the potential “tax gap” from lost revenues is not known. We also found that the process for estimating revenue budgets could be improved. I have made a number of recommendations to the Ministry of Finance and Economic Development to strengthen budgeting for and collecting future revenues.
135. At the time of our audit, Customs was in the process of modernising its approach to protecting the borders by moving away from the traditional “gatekeeper” role to a more risk-based and intelligence-led approach. However, more needs to be done to embed the new approach. We found that Customs needs to make better use of intelligence to identify risks and ensure that it allocates its resources accordingly.
136. While we were carrying out our audit, the Government was in the process of merging Customs with elements of the Immigration Department to create Customs and Border Control (CBC). CBC was created on 1 February 2019. I have therefore made a number of recommendations to CBC to strengthen its strategic and business planning, monitoring of the revenues it collects on behalf of the Government and further develop its approaches to protecting the borders.



Sue Winspear, CPFA  
Auditor General  
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27 May 2019

# APPENDIX 1 – ABOUT THE AUDIT

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## OBJECTIVE

1. The objective of the audit was to determine how efficient and effective Cayman Islands Customs is at collecting revenue and protecting the borders. The audit sought to answer the following questions:
  - Are Customs’ operations supported by sound legislation and strategic direction?
  - How efficient and effective is Customs at collecting revenue and facilitating trade?
  - How efficient and effective is Customs at protecting the border?
  - How well does Customs plan and manage its workforce to achieve its strategic objectives?

## CRITERIA

2. Audit criteria are a key component of a performance audit, setting out the expectations against which the auditor will assess performance and conclude on the audit objectives. Normally, the criteria reflect regulatory requirements and established business practices that management uses to assess its own performance. In the absence of such practices, it is the auditor’s responsibility to develop criteria that are reasonable under the circumstances based on best or reasonable practices and, to the extent possible, to obtain agreement from the organisation being audited.
3. The 19 criteria below were shared with and agreed by the Collector of Customs at the conclusion of the planning phase of the audit.
4. The following audit criteria were used to assess Customs’ performance against the audit questions:

### Legislation and Strategic Direction

- 1) Roles and responsibilities are clearly defined in legislation and are translated into policies and procedures that provide adequate direction to staff.
- 2) Customs organisation and operations are operating as intended by legislation.
- 3) There is a long-term strategy for Customs that is in line with good practice.
- 4) The modernisation project is being managed in an effective way.

### Revenue Collection and Trade Facilitation

- 5) Customs collects all the revenue that the law requires.
- 6) Programs are in place to reduce the burden of Customs’ administration on shippers, importers and travellers.

- 7) Customs monitors traveller and importer satisfaction with their services and acts on the information obtained.
- 8) Customs provides adequate, timely and relevant information about regulations and procedures to travellers and importers.

#### Efficiency and Effectiveness (Revenue Collection and Border Security)

- 9) Customs maintains adequate performance measurement systems to assess and manage the efficiency and effectiveness of its operations.
- 10) Customs compares its activities and processes against best practices.

#### Risk Management

- 11) The risk management approach employed conforms to the World Customs Organisation best practice.
- 12) Intelligence is managed according the UK and Royal Cayman Islands Police National Intelligence Model.
- 13) Intelligence is disseminated in a timely fashion only to staff who require it.
- 14) Risk management and intelligence activities are adjusted based on results achieved.

#### Workforce Management

- 15) There is a workforce plan that sets out workforce needs in the longer term and is aligned to strategic plans and corporate priorities.
- 16) Customs effectively manages its staff, and has the necessary workforce management tools.
- 17) Management has set clear ethical standards and consistently emphasizes ethical tone at the top.
- 18) Customs officers are vetted upon employment and regularly thereafter using a set of fit-for-purpose parameters focussed on ensuring staff integrity.

### **AUDIT SCOPE AND APPROACH**

5. The audit was carried out during 2018, as plans were being developed to merge the Customs Department and elements of the Immigration Department into a new body – Cayman Islands Customs and Border Control (CBC); and to create the Cayman Islands Coast Guard. Both of these new bodies are aimed at enhancing border protection in the Cayman Islands. Our report refers to operations that were in place in the previous Customs Department. Since completion of the audit the Customs and Border Control Service has been established. Our recommendations are therefore directed to Customs and Border Control Service.
6. Our audit covered both the revenue collection and border security operations of Cayman Islands Customs in the Cayman Islands. It covered the Department of Customs, the Ministry of Finance and Economic Development (MFED) and Customs within District Administration and the Ministry of District Administration, Tourism and Transport (MDATT). We also covered partner agencies such as

the Royal Cayman Islands Police Service (RCIPS), including the Joint Marine Unit, Department of Immigration, and Department of Agriculture.

7. The audit did not include border protection issues outside the responsibility of Cayman Islands Customs.
8. The audit was conducted in accordance with International Standards on Assurance Engagements. The approach to the audit included:
  - obtaining the agreement of relevant government officials to the audit criteria;
  - documenting statutory requirements, policies and practices for the management and planning of Customs activities within our audit scope;
  - conducting interviews with senior officials, including the Deputy Governor, Chief Officers and senior officials responsible for Customs activities and border security;
  - meeting with a selected sample of Customs customers including major import and courier firms, brokers, shippers and other importers;
  - reviewing documents such as the *Customs Law*, government studies relating to border security reform, corporate plans, project reports, financial data and intelligence data and reports;
  - analysing financial data, including calculating the cost per dollar of revenue collected, and human resource management data;
  - reviewing plans and reports relating to the Customs modernisation initiative;
  - analysing audit evidence and assessing it against agreed criteria to develop findings, recommendations and a conclusion on the audit objective;
  - providing a draft report to relevant government officials for review of factual accuracy and obtaining responses to the report's recommendations (see Appendix 3); and
  - presenting a final report on the audit to the Legislative Assembly.

#### AUDIT STAFF

9. The audit was carried out under the direction of Angela Cullen, Director of Performance Audit and assisted by Julius Aurelio (Audit Manager), Kwame Afrane (Audit Project Leader) and an external consultant.

## APPENDIX 2 – DUTY-FREE GOODS

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A wide range of foods are zero-rated for duty, such as:

Fresh fish

Seeds (for sowing)

Vaccines (for human and veterinary medicine)

Orthopaedic appliances

Corrective contact lenses, non-contact lenses, eye glasses, sun glasses and spectacles

Documents

Notebooks/composition books

Printed books (excluding professional books), brochures, newspapers, maps, calendars, pictures, prints and photographs

Bullion (gold, silver)

Jewellery of precious or semi-precious stones

Perfume

Cameras, lens, filters, flashes and tripods for cameras

Samples (carpet, tiles)

Samples (liquor for promotional purposes)

Tableware and kitchenware (porcelain and china, wood)

Antiques (over one hundred years)

Instruments and tools of trade

Leather (including some leather goods such as trunks, suitcases, handbags, wallet, purses)

Imported goods for re-export

Dutiable personal goods or household articles purchased by residents returning from overseas visit with a value not exceeding \$500 (previously \$350)

## APPENDIX 3 – RECOMMENDATIONS

| Recommendation  | Management Response   | Responsibility   | Date of planned implementation |
|---|---|--|--------------------------------|
| <p>1. Customs and Border Control should develop a strategic plan as soon as possible. The plan could build on the Customs Department’s Business Process Document and should ensure that it captures all of the relevant activities of both predecessor organisations.</p> | <p>We agree with and accept this recommendation. During the audit we advised the Office of the Auditor General that we had plans in late 2017 and early 2018 to develop and roll out a Customs Department Strategic Plan. However, that plan was overtaken by the announcement in early 2018 of the policy to merge our Customs and Immigration departments. We took the decision at that point that it was prudent to postpone the development of a Strategic Plan and instead focus on preparing for the merger on the 1<sup>st</sup> January 2019. Once we were clear on the responsibilities, focus and composition of the new agency, we could then development a meaningful Strategic Plan for our new agency. We expect to have a CBC Strategic Plan in place in 2019.</p> | <p>Director of Customs and Border Control.</p>                               | <p>2019</p>                    |
| <p>2. Customs and Border Control should develop and implement a range of performance measures that cover inputs, outputs and outcomes and that allow it to determine whether strategic goals are being met.</p>   | <p>We agree with this recommendation. Unfortunately, this problem is not unique to the Customs Department and work is underway across government to improve our systems for measuring performance and therefore improve planning and business decisions.</p>  | <p>Director of Customs and Border Control and the Senior Management Team</p> | <p>2020 - 2021</p>             |



| Recommendation  | Management Response  | Responsibility  | Date of planned implementation |
|---|--|---|--------------------------------|
| 3. Customs and Border Control should develop a workforce plan that aligns with its strategic priorities and demonstrates how it will address existing pressures on the workforce and anticipate future needs. | We accept this recommendation. The Caribbean Customs Law Enforcement Council is working on an IT based Human Resources Management System that will assist all member countries, including the Cayman Islands, with improving the management and deployment of our workforce. This new programme will be reviewed and hopefully adopted by member countries at our annual conference in Havana Cuba in May this year.   | Director of Customs and Border Control                                | 2020                           |
| 4. Customs and Border Control should develop a HR database to ensure that it has easy access to comprehensive data on staff qualifications and training needs.  | We accept this recommendation. As mentioned under Recommendation No 3, the Caribbean Customs Law Enforcement Council is working on an IT based Human Resources Management System that will assist all member countries, including the Cayman Islands, with improving the management and deployment of our workforce. This new programme will be reviewed and hopefully adopted by member countries at our annual conference in Havana Cuba in May this year. | Director of Customs and Border Control                                | 2020                           |
| 5. Customs and Border Control should review its training and development needs and ensure that staff are sufficiently trained in profiling, customer service, data analysis and post-clearance audit.         | We accept this recommendation. Moreover, Post Auditing is now a Unit in the new CBC Organisational Structure which was shared with the Office of the Auditor General during the audit. The development and staffing of this new unit will commence in 2019.  | Director of Customs and Border Control and the Senior Management Team | 2019 – 2022                    |

| Recommendation  | Management Response  | Responsibility  | Date of planned implementation |
|---|--|---|--------------------------------|
| <p>6. Customs and Border Control should strengthen its integrity management by ensuring Workplace Rules include direction on staff purchase of government property, especially seized or forfeited goods; there is effective and regular rotation of staff; and by adding financial stability of CBC Officers to its annual vetting process.</p>  | <p>We accept this recommendation and will commence implementation in 2019. The proper and effective rotation of staff has been constrained by a number of legacy issues including the following: Customs was traditionally focused on revenue collection with insufficient staff trained in border control and enforcement duties; and, medical issues which were never properly addressed by medical boards and these issues prevented some staff from performing enforcement related duties.</p> | <p>Director of Customs and Border Control</p>                                 | <p>2019</p>                    |
| <p>7. Customs and Border Control should ensure that effective project management is put in place for the remainder of the IT modernisation project. This should include an updated plan that meets the needs of the new organisation; training and human resource requirements; monitoring of costs and timescales against budget; and adequate stakeholder involvement to ensure that user needs are built into the IT system.</p> | <p>We accept this recommendation and, subject to funding, will employ a Project Manager asap to take over those responsibilities from the CBC's Deputy Director of Trade and Revenue.</p>  | <p>Director of Customs and Border Control</p>                                 | <p>2019</p>                    |
| <p>8. The Ministry of Finance and Economic Development's Revenue Unit should ensure that its process for preparing the</p>  | <p>The Treasury Department will establish a Revenue Committee that will comprise of the Revenue Unit and the Customs and Border</p>  | <p>Financial Secretary &amp; Chief Officer and Senior Assistant Financial</p> | <p>30 June 2019</p>            |

| Recommendation   | Management Response  | Responsibility  | Date of planned implementation |
|--|--|---|--------------------------------|
| <p>revenue budget includes reasonable forecast and assumptions and that these are documented to provide an adequate audit trail for changes, review, discussions (including with Customs and Border Control) and approval.</p> | <p>Control for budgetary forecasting. It is envisaged that both agencies will complete their own forecasts, and before they are submitted to the Budget Unit, the Committee will meet to compare the respective forecasts. Meetings will be held during the budget process and quarterly to consider potential reforecasting. Committee meetings will compare assumptions, identify variances between the two forecasts thereby establishing reasons for the variances. Also, a detailed summary, breaking down how the figures were arrived, will be provided by both agencies which will provide evidence for adjustments to the forecast and also assist with day to day duties for reporting actual results compared to forecast. This will allow the Customs and Border Control to take ownership of its forecast and explain any variances as they have more insight on how their revenues perform.</p> <p>The Ministry of Finance will make recommendations to the Cabinet not later than 30 June 2019 on a substantive Concessions Policy governing how concessions are assessed, awarded, monitored and reported.</p> | <p>Secretary, Ministry of Finance and Economic Development</p>                |                                |
| <p>9. The Ministry of Finance and Economic Development should develop a formal, comprehensive concession policy and</p>  | <p>The Customs Department was supporting the Ministry of Finance and Economic Development with the formulation of a</p>  | <p>Financial Secretary &amp; Chief Officer and Senior Assistant Financial</p> | <p>30 June 2019</p>            |

| Recommendation  | Management Response   | Responsibility  | Date of planned implementation |
|---|---|---|--------------------------------|
| <p>procedures that sets out consistent roles, responsibilities and accountabilities and includes criteria for the assessment of concession requests.</p>  | <p>comprehensive concession policy. CBC will continue this support until this objective is achieved.</p> <p>The Ministry of Finance will make recommendations to the Cabinet not later than 30 June 2019 on a substantive Concessions Policy governing how concessions are assessed, awarded, monitored and reported.</p> | <p>Secretary, Ministry of Finance and Economic Development</p>  |                                |
| <p>10. The Ministry of Finance and Economic Development should ensure that approval letters awarding concessions clearly specify the total value of concession awarded, types of goods covered by the concession, expiration date, any secondary beneficiaries to be covered by the concession, and any related conditions.</p> | <p>The Ministry already has procedures in place which comply with most of the recommended information and will take action to address the gaps remaining.</p>   | <p>Financial Secretary &amp; Chief Officer and Senior Assistant Financial Secretary, Ministry of Finance and Economic Development</p> | <p>30 June 2019</p>            |
| <p>11. The Ministry of Finance and Economic Development should ensure that approved concessions are validated, monitored and reported upon, including the cumulative value of imported goods against the total value of the concession awarded, site visits for concession applications to validate the assertions in</p>       | <p>The Ministry accepts that there are improvements needed to enhance the monitoring and reporting of concessions and will seek to address these concerns in the substantive Concessions Policy following consultation with Customs and Border Control.</p>   | <p>Financial Secretary &amp; Chief Officer and Senior Assistant Financial Secretary, Ministry of Finance and Economic Development</p> | <p>30 June 2019</p>            |

| Recommendation   | Management Response  | Responsibility                         | Date of planned implementation |
|--|--|--|--------------------------------|
| the request and to enhance compliance, and any conditions attached to approved concessions.  |  |  |                                |
| 12. Customs and Border Control should develop an approach to ensure that it can monitor concessions effectively.   | As mentioned under recommendation No. 9, the Customs Department was supporting the Ministry of Finance and Economic Development with the formulation of a comprehensive concession policy. CBC will continue this support until that objective is achieved and recommendation No 12 will be addressed during that process.   | Director of Customs and Border Control | 2019                           |
| 13. The Ministry of Finance and Economic Development should determine the level of the “tax gap”, and should take appropriate actions to close any such gap. | The Ministry of Finance accepts the recommendation   | Financial Secretary & Chief Officer    | 31 December 2019               |
| 14. Customs and Border Control should ensure that it has appropriate systems and processes in place to capture, analyse and use intelligence effectively.    | As CBC continues its transformation from the traditional gate keepers approach to an intelligence-led risk management organization, it will continually refine its business processes, intelligence and risk-based strategies using a variety of techniques, technology, training and development in order to provide the best means of identifying and addressing threats at the earliest possible point. |  |                                |

| <b>Recommendation</b>  | <b>Management Response</b>   | <b>Responsibility</b>                  | <b>Date of planned implementation</b> |
|--|--|--|---------------------------------------|
| 15. Customs and Border Control should reallocate staffing to ensure that high-risk areas are sufficiently resourced. | This is already being done within the confines of limited resources and available funding for new staff. | Director of Customs and Border Control | Ongoing                               |

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## **Complaints**

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