

# Mutual recognition of Authorised Economic Operators and security measures

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## Abstract

For several years, customs administrations and international organisations like the World Customs Organization (WCO) have considered and promoted the idea and objective of achieving mutual recognition of Authorised Economic Operators (AEO) and security measures. The *WCO SAFE Framework of Standards to Secure and Facilitate Global Trade* encourages customs administrations to agree on the mutual recognition of AEO and security measures to enhance security of international supply chains while providing increased facilitation for secure and reliable economic operators. A number of AEO mutual recognition arrangements and agreements have been concluded or are being negotiated among customs administrations that have sufficient trust in each others' audit, control and authorisation procedures. This paper identifies some features as well as challenges of mutual recognition and aims to provide some clarification as to what different customs administrations understand under the term of 'mutual recognition'.

## Introduction

Customs plays an important role in the fight against cross-border crime and terrorism. Customs expertise in controlling goods, backed up by the use of modern IT systems and an efficient risk assessment and border control management, is vital to detect illegal goods such as drugs, explosive materials or nuclear and chemical weapons.

The terrorist attacks on September 11, 2001 gave a new momentum to customs administrations, including in the European Union (EU), to combat terrorism and other cross-border crimes such as drug trafficking, human trafficking and financial fraud. Many administrations reacted to this tragic event with great determination with a view to promoting the broadest possible international cooperation for preventing terrorism. It was obvious that the global threats of terrorism and also of organised crime would better be addressed at the international level by joining efforts and knowledge to reply more efficiently to the increasingly globalised threats.

With this in mind, the global customs community developed the World Customs Organization's (WCO) *SAFE Framework of Standards to Secure and Facilitate Global Trade* (WCO 2007) which provides a model for administrations and governments wishing to develop security measures that aim to facilitate and secure global supply chains. The SAFE Framework was adopted by the WCO Council in June 2005 and completed by a chapter on Authorised Economic Operators (AEO)<sup>2</sup> in June 2006. Only a short while after its adoption in 2005, many WCO members signed the so-called 'Letters of intent' to implement the SAFE Framework. In the meantime, more than 160 WCO members have agreed to implement the SAFE Framework by adopting and implementing equivalent measures.

The SAFE Framework is not a binding instrument but a model for administrations to follow – on a voluntary basis – when developing measures to secure and facilitate trade. It promotes closer cooperation amongst customs authorities. It recognises the importance of agreeing mutual recognition of AEO and

security measures, including customs controls and control results in view of securing end-to-end supply chains. Closer cooperation among customs administrations will, without doubt, enhance security and facilitation. Administrations that merge their efforts and work towards mutual recognition will usually not only address mutual recognition of AEO or security measures as such but also strengthen their overall cooperation, including exchange of risk related and intelligence information.

### Understanding the term ‘mutual recognition’

The SAFE Framework does not provide for a very detailed definition but refers to the mutual recognition of AEO and customs controls as a means to increase security and facilitation.

The mutual recognition of AEOs is mentioned under ‘Future Developments’ in the AEO chapters where it states that:

The standardized approach to AEO authorization provides a solid platform for development of international systems of mutual recognition of AEO status at bilateral, sub-regional, regional and, in the future, global levels. Such systems will involve a WCO Member Customs administration recognizing the AEO authorization system in another WCO Member with an operational AEO programme as being equivalent to its own. This will afford the AEO the same benefits and therefore improve predictability and efficiency of operation in all countries applying the AEO standards (WCO SAFE Framework 2007, p. 52).

SAFE also contains a chapter on Mutual Recognition (WCO SAFE Framework 2007, pp. 54-56), which refers to the SAFE Resolution, calling on WCO members that have agreed to implement SAFE, to cooperate to develop mechanisms for mutual recognition of AEO validations and authorisations and Customs controls results and other mechanisms that may be needed to eliminate or reduce redundant or duplicated validation and authorisation efforts. Here too, mutual recognition is referred to as a broad concept whereby an action or decision taken by one administration is recognised and accepted by another customs administration.

SAFE also describes the challenges of mutual recognition and points, in particular, to the challenges linked to negotiating mutual recognition of controls as this makes the routine sharing of information and control results necessary.

Administrations that are negotiating the mutual recognition of AEO or security measures will have some room to manoeuvre to define what exactly is meant by mutual recognition within the arrangement or agreement they are negotiating. Generally (and in line with the WCO approach), mutual recognition of AEO is perceived as an arrangement or agreement between two or more customs administrations (or governments) that recognise each other’s audits, controls and authorisations as equivalent and therefore provide reciprocal benefits to AEOs. In practice, this means that AEOs authorised by the partner country are recognised as being as secure and reliable as AEOs authorised by their own administration and will, therefore, receive benefits such as a reduced risk score and reduced controls when importing into the customs territory.

Contrary to customs administrations’ approach, trade sometimes appears to prefer a different interpretation of AEO mutual recognition. Traders sometimes suggest that customs administrations should include a clause in mutual recognition agreements that a company which is an AEO in country ‘x’ does not have to become an AEO in country ‘y’ since the former country already recognises it as a secure partner.

Customs generally does not share this approach as the AEO status is always attributed to a specific legal entity. The company that has achieved AEO status in country ‘x’ will always be a different legal entity to the company established in country ‘y’, even if both belong to the same multinational company. It has also to be kept in mind that the majority of AEO programs are based on SAFE and will therefore require customs checks during authorisation and audit procedure to determine whether the management

and those responsible for customs matters are reliable, and have not committed customs infringements within a certain period prior to the application. Not only would Customs in country 'x' not be in a position to carry out the relevant checks on relevant persons in country 'y', but it would also not make sense to do so, as it would only increase the burden on the relevant companies. Another disadvantage would be that if the management in country 'y' was found to be unreliable, the company in country 'x' would not achieve AEO status, despite the fact that the management in country 'x' is different and therefore may well be reliable and fulfil all conditions for AEO status.

## **Features of mutual recognition arrangements/agreements**

### **Recognition of authorisation and audit process**

One of the main features of arrangements/agreements on mutual recognition is that 'mutual recognition' is based on the trust between the parties in agreeing to mutually recognise AEO and/or security measures. In general terms, only administrations/governments that have confidence in the control mechanisms of another administration will enter into negotiations on mutual recognition. One of the reasons is that once governments make it publicly known that they have confidence in the control mechanisms of another government, any event that would provide evidence that this confidence is not justified (such as a terrorist attack linked to the import of goods from the partner country or linked to a company that was authorised as AEO by the partner country) would have a disastrous effect on the credibility of that government or authority. Also, issues of data protection need to be taken into consideration because a lot of sensitive information will be exchanged or at least made accessible to the partner country's administration during the cooperation, ultimately leading to mutual recognition. No administration can afford this information being leaked – especially if it concerns sensitive or personal data.

This trust factor also makes it very difficult to move from bilateral to multilateral or global mutual recognition because mutual recognition necessitates that all parties have the same level of trust in each other's programs, controls, audits and authorisation procedure. While bilateral arrangements/agreements can at some stage certainly be merged to produce a trilateral arrangement/agreement, it seems very difficult to agree mutual recognition on a more global scale. As well, negotiations on mutual recognition between the EU (and its 27 Member States) and a third country often focus on the necessity for the EU and, in particular, the European Commission to prove that all 27 Member States are implementing the AEO and relevant risk management and controls in a uniform manner. Fortunately, the AEO and other security measures, including the Community Risk Management Framework are based on streamlined and uniform rules, introduced through the Community Customs Code and its Implementing Provisions which are applicable in all 27 Member States. The AEO Network and, in particular, the AEO database demonstrate how closely the 27 cooperate to ensure a level playing field among economic operators and ensure uniform implementation throughout the EU. The latter allows timely access to AEO applications in one Member State by all other Member States as well as an online consultation process among all 27 customs administrations. From May 2008 to February 2009, relevant monitoring carried out in all 27 Member States confirmed the uniform implementation of the AEO in all of those Member States.

### **Process leading to mutual recognition**

Customs administrations that wish to agree mutual recognition of AEO and/or security measures will not want to trust 'blindly' but will insist on comparing legislation and rules and on verifying whether the practical implementation is equivalent. Usually, this will require audit and risk management methods ('joint audit/monitoring visits') to be compared, which might also include a visit to a company that has been authorised or is being audited in view of attaining AEO status. The programs and concepts do not need to be exactly the same but they have to achieve equivalent levels of security and control. The process is relatively time consuming: the paper-based comparison is normally followed by an in-depth

discussion to clarify any open questions (for example, definitions might often differ and clarification might be needed on terms such as ‘audit’ or ‘validation’).

The joint audit/monitoring visits are necessary to assess the uniformity of practical implementation. The on-site visits and discussions with auditors sometimes show that legislation which appears uniform on paper is in fact complemented by internal audit rules which provide for exemptions and specific rules and thus, have an impact on the practical implementation of AEO.

The joint audit/monitoring visits may be time consuming but they usually lead to fruitful discussions amongst the relevant experts – gaining insights and learning from the best practices of a partner country is certainly one of the advantages of the process leading to mutual recognition.

### **Benefits of mutual recognition**

The main objective of arrangements/agreements on the mutual recognition of AEO and security measures is to increase security and trade facilitation.

Customs administrations expect closer cooperation with third country customs administrations, more information on supply chains and high risk consignments and, as they can focus their resources on the high risk, a better and more efficient use of scarce resources. Economic operators that have received AEO status or are applying for AEO status expect to get benefits in return for their efforts to comply with high security requirements (for example, in the form of reduced controls and priority treatment and potential further advantages). Many AEOs have indicated that they only applied for AEO status due to their expectation that mutual recognition of AEO among major trading partners would soon be more widespread and lead to benefits.

If the mutual recognition of controls and control results becomes a reality, Customs as well as trade will expect export declarations to serve as import declarations, and that the control at export to normally be accepted as sufficient by the importing customs administration (unless there is an indication that controls are needed on imports (for example, due to intelligence information or because intellectual property rights (IPR) are registered only in the importing country). While the mutual recognition of AEO has already become a reality owing to the number of arrangements/agreements which have been signed and implemented, ongoing cooperation and projects show that it is more difficult to recognise controls and control results.

The benefits stemming from mutual recognition of AEOs will primarily be import/export related and usually reciprocal. In many cases, the benefits will initially be limited to reduced risk scores and thus reduced controls on and priority treatment of AEOs. Discussions held between the EU and third countries’ administrations have shown that it would be very difficult to grant benefits other than those applicable upon entry to third country AEOs. In addition, the traditional simplifications of customs rules (such as reduced guarantees or guarantee waivers for certain procedures) cannot be granted to third country AEOs since AEOs will usually not apply for such procedures in a third country. What also has to be borne in mind is that benefits should be granted on a reciprocal basis. As customs administrations outside the EU do not currently provide for reduced data sets for entry and exit summary declarations, this benefit will not be available to third country AEOs under the mutual recognition agreements the EU is currently negotiating.

The reduced risk scores and, therefore, reduced controls on AEOs are benefits which are granted under all existing mutual recognition of AEO arrangements/agreements and will significantly contribute to the facilitation of legitimate trade. The reduction of controls will lead to a quicker release of goods and more predictability for trade. Furthermore, a major benefit stemming from mutual recognition of the AEO will be that AEOs, including those in third countries, will primarily seek cooperation with other AEOs. This will lead to an increase in profit made by AEOs and raise their general and global reputation as reliable trading partners (‘reputational and competitive advantage’).

In its negotiations on mutual recognition, the EU is emphasising the need to develop further benefits under mutual recognition agreements. It therefore includes a clause in its agreements that both sides will work towards further benefits to be granted to AEOs.

## **Models for arrangements/agreements**

It is expected that the WCO will play an important role in the promotion of mutual recognition arrangements and agreements (WCO SAFE Framework 2007, p. 56). For the time being, it seems as if there will be two parallel developments: on the one hand, the Memoranda of Understanding which the United States Customs and Border Protection (US CBP) has signed with a number of customs administrations (New Zealand, Jordan, Canada and Japan), which are non-legally binding arrangements aimed at developing the mutual recognition of AEO status and providing benefits to AEOs. On the other hand, there are the legally binding agreements which the EU is negotiating with a number of its trading partners, including the US and Japan. It is expected that some countries will follow the example set by the US while others may opt for the EU model of a legally binding agreement.

The WCO has already started to compile information on existing mutual recognition agreements and their basic features. One of the objectives is to avoid a proliferation of model agreements/arrangements with too divergent features because they could prove counterproductive: they would not make any contribution to trade facilitation and could operate as a trade barrier.

The EU chose to adopt legally binding Decisions by the Joint Customs Co-operation Committee as provided for by the Customs Co-operation Agreements which the EU has signed with its main trading partners. It would obviously also be possible to sign a fully fledged independent agreement but, according to legal experts, the form of decision is sufficient to agree the mutual recognition of AEO and reciprocal benefits.

## **Legal aspects**

Questions relating to, for example, data protection and enabling legislation will play an important role. The EU customs security legislation (Customs Code and Implementing Provisions) provides for the possibility to conclude international agreements with third countries on the reciprocity and mutual recognition of security standards, control results and AEO concepts. As far as the EU is concerned, the necessary data protection is catered for since mutual recognition will usually be agreed under the umbrella of the Customs Co-operation Agreements which contain provisions to ensure that Contracting Parties respect equivalent data protection rules.

## **Challenges**

### **Equivalence**

One of the biggest challenges of mutual recognition is the need for interested countries to develop equivalent measures. The requirement of developing equivalent measures does not mean that the legislation/rules have to be identical but they must lead to equivalent control and security levels. When deciding whether or not measures are considered equivalent, administrations/governments will always take political and/or economic considerations into account. Specific risks, specific threats, geographical and geopolitical aspects as well as specific interests will be taken into consideration.

The role of SAFE as a model to be followed cannot be underestimated in this respect. Obviously, this makes it necessary to ensure that SAFE is always kept up-to-date in order to incorporate recent developments (for example, new standards, new technology). Also, the experience of WCO members that have implemented legislation based on SAFE and faced challenges when doing so (for example,

reliability of data elements required prior to entry and exit) or the experience of pilot testing SAFE (for example, the EC-China Smart and Secure Trade Lanes (SSTL) project which revealed the challenges of implementing technology like eSeals or of using Uniform Crime Reporting [UCR]) should be harnessed to keep the SAFE relevant as a model. For SAFE to keep its importance as a model, it is necessary that the WCO members who have agreed to implement SAFE avoid implementing unilateral measures or measures that are not in line with SAFE. Instead, they should seek approval from the WCO membership to introduce equivalent measures in SAFE. The relevant SAFE maintenance and review mechanism as well as the SAFE data requirements maintenance mechanism agreed by the WCO Council in 2008 and have to be followed by members that wish to amend SAFE.

### Exchange of relevant AEO data

An important challenge is the need to ensure the timely exchange of relevant AEO data between administrations that have agreed the mutual recognition of AEO. This is necessary to ensure that Customs has the relevant data so that the risk analysis on both sides can take the AEO status into account with a view to granting AEOs the agreed benefits of reduced risk scores and thus reduced controls.

The EU is currently exploring which data will have to be exchanged. It is expected that at least the name of the AEO, the trader identification (in the EU, the so-called 'EORI' number under which any economic operator exporting from or importing to the EU is registered), the AEO certificate number and its validity will have to be exchanged regularly to ensure that recently authorised AEOs can benefit from mutual recognition as soon as possible after having received status and, also, that a company that loses AEO status (as not any longer complying with AEO criteria) cannot benefit from mutual recognition.

The EU is developing a secure and IT-supported system for the exchange of AEO data which can be used for all mutual recognition agreements. Discussions on the methods and frequency of AEO data exchange are currently being held with a number of partner countries. It is obvious that a global system or number of systems which basically have the same features and functionalities would facilitate the exchange of AEO data – again something that will have to be explored at WCO level.

One additional challenge is that so far all available advance cargo reporting systems identify primarily importers/exporters, consignors/consignees but not carriers, port operators, customs agents, warehouse keepers or manufacturers. Also, the EU advance data requirements are limited to information on importers, exporters, consignors, and consignees. The recently introduced Import and Export Control Systems (ICS and ECS) will have to be amended if further data identifying additional players in the supply chain have to be provided to be able to identify additional AEOs. As the development of these systems by the 27 Member States' customs authorities and of the relevant trader systems has been very costly for trade and authorities, any requirements to provide additional data and thus amendments to the systems would have to be justified.

While the overall objective should be to identify as many AEOs as possible, exploratory discussions have shown that administrations as well as traders appear opposed to any additional advance data requirements before the added value can be demonstrated through facts. It therefore appears better to wait and see whether the introduction of mutual recognition of AEO on a reciprocal basis will lead to tangible benefits for trade, and whether an obligation to provide further data to identify additional stakeholders can be justified. A unilateral introduction of further data requirements by the EU is certainly not justifiable as mutual recognition should lead to reciprocal benefits; it would also make no sense to do so as long as other administrations are not willing to require additional data on further stakeholders, and this is not reflected in SAFE.

## **Approach to controls, integrity, data protection, etc.**

The need to ensure a necessary level of data protection has already been touched upon under the features of mutual recognition. A divergent approach to data protection can certainly be a stumbling block for countries/administrations seeking to agree mutual recognition. The same has to be said of a divergent approach to controls (for example, 100 per cent physical inspections or 100 per cent sealing of containers by Customs). In particular, the attitude towards integrity of Customs and other officials will have an impact as well. If the approach to integrity is different, the necessary trust between parties will not exist.

However, through negotiations between parties that might initially have had a slightly different view as regards controls, sealing or legal issues, the understanding on both sides might enable administrations to develop a more common approach and thus lead to a common understanding.

## **State of play of negotiations in the EU**

While this article mainly describes the features and challenges of mutual recognition, it may also be interesting to mention the current position of the EU in its negotiations on mutual recognition.

The EU directs enhanced cooperation on security mainly under the umbrella of its customs cooperation agreements as these agreements form a sound legal basis for enhanced cooperation on customs procedures and customs policy.

Each agreement establishes a Joint Customs Co-operation Committee consisting of representatives of the customs authorities of the Contracting Parties, that is, representatives of the third party competent services (for example, US CBP), the European Commission and of the customs authorities of Member States. The Joint Customs Co-operation Committee ensures that the agreement is correctly applied and can adopt decisions and recommendations to strengthen cooperation and amend the agreement. The Contracting Parties may expand the scope of the Agreement by mutual consent in order to supplement the areas of cooperation on specific areas (for example, security). Unless both parties decide to sign a separate agreement, it will usually be up to the Joint Customs Co-operation Committee to take the decision to agree the mutual recognition of AEOs or security measures. Decisions by the Committee have the same legal value as the agreement itself since the Committee is authorised to take decisions to make progress in customs matters and further develop the agreement.

One example of the expansion of an existing customs cooperation agreement and bilateral cooperation on security and facilitation is the ongoing cooperation with the US. In April 2004, the European Community (EC) and US formally expanded the customs cooperation agreement to closely cooperate on security. The aims of the agreement are to improve security on a reciprocal basis for both the EU and US, ensure that general customs control of legitimate trade takes due account of security concerns, and create equal levels and standards of controls for US and EC operators.

The measures that are currently being implemented include minimum standards for controls by EC and US customs authorities for the control of high risk containers and the enhanced exchange of risk related information in addition to other minimum requirements applicable to all European ports willing to participate in the US Coalition of Service Industries (CSI). An important part is the cooperation towards mutual recognition of the US C-TPAT (Customs and Trade Partnership Against Terrorism) and EU AEO. The comparison of both systems was, in principle, finalised at the end of 2009 and both sides are currently evaluating whether both programs are indeed equivalent. Parallel to the more technical cooperation to compare both programs, a high level EU-US meeting at the end of October 2009 (TEC) agreed that the mutual recognition of AEO and C-TPAT should be achieved in 2010. Both sides are busy drafting texts to formalise the agreement on mutual recognition.

As far as cooperation with Japan is concerned, the comparison process (which included joint audit visits to Japan and EU Member States) was finalised in autumn 2009. Both sides established the equivalence of legislation and implementation of AEO. The agreement will be formalised in spring 2010 and will take the form of a Decision by the EU-Japan Joint Customs Co-operation Committee.

The cooperation on AEO with China started with a pilot project on SSTL with a view to testing how to facilitate and secure end-to-end supply chains between the EC and China. The pilot project tests the WCO SAFE Framework of Standards and aims to achieve the mutual recognition of AEOs (in 2010) and, at some stage, possibly security measures and control results as well. The exchange of information between customs allows the better targeting of illicit (including counterfeit and unsafe) products and wrongly declared waste. Following the launch of the project and cooperation on AEO matters, both sides carried out joint AEO monitoring actions to ascertain whether the programs are equivalent. It is expected that equivalence can be achieved and that negotiations towards mutual recognition of AEO can be launched during 2010. Enhanced cooperation on counterfeit and unsafe products continues under an Action Plan on IPR and within the EU-China SSTL which will continue after its evaluation, involving more ports and putting more emphasis on counterfeit goods and waste exports.

The cooperation is not limited to these countries: in the near future, close cooperation will start with Canada and other trading partners. It is obvious that the cooperation with third countries is work-intensive and, considering that all administrations are suffering from a lack of human resources, many may decide to start with a limited number of partner countries and sign standard form agreements which allow progress to be made more quickly with other like-minded administrations. The EU hopes to sign the first standard form agreements in early 2010 in order to make quicker progress with other partner countries which have shown interest in achieving mutual recognition with the EU. However, those countries that wish to sign mutual recognition agreements with only some EU Member States will be disappointed: owing to the legal structure of the EU, the mutual recognition of AEO and/or security measures can only be agreed at EU-level and not with individual Member States.

## Endnotes

- 1 This article reflects the opinion of the author and does not bind the European Commission.
- 2 An Authorised Economic Operator (AEO) is defined in the *WCO SAFE Framework of Standards* as a party involved in the international movement of goods...complying with WCO or equivalent supply chain security standards. See World Customs Organization (WCO) 2007, *WCO SAFE Framework of standards to secure and facilitate global trade*, WCO, Brussels, p. 6, footnote 1, and also pp. 17 and 36 (definitions).

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At the time of preparing this paper, Dr Susanne Aigner was Acting Head of Unit Risk Management and Security in the European Commission's Directorate General for Customs and Taxation. At the time of publishing, Susanne had been appointed to the position of Deputy Director Compliance and Facilitation at the World Customs Organization.