Governance and Collaboration in Regulatory Supervision: A Case in the Customs Domain

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ABSTRACT

This article describes how in regulatory supervision some form of collaboration is necessary between regulator and company in the way evidence about compliance is collected and evaluated. How to arrange such collaboration? In this article, we investigate specific ideas about continuous control monitoring and apply them to regulatory supervision. By means of a design science approach, we propose a particular governance mechanism for continuous monitoring of compliance. We derive objectives based on the literature about regulatory supervision and about auditing. By means of a case study of a new customs supervision mechanism for container terminals in a large port, we identify legal, economic and technical feasibility conditions. In particular, we discuss the role of an intermediary. The case shows that continuous control monitoring is legally and technically feasible in the customs domain, and that a suitable party can be found to play the role of intermediary. However, a good business case for parties to invest in such a system needs to be developed.

KEYWORDS

Compliance, Continuous Control Monitoring, Public-Private Collaboration, Regulatory Supervision

1. INTRODUCTION

Companies must demonstrate compliance with rules and regulations. When government regulators assess whether a company is compliant, they have to rely on evidence provided by the company itself. This leads to a paradox: evidence must be collected and evaluated in order to demonstrate compliance, but that evidence is generated by the company and can in principle be manipulated! The paradox can be solved by the company implementing internal controls: organizational, procedural or technical measures to guarantee that the evidence collected is reliable (COSO, 1992). This shows that in many regulatory supervision relationships, at least some form of collaboration is essential: companies have to implement controls, provide evidence in a particular format, and provide access to inspectors when requested (Mertens, 2011).

On the other hand, regulators have to collaborate, in the sense that they have to adjust their assessments to the specific circumstances of the company or sector. Legislation is generic in order to be applicable in many different situations (Dworkin, 1977). In order to deal with such open norms
and adapt them to the circumstances, legal interpretation is crucial. This leads to a form of dialogue between regulator and company (Burgemeestre, Hulstijn, and Tan, 2011). There is also collaboration at sector level. Alternative interpretations of new legislation are actively debated. Branch organizations are trying to influence the debate. Black (2002) calls such debates regulatory conversations. Taking part in such debates also signifies a form of collaboration on the part of the regulator. Without notification, regulatory changes will appear to be sudden and impractical, and companies will not have enough time to adjust processes and software.

There are reasons to suggest that collaborative forms of regulatory supervision are more effective and more efficient, because companies have internalized the norms. Influenced by such approaches as self-regulation (Rees, 1988), responsive regulation (Ayres and Braithwaite, 1992), or risk-based supervision (Black, 2005), governments have experimented and adjusted regulatory arrangements (OECD, 2014). For example, modern approaches to tax compliance are now called ‘cooperative compliance’ (OECD, 2013). These cooperative approaches to regulatory supervision are often characterized by a shift in regulatory responsibilities from the regulator to the companies involved (Burgemeestre et al., 2011). For example, under many safety regulations, companies must make a risk assessment and determine themselves how to mitigate the risks by controls. Regulators only assess at a meta-level whether the company is ‘in control’.

Similar developments exist in the business domain, specifically in financial auditing. The world is changing continuously. Computational audit approaches make it possible to provide assurance (certainty) over the reliability of a data stream, at or near real time (Vasarhelyi, Alles, and Kogan, 2004). Consider online auditing (Koch, 1981; Vasarhelyi and Halper, 1991), continuous control monitoring (Alles, Brennan, Kogan, and Vasarhelyi, 2006) or continuous auditing (Kogan, Sudit, and Vasarhelyi, 1999; Kuhn and Sutton, 2010). Note that here too, financial auditors must rely on evidence, prepared by the company itself. Reliability of the data stream is ensured by internal controls. According to a recent survey (Chiu, Liu, and Vasarhelyi, 2014) most research papers on continuous auditing are either conceptual, or focus on the technical aspects. The governance aspects are largely left unexplored. Moreover, most reported applications are positioned in the financial sector; other application domains have not been explored (Chiu et al., 2014).

In the e-government literature several kinds of public-private collaboration arrangements have been proposed, to facilitate information sharing. For instance, Tan, Bjørn-Andersen, Klein, and Rukanova (2011) look at collaborative data sharing for supply chain supervision. They discuss the ‘piggy-backing’ principle: re-using commercially available information for regulatory purposes. Bharosa et al. (2013) look at representation standards and agreements for filing financial reports. Klievink, Janssen, and Tan (2012a) look at stakeholder analysis in establishing an information platform for sharing regulatory information. Klievink et al. (2012b) discuss the advantages of the ‘data pipeline’ concept for information sharing in order to enhance supply chain visibility, with expected benefits for both regulators and companies. Many of the cases and examples of these papers are set in the application domain of international supply-chains and customs supervision. We would like to follow in this tradition. However, these studies have mostly looked at sector-wide initiatives, such as the adoption of representation standards. They have not looked in as much detail at the governance relation between company and regulator.

In this paper we would like to combine ideas about collaborative forms of regulatory supervision, with auditing literature on continuous control monitoring. In this way, we hope to answer the following research question:
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