

How to Withstand CBSA's Scrutiny of Import Origin Claims and Import/Export Controls

By Jamie M. Wilks, Partner, McMillan Binch Mendelsohn LLP, Commodity Tax, Customs and Trade Law

Presented at:

Customs Compliance and Border Security

Best Practices in Regulatory Issues and Cross-Border Security

January 22 and 23, 2008

Delta Toronto Airport West, 5444 Dixie Rd.,
Mississauga, Ontario

A. Recent Case Law on Origin Verification

3 CITT cases of interest:

1. *Duhamel & Dewar Inc. v. CBSA*;
(AP-2005-046)
2. *Western RV Coach Inc. v. CBSA*; and
(AP-2006-002)
3. *MRP Retail Inc. v. CBSA*.
(AP-2006-005)

A. Recent Case Law on Origin Verification

The Law:

Imported goods are entitled to preferential NAFTA tariff treatment only if:

- (a) proof origin in the form of a NAFTA CO obtained by the importer from the exporter (or possibly from the producer); and
- (b) the goods are entitled to that treatment under the *NAFTA Rules of Origin Regulations*.

Customs Tariff, s. 16 and 24(1) and *Customs Act*, s. 35.1 and *Proof of Origin of Imported Goods Regulations*, s. 6.

A. Recent Case Law on Origin Verification

1. *Duhamel & Dewar Inc. (D&D)* and
2. *Western RV Coach Inc. (Western RV)*

Both cases concerned:

- Used RV's imported into Canada.
- NAFTA preferential tariff treatment denied by CBSA and CITT upheld CBSA's decisions. As a result, 6.1% MFN duty rate applies rather than NAFTA duty-free tariff treatment claimed.

A. Recent Case Law on Origin Verification

1. D&D and 2. Western RV (*continued*)

In response to a CBSA NAFTA verification origin audit:

- (a) D&D's foreign vendor withdrew its NAFTA CO and CBSA rejected the producer's NAFTA CO; and
- (b) Western RV's foreign vendor provided a NAFTA CO issued by the producer to the original purchaser of the RV. Since producer could not provide additional supporting documentation requested by CBSA to verify origin (no longer available 8 or 9 years after the RV manufactured), CBSA rejected NAFTA preferential duty-free tariff treatment.

A. Recent Case Law on Origin Verification

3. MRP Retail Inc. (MRP)

- MRP imported women's cotton knit T-shirts and tank tops (the "Women's Shirts") from California Sunshine (CS) of the U.S.A. between April 10 and July 24, 2001.
- MRP claimed NAFTA preferential tariff treatment at the Mexican Tariff rate. CBSA denied the preferential tariff treatment and the CITT allowed MRP's appeal.
- CS's Mexican supplier, Alimex, manufactured the Women's Shirts in Mexico, in certain cases jointly with CS in the U.S.A.

A. Recent Case Law on Origin Verification

3. MRP (*continued*)

- If the Women's Shirts were cut (or knit to shape) and sewn or assembled in the U.S.A. or Mexico from cotton that was grown in the U.S.A. or Mexico, they would be originating goods under NAFTA.
- Fabric suppliers provided NAFTA COs certifying that the cotton from which the Women's Shirts were made were grown in North America.

NAFTA Rules of Origin Regulations, s. 4(1)(b) and (j).

A. Recent Case Law on Origin Verification

3. MRP (*continued*)

(a) Proof of Origin:

- CBSA challenged the “proof of origin” alleging that the NAFTA COs incorrectly referred to CS as the “producer”.
- CITT disagreed. The *Proof of Origin of Imported Goods Regulations* do not prescribe a specific form of CO or indicate that it must be provided by a “producer”.
- In any event, CS is a “producer” within the meaning of those Regs since it in all cases commissioned and directed the processing.
- The NAFTA COs satisfied the low legal threshold for proof of origin.

A. Recent Case Law on Origin Verification

3. MRP (*continued*)

(b) Whether Rules of Origin Satisfied:

- “In the Tribunal’s view, the real issue in the appeal is whether or not MRP has proved that the goods in issue met the prescribed rules of origin”.
- There was conflicting evidence whether CS commingled Alimex’s Women’s Shirts with other shirts that were not NAFTA qualifying, thereby making it impossible to trace and verify whether CS’s exports to MRP were NAFTA qualifying.
- Despite the conflicting evidence, CITT gave the benefit of the doubt to MRP.

A. Recent Case Law on Origin Verification

3. MRP (*continued*)

- CITT will not be CBSA's "rubber stamp" by holding importers to CBSA's exacting audit standards requiring proof of an unbroken chain of custody of NAFTA originating goods.
- CBSA was not without blame in its untimeliness in conducting its verification review.

A. Recent Case Law on Origin Verification

Lessons Learned:

- (a) A CO does not immunize an importer from duty assessments.
- (b) There appears to be a low legal threshold for “proof of origin” in the form of a NAFTA CO.
- (c) In the case of used goods (D&D and Western RV), it might be difficult to obtain evidence of origin from the producer given the time lag between production of the good and re-sale as a used good. Supplementary evidence may be needed from the exporter and others of any alterations or repairs made to the used goods.

A. Recent Case Law on Origin Verification

(d) CBSA should not hold an importer to the exacting audit standard of providing origin evidence that is beyond any doubt, especially where CBSA's conduct has contributed to the difficulty in obtaining records.

Unanswered Question:

(a) Would CBSA accept a producer's (rather than an exporter's) CO as proof of origin in any circumstances?

A. Recent Case Law on Origin Verification

What can you as an importer do:

- (a) Indemnification from a foreign vendor.
- (b) Covenant from the foreign vendor to cooperate in a NAFTA origin verification review.
- (c) Do not accept NAFTA COs blindly. Take pre-emptive, pro-active due diligence before/in case the CBSA conducts a NAFTA origin verification review.

A. Recent Case Law on Origin Verification

What kind of due diligence?

- Depends on the applicable NAFTA rule of origin, whether:

Criterion A: Wholly obtained or produced (100% NAFTA territorial content).

Criterion B: Non-originating materials meeting:

- (i) tariff shift only rules or
- (ii) tariff shift & Regional Value Content (RVC) threshold.

Criterion C: All originating materials.

Criterion D: Special cases permitting non-originating materials to meet RVC threshold only.

NAFTA, Chapter 4 and *NAFTA Rules of Origin Regulations*.

A. Recent Case Law on Origin Verification

What kind of due diligence? *(continued)*

- Importer requesting exporter complete CBSA origin verification questionnaire. Specific questionnaires developed depending on the applicable rule of origin criterion.
- Importer requesting an independent confidential audit conducted at their supplier. Report to remain confidential (Solicitor/client privilege).

A. Recent Case Law on Origin Verification

- This case law is relevant to consider when seeking preferential tariff treatment under Canada's bilateral free trade agreements with Chile, Costa Rica or Israel.
- Also should be borne in mind when seeking preferential tariff treatment under multi-lateral arrangements (e.g., GPT and LDC).

B. Export and Import Controls

- *Export and Import Permits Act (EIPA)* administered by the Export and Import Controls Bureau (EICB) of the Department of Foreign Affairs and International Trade (DFAIT).
- The specified lists controlling the import and export of goods are the Import Control List (ICL), the Export Control List (ECL), and the Area Control List (ACL).

B. Export and Import Controls

Overview – Permits

- All goods on the ICL require an import permit.
- All goods on the ECL require an export permit.
- The ACL is a list of countries for which export permits are required to export any and all goods (Belarus and Myanmar).

B. Export and Import Controls

Import Controls

- Textiles and Clothing
- Agricultural Products
- Steel Products
- Weapons and Munitions

B. Export and Import Controls

Export Controls

The ECL includes eight groups:

- **Group 1:** Dual Use List
- **Group 2:** Munitions List
- **Group 3:** Nuclear Non-proliferation List
- **Group 4:** Nuclear-Related Dual Use List
- **Group 5:** Miscellaneous Goods (e.g. U.S. origin goods, roe herring, cedar shakes and shingles, logs, softwood lumber)
- **Group 6:** Missile Technology Control Regime List
- **Group 7:** Chemical and Biological Weapons Non-Proliferation List
- **Group 8:** Chemicals for the Production of Illicit Drugs

B. Export and Import Controls

Applying for a Permit

- Certain controlled goods require an Individual Permit for import or export.
- Certain goods may only require reference to a General Permit, which is not specific to an individual importer or exporter and allows for the pre-authorized export or import of goods in specified conditions (e.g. most U.S. origin exports to third countries).

B. Export and Import Controls

Applying for a Permit *(continued)*

- Individual permits can take 10 days to several months depending on the good and the destination.
- Alternatively, non-binding opinions can be sought from the EICB to determine if a permit is required (2-6 weeks for a response).
- Certainty versus timing and release of sensitive data.

B. Export and Import Controls

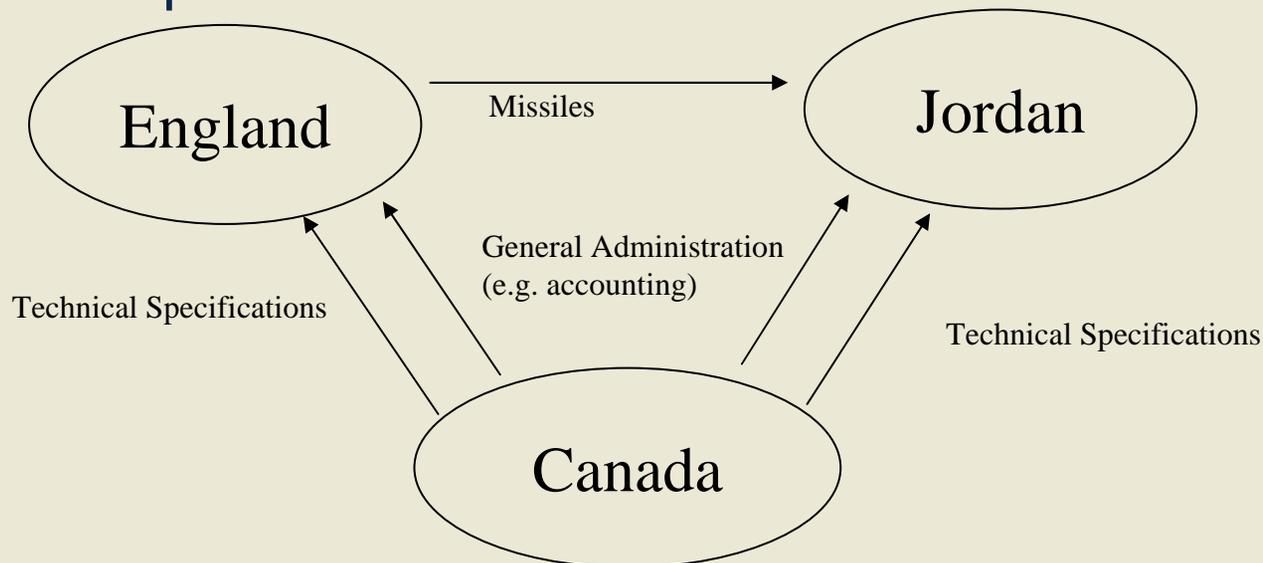
Technology

- Export of “technology” related to a controlled product requires an export permit.
- For military goods, for example, “technology” means specific information which is required for the development, production or use of a controlled product, and not generally available “in the public domain”.
- Very broad definition - most technical specifications and data will fall under the definition.
- Narrow exception if “in the public domain”.

B. Export and Import Controls

Case Study with Technology

- Export permits can be required even if no goods are exported from Canada



B. Export and Import Controls

Violations:

- CBSA and RCMP enforce the EIPA.
- Both corporations and their officers are potentially liable for prosecution and penalties for contravention of the EIPA, the *Customs Act* and their respective regulations.
- Fines and imprisonment of officers and directors.
- Goods may be detained and seized at the border.

B. Export and Import Controls

How to prevent non-compliance:

- Be aware of the types of goods covered under the ECL and ICL.
- Implement appropriate preventative procedures.
- Common compliance pitfalls under the ECL:
 1. Group 1 Dual Use Goods; and
 2. Group 5 Miscellaneous Goods.

B. Export and Import Controls

How to prevent non-compliance: *(continued)*

1. Dual Use Goods:

- May appear to be only for benign use.
- Could it be put to dangerous use in the wrong hands?
- Could it be weaponized?
- May require technical and scientific expertise to determine whether chemicals, gases, etc. are caught.

B. Export and Import Controls

How to prevent non-compliance: *(continued)*

2. Group 5 Miscellaneous Goods:

- Random, *ad hoc*, to suit specific policy purposes
- Examples: Softwood lumber products; various foods and agricultural products; U.S. origin goods; and goods intended for use in WMD

B. Export and Import Controls

How to mitigate the damage once non-compliance has occurred:

- No formal voluntary disclosure program for EIPA violations.
- Informally make voluntary disclosure to CBSA seeking favourable settlement terms.
- Seek input from legal counsel.

B. Export and Import Controls

How to mitigate the damage once non-compliance has occurred: *(continued)*

- May be room for negotiation.
- CBSA may want some form of penalties, albeit reduced (for example, AMPs or discretionary penalties under an ascertained forfeiture), to recognize the degree of seriousness of the infractions.
- Depends on the nature of the infraction (ranging from failure to indicate GEP # on a customs export declaration to exporting nuclear materials to Iran).

McMILLAN BINCH MENDELSON

Toronto Montréal