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5x5 series: Insights and actions

NAFTA and USMCA origin verification audits

Businesses in the Americas continue to benefit from duty free imports for qualified products under free trade agreements (FTAs), resulting in significant savings opportunities. A key FTA utilized by businesses is the United States-Mexico-Canada Free Trade Agreement (USMCA) which entered into force on 1 July 2020 and superseded the North American Free Trade Agreement (NAFTA). Please take 5 minutes to gain 5 insights and 5 actions related to the ongoing enforcement activities of FTA rules of origin and requirements, particularly related to NAFTA and USMCA preferential treatment claims.

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5 insights to consider

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Customs authorities may conduct **NAFTA origin verification audits of foreign exporters** to validate that their products meet rules of origin and other requirements. While the NAFTA expired on 30 June 2020, the statute of limitations is five years for the United States and Mexico, and six years for Canada, so goods exported **between November 2017 and June 2020** remain subject to origin verification audits by the US and Mexican customs authorities.

Customs authorities may similarly conduct **USMCA origin verification** audits on foreign exporters to validate compliance with the rules of origin.

If the customs authorities determine that the rules of origin were not met, the **importer may be subject to payment of omitted duties and taxes**, **as well as significant penalties**. Business consequences can result for both importers and exporters and, if this becomes a repeated pattern of conduct, the exporter may be prohibited from making USMCA preferential claims.

In the past two years, the Mexican customs authorities have increased their enforcement actions related to FTAs and they are regularly conducting origin verification audits on US and Canadian exporters of goods.

Key industries and goods Mexican customs authorities are focusing on for NAFTA and USMCA origin verification audits include **automotive**, **pharmaceutical**, **iron and steel**, **machinery** (e.g., for cooking or heating food and drinks, presses), electrical transformers, electronic gaming machines, special woven fabrics (e.g., tulles and other net fabrics), among others.

5 actions to take now

Prepare for a complex audit process. During an origin verification audit, exporters must provide detailed documentation demonstrating the production process of the exported products. The Mexican customs authorities are requiring extensive amounts of documentation, including transactional evidence for the purchase of all components used in the production (e.g., purchase orders, commercial invoices, proof of payment, etc.), and detailed tracing of all documentation (e.g., tracing purchase to production to export).
Organize an origin verification audit defense file. Exporters, particularly

those in industries that Mexican customs authorities are focusing on, should organize defense files. These should include the transactional evidence that traces the production process, to provide during an origin verification audit.

Review historical filings. Conduct a risk-based review of NAFTA and USMCA exports, to identify any exports that did not meet the applicable rules of origin. If applicable, prepare an origin qualification analysis to determine whether the product-specific rules of origin are met.

Understand your trade profile. Analyze government trade data to assess your business's import and export profile including duties paid, duties saved under FTAs, potential savings opportunities, etc.

Conduct an FTA process improvement review. Review the business's FTA policies and procedures and, through data analytics and transactional sample analysis, identify risks and gaps. Establish a roadmap to define and implement an effective operating model (e.g., updates to process flows, work instructions, training materials, origin verification audit defense strategy, etc.).



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