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United States and Canada Conclude Negotiations to Revise NAFTA

Text of United States-Mexico-Canada Agreement ("USMCA") Released

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International Trade

On September 30, 2018, the United States and Canada announced the successful conclusion of negotiations that will allow Canada to join the United States and Mexico in signing a revised North American Free Trade Agreement ("NAFTA"). The conclusion of this revised agreement, which will be known as the United States-Mexico-Canada Agreement ("USMCA"), follows months of negotiations that commenced after the Trump Administration notified Congress in May of its intent to renegotiate NAFTA. The Office of the U.S. Trade Representative ("USTR") has published the text of the new USMCA on its website.

The Agreement follows the August 27, 2018 announcement by the United States and Mexico of a preliminary agreement to move forward with a revised NAFTA. Both countries expressed their desire to sign a revised agreement prior to the departure from office of current Mexican President Enrique Peña Nieto, whose term ends on November 30, 2018. On August 31, 2018, the Trump Administration notified Congress that it intended to move forward with the deal with Mexico, without Canada if necessary. Also at play were U.S. procedural requirements established under Trade Promotion Authority ("TPA") legislation, which require the President to make public the text of a proposed trade agreement 60 days before the President can sign it. This effectively established September 30 as the last day that the Trump Administration could publish the text of the revised agreement while still permitting signature by November 30, 2018.

The Parties are expected to sign the USMCA by November 30, 2018. Following signature, the terms of TPA legislation provide that the Administration will have up to 60 days to submit to Congress a description of changes to U.S. law necessary to implement the Agreement. The International Trade Commission must also complete a study of the potential economic impact of the revised agreement within 105 days from signature. Finally, 30 days before a bill is formally introduced, the Administration must submit to Congress a final text of implementing legislation and a draft Statement of Administrative Action. Because of these procedural requirements, the USMCA is not expected to be approved before the next session of Congress convenes in 2019. The Agreement enters into force on the first day of the third month after it is approved by all three countries.

The USMCA makes some important changes to substantive provisions of NAFTA, including in some of the areas subject to controversial negotiations over recent months. Below is a summary of some of the most notable changes.

Increased Regional Content for Auto Rules of Origin and New Wage Requirements

Among the most contentious issues negotiated as part of the revision of NAFTA have been the rules of origin relating to automotive products, and in particular, the minimum regional content requirement that such products must meet in order to benefit from the preferential tariffs in place among North American partners. The USMCA increases the regional value content for passenger vehicles and light trucks above the 62.5 percent currently required under NAFTA to 75 percent, under the net cost method of calculating content. In addition, the USMCA would increase the content requirement for auto parts for use in passenger vehicles and light trucks by adopting a tiered approach. Specifically, the USMCA would require 75 percent content for the most critical components, while additional categories of products are subject to content requirements between 60 and 70 percent.

In addition, auto producers must also meet requirements that at least 70 percent of steel and aluminum purchases for the previous year were made in North America. Finally, producers must also certify annually that production meets certain Labor Value Content (“LVC”) requirements, which specify thresholds above which production must be manufactured by workers making at least $16 per hour.

Elimination of Certain Canadian Dairy Pricing Classes

Canada agreed in bilateral commitments to the United States to eliminate key aspects of its milk class pricing system known as milk classes 6 and 7, which had been criticized by U.S. producers for incentivizing Canadian cheese producers to use Canadian milk ingredients—specifically milk protein concentrates and skim milk powder—for production. In addition, to safeguard against an increase in exports of Canadian milk protein concentrates and skim milk powder, Canada also agreed to apply export duties to such products if total global exports from Canada exceed specified thresholds. The Agreement also imposes certain information sharing and public comment requirements on Canada and the United States before any new milk classes may be introduced.

Enforceable Currency Provisions Appear for First Time in a U.S. Trade Agreement

A significant development in the USMCA is the inclusion of binding obligations relating to currency manipulation and misalignment. This marks the first time such provisions have been included in a U.S. free trade agreement, despite currency manipulation having been a longstanding focus of many in Congress and past Administrations. Among the obligations included in this chapter, the Parties agree to “achieve and maintain a market-determined exchange rate regime,” and to “refrain from competitive devaluation, including through intervention in the foreign exchange market.” The Agreement also contains a commitment to “strengthen underlying economic fundamentals, which reinforces the conditions for macroeconomic and exchange rate stability.”

Notably, footnote 1 of this chapter of the Agreement exempts from coverage activities carried out by an “exchange rate or fiscal or monetary authority” of a party, including central banks, likely exempting action by the Federal Reserve, such as previously employed “quantitative easing” policies. Also of significance is the ability of Parties to enforce certain currency-related obligations through dispute settlement, though such dispute settlement provisions only apply to limited obligations. Specifically, obligations subject to dispute settlement include those relating to transparency.

Canada Excluded from Government Procurement Access

Notably, the revisions made under the USMCA exclude Canada from the government procurement obligations of the Agreement, noting in sub-paragraph *2bis* that the obligations of that chapter apply only between the United States and Mexico. While the United States and Canada will still benefit from reciprocal market access under the World Trade Organization ("WTO") Government Procurement Agreement ("GPA"), there are significant differences in market access between the WTO GPA and access currently available under NAFTA.

Among the most consequential differences are the higher thresholds that apply to what is considered "covered procurement" under the WTO GPA. Specifically, under NAFTA, suppliers in Canada and the United States enjoy access to their respective neighboring procurement markets for the supply of goods to the central government valued at or above $25,000. However, under the WTO GPA, the threshold for market access for such contracts is $180,000. As a result, the USMCA now contemplates reduced market access vis-à-vis Canada for such contracts valued between $25,000 and $180,000. The thresholds agreed to between Mexico and the United States, in contrast, remain the same as those thresholds currently applicable under NAFTA, which have periodically been adjusted for inflation from their original value.

Limitations on Investor-State Dispute Settlement, but Other Dispute Provisions Remain Largely Intact

NAFTA includes provisions providing for State-to-State dispute settlement under NAFTA Chapter 20, investor-state disputes settlement ("ISDS") under NAFTA Chapter 11, and specific trade remedy proceedings under Chapter 19. While the Trump Administration had previously taken a hard line against the inclusion of binding dispute settlement provisions in trade agreements, the majority of these NAFTA provisions have survived and appear in similar form in the USMCA. Specifically, State-to-State dispute settlement provisions remain almost entirely unaltered in substance, as do provisions relating to disputes specific to trade remedy proceedings.

With regard to ISDS provisions, however, the USMCA contains important changes, most notable of which is the exclusion of Canada from these provisions of the Agreement. As a result, the ISDS provisions will apply only to investment disputes between the United States and Mexico. With respect to U.S.-Mexico investment disputes, investors' recourse to arbitration will be meaningfully narrower than that available under NAFTA. For example, except in certain specified sectors, investors may only arbitrate claims for breaches of national treatment or most-favoured nation treatment, as well as cases of direct expropriation. The USMCA excludes investor claims relating to the establishment or acquisition of an investment, as well as claims of indirect expropriation and violations of the fair and equitable treatment standard. Additional procedural requirements also require that claims relating to these investments first be brought in national courts, subject to a few exceptions, before an arbitration under the ISDS provisions is commenced. By contrast, investors operating within a limited number of enumerated sectors may pursue broader claims (including claims relating to fair and equitable treatment and indirect expropriation) for investments involving written contracts with national authorities, and also need not first pursue recourse in national courts. These enumerated sectors include: oil and natural gas, telecommunications, transportation, infrastructure ownership and management, and power generation. Under the USMCA, investments made before the termination of NAFTA will continue to be protected by NAFTA Chapter 11 for a period of three years from the date NAFTA is terminated.

Sunset Clause for Automatic Termination of the Agreement After 16 Years

Similar to the U.S.-Mexico Agreement announced in August, the final provisions of the USMCA contain a "sunset clause" providing for the automatic termination of the Agreement after 16 years, unless the United States, Canada, and Mexico all confirm the Agreement for a new 16-year term. Review procedures for the Agreement actually begin much earlier, however, with the first "joint review" taking place no later than the sixth anniversary of the entry into force of the Agreement. If all three countries confirm their desire to extend the term of the Agreement at that time, the extension will be automatically extended for another 16 years. If, however, there is not consensus to confirm the Agreement at that first review, the Parties will continue to conduct a joint review annually for the remainder of the term of the agreement. During that time, the Parties may at any time extend the term of the Agreement for another 16 years by confirming in writing through their heads of government their wish to do so.

Side Agreements on U.S. Section 232 Measures

In addition to the text of the Agreement itself, a number of side letters were also concluded as part of the USMCA negotiations. In particular, the United States reached agreement with both Canada and Mexico on issues relating to the Administration's use of Section 232 measures against exports from Canada and Mexico. With regard to the pending Section 232 investigation on autos, the United States will not exempt Canada and Mexico from that investigation, though it agreed to exclude certain quantities of Canadian and Mexican auto exports from any measure imposed. No similar exclusions for Canada and Mexico were agreed to with regard to tariffs already imposed under Section 232 against U.S. imports of steel or aluminum, though agreement was reached relating to various procedural steps that the United States would follow for all Section 232 measures impacting Canada and Mexico. These procedural steps include a 60-day delay of imposition of measures against Canada and Mexico, to allow for a possible negotiated outcome, as well as an explicit recognition that both Canada and Mexico may impose retaliatory trade measures against the United States in the event that any U.S. Section 232 actions constitute a breach of the WTO Agreement or the USMCA.

Other Areas Covered by the Agreement

In addition to the specific changes noted above, the USMCA also makes notable changes in other areas. For example, the Agreement significantly updates the competition obligations between the Parties, including by requiring increased procedural fairness in competition law enforcement. A new Digital Trade chapter also addresses trade and investment in innovative products and services, including by limiting the application of customs duties to digital products and minimizing restrictions to the cross-border transfer of data. Finally, protections for intellectual property in the USMCA include 10 years of data protection for biologic drugs, a minimum copyright term of life of the author plus 70 years, procedural provisions relating to the recognition of new geographical indications ("GIs"), and obligations relating to civil and criminal procedures for protection of trade secrets.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our International Trade practice:

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