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We Have a Deal - The U.S. Trade Representative and House Democrats Reach an Agreement on the Revised Version of the USMCA

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House Democrats and the White House announced an agreement on a revised version of the United States Mexico Canada Agreement ("USMCA"). The USMCA was originally signed on November 30, 2018, by the three countries. Since then, House Democrats and the White House have bargained for more than a year to address concerns relating to labor enforcement, environmental standards, and pharmaceutical protections stemming from the original version of the USMCA. In addition to those, the White House asked for additional changes to vehicle rules of origin requiring steel and aluminum to be produced in the NAFTA region.

Next Steps

The new revised accord was signed on December 10, 2019, in Mexico City ("Addendum"). The USMCA and the Addendum still need to follow each country's domestic ratification process. Mexico was the only country to have ratified the USMCA, and they will now need to reopen and ratify an Addendum. For Canada, the USMCA will require consideration of implementing legislation by Parliament in line with normal parliamentary procedures. For the United States, the Bipartisan Congressional Trade Priorities and Accountability Act of 2015 (a/k/a Trade Promotion Authority, Fast Track or "TPA") allows the President to submit an implementing legislation bill under expedited procedures, pursuant to which the bill may come to the floor without action by the leadership, and can receive a guaranteed up-or-down vote with no amendments. It is expected that the pact will be discussed in the House on December 15 with the goal of voting on it by the 18th. However, there are reports indicating that the deal may get stuck in the Senate. Senate Majority Leader Mitch McConnell says it won't take up USMCA this year and he will wait for the impeachment trial to be over. The USMCA is expected to be bipartisan and will pass the House. The

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revised version was also approved by Richard Trumka, the AFL-CIO President, who visited Mexico on several occasions.

As of the date of this Client Alert, the exact language of the Addendum has not been disclosed to the public, however, we will generally summarize the major improvements as published in a House Committee on Ways and Means fact sheet and a summary of revised outcomes published by Canada. Be cautioned this information might be adjusted and that this is not a complete analysis of all aspects of the Addendum and USMCA.

What's different?

1. **General Enforcement.** The state-to-state dispute settlement chapter has been changed in a manner that strengthens enforcement, including in the areas of labor and the environment.
 - Removed language allowing a responding party to block the formation of a dispute settlement panel.
 - Created rules of evidence meant to be used in labor litigation, environment, and other fact-intensive disputes.
 - Creates a roster of potential panelists to provide for additional clarity and transparency in the rules of procedure that provide guidance on the operation of panel hearings.
2. **Labor Enforcement.** The labor chapter has been further strengthened so that the parties have increased flexibility to pursue violations of the Agreement under the dispute settlement mechanism. This is made possible through the removal of the requirement that violations be committed “through a sustained and recurring course of action or inaction” when it relates to violence against workers. Additionally, the burden of proof has been reversed, in that failure to comply with an obligation in the chapter is now presumed to be “in a manner affecting trade or investment between the parties,” unless the defending party can demonstrate otherwise.
 - Removed obstacles that made it difficult to prove that member countries are failing to live up to commitments to protect workers from violence.
 - Created a presumption that labor violation affects trade and investment and will require the other governments to prove otherwise.
 - Removed language in the Forced Labor provision that made it effectively unenforceable.
3. **Robust Monitoring.** Inclusion of mechanism and resources that ensure the U.S. government will effectively monitor compliance with the agreement’s labor obligations specific to Mexico. The latter includes:
 - Creation of an interagency committee that will monitor Mexico’s labor reform implementation and compliance with labor obligations.
 - Reporting requirements to Congress.
 - Established key benchmarks for Mexico’s labor law implementation process.

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- Established labor attaches located in Mexico that will provide on-the-ground information about Mexico's labor practices.
4. **Enhanced Labor Enforcement.** Creation of new labor-specific enforcement mechanism that provides for facility-based enforcement of labor obligations in the agreement within a rapid timeframe (85 days is believed).
- Takes immediate effect upon entry into force of the Agreement.
 - It covers all manufactured goods and services traded between the United States and Mexico.
 - Requires verification of compliance by independent labor experts; and
 - Leads to penalties on goods and services that are not produced in compliance with the freedom of association and collective bargaining obligations.
5. **Environment and environmental monitoring.**
- Created a presumption that an environmental violation affects trade and investment and will require the other government to prove otherwise.
 - Added a commitment that all Parties will adopt, implement, and maintain seven multilateral environment agreements (MEAs), and additional language that allows all Parties to agree to add to the list of covered MEAs.
 - Restored a provision in the old NAFTA that prioritizes MEA commitments when implementing MEA and trade agreement obligations.
 - Removed language in order to allow Montreal Protocol to be covered in this agreement.
 - Created interagency committee that will: 1) conduct assessment of the current environmental landscape of Canada and Mexico; 2) Monitor implementation of the environmental obligations and recommend enforcement actions in connection to the new NAFTA; and 3) Provide platform for better coordination, utilizations, and funding of U.S. Government efforts to strengthen environment practices amongst USMCA Parties.
 - Established environment-focused attachés in Mexico City that will regularly monitor Mexico's environment laws, regulations, and practices.
 - To hold partners and actors accountable to the agreement, it was insisted to create and enhance relevant mechanisms, resources, and commitments: 1) New customs verification mechanisms to ensure that only legally harvested and taken flora and fauna are traded through Mexico; 2) A new authorization of the North American Development Bank and funding for EPA grants under the Border Water Infrastructure Program to address pollution on the U.S.-Mexico border; 3) Additional funds to the Trade Enforcement Trust Fund to be used for environment-focused enforcement efforts.
6. **Rules of origin for vehicles.** Rules of origin are the criteria used to determine whether a good has undergone sufficient production in a free trade area to be eligible for preferential tariff treatment, ensuring that the benefits of an agreement accrue primarily to producers located in the member countries. USMCA automotive rules of origin contain a requirement that 70% of the steel purchased by vehicle assemblers qualify as originating in the USMCA region. This requirement has been

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clarified that all steel manufacturing processes must occur in one or more of the parties, except for metallurgical processes involving the refinement of steel additives, for purposes of meeting the 70% requirement. It has been reported that these new additional requirements have a seven-year phase-in period.

- As you may recall, the USMCA rules of origin follow the NAFTA concept of Regional Value Content but raise this for automobiles and light trucks from 62.5% to as high as 75% for “Core” parts (e.g. engines, transmissions); 70% for “Principal” parts (e.g. brakes, tires, glass); and 65% for “complementary” parts (such as pipes, valves, and radios). The NAFTA *de minimis* exception is increased from 7% to 10%.
- Labor Value Content – For the first time in a trade agreement, the new USMCA includes new rules whereby 40% of passenger vehicles and 45% of trucks must include content made by workers earning at least \$16 U.S. dollars per hour. Up to 10% of this can be R&D expenses. This provision will be phased in starting in 2020.

7. Pharmaceuticals and Intellectual Property.

- Removed provisions requiring the Parties to provide 10-years of exclusivity for biologics.
- Removed provisions requiring Parties to confirm that patents would be available for new uses of known products. This provision would have locked in the practice of “patent ever-greening” in which pharmaceutical companies obtain hundreds of patents related to a product to block generic competition and price reductions.
- Removed provisions requiring three additional years of exclusivity for clinical information submitted in connection with new uses of previously-approved pharmaceuticals products.
- Revised regulatory review provision to clarify the circumstances in which generic and biosimilar companies may use patented invention so they can obtain marketing approval on day one of the patent expiration. Revised data protection provision to incorporate limitations in U.S. law that foster generic competition.
- Revised patent linkage to remove the “hard linkage” of regulatory approval and patent status. Mexico must ensure that all interested parties receive notice and an opportunity to be heard. The revision also includes language that permits incentives for generic competition and improves transparency.
- Revised patent term adjustment provision to provide non-exhaustive examples of limitations on the adjustment of patent terms for regulatory delays

Conclusion

USMCA succeeds in updating some parts of NAFTA. However, the new rules of origin will make it harder for manufacturers to comply and obtain preferential treatment. In some situations, importers might find more expensive complying with rules of origin than paying the standard bounded tariff rate. Keep in mind the agreement is not yet concluded. The exact language has not been made public. As we are all too familiar, the devil is in the details. Moreover, the U.S. Senate Majority leader has already stated that they will not review the revised agreement this year (possibly until the impeachment trial is

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concluded). There's still room for events that might further delay the approval.

Since the start of NAFTA renegotiations and tariff implementations (Section 232 and 301), we have been helping clients navigate the implications of new trade regulations in their business. We can assist you in developing strategies to assess and mitigate risk arising from regulation changes.

Butzel will be providing further Client Alerts and other updates as we analyze the complete the USMCA and Addendum specifically tailored to global supply chains and the auto industry.

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