U.S.-Mexico-Canada Agreement: Preliminary Insights For Business

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Last night, Canada and the United States reached an agreement, together with Mexico, on what is essentially a revised NAFTA. The new agreement will be renamed the United States-Mexico-Canada Agreement (USMCA). This update provides preliminary insights into what the USMCA will change from the NAFTA, what it will not change, and what will be required for the USMCA to enter into force.

What Will Change

- **Stricter rules of origin for automobiles and parts**
  - Including a 75 per cent regional value content (RVC) requirement for passenger vehicles and light trucks; 75 per cent or less for parts; 70 per cent for steel and aluminum and minimum high-wage (US$16) labour value content requirements of 40/45 per cent for passenger vehicles and light trucks respectively.
  - Because the new automotive rules of origin are prescriptive and complex, compliance is likely to be logistically and administratively challenging.

- **Origin Procedures**
  - Made more flexible, including with respect to certification of origin.
  - Removes the "one year rule" for parties to retroactively change non-NAFTA origin of a good to NAFTA origin in order to qualify for refund of customs duties paid; the normal four year period will apply.

- **Agricultural goods**
  - Canada has granted the U.S. additional in-quota access to various dairy products. For some products, the new allowances are greater than those offered in the Trans-Pacific Partnership Agreement and in some cases less but with shorter phase-ins.
  - Canada has agreed to eliminate "Class 7" milk, which has enabled processors to purchase milk for production of certain products, including milk protein substances, at world prices rather than higher supply-managed prices. This could prove to be a more substantive concession than the additional in-quota access, although it may be mitigated by the

fact that Canada does not appear to have agreed to restrictions on compositional standards for cheese.
    - Canada has granted the U.S. significant new in-quota access for poultry and eggs.
    - The U.S. has granted Canada some new in-quota access for products made from sugar refined in Canada.
    - Canada has agreed to disciplines on what the U.S. considers to be discriminatory grading practices for wheat.

- **Rules of Origin De Minimis**
    - Raised to 10 per cent as in the CPTPP.

- **De Minimis Import Thresholds for Duty and Tax Collection**
    - Canada has agreed to *De Minimis* thresholds of C$150 and C$40 for the collection of customs duties and taxes (GST/PST/HST) at the time or point of importation by express shipment. The lower threshold for tax collection and the fact that these thresholds do not restrict subsequent assessment and collection of these duties or taxes may help to mitigate the effect on Canadian retailers.

- **Textiles and Apparel**
    - Cuts in half annual Canadian TPL entitlement for exports of cotton and man-made fiber apparel, and reduces the wool apparel based entitlement by a little bit over 20 per cent.
    - More than doubles U.S. access for cotton and man-made fibre apparel to Canada (although U.S. wool apparel access is slightly lower than under the NAFTA).

- **Intellectual Property**
    - Parties will be required to provide 10 years of market exclusivity for biologic drugs, rather than the 8 years provided under current Canadian law.
    - Parties will be required to provide copyright protections beyond those under current Canadian law: from life of the author plus 50 years to life plus 70 years, and 75 years from the end of the calendar year of the first authorized publication for copyright held by other than a natural person.
    - Despite the “notice-and-takedown” provisions in the USMCA, Canada is exempt from this provision due to its current “notice-and-notice” system as well as other safeguards in its copyright law.
    - Parties will be required to provide patent term adjustment as compensation for delays in the issuance of patents of more than five years after filing or three years after request for examination. Periods of time not directly attributable to the granting authority as well as periods of time that are attributable to the patent applicant may be excluded from the adjustment term.

- **Investment**
    - Investor-state dispute settlement (ISDS) claims against Canada and by Canadian investors are sunsetted; they will no longer be available three years after the USMCA enters into force or for investments not existing as of entry into force. Considering that Canada has faced numerous claims

by U.S. investors, including some successful ones, but Canadian investors have never had a successful claim against the United States, this will be seen as mostly benefitting Canadian governments. Canadian investors will continue to have access to ISDS against Mexico under the CPTPP.

- **Section 232**
  - Canada and the U.S. have prepared two side-letters to reflect their understanding on the application of U.S. Section 232 "national security" measures on Canadian goods:
    - One letter provides that, if the U.S. does impose Section 232 measures on automotive goods, imports from Canada will be exempt up to certain thresholds: 2.6 million passenger vehicles per year, all light trucks and US$32.4 billion in auto parts per year. These thresholds are well above existing trade levels.
    - The second letter provides for a 60-day "cooling off" period before any U.S. Section 232 actions will apply to imports from Canada. It also provides that Canada has the right to take trade retaliation if the U.S. takes a Section 232 action that is "inconsistent with" the NAFTA, the USMCA or the WTO Agreement. However, because the U.S. has insisted that those agreements give it full discretion to use Section 232, the retaliatory right may itself be subject to dispute.
  - Importantly, Canada did not obtain a commitment from the U.S. to lift its Section 232 tariffs on Canadian steel and aluminum. It remains unclear whether the U.S. will insist on quotas as part of any subsequent agreement to remove those tariffs.

- **Sunset**
  - The "sunset" clause demanded by the United States has been watered-down to the point where it is unlikely to materially affect business planning. The Agreement will terminate after 16 years (not the 5 the U.S. had demanded) with reviews every 6 years during which it can be extended for another 16 years.

What Will Not Change, or Not Change Much

- **Chapter 19**
  - The ability of Canadian companies and governments to challenge U.S. anti-dumping and subsidy determinations before a bi-national panel rather than in U.S. courts has been preserved, now in Chapter 10. Chapter 19 will continue to apply to all ongoing reviews related to Final Determinations published before entry into force of the new Agreement. The elimination of Ch. 19 had been a key U.S. demand and its preservation as between Canada and the U.S. is an important win for Canada and Canadian businesses, including the softwood lumber industry.

- **Chapter 20**
  - The NAFTA’s state-to-state dispute settlement mechanism has been preserved, now in Chapter 31, but will continue to be non-functioning unless new panellist rosters are appointed and maintained. This has

implications too for the Labour and Environment chapters, compliance with which is ultimately subject to dispute settlement under Chapter 31.

- **Temporary Entry**
  - The NAFTA provisions appear to be unchanged or mostly so.

- **Government Procurement**
  - The Government procurement provisions will apply as between the United States and Mexico only. Canada–U.S. procurement will continue to be governed by the WTO Government Procurement Agreement (GPA). Mexico is not a party to the GPA and Canada-Mexico procurement will be governed by the CPTPP.

- **Global Safeguards**
  - The higher thresholds for imposing global safeguards against other NAFTA/USMCA Parties remain.

- **Cultural Industries Exemption**
  - The substance of the exemption remains unchanged but the circumstances in which the United States (or Mexico) are entitled to take offsetting measures if Canada invokes the exemption are more expansive than under the NAFTA.

What Comes Next

The Agreement is subject to a legal scrub. As released today, and reflecting the haste with which it was concluded, it is also missing certain elements that would apply to Canada, including Canada's Tariff Schedule. Once the Agreement is signed, likely by December 1, 2018, the Parties will need to complete their domestic procedures before it can be ratified and enter into force. In particular, the Parties will need to draft, and their legislatures approve, implementing legislation. Approval by the U.S. Congress is far from certain particularly if the composition of Congress changes significantly in the November 6, 2018 mid-term elections. One can expect the Trump Administration to press the issue by threatening nevertheless to withdraw the U.S. from the NAFTA if Congress does not approve the USMCA.

In the coming days we will be publishing more detailed analysis and commentary on specific aspects of the USMCA text.

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