MEMORANDUM

To: **PRG/Bracewell Clients**

From: **Policy Resolution Group (PRG) at Bracewell LLP**

Date: **November 30, 2018**

Subject: **Update on the US-Mexico-Canada Agreement (USMCA)**

President Trump, Canadian Prime Minister Justin Trudeau, and outgoing Mexican President Pena Nieto signed the US-Mexico-Canada Agreement (USMCA) at the G-20 meeting in Buenos Aires, Argentina this morning. The USMCA is intended to replace the North American Free Trade Agreement (NAFTA) that has been in force since 1994. Today's signing is an important step towards adoption of the USMCA, but much work remains to be done by all three governments before it is fully adopted and implemented.

The agreement signed today includes aspects of the USMCA that all three countries agreed to earlier this year, with a wide range of clarifications and refinements to the original language made public in September (we continue to analyze the specific changes made in the agreement). See attached fact sheet.

Next Steps

The agreement must now be passed by the legislatures in Canada, Mexico, and the United States. And while the agreement is encountering some opposition in Canada (most notably from the dairy industry) and Mexico, the U.S. Congress is seen as ultimately holding the fate of the USMCA in its hands.

In accordance with Trade Promotion Authority (TPA or "fast track") rules governing Congressional consideration of the agreement, President Trump will benefit from a range of measures expediting the debate over the USMCA and limiting the power of Congress to filibuster, delay, or make changes to the agreement as long as he complies with a variety of procedural requirements. While a variety of reports and analyses must be completed pursuant to TPA, the most significant stages of the Congressional debate are as follows:

- Now that the President has released the final text of the signed agreement, the White House must submit to Congress a description of changes in existing U.S. law required by the agreement within 60 days. Additionally, 30 days before submitting draft implementing legislation, the President must submit the final legal text of the agreement and a draft statement of administrative action (SAA) to Congress.

- No later than 105 days after signing the agreement, the International Trade Commission (ITC) must report to Congress and the President on the impact of the agreement on the U.S. economy.

- Once Congress receives that legislative text from the White House, it will have 90 in-session days to consider the legislation before it is required to take final votes.

- The House Ways & Means Committee and the Senate Finance Committee are given jurisdiction over USMCA's implementing legislation. House Ways & Means has 45 session days to consider the bill and report it to the House floor, with the bill automatically discharged from committee if no vote is taken. The Senate Finance Committee is given 15 session days to vote on the legislation, with automatic discharge applying to that deadline as well.

- Once the bill is sent to the floors of the House and Senate, each chamber has 15 session days to take a final vote on the legislation. The legislation is not subject to amendment, and the votes are subject to a simple-majority rule, preventing a filibuster in the Senate.

Several members of Congress have tried to persuade President Trump and Congressional leadership to attempt to secure passage of the USMCA during the current "lame duck" session of Congress while Republicans have a majority in the House. However, this effort has been met with widespread skepticism, and Congressional leadership has dismissed it as an option. The practical realities of the Congressional calendar and the burdens associated with trying to satisfy TPA requirements do not appear to provide sufficient time for Congress to consider the USMCA.

The new Congress, with Democrats holding a majority in the House, will likely take up the USMCA legislation during the first few months of 2019. Congressional leadership from both parties has approached the USMCA very carefully, looking for opportunities to engage the debate in ways that appeal to specific constituencies such as the energy industry, manufacturing, and labor. However, leadership in both parties has avoided broad statements either endorsing or condemning the agreement—although there has been a consistent and bipartisan message about the importance of not undermining the efficient operation of the North American market. Walking this line will prove impossible in the coming months, however, as members of Congress are required to take firm positions on the agreement.

Some partisan lines are already beginning to emerge. For example, Senator Elizabeth Warren (D-MA) and other Democrats who are trying to appeal to labor and environmental constituencies have begun to criticize the USMCA for not doing enough on those issues. At the same time, groups of conservative members have also expressed concerns that the USMCA extends aspects of multilateralism that they find undesirable. Specific criticism has also been leveled at language in the USMCA relating to protection against discrimination on the basis of sexual identity. These critiques are likely to sharpen over coming months, potentially making it very difficult for the White House to assemble a majority in a House now controlled by Speaker Nancy Pelosi.

Given the obstacles ahead for the USMCA in the new Congress, it is possible that the White House may be drawn to (yet another) "nuclear option" involving the termination of NAFTA in an attempt to force Congress's hand in the USMCA debate. Even preliminary discussion of this "nuclear option" from official Washington would create significant political, legal, and investment uncertainty.

We will keep you updated on USMCA-related developments in the coming weeks and months.

USCMA FACT SHEET

For most stakeholders, the USCMA will represent a welcome continuation of existing tariff-free treatment for trade between the US, Canada, and Mexico. What follows are some of the major areas that the USMCA addresses, and over the course of this week we will produce more in-depth analytical pieces on the changes to investor-state dispute settlement (ISDS) and the new sunset clause.

Dispute Settlement

Dispute resolution provisions have been controversial in several respects, ranging from how to settle trade-related disputes among the states themselves, to protections for investors doing business in member countries. Chapter 19, which governs intergovernmental disputes like the imposition of anti-dumping duties, was a major issue for Canada, which succeeded in retaining many of its protections. However, in Chapter 31, the USMCA contains significant restrictions on the investor-state dispute settlement (ISDS) process established in the original NAFTA.

First and foremost, the new agreement eliminates ISDS with Canada entirely, and what remains of it with respect to Mexico has been significantly curtailed. Investors' ability to settle disputes with Mexico under USMCA is limited to specific sectors and types of contracts:

- The Agreement allows claims in three areas: legacy investments, breaches of national treatment or compensation provisions, and certain government contracts.
- The government contracts provision applies to specific sectors including oil and gas, power generation, transportation services, telecommunications, and transportation infrastructure. Protections are, however, subject to a number of conditions. Only claimants that are party to "covered government contracts" are able to engage in investor-state dispute settlement. "Covered contracts" are defined as written agreements between a *"national authority"* of a North American country and an investor. While "national authority" is defined as authority at the "central level of government" it includes persons or state enterprises exercising delegated authority. It is unclear what delegated central government authority means in practice and eventual guidance or clarification of this provision will have important consequences for investments in this sector.

Dairy

Canada agreed to eliminate its controversial "Class 6 and Class 7" dairy pricing system which adjusts the price of domestic milk ingredients used to make cheese and yogurt. It also agreed to a number of other provisions that will allow U.S. producers access to the Canadian dairy market and marginally restrict excessive Canadian exports. Negotiations on dairy were one of the main sticking points during negotiations over the weekend and the Agreement represents a key concession to the U.S.

Sunset

The USMCA contains a clause that the agreement will sunset after 16 years if it is not renewed or renegotiated. Under the Agreement the three North American partners would meet every six years to decide whether to renew or revise the pact. A vote to renew the Agreement would restart the 16-year clock, keeping the USMCA perpetually a decade and a half away from termination. This clause, however, is much less than the five year sunset initially proposed by USTR. Multiple parties have argued that the uncertainty occasioned by sunset clauses harms investment decisions and future planning. The 16-year compromise is hardly ideal especially if the discussions every six years are as tense as negotiations this year, but the longer horizon should help alleviate any broader uncertainty.

Automobile Content

The agreement contained a key USTR demand to increase the North American content requirement for automobiles receiving duty-free status. The requirement will move from 62.5% to 75% (see Chapter 4) and require that all "core parts" originate in North American countries. Additionally, the USMCA contains a provision sought by labor unions requiring that at least 40% of automobile contents be made by workers earning an average base wage of $16 per hour or more.

Tariffs

The agreement negotiated Sunday also included several side letters on tariffs. Canadian negotiators sought to address two particular issues: the section 232 steel and aluminum tariffs and potential section 232 action on automobiles. Canada requested that the Trump Administration lift steel and aluminum tariffs on the two USMCA partners as part of the agreement, something the Administration declined to do. The U.S. did agree, however, to exempt the current automobile and auto-part production capacity of Canada and Mexico from any new section 232 action. The Department of Commerce is still investigating potential harms from automobile imports and the Administration stressed that it has not yet decided to move forward with tariff action.

In a separate set of letters, the U.S. committed to exempt both Mexico and Canada from any new section 232 actions for 60 days after a measure is imposed in order to “seek to negotiate an appropriate outcome.”

The full text of the USCMA, posted on the USTR website, can be found here.