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Important New Features in the USMCA

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INTRODUCTION

As in the case of an earlier Baker Institute report[1] discussing provisions that carry over from NAFTA to the USMCA, it should not be assumed that the provisions discussed in this report are the only significant USMCA innovations. Among others are the new automotive rules or origin (second report) and the elimination of investor-state dispute settlement for United States-Canada relations and the restriction of ISDS in many matters affecting U.S. persons with claims against Mexico (third report). Several of the provisions discussed in this report could have a very significant impact on the interpretation, application, and longevity of the USMCA in the future.

I. LIMITATIONS ON CURRENCY MANIPULATION

There is more than a little irony in the fact that the first U.S. free trade agreement (FTA) chapter on currency manipulation is found in an agreement where none of the parties (except perhaps the United States) have a history of manipulating their currencies. As one observer has noted, "The United States, Mexico, and Canada already have floating exchange rate regimes and currently meet the transparency and reporting requirements under USMCA Chapter 33, so the practical impact of Chapter 33 on current policies and practices of the three countries is limited."[2] Under the circumstances, the chapter is probably more significant as a model for future trade agreements with countries where currency manipulation has been a major U.S. concern.

Given this history, it was no surprise that in the "Phase One" agreement between the United States and China concluded in January 2020, currency manipulation was extensively addressed.[3] The fact that as of August 2019 China has been formally branded as a currency manipulator (rescinded in February 2020) even though it did not meet the criteria in U.S. law,[4] further reinforces the utility of the U.S. negotiators having recently dealt with the issue in the USMCA. While one might have expected that the U.S. trade agreement with Japan would have addressed currency manipulation since Japan has been so accused in the past, that agreement is silent on the subject.[5]

The USMCA was not the United States' first effort to address exchange rate policies in a trade agreement. While the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) contains no chapter on currency manipulation, a joint declaration of the original Trans-Pacific Partnership (TPP) parties (including the United States), was released in November 2015 at the same time as the text.[6] That declaration incorporated some of the same principles now found in the USMCA, including adherence to International Monetary Fund (IMF) requirements, transparency and reporting, and macroeconomic policy consultations.[7] The declaration was to

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become effective for each party's relevant authority "immediately after entry into force for the country of that Authority."[8] However, the joint declaration appears to have disappeared when the TPP was replaced by the CPTPP.[9]

The USMCA chapter on "Macroeconomic Policies and Exchange Rate Matters" is summarized by the Office of the U.S. Trade Representative (USTR) as follows:

> *The chapter will address unfair currency practices by requiring high-standard commitments to refrain from competitive devaluations and targeting exchange rates, while significantly increasing transparency and providing mechanisms for accountability. This approach is unprecedented in the context of a trade agreement, and will help reinforce macroeconomic and exchange rate stability.*[10]

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The chapter confirms the commitment of the USMCA parties to market-determined exchange rates and adherence to IMF requirements.[11] It contains various transparency and reporting requirements, including public disclosure of data on international reserve balances and intervention in foreign exchange markets, both on a monthly basis.[12] A macroeconomic eommittee consisting of government officials of the three parties will meet at least annually to "monitor the implementation of this Chapter and its further elaboration."[13] "Expedited bilateral consultations" are available if a party believes that another party is failing to comply with policy and reporting requirements.[14] Disputes over a party's alleged failure to comply with the chapter are subject to state-to-state dispute settlement under Chapter 31.[15]

II. RESTRICTIONS ON TRADE AGREEMENTS WITH CHINA

Among the most unusual and unexpected provisions in the USMCA is effectively a ban against Mexico or Canada concluding a trade agreement with a "non-market country," e.g., China. Under the USMCA language, a non-market economy country is one which a "Party (e.g., the United States) has determined to be a non-market economy [NME]for purposes of its trade remedy laws" and "with which no Party has signed a free trade agreement."[16] Both of these limitations are significant. Although the language does not mention China, it is one of several countries (including Vietnam) that have been designated NMEs for purposes of trade remedies.[17] The second proviso is important because at the time the USMCA was signed both Mexico and Canada had signed the CPTPP (March 8, 2018), which included among its parties another NME, Vietnam.

The restrictions require that if Mexico or Canada considers such negotiations with China it must provide three months' notice to the other Parties with "as much information as possible regarding the objectives for those negotiations" and an opportunity for the other Parties to review the proposed text 30 days before signature so the reviewing Parties may "assess its potential impact on this agreement."[18] Most significantly, if a party enters into such a trade agreement with an NME, the other parties have the option to terminate the USMCA with regard to that party on six months' notice and replace it with a bilateral agreement between the remaining two parties.[19]

The NME trade agreement ban has met with criticism in both the United States and elsewhere. The Heritage Foundation argues that "A trade agreement should not prevent the Party countries from advancing efforts to liberalize with trade, especially with countries [i.e., China] which have so much to do in terms of lower trade barriers."[20] The Asia Pacific Foundation of Canada complained (with perhaps some exaggeration), "There are no two ways about it. Washington wants to limit the trade options of its allies and to isolate China. And it is just getting started."[21]

U.S. insistence on the restriction may have been triggered not only by the U.S.–China trade war that was already well under way when the USMCA was concluded September 30, 2018, but as a result of the fact that Canada and China had begun exploratory talks toward a bilateral trade agreement in September 2016. Former Mexican president Enrique Peña Nieto in September 2018 attended a meeting in China for the ninth summit of the BRICS (Brazil, Russia, India, China, and South Africa) at a time when Mexico and China were enjoying "a close and rosy relationship."[22] One necessarily wonders whether the Trump administration will seek similar restrictions in future trade agreements where the U.S. also has a significant negotiating advantage, although none is found in the United States–Japan Agreement, and such restrictions would be virtually inconceivable in any agreement that might emerge with the EU or with the United Kingdom after Brexit. One of the challenges for both Mexico and Canada will be making efforts to develop mutually beneficial economic relations with China to the extent possible without seriously alienating the United States. Given that many believe that U.S.–China economic competition and rivalries are likely to affect the world economy for decades, this provision may be only the first in which U.S. efforts to isolate China conflict with Mexican and Canadian economic objectives.

III. SUNSET PROVISIONS

The USMCA provides that "A Party may withdraw from this Agreement by providing written notice of withdrawal to the other Parties. A withdrawal shall take effect six months after a Party provides written notice to the other Parties. If a Party withdraws, this Agreement shall remain in force for the remaining Parties."[23] This is substantively identical to the parallel language in NAFTA.[24] In both cases the issue is whether a U.S. president can withdraw from NAFTA (or from the USMCA) under the U.S. Constitution without congressional approval as President Trump repeatedly threatened to do, has not been resolved.[25] There appears to be little question that under international law the president may withdraw after the relevant notice has been given and the six month period has elapsed.[26] In any event, no party to NAFTA or the USMCA could be forced to remain a party for more than six months after its decision to withdraw. Short of withdrawal the parties to most U.S. trade agreements have specifically contemplated amendments, and all have a Free Trade Commission or something similar that could be tasked with considering modifications.[27]

Under such circumstances, most trade agreements, including as far as I can determine all those that have been negotiated by the United States since its first FTA (with Israel, in 1986), have included no fixed date of termination or sunset clause.

Why then did the United States insist on a separate sunset provision, a "ticking time bomb" in the words of several observers,[28] one that would terminate the USMCA 16 years after its entry into force unless the parties confirm that they wish to extend it for another 16 years? USTR, in its principal fact sheet, did not mention the sunset clause for which it has so steadfastly fought despite Canadian and Mexican opposition.[29] Perhaps the best that can be said for the provision is that it is far less potentially damaging than the five-year sunset clause originally sought by the United States,[30] likely reflecting the Trump administration's skepticism about any international agreement that actually or potentially restricts the government's unilateral actions. The original five-year plan was, as explained by Commerce Secretary Wilbur Ross, designed to force regular, "systematic re-examination" of the revised agreement.[31]

The essential elements of the sunset clause can be summarized as follows: a) the USMCA terminates 16 years after entry into force unless each party confirms that it wants the agreement to continue

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for a further 16 years; and b) on the sixth anniversary of its entry into force, a "joint review" of the agreement must be conducted by the commission created under the USMCA, with any party able to provide "recommendations for action."[32] If c), each party confirms in writing it wishes to extend the agreement, no further action is required until the end of the next six year period.[33] However, d), if any party dissents, a further joint review is required each subsequent year, again unless and until all parties have agreed on a sixteen-year extension.[34] Even if there is an extension, e) joint reviews are required every six years thereafter.[35]

According to the implementing legislation, the president is required to consult with appropriate congressional committees and stakeholders before each joint review takes place, and to keep the committee apprised of any progress and intended actions.[36] However, Congress has no veto over any actions that are taken by the president to withdraw (or remain.)

Support for a sunset clause in an agreement as politically sensitive as NAFTA or the USMCA reflects, in my view, a stunning level of naivete and lack of basic understanding of how businesses operate. Naivete because such agreements, including any amending protocols, must be ratified by the U.S. Congress. One needs only to look at the USMCA, which was signed November 30, 2018, but could not even be submitted to Congress until almost year later, on December 13, 2019, because of the time required to reach a political agreement with Congress on changes to the agreement and to the content of the implementing legislation.[37] Does it really make sense, even if the three USMCA parties could agree on changes, to force Congress and the president to go through a ratification process every five years or so?

The concept also flies in the face of the basic fact that businesses by and large do not invest in new or expanded facilities when economic uncertainty abounds. North American business investment has been sluggish because of the uncertainty as to whether NAFTA would be terminated or replaced by the Trump administration.[38] Such uncertainty was resolved only when it became apparent that the USMCA would be approved by all three USMCA parties and enter into force by or perhaps before July 1, 2020.[39]

It is difficult to understand how even a 16-year sunset clause would eliminate the threat of another period of business uncertainty, even if it does not occur for some years. Under the best of circumstances, all three parties might confirm after the six-year joint review that they wish to extend the USMCA for another 16 years. If not, joint reviews would have to be conducted by the commission each year for the remainder of the six-year period, or until all parties agree, or until the USMCA terminates under the provision. It is difficult to imagine any policy that could result in business uncertainty on a potentially continuing basis beginning in 2026 would benefit the United States or its USMCA partners. One can make a reasonable argument that North American business investment and employment, already suffering from what promises to be a long-term trade conflict with China, will not benefit from yet another layer of economic uncertainty.

IV. INDIGENOUS PEOPLES' RIGHTS

The preamble to the USMCA, for the first time in a trade agreement concluded by the United States,[40] recognizes, inter alia, "the importance of increased engagement by indigenous peoples in trade and investment . . ."[41] More significantly, the USMCA, at Canada's insistence, includes a general exception—applicable to the entire USMCA—for obligations to indigenous peoples, protecting legal obligations of Canada or other parties to indigenous groups:

> *Provided that such measures are not used as a means of arbitrary or unjustified discrimination against persons of the other Parties or as a disguised restriction on trade in goods, services, and investment, this Agreement does not preclude a Party from adopting or maintaining a measure it deems necessary to fulfill its legal obligations to indigenous peoples.*[42]

Other chapters of the USMCA also are relevant to the interests of indigenous peoples. Specifically, indigenous handicraft goods are eligible for duty-free treatment.[43] Several USMCA chapters are designed to protect the environment and encourage corporate social responsibility and responsible business conduct as they relate to the environment, and also address matters of particular importance to indigenous groups.[44] While some have criticized the USMCA for not explicitly referring to the United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP) despite its endorsement by the USMCA parties, it is arguable that the general reference to obligations to indigenous peoples encompasses those legally binding principles.[45]

ENDNOTES

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2. Stephanie Segal, "USMCA Currency Provisions Set a New Precedent," *Center for Strategic and International Studies*, October 5, 2018, https://www.csis.org/analysis/usmca-currency-provisions-set-new-precedent.

3. Economic and Trade Agreement between the United States of America and the People's Republic of China, Ch. 5, January 15, 2020, https://ustr.gov/sites/default/files/files/agreements/phase%20one%20agreement/Economic_And_Trade_Agreement_Between_The_United_States_And_China_Text.pdf.

4. "Treasury Designates China as a Currency Manipulator," U.S. Dept. of the Treasury, August 5, 2019, https://home.treasury.gov/news/press-releases/sm751.

5. U.S.-Japan Trade Agreement, October 7, 2019, https://ustr.gov/countries-regions/japan-korea-apec/japan/us-japan-trade-agreement-negotiations/us-japan-trade-agreement-text; see Leika Kihara, "Japan May Face Trump's Heat as Currency Manipulator: ex-FX Diplomat," Reuters, https://www.reuters.com/article/us-japan-usa-trade-currency/japan-may-face-trumps-heat-as-currency-manipulator-ex-fx-diplomat-idUSKBN1H51BB.

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7. bid., secs. I, II, and III.

8. Ibid., sec. V.

9. Segal, "USMCA Currency Provisions."

10. USTR, "United States-Mexico-Canada Trade Fact Sheet: Modernizing NAFTA Into a 21st Century Trade Agreement," 2018, https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/fact-sheets/modernizing.

11. Agreement between the United States of America, the United Mexican States, and Canada (USMCA), arts. 33.4.1,33.4.2, November 30, 2018, http://bit.ly/2YSXFL9.

12. USMCA, art. 33.5.

13. USMCA, art. 33.6.

14. USMCA, art. 33.7.

15. USMCA, art. 33.8.

16. USMCA, 32.10.1.

17. See 19 U.S.C. § 1677(18)(B) (2000). Applicable factors include "(i) the extent to which the currency of the foreign country is convertible into the currency of other countries; (ii) the extent to which wage rates in the foreign country are determined by free bargaining between labor and management; (iii) the extent to which joint ventures or other investments by firms of other foreign countries are permitted in the foreign country; (iv) the extent of government ownership or control of the means of production; (v) the extent of government control over the allocation of resources and over the price and output decisions of enterprises; and (vi) such other factors as the administering authority considers appropriate."

18. USMCA, arts. 32.10.2, 32.10.3, 32.10.4.

19. USMCA, art. 32.10.5.

20. Tori K. Whiting and Gabriella Beaumont Smith, eds., "Backgrounder: An Analysis of the United States-Mexico-Canada Agreement," *Heritage Foundation*, January 28 2019, 55, https://www.heritage.org/trade/report/analysis-the-united-states-mexico-canada-agreement.

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22. bid.

23. USMCA, art. 34.6

24. North American Free Trade Agreement, U.S.-Can.-Mex. (NAFTA), Dec. 15, 1992, art. 2205, http://bit.ly/2FZ8d3z.

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26. See Vienna Convention on the Law of Treaties, May 23, 1969, arts. 54-56, https://www.oas.org/legal/english/docs/Vienna%20Convention%20Treaties.htm.

27. See, e.g., NAFTA, art. 2001 (Free Trade Commission), art. 2202 (amendments).

28. Simon Lester and Inu Manak, "New NAFTA's Sunset Clause is a Ticking Time Bomb," *Cato Institute*, November 7, 2018, https://www.cato.org/publications/commentary/new-naftas-sunset-clause-ticking-time-bomb.

29. USTR, "United States-Mexico-Canada Trade Fact Sheet."

30. Lester and Manak, "New NAFTA's Sunset Clause."

31. David Lawder, "U.S. Pushes for 'Sunset Clause' to Re-examine NAFTA Every Five Years," *Bloomberg News*, October 12, 2017, https://www.bnnbloomberg.ca/u-s-pushes-for-sunset-clause-to-re-examine-nafta-every-five-years-1.883334.

32. USMCA, arts. 34.7.1, 34.7.2.

33. USMCA, art. 34.7.3.

34. USMCA, art. 34.7.4.

35. USMCA, art. 34.7.5.

36. USMCA Implementation Act, December 13, 2019, H.R. 5430, 116th Congress, 1st Session, https://www.congress.gov/bill/116th-congress/house-bill/5430/text#toc-H7B2A937BE4154D6CAD827CE4149F1E70, sec. 611.

37. Ibid.

38. See Leah Schnurr and Andrea Hopkins, "Bank of Canada Says NAFTA Uncertainty Weighing on Investment," *Reuters*, May 16, 2018, https://www.reuters.com/article/us-canada-cenbank/bank-of-canada-says-nafta-uncertainty-weighing-on-investment-idUSKCN1IH2AV.

39. The Protocol Replacing the North American Free Trade Agreement with the Agreement Between the United States of America, the United Mexican States, and Canada, November 30, 2018 (to which the USMCA is annexed), art. 2, https://ustr.gov/sites/default/files/files/agreements/FTA/USMCA/Text/USMCA_Protocol.pdf, provides that the USMCA will enter into force on the first day of the third month following the last notification by a party of its approval of the agreement. As of January 31, 2020, Mexico and the United States had ratified the agreement, and it was expected that Canada would complete its parliamentary approval process by the end of April.

40. Similar provisions have existed since 2001 in all of New Zealand's trade agreements beginning with Singapore, including the CPTPP, for the obligations under of the New Zealand government to the Maori in the Treaty of Waitangi. See "Waitangi Tribunal Report on the Trans-Pacific Partnership Agreement" (Wai 2522, 2016), https://forms.justice.govt.nz/search/Documents/WT/wt_DOC_104833137/Report%20on%20the%20Trans-Pacific%20Partnership%20Agreement%20W.pdf.

41. USMCA, Preamble, clause 17.

42. USMCA, art. 32.5. A footnote clarifies that for Canada "the legal obligations include those recognized and affirmed by section 35 of the *Constitution Act 1982* or those set out in self-government agreements between a central or regional level of government and indigenous peoples."

43. USMCA, art. 6.2. An excellent summary of the benefits of the USMCA for indigenous groups is Kevin O'Callaghan, Emilie Bundock and Madison Grist, "USMCA Aims to Protect the Interests of Indigenous Peoples in International Trade," *Fasken Indigenous Bulletin*, October 23, 2018, https://www.fasken.com/en/knowledge/2018/10/van-usmca-aims-to-protect-the-interests-of-indigenous-peoples-in-international-trade/.

44. USMCA, ch. 24, esp. art. 24.13.

45. O'Callaghan, Bundock and Grist, "Indigenous Peoples."

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