



Government Affairs Office

Memorandum

DATE: October 5, 2018

TO: MEMA Government Affairs Committee
MEMA Trade Working Group
MEMA Rules of Origin Task Group

FROM: Ann Wilson, Senior Vice President, Government Affairs
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RE: U.S.-Mexico-Canada Agreement (USMCA)

Before midnight on September 30, 2018, Canada joined the U.S. and Mexico to form the “U.S.-Mexico-Canada Agreement” (USMCA), designed to replace the current NAFTA. MEMA issued a statement (click [here](#)). The agreement has 34 chapters and over 1,700 pages of text – all posted on the USTR’s website (click [here](#)). Below is a high-level summary of the main outcomes of interest to the vehicle industry, but the main focus is on Chapter 4 “Rules of Origin” and the Auto Sector Specific side letters on standards and on possible Sec. 232 autos/auto parts tariffs.

Timing & Process

Signing the Agreement – Now that the USTR has posted the agreement’s text for public view, the next stage is the signing of the agreement among the Parties. President Trump has long expressed a desire to sign the deal while outgoing Mexican President Peña Nieto is still in office even though there is no legal obligation for him to do so. Under the current timeline, the earliest President Trump can sign is Nov. 29; President Peña Nieto exits office Nov. 30.

Next Steps, Ratification & Entry into Force – Once the U.S. signs the agreement, the 90-day clock commences on a series of actions that must take place before the Agreement can be presented to the U.S. Congress for ratification. For instance, after the President signs it, he has up to 60 days to send Congress a description of changes to existing laws required to bring the U.S. into compliance with the new Agreement. Then, at least 30 days before submitting the implementing bill, the President sends Congress a draft statement of administrative action to implement the Agreement and a copy of the final legal text of the USMCA.

After all the procedural requirements and ratifications are complete in each respective nation, the Parties then notify each other. The USMCA would then enter into force three months after the last Party’s notification. **NOTE:** that the regional value content requirements for vehicles (passenger cars, light trucks and heavy trucks) will not go into force before Jan. 1, 2020.

Side Letters Effective Immediately Upon Signature – These pre- and post-ratification processes do not apply to the two automotive side letters between the U.S. and Mexico and the U.S. and Canada related to potential tariffs that may be imposed under Sec. 232 automobile and automotive parts. Those side letters are effective immediately upon signatures from both Parties.

Automotive Rules of Origin

The Automotive Rules of Origin (ROO) includes requirements for: Regional Value Content, Steel and Aluminum, and Labor Value Content. While the requirements are essentially the same framework and figures that MEMA staff have previously reported to members as it pertained to the U.S.-Mexico Agreement from Aug. 27, there are some noteworthy elements that are clearer now that Canada has joined the agreement and the draft text of the Agreement is public.

The USMCA maintains the NAFTA criteria for originating goods: (a) wholly obtained or produced; (b) product-specific rules of origin (tariff shift, RVC and/or specific processing requirements); (c) produced exclusively from originating materials; (d) and unassembled parts rule.¹ Additionally, the Chapter on Rules of Origin addresses the following:²

- Retains the NAFTA transaction value and net cost methods for calculating Regional Value Content;
- Preserves rules relating to intermediate materials, indirect materials, accumulation, and fungible goods;
- Increases the *de minimis* exception to 10 percent, subject to exceptions for certain products;
- Sets forth a special rule for sets classified pursuant to GRI 3 [[General Rules of Interpretation](#)], a provision allowing for a set that meets certain criteria to be classified in a single tariff number for duty purposes. Under the special origin rule, a set is originating only if each good in the set is originating and both the set and the goods meet the other applicable requirements; except that a set may be originating if the value of all non-originating goods does not exceed seven percent of the value of the set;
- Provides that the “Shipped Directly” requirement continues to apply;
- Defines “Non-Qualifying Operations” to include mere dilution, or production or pricing practice, the object of which was to circumvent the rules of origin;

Regional Value Content (RVC)³

- **Passenger Vehicles and Light Trucks** – 75% RVC
- **Parts** used on Passenger Vehicles and Light Trucks – Broken into three categories (see Chapter 4, Tables A, B and C):
 - **Core** - 75% RVC
 - **Principal** - 70% RVC
 - **Complementary** - 65% RVC
- **Heavy Trucks** – 70% RVC
- **Parts** used on Heavy Trucks – Broken into two categories (see Chapter 4, Tables D and E):
 - **Principal** - 70% RVC
 - **Complementary** - 60% RVC

¹ “We Have a Deal! USTR Publishes Text for US-Mexico-Canada Agreement Slated to Replace NAFTA” article, Arent Fox LLP newsletter, October 2018.

² *Ibid.*

³ The RVC for “other vehicles” are 62.5% RVC and 60.0% RVC – depending on the subheading (e.g. multi-person vehicles, motorhomes, entertainment motorcoaches, 3- or 4-wheeled vehicles, off-road vehicles). The list of components and materials for other vehicles are listed in Chapter 4, Tables F and G.

Transition Period Phase-In

- Passenger Vehicles and Light Trucks – 3-years⁴
- Core, Principal and Complementary Parts used on passenger vehicles or light trucks – 3 years
- Heavy Trucks – 7 years
- Principal and Complementary Parts used on heavy trucks – 7 years

Steel and Aluminum Requirement

- 70% of a vehicle producer's annual purchases of steel and aluminum would have to be of North American origin
 - Applies to vehicle manufacturers of passenger vehicles, light trucks and heavy trucks
 - **NOTE:** The Parties can “develop any additional description or other modification ... if needed, to facilitate implementation of this requirement.”
- The USMCA does not resolve or address the Sec. 232 tariffs on imported steel and aluminum from Canada and Mexico. However, the general sentiment is that the Parties will continue to talk about resolving this matter soon. Whether or not such an agreement to exempt Canada and Mexico to instead apply quotas is to be determined.

Labor Value Content

- Minimum US\$16/hour high-wage requirement
- Applies to vehicle manufacturers
- Passenger vehicles:
 - Phases-in starting Jan. 1, 2020 at 30% and increases to 40% by Jan.1, 2023
 - During the phase-in:
 - Begins with at least 15 points (in 2020) and increases to at least 25 points (2023) for high-wage material and manufacturing expenditures
 - At all years/stages, up to 10 points can come from high-wage technology expenditures and up to 5 points can come from high-wage assembly expenditures
- Light Trucks and Heavy Trucks:
 - At least 30 points for high-wage material and manufacturing expenditures
 - Up to 10 points can come from high-wage technology expenditures and up to 5 points can come from high-wage assembly expenditures
- Research and development and information technology (see Chapter 4, Footnotes 105-106)
- Assembly expenditures relate to a vehicle manufacturer demonstrating it has high capacity engine or transmission assembly (at least 100,000 units) or has advanced battery assembly (at least 25,000 units) (see Chapter 4, Footnote 107)

⁴ With some exceptions for advanced technology vehicles, which will have two more years.

- Calculating the LVC – Applies to plants/facilities in North America. Key details are in the ROO Chapter 4 in footnotes 102-104.
A vehicle producer of passenger vehicles, light trucks and heavy trucks has two ways to calculate:
“For high wage material and manufacturing expenditures, the Annual Purchase Value (APV)¹⁰² of purchased parts or materials¹⁰³ produced in a plant or facility, and any labor costs in the vehicle assembly plant or facility, that is located in North America with a production wage rate that is at least US\$16/hour¹⁰⁴ as a percentage of the net cost of the vehicle, or the total vehicle plant assembly APV, including any labor costs in the vehicle assembly plant or facility
- MEMA has received many questions on this element of the Automotive ROO and potential commercial impacts on suppliers, should the vehicle manufacturer opt to figure in parts/materials as part of their LVC. We will continue to seek implementation clarifications.

U.S.-Mexico and U.S.-Canada Side Letters re: “Cap” and Process IF Section 232 Autos/Auto Parts Tariffs Imposed

To mitigate the impact on the Parties of any potential Section 232 Tariffs on Imported Autos/AutoParts the U.S. prepared two side-letters with Canada and Mexico, respectively, to reflect their understanding on the application of potential autos/auto parts 232 actions and reflects the intended scope of the investigation (passenger vehicles and automotive parts).

Passenger vehicles (8703.21 through 8703.90), light trucks (8704.21 and 8704.31), or auto-parts (as determined in Appendix I 4B index under Chapter 4 of the USMCA)

- Canadian imports will be exempt up to a cap of 2.6 million passenger vehicles per year, all light trucks, and \$32.4 billion in auto parts per year.
(USTR 2017 baseline \$22.9 billion)
- Mexican imports will be exempt up to a cap of 2.6 million passenger vehicles per year, all light trucks, and \$108 billion in auto parts per year
(USTR 2017 baseline \$76 billion)
- These cap thresholds are well above existing trade levels
- The letters each contain review language and indicate that the Parties *“will determine how to monitor and allocate or otherwise administer quantities of passenger vehicles and auto parts eligible for this treatment”*

There are also a second set of side letters with each Party that provides for a 60-day “cooling off” period before any Section 232 actions on autos/auto parts will apply to imports. During that time, the Parties can *“seek to negotiate an appropriate outcome based on industry dynamics and historical trading patterns.”* It also provides that the impacted Parties have the right to take trade retaliation if the U.S. takes a Section 232 action “inconsistent with” the NAFTA, the USMCA or the WTO Agreement.

Remanufactured Goods

The USMCA includes a modern update on remanufactured goods, essentially aligns with what had been developed during the TPP negotiations. The part/good must meet the definition and be substantively and sufficiently transformed in order to confer originating. Originating remanufactured goods are duty-free under the USMCA.

Under Chapter 1, under Definitions:

Remanufactured good means a good classified in HS Chapters 84 through 90 or under heading 94.02 except goods classified under HS headings 84.18, 85.09, 85.10, and 85.16, 87.03 or subheadings 8414.51, 8450.11, 8450.12, 8508.11, and 8517.11, that is entirely or partially composed of recovered materials and: (a) has a similar life expectancy and performs the same as or similar to such a good when new; and (b) has a factory warranty similar to that applicable to such a good when new.

Under the Chapter on National Treatment and Market Access:

Article 2.11: Remanufactured Goods

1. For greater certainty, paragraph 1 of Article 2.10 (Import and Export Restrictions) applies to prohibitions and restrictions on remanufactured goods.
2. Subject to its obligations under this Agreement and the WTO Agreement, a Party may require that remanufactured goods: (a) be identified as such, including through labelling, for distribution or sale in its territory, and (b) meet all applicable technical requirements that apply to equivalent goods in new condition.
3. If a Party adopts or maintains prohibitions or restrictions on used goods, it shall not apply those measures to remanufactured goods.

Under the Chapter on Rules of Origin Chapter

Article 4.4: Treatment of Recovered Materials Used in the Production of a Remanufactured Good

1. Each Party shall provide that a recovered material derived in the territory of one or more of the Parties is treated as originating when it is used in the production of, and incorporated into, a remanufactured good.
2. For greater certainty: (a) a remanufactured good is originating only if it satisfies the applicable requirements of Article 4.2 (Originating Goods); and (b) a recovered material that is not used or incorporated in the production of a remanufactured good is originating only if it satisfies the applicable requirements of Article 4.2 (Originating Goods)

Chapter 20 - Intellectual Property

The Intellectual Property (IP) chapter provides protection and enforcement of IP rights relating to copyrights, trademarks and patents. Notably, the Agreement includes key enforcement provisions, including ex officio authority for law enforcement officials to stop suspected counterfeit or pirated goods at every phase of entering, exiting, and transiting through the territory of any Party.⁵

With regard to protection of trade secrets, the IP chapter of the USMCA includes various protections against misappropriation of trade secrets, including by state-owned enterprises. Such protections

⁵ "We Have a Deal! USTR Publishes Text for US-Mexico-Canada Agreement Slated to Replace NAFTA" article, Arent Fox LLP newsletter, October 2018.

include civil procedures and remedies, criminal procedures and penalties, prohibitions against impeding licensing of trade secrets, judicial procedures to prevent disclosure of trade secrets during the litigation process, and penalties for government officials for the unauthorized disclosure of trade secrets.⁶

General (claims, certificate, fees)

Certificate of Origin – A formal Certificate of Origin will no longer be required under the USMCA. Instead, the preferential claim can be made in any form, including on the commercial invoice or other transaction document. The agreement lists the required data elements for certification, regardless of what form that certification takes. In addition, USMCA origin claims can now be certified by the importer of record, a requirement previously reserved for the exporter.

Support for Claim – The importer must have all required support to certify a USMCA claim at the time of entry.

De Minimis – Increase in the value of non-originating goods that may be used under the de minimis provision from 7% to 10%.

Fees – The USMCA will continue to allow for an exemption of merchandise Processing Fees for qualifying products upon making a valid duty preference claim.

Post Entry Claims – Duty preference claims under the USMCA can still be made up to one year after the entry date.

Verifications – Under the proposed USMCA, verifications for duty preference qualification will still be authorized, allowing the customs authorities of one country to review the producer or exporter records in another country, and will now also provide for audits of the importer who made the duty preference claim.

Trade Enforcement and Dispute Settlement – The USMCA preserves the Chapter 19 trade dispute settlement mechanism, a concession Canada fervently demanded leading up to finalization. New provisions were added that allow for closer cooperation between the signatories in the enforcement of antidumping and countervailing duty orders, with a focus on transshipment and evasion.

Prohibition on Deals with Non-Market Economies – In an apparent attempt to curb free-trade negotiations with China and other non-market economies, the USMCA contains language limiting the negotiations of another member. Three months before starting negotiations with a non-market country, the other USMCA partners must be officially informed, and "as much information as possible" must be provided about the objectives of the negotiation. Before signing a new agreement, the other parties in the USMCA must be given an opportunity to review it and assess its impact on them, and to decide whether amendments are required to address concerns. Failure to do so would terminate the North American deal.

The Sunset Clause

- After 16 years the USMCA will terminate unless the Parties wish to renew for another 16-year term.

⁶ Ibid.

- However, prior to that point, the Parties will conduct a “joint review” of the “operation of the Agreement” every 6 years.
 - each Party must confirm, in writing, their desire to extend the Agreement
 - if Parties do not agree to extend during any “joint review” then annual reviews will take place for the remainder of the term of the Agreement or until the Parties agree to extend for another 16-year period, at which point the 6-year “joint review” cycle will be reinstated.