

Amendments to the USMCA Spotlight Labor Standards Compliance in Mexico

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With the signing of a Protocol of Amendments (“PoA”) and the approval by the U.S. House of implementing legislation, the United States, Canada and Mexico are on track for final approval of the US-Canada-Mexico Agreement (the “USMCA”) by the middle of February 2020, which is the anticipated time frame for the vote by the U.S. Senate. If that proceeds as expected, the USMCA would take effect 90 days later, before the end of May. Certainly, a sigh of relief has been heard throughout the continent, as the new agreement has been reached without the original NAFTA having been discarded and avoiding the interruption of supply lines and cross-border trade. Instead, the parties have succeeded in modernizing much of NAFTA while still incorporating rules that may help achieve the Trump Administration’s stated goal of providing a boost to U.S. domestic manufacturing.

As noted in our [earlier reports](#), the USMCA modernizes and expands NAFTA, covering several aspects of trade, a few of the more significant of which are:

National Treatment and Market Access for Goods

- Keeps the benefits of tariff-free imports for a large portion of trade.
- Incorporates the 1994 General Agreement on Tariffs and Trade unless otherwise provided in the USMCA.
- Provides a framework for faster and more transparent administrative processes to enable the delivery of goods in customs throughout the North American region.
- Simplifies procedures for certifying the origin of qualifying goods and greatly expands the types of documents that can be used for such certifications.
- Increases cooperation and transparency regarding the creation of regulatory barriers and evaluation of conformity procedures for certain products so as to facilitate trade among the Parties and thus prevent or avoid unnecessary barriers to trade.

Agriculture

- Preserves existing commitments among Canada, Mexico and the United States.
- Increases U.S. access to the Canadian market for dairy (in particular for non-fat milk solids), chicken and eggs.
- Increases Canadian access to the U.S. market for sugar and products containing sugar.

Automotive Vehicles and Component Parts

- North American Content will increase from 62.5 percent to 75 percent by 2023 to qualify for duty-free treatment under USMCA.
- 40 percent (in the case of cars) and 45 percent (in the case of trucks) of the vehicle is to be manufactured by workers earning on average at least \$16 per hour.

- 70 percent of the steel and aluminum used in vehicle production must be originated in North America to comply with the rule of origin.

Investment

- Sets minimum standards for protection of investments.
- Maintains Investor-State Dispute Settlement (“ISDS”) for some types of government actions (violations of most-favored nation obligations and direct expropriations) involving U.S. investments in Mexico, and vice versa. The USMCA requires, however, that investors initiate and continue (for a minimum of 30 months) proceedings in local courts before resorting to USMCA arbitration. There is an exception to this requirement for disputes over government contracts involving oil and gas, power, infrastructure and telecommunications, in which in limited circumstances direct resort to arbitration is permitted.
- Disputes between Mexico and Canada will be governed by the ISDS provisions of the Trans Pacific Partnership, to which both are signatories.
- There is no ISDS provision for disputes between the United States and Canada.

Digital Trade

- Generally prohibits application of customs duties and other discriminatory measures to digital products distributed electronically (music, videos, software, etc.).
- Prohibits a Party from requiring the disclosure of proprietary computer source code and algorithms by a person of another Party as a condition for doing business in its territory.
- Limits the civil liability of providers of Internet platforms for third-Party content.
- Bars requirement for data localization.

Intellectual Property

- Sets standards for trademarks, country names, geographical indications, patents, industrial designs, copyright and related rights, and trade secrets.
- Establishes a new tri-partite Committee on IP Rights that will consider such issues as enhancements of IP rights protections, strengthening border measures and approaches for reducing infringement.
- Ensure that Parties are compensated by patent term adjustment for an unnecessary or unreasonable delay in the processing of a patent application. (A provision in the USMCA, however, providing 10-year protection for data used in approving biologic pharmaceuticals was dropped in the PoA as part of the Administration effort to garner support for the agreement from Democrats who see such protections as contributing to excessive drug prices.)
- Requires criminal penalties for at least 14 different acts of infringement, such as circumventing technological protection measures, tampering with rights management information, and performing unauthorized decoding of an encrypted program-carrying satellite signal.

Labor

- Incorporates several widely-recognized International Labor Organization (“ILO”) rights, such as freedom of association, collective bargaining and elimination of discrimination with respect to employment and occupation.
- Requires acceptable conditions of work with respect to minimum wages, hours of work, and occupational safety and health.

- Mandates access to fair, equitable, and transparent administrative and judicial proceedings to ensure that labor standards and rights are more strictly enforced. (In September 2018, Mexico ratified ILO Convention No. 98 regarding the protection of workers' right against any acts of anti-union discrimination and collective negotiation, thereby granting workers full power and freedom to elect whether to belong to a union.)
- Mexico agreed, and subsequently took, specific legislative actions to strengthen collective bargaining, including the right of workers to engage in concerted activities for collective bargaining or protection and to organize, form, and join the union of their choice. Mexico has also adopted legislation that will (i) prohibit employer domination or interference in union activities, and (ii) require verification that collective bargaining agreements meet the legal standard of workers support in order for them to be registered and have legal effect. In addition, collective bargaining agreements will be publicly available through the Mexico's General Law on Transparency and Access to Public Information.

Environment

- Incorporates commitments to address global environmental challenges such as ozone-depleting substances and marine pollution, illegal fishing and the depletion of fish stocks, illegal wildlife trade, species at risk, and conservation of biological diversity.
- Contains commitments to prevent and reduce marine litter, promote sustainable forestry management, and to consider intentional transnational trafficking of protected wild species as a serious crime.
- Acknowledges that it is inappropriate to encourage trade or investment by weakening or reducing the protections afforded in national environmental laws.
- To ensure effective enforcement (the absence of which was a marked deficiency of the NAFTA side agreement on environment), any person of a Party may file with the Secretariat of the Commission for Environmental Cooperation a submission asserting that a Party is failing to effectively enforce its environmental laws.

Sunset

- Includes an initial 16-year term.
- After six years, however, the Parties are required to review the agreement and can, at that time, push out the expiration to a date sixteen years later, with reviews on the same terms every six years, or they can agree to meet annually, with the possibility of later agreeing on an expiration date sixteen years in the future.
- Any Party may withdraw with six months prior notice.

Critics of NAFTA, including President Trump, contend that it contributed to the decline in U.S. manufacturing, particularly in midwestern states, by making possible the flight of manufacturing industries to destinations south of the border. The most important Administration objective economically – and certainly politically – in the new USMCA has therefore been to stem that flow and provide incentives for the reinvigoration of manufacturing – including manufacturing employment – in the United States. That is why, even with the many elements of the USMCA that will stimulate and streamline trade, most interest has been focused on the new rules governing the production of automobiles and auto parts.

Automobiles are the quintessential manufactured product, and the related supply chain is crucial to maintaining a strong manufacturing base. As noted above, under the USMCA, to move their products across the U.S. border free of the passenger car tariff of 2.5 percent auto manufacturers will have to achieve higher North American content than under NAFTA (increasing over time from

62.5 percent to 75 percent), pay wages of at least \$16 per hour on a share of approximately 40 percent of their production and use at least 70 percent aluminum and steel of North American origin. Moreover, within seven years that steel will have to be melted and poured, not just rolled from slabs, in North America.

Notwithstanding these provisions, after the USMCA was announced late in 2018, Democrats in the U.S. Congress expressed concern that, absent strict enforcement of Mexico's promises to respect the ILO commitments made by Mexico and improve the rights and conditions of its workers, these increased regional content rules would not be sufficient to stem the flow of industry moving out of the United States to Mexico. After all, according to critics, if workers in Mexico can be paid so little that the savings to auto producers exceed the standard 2.5 percent tariff on completed cars, it might still make sense for a manufacturer to disregard the complex USMCA rules of origin and instead move production in its entirety to Mexico.

To make this less likely, Democrats in the U.S. Congress pressed the Administration and the government of Mexico to take steps to assure enforcement of the labor standards negotiated in the USMCA. Both the Trump Administration and Mexico agreed, and thus, the PoA contains a detailed "Rapid Response Labor Mechanism" that addresses these concerns.

The Rapid Response Labor Mechanism, which is structured as an Annex to USMCA Chapter 31 on Dispute Resolution, provides, upon an allegation that Mexican workers' rights to free association or collective bargaining are being hindered, for consultations among the concerned parties, and if they cannot resolve the issue promptly, for "Labor Panelists" to be dispatched to investigate and file a report, all within specified tight time limits. Upon a finding of a violation, trade remedies can be imposed, including loss of USMCA duty-free status for goods produced at the facility, or in the event of multiple violations, being barred from entry into the United States.

The PoA requires that a Party have "a good faith basis to believe that a Denial of Rights is occurring at a Covered Facility" before invoking its rights to remediation. There is no direct private right of action under Chapter 31. Instead, the PoA contemplates that a Party will have established "a process for determining whether to invoke" the Rapid Response Labor Mechanism and "shall notify the other Party within five business days of initiating such process." The United States notes in the PoA that it "intends to establish such a domestic process under which the United States government will strive to complete initial reviews of complaints received by the government about a "Covered Facility" in the other Party in 30 days." Presumably regulations will be issued specifying how and on what basis a private U.S. party can file a complaint.

To help enforce these elements of the PoA, the U.S. implementing legislation provides for the assignment of five U.S. labor attachés to the U.S. diplomatic mission to Mexico. Mexican officials have voiced objection to the assignment of U.S. monitors on Mexican soil as a breach of its sovereignty and as being outside of their amended agreement with the United States. They note that the agreement provides for three-person panels to resolve labor and other disputes. These panels would comprise a person chosen by the United States, one by Mexico and a third-country person agreed upon by both countries.

For companies with operations in Mexico, be they Mexican or U.S. owned, the labor enforcement mechanisms and potential penalties set forth in the PoA make it clear that to avoid being caught up in any disputes it will be crucial for labor and human resources policies to meet the standards negotiated in the USMCA. Haynes Boone, with its significant presence and experience in Mexico, has already been working with clients in the implementation of the new labor reforms regarding

collective bargaining agreements in Mexico. We will continue to monitor developing standards, practices and issues in this and other areas of USMCA implementation and enforcement.

Overall, although there are some concepts that are more restrictive than under the original NAFTA, the ratification of the USMCA represents a step forward for the cross-border trade among the three countries and eliminates a possible drag on future growth for Mexico by mitigating investor uncertainty. It also helps achieve some much desired societal consensus in the United States on the importance of trade with our North American trading partners (particularly Mexico), while placing more emphasis on worker rights. However, it is clear that foreign investors in Mexico will likely have to devote more effort and planning on human relations and labor issues going forward as Mexico implements new labor rules.