

International Trade and Customs Practice Group Newsletter



Treaty between the United States, Mexico, and Canada (USMCA)

What to expect and how to be prepared upon its entry into force in a few days?

After more than twenty-five years in force, on July 1st, 2020, the North American Free Trade Agreement (NAFTA) will cease to exist, to welcome the USMCA, which is adjusted to current reality, incorporating significant changes for all foreign trade in a globalized world.

Among several specific important topics, we begin with USMCA's Chapter 4 related to the Rules of Origin. It sets out the criteria under which merchandise would be considered originated within USMCA's region, as well as the incorporation of new Articles to said Chapter and the modernization of some Articles within NAFTA. We will continue with relevant changes to Specific Rules of Origin, especially those related to the automotive industry, and USMCA's new certification of origin procedure that replaces the NAFTA certificate of origin; and conclude by discussing generally the Labor Rapid Response Mechanism.

The USMCA comprises 34 Chapters (12 more than NAFTA), within which the following **new Articles** in Chapter 4 stand out:

New Articles

- » Wholly obtained or produced goods
- » Treatment of recovered materials used in the production of a remanufactured good
- » Value of materials used in production
- » Further adjustments to the value of materials
- » Sets of goods, kits or composite goods

Within these new Articles, the one related to **"Treatment of recovered materials used in the production of a remanufactured good"**, through which new business models based on recycling are recognized,

stands out. In order to facilitate business opportunities in an environmentally friendly industry, a provision is incorporated specifically for remanufactured goods for the purpose of recognizing the originating status of materials, parts or components that were recovered and subject to disassembly for its subsequent remanufacture.¹

Another Article that stands out is related to **"Sets of goods, kits or composite goods"**, since presenting goods in sets or in a composite manner has become an increasingly common marketing strategy. This Article establishes that, in sets or composite goods with non-originating goods, such should not exceed 10% of the value of such set or composite in order to qualify as originated in the USMCA region.

In addition, Chapter 4 includes some **modifications to certain Articles**, as follows:

Modernized Articles

Definitions

NAFTA contemplates a definitions in Article 415, which is the last Article of Chapter IV. With USMCA, the definitions section is incorporated in the first Article of Chapter 4 instead, plus new definitions.

Originating goods

Change in wording. **The Article was updated regarding wholly obtained goods, in order to expressly and clearly recognize that fish obtained from aquaculture in the region are considered originating.**

Regional Value Content

Changes in structure and division to create separately Articles 4.6 "value of materials used in production", 4.7 "additional adjustments to the value of materials", 4.8 "intermediate materials", 4.9 "indirect materials".

Intermediate materials

Comprised in numerals 10 and 11 Art. 402 NAFTA, now such are located in Article 4.8 of USMCA.

Indirect materials

Minor adjustments in wording within Article and definitions chapter.

Automotive goods

Suffered major changes, substantially modified and included in Annex 4-B of USMCA's Chapter 4, which comprises products Specific Rules of Origin. Such relevant changes are explained further on.

Accumulation

Allows recognizing as originating both the materials of the signatory countries and the processes carried out in any of its territories. This strengthens regional value chains.

De Minimis

Increases to 10%

Consumable goods

An obligation to use an inventory management method is included for the entire tax year.

Accessories, spare parts, tools and materials for instruction or of other information

Change in wording and structure but the essence remains the same, being that such goods must be invoiced together with merchandise, and their type, quantity and value must be the same as usual for such merchandise.

Packaging materials and retail containers

Change of structure and wording but it keeps the essence, in the understanding that when they are classified with the good, they will not be taken into account to determine the tariff jump of non-originals and in the case of RVC, they will be taken into account for the calculation.

Packaging materials and shipment containers

Change in wording but remains the same, not being part of the Rule of Specific Origin determination and RVC calculation.

Transit and Transshipment

Wording change, previously only "transit" was contemplated. It is included in the text of the Treaty that goods are transported outside the territories of the parties, must remain under customs control and not be subject to processes other than storage, labeling, etc.

Non-origin operations

Remains the same, simple dilution with water or another substance that does not materially change the characteristics, as well as enough evidence of evasion of Chapter 4.

¹ Remanufacturing is an important and growing sector in the United States, which is the largest consumer of remanufactured products.

Among the modified articles, the one relating to the **updating of the De Minimis provision in order to increase the percentage from 7 to 10% of the value of all non-originating materials** used in the production of the merchandise that do not meet the requirement of tariff shift, a percentage that corresponds to that established with the rest of Mexico's commercial partners, stands out. There are some exceptions established in Annex 4-A of Chapter 4.

Finally, within the modified Articles, **important changes to automotive goods stand out** with an increase of the Regional Value Content for vehicles progressively or gradually from current 62.5% to 75%, which are incorporated into Annex 4-B of Chapter 4 at hand that contains Specific Rules of Origin of products. Concretely, the modifications consist in the following:

VEHICLES AND LIGHT TRUCKS

- 1. Regional Value Content (RVC)** 75%
- 2. Labor Value Content (LVC)** 40% (light vehicles) 45% (light trucks)
- 3. Essential Auto Parts** original
- 4. Originating Steel and Aluminium** 70%

HEAVY TRUCKS

- 1. Regional Value Content (RVC)** 70%
- 2. Labor Value Content (LVC)** 45%
- 3. Originating Steel and Aluminium** 70%

Regarding the above, it should be noted that the 'essential auto parts' which must be originating include the (a) engine, (b) transmission, (c) chassis and body, (d) suspension system, (e) steering system, (f) axles and (g) batteries.

It should be noted that the Treaty provides for a periodic and gradual implementation of these requirements, specifying that the final percentages should be reached after a period of three years of USMCA's entry into force, according to the following schedule:

Schedule, transition periods for vehicles and light trucks				
ELEMENT	ENTRY INTO FORCE	1 YEAR LATER	2 YEARS LATER	3 YEARS ONWARDS
Regional Value Content	66%	69%	72%	75%
Labor Value Content	30%	33%	36%	40%
Essential Auto Parts	66%	69%	72%	75%

Due to the complexity of compliance with the Specific Rule of Origin for the automotive industry in terms of the new percentages specified above, the Ministry of the Economy published on April 30th, 2020, the Agreement through which it requires North American producers of passenger vehicles or light trucks to file applications **no later than July 1st, 2020**, to use an Alternative Transitional Regime (ATR) established in the Appendix to Annex 4-B of Chapter 4 of the USMCA, unlike in the standard transition regime contemplated in the Automotive Appendix of the USMCA, which does not replace any other Rule of Origin.

Under the ATR, passenger vehicles and light trucks will be able to comply with the 75% Regional Value Content after 5 years, reaching that percentage through an alternative transition regime, instead of applying the percentages provided in the Specific Rules of Origin set forth in the USMCA, in addition to being exempted from the requirement of having original essential auto parts as stated above.

In addition, the ATR in question establishes the possibility of covering the origin of 70% of steel and aluminum purchases through contracts or memoranda with suppliers, without the need to carry out the specific certification methods established in the USMCA.

Finally, one of the advantages provided by the ATR is having a Labor Value Content of 25% over a period of 5 years, instead of the standard regime provided by the USMCA which will progressively reach the Labor Value Content of 40% or 45%.

It should be noted that the ART may also be applicable to producers of heavy trucks under particular

premises and standards, and this will be granted provided that the relevant application is submitted before the corresponding authorities no later than July 1st, 2020, and a number of pre-established requirements are met.

It is very important to mention that the automotive industry was not the only one to undergo changes to the Specific Rules of Origin, so prior to the certification of origin of other USMCA goods, we strongly recommend conducting an analysis and review of compliance with the applicable Rules of Origin. For further reference, below are some Specific Rules of Origin that were modified in the USMCA:

Intensive Steel Products

Original Steel
Alternative RVC rules
70% original weight
Transition periods

Electrical Manufacturing

RVC % reduction
Flexibility Tariff jumps

Optical Fiber

RVC % reduction
Tariff shift flexibility

Glass Manufacturing

Originating glass

Automotive

RVC % gradual increase 62.5% to 75%
Labor Value Content
Auto parts: essential, principal, complementary

Chemicals

New alternative rules for chemical processes (chemical reactions)

TVs and Projectors

Simplification

Arabic Rubber

Pulverization confers origin

Titanium Products

Originating Titanium
Alternative RVC rules

In addition to these most relevant modifications in the USMCA regarding Rules of Origin and Specific Rules of Origin, it also contemplates a **new certification scheme** that replaces the NAFTA certificate of origin.

In addition, under the new certification scheme, importers will now be allowed to carry out the corresponding certification, since under NAFTA only producers and exporters were entitled to issue the corresponding certificates of origin. **In the case of Mexico**, it is important to note that upon the entry into force of the USMCA, **importers will not be able to issue such certification and it is expected that they will be able to do so within three years and six months after the USMCA's entry into force.**

Significantly, as of July 1st of 2020, the NAFTA certificate of origin format will be eliminated, and instead, the new certification scheme will have to be implemented in accordance with the USMCA, which need not follow a prescribed format and may be provided on an invoice or any other document, as long as it contains a set of minimum data elements as set out in Annex 5-A of Chapter 5:

1. Importer, Exporter, or Producer Certification of Origin.
2. Certifier's name, title, address (including country), telephone number, and email address.
3. Exporter's name, address (including country), e-mail address, and telephone number if different from the certifier. This information is not required if the producer is completing the certification of origin and does not know the identity of the exporter. The address of the exporter shall be the place of export of the good in a Party's territory.
4. Producer's name, address (including country), e-mail address, and telephone number, if different from the certifier or exporter or, if there are multiple producers, state "Various" or provide a list of producers. A person that wishes for this information to remain confidential may state, "Available upon request by the importing authorities". The address of a producer will be the place of production of the good in a Party's territory.
5. If known, the importer's name, address, e-mail address, and telephone number. The address of the importer shall be in a Party's territory.
6. Description of the good and the HS tariff classification of the goods to the 6-digit level. The description should be sufficient to relate it to the good covered by the certification. If the certification of origin

covers a single shipment of a product, indicate, if known, the invoice number related to the exportation

7. Origin criteria.

8. Indicate whether the certification covers multiple shipments of identical goods for a specified period of up to 12 months.

9. Authorized Signature and Date.

The certification must be signed and dated by the certifier and accompanied by the following statement:

"I certify that the goods described in this document qualify as originating and the information contained in this document is true and accurate. I assume responsibility for proving such representations and agree to maintain and present upon request or to make available during a verification visit, documentation necessary to support this certification."

It should be noted that the USMCA gives continuity to NAFTA provisions in relation to the obligation to keep the information and documentation supporting the origin of the products that are produced and exported from the territory of one of the Parties to another Party:

1. The **exporter or a producer** in its territory that completes a certification of origin or a producer that provides a written representation shall maintain in its territory for **five years after the date on which the certification of origin was completed**, or for such longer period as the Party may specify, all records necessary to demonstrate that a good for which the exporter or producer provided a certification of origin or other written representation is originating;
2. An **importer** claiming preferential tariff treatment for a good imported into its territory shall maintain, **for a period of no less than five years from the date of importation of the good**, all records necessary to demonstrate that the product is originating, if the claim was based on a certification of origin completed by the importer.

In relation to the above, the USMCA establishes that importers, exporters or producers may choose to keep the records or documentation on which the corresponding certification of origin was based, by any means including electronic form, provided that such records or documentation can be retrieved and printed promptly.

However, it should be noted that, in accordance with what is currently established in NAFTA, the USMCA provides that the customs authority of the importer country may verify the veracity of the certification, through questionnaires or visits to the facilities of the exporter or producer, and if it is found that the product did not comply with the rule of origin, the appropriate sanctions will be imposed.

In this regard, the issue of verification of origin becomes extremely important **when it comes to goods from the textile sector**, in which case, and considering the complexity involved in certifying the origin of this type of goods, the USMCA has established that the customs authorities of the importer country can verify the origin of these goods by conducting physical or in situ inspections in the exporter's country, following the rules of a specialized and stricter procedure, as set out in Chapter 6 of the USMCA.

Thus, based on the above, we can conclude that as it currently occurs with NAFTA, it is of great importance that importers, producers or exporters keep the documentation, information and records based on which a certificate of origin has been issued.

Otherwise, as is currently the case, if it is determined that the goods do not qualify as USMCA originated, the immediate consequence will be the denial of the application of preferential duty treatment and a tax assessment against the importer, consisting in the omitted import duties duly updated upon inflation, with surcharges and applicable penalties.

It is worth mentioning that on June 3rd, 2020 (almost a month before the USMCA enters into force), in accordance with Article 5.16 of the USMCA, **the Ministry of the Economy published only for informative purposes the draft of the Uniform Regulations (URs) in the USMCA, which at this stage are only available in English and subject to legal review and translation into Spanish and French.**

It is important to note that these URs are related to the procedures and steps to be followed in order to fully comply with Chapters 4, 5, 6 and 7 of the USMCA, among others (being of crucial importance for several sectors that will be affected by the USMCA entry into force, such as the automotive sector referred above).

In this regard, we believe it is important to point out that such UR become of great importance in the application and implementation of the USMCA as they abound and clearly establish different issues related to the proper interpretation and application of the Rules of Origin comprised in the USMCA. We anticipate that the USMCA Uniform Regulations will be very similar to NAFTA's, as the Rules of Origin and their criteria will only vary slightly in general terms.

It is worth noting that the UR official publication through the Federal Official Gazette is still pending. We expect such will be published on July 1st, 2020, which is the same day that the USMCA will enter into force, as indicated by the Ministry of Economy.

In accordance with the liberalization of trade at the moment of NAFTA's negotiation, Article 303 was established in the same, comprising import duties drawback and duty deferral on exported products.

Regarding this point, it should be noted that in the USMCA the Parties intended to keep this provision in the same terms established under the NAFTA, although the USMCA incorporates several provisions and regulations for the application of the drawback and duty deferral, according to the type of products exported, their use, and treatment they receive.

Finally, based on the USMCA amending protocol of December 10th, 2019, new labor provisions applicable only to Mexico and the United States were included in Chapter 23 and Annex 23-A, **specifically related to representation in collective labor agreements, which force Mexico to implement certain amendments to its Federal Labor Law.**

In addition, the three parties have established a **Labor Rapid Response Mechanism** for the resolution of disputes in case of violations of the rights included in the referred Chapter, such as the right to free association and collective bargaining and selection of unions.

If panels established under this mechanism consider that Mexico is not complying with its labor obligations under the USMCA and its domestic labor laws, this could result in the imposition of remedies and sanctions that include **prohibiting the entry of goods into the U.S.** that were manufactured in those facilities in violation in Mexico.

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