

The Latest on the New NAFTA and Trump's Continuing Tariff Threats: Perspectives from the United States, Mexico and Canada / Doing Business in Mexico

Tuesday, June 4, 2019



Table of Contents

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Agenda	Page 1
Panel 1 : The Latest on the New NAFTA and Trump’s Continuing Tariff Threats: Perspectives from the United States, Mexico and Canada / Doing Business in Mexico	Page 4
U.S.: Nicolas Guzman, Associate, International Trade – Drinker Biddle & Reath LLP	Page 5
Mexico: Jose Alberto Campos Vargas, International Trade and Alfredo Kupfer Domínguez, Labour, Partners – Sánchez Devanny	Page 9
Canada: Carmen Francis, Senior Associate, International Trade and Investment Law Group – McCarthy Tétrault LLP	Page 14
Panel 2: Doing Business in Mexico	Page 24
Francisco Andrés Gámez Garza, Partner, Corporate and M&A, Alfonso López-Lajud, Partner, Energy and Litigation and Abel Francisco Mejía-Cosenza, Partner, Tax – Sánchez Devanny	Page 25

Agenda

The Latest on the New NAFTA: Perspectives from the United States, Mexico and Canada / Doing Business in Mexico

Tuesday, June 4, 2019

TIME (EST)	TOPIC	PRESENTERS
7:30 a.m. – 8:00 a.m.	Registration and Breakfast	
8:00 a.m. – 8:05 a.m.	Opening Remarks	John Boscariorl
8:05 a.m. – 8:35 a.m.	The Latest on the New NAFTA and Trump's Continuing Tariff Threats: Perspectives from the United States, Mexico and Canada / Doing Business in Mexico	Nicolas Guzman, Jose Alberto Campos Vargas, Alfredo Kupfer, Carmen Francis
8:35 a.m. – 8:45 a.m.	Q&A Session	Etienne Ravilet Guzman
8:45 a.m. – 9:15 a.m.	Doing Business in Mexico	Francisco Andrés Gámez, Alfonso López-Lajud, Garza, Abel Francisco Mejía-Cosenza
9:15 a.m. – 9:25 a.m.	Q&A Session	Etienne Ravilet Guzman
9:25 a.m. – 9:30 a.m.	Closing Remarks	John Boscariorl

Panel 1 - The Latest on the New NAFTA and Trump's Continuing Tariff Threats: Perspectives from the United States, Mexico and Canada

**U.S.: Nicolas Guzman, Associate,
International Trade – Drinker Biddle &
Reath LLP**

USMCA – Current Status

- Administration submitted last week a draft statement of administrative action on the USMCA, starting the 30-day clock allowing for the submission of final implementing legislation to Congress.
- Congressional representatives and staff in Mexico this week meeting on labor standards.
- Congressional vote needed to ratify the agreement, which will then make way for implementing legislation.
- Democratic majority in the House of Representatives has been vocal in opposition without:
 - Mexico satisfying heightened labor requirements
 - Changes allowing for lower prescription drug costs
 - Heightened environmental standards
- TPA limits changes to the text of the agreement by allowing Congress only an up or down vote on the agreement.
- Democrats could delay a vote on ratification, but President Trump can announce withdrawal from NAFTA starting 6-month clock.

Complicating Factors

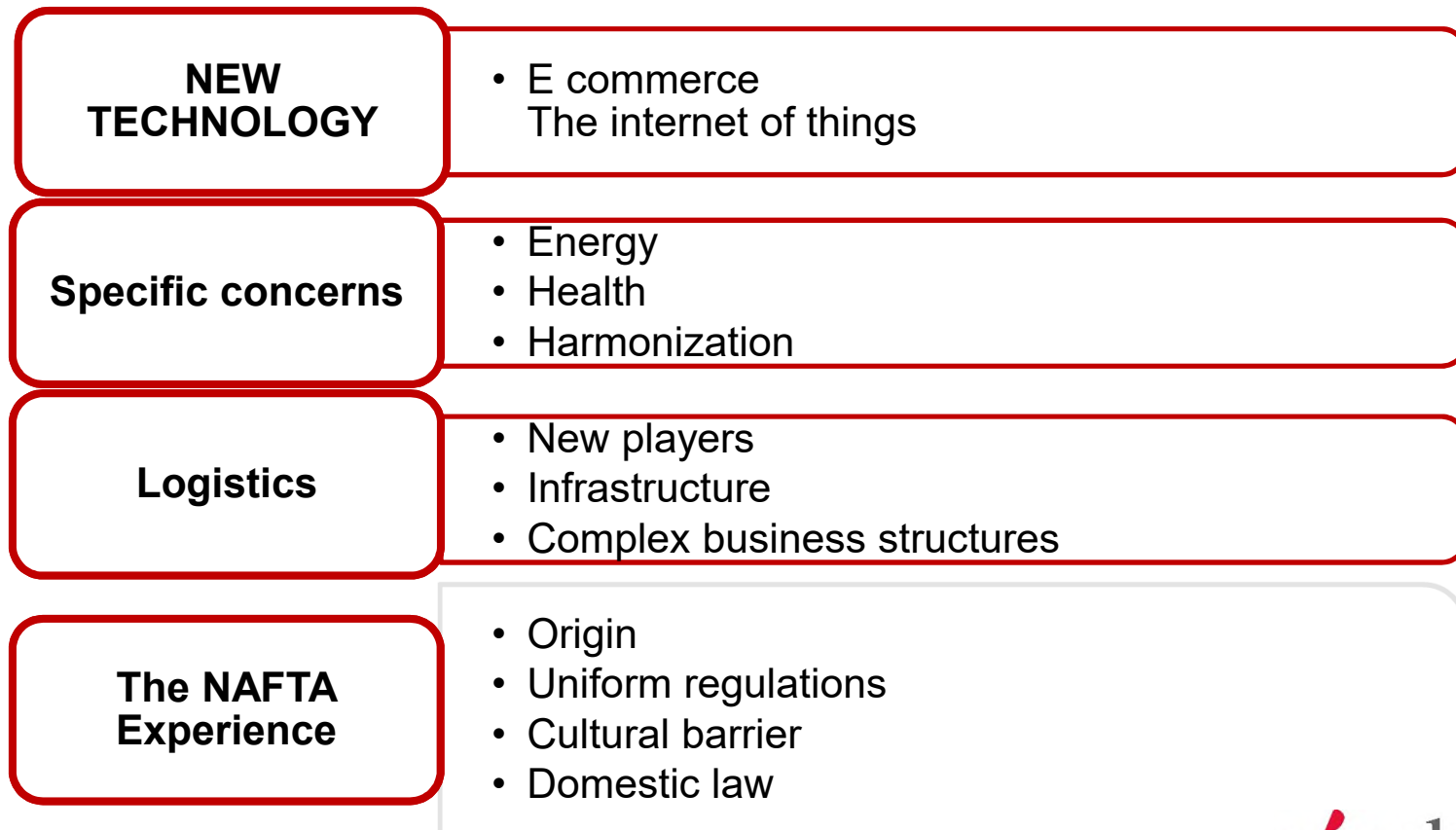
- President Trump announced tariffs on imports from Mexico until Mexico's immigration enforcement measures are determined to be effective.
- Tariffs will be implemented through the International Emergency Economic Powers Act (IEEPA).
 - "5% tariff on all imports from Mexico" beginning June 10, with increases of 10% on July 1, 15% on August 1, 20% on September 1, and 25% on October 1 and thereafter.
- IEEPA provides wide latitude for President to act when an "unusual and extraordinary threat" that has its source outside the U.S. requires the President to Act.
- IEEPA was used to justify a prohibition of Nicaraguan goods and services in the 1980s and is the basis to block imports from Iran and North Korea. However, no President has used IEEPA to place specific tariffs on imported products from a country.

Mexico Tariff Questions

- What will be the scope of the tariffs?
 - “Tariff on all imports from Mexico” – Country of Export or Country of Origin?
- If Mexican origin is used as the limitation, how will origin be determined? NAFTA Rules of Origin v. Substantial Transformation?
- Will there be any exemptions for NAFTA qualifying goods?
- How will tariffs impact ongoing USMCA discussions?
- Tariffs on Mexico will impact many companies that previously looked to Mexico as an alternative for Section 301 tariffs on China.

Mexico: Jose Alberto Campos Vargas, International Trade and Alfredo Kupfer Domínguez, Labour, Partners – Sánchez Devanny

NAFTA's 25th Birthday / CUSMA, the new NAFTA



NAFTA vs CUSMA

Position on NAFTA renegotiation:

- "Maintain the Agreement as long as it doesn't become a burden for Mexicans."
- "It's not appropriate to pursue an agreement under pressure."
- Regional integration MX-USA-CANADA to compete commercially with China;
- Increase in national content of strategic sectors.

Other FTAs

EU-Mexico Free Trade Agreement (FTA) renegotiation:

- On June 2016, Mexico and the European Union began negotiations to update the EU-Mexico FTA and on April 21, 2018, an **"agreement in principle"** (agreement on substantive issues) was reached, pending issues will be resolved by the technical teams). Possible entry into force on 2020;

CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership):

- On February 20, 2018, the Ministry of Economy released the final text of the Treaty and it was signed on March 8, 2018, in Santiago, Chile (representatives of the 11 countries);
- It incorporates most of the provisions of the TPP, including CHAPTER 3 RULES OF ORIGIN;

Sensitive sectors in Mexico

STEEL

a) Sector Importers' Registry, applicable to any customs regime:

Sector 14 Steel, with 203 HS Codes, Chapters 72 and 73 of the TIGIE, including intermediate products of iron or steel; flat-rolled products of iron or steel; wire rod of iron or steel; bars and rods of iron or steel; flat-rolled products of stainless steel; tubes, pipes and hollow sections; among others.

Sector 15 Steel products, with 104 HS Codes, Chapters 72 and 73 of the TIGIE, such as flat rolled products of iron or steel; stainless steel wire; chains and parts thereof, of iron or steel; pointed, corrugated or beveled points, nails or staples, among others.

b) Automatic notices (Non-tariff restriction):

Its nature is that of a notice to the authority, however it is used as an import restriction.

c) IMMEX Program

Restricted authorization

Canada: Carmen Francis, Senior Associate, International Trade and Investment Law Group – McCarthy Tétrault LLP

mccarthy
tétrault

The Latest on the New NAFTA and Trump's Continuing Tariff Threats: Perspectives from the United States, Mexico and Canada

Carmen Francis

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A large, stylized graphic of the McCarthy Tétrault logo. The letters are white and semi-transparent, overlaid on a background of a stack of papers and a black pen. The logo is positioned in the lower half of the slide.

- IF ratification, what are the implications for Canada?
- WHEN can we expect ratification?

What will change? 3 Key implications for Canada

- Chapter 11, investor-state dispute settlement
- Origin requirements for auto sector
- Preservation of Chapter 19 review mechanism

Elimination of Ch. 11

- Binding arbitration and protection of investors' rights
- US historical “winner” under Ch. 11
- Investor assurance
- Continuation with Mexico via CPTPP

Origin in the Auto Sector

- Regional Value Content requirement increases by 20%
- Labour cost element – 30% at \$16/hr
- Cost implications on both fronts

Ch. 19 Independent Review Mechanism

- Review of anti-dumping and countervailing duty rulings
- Practical tool that Canada has leveraged in the past
- A check on US actions that remains in place under USMCA

Ratification – the ground is prepared...

- Canadian political landscape
- Removal of steel and aluminum tariffs
- Implementation bill
- ...and then, Friday

Thank you!

Carmen Francis
cfrancis@mccarthy.ca

VANCOUVER

Suite 2400, 745 Thurlow Street
Vancouver (Colombie-Britannique) V6E 0C5
Tél. : 604-643-7100
Télééc. : 604-643-7900
Sans frais : 1-877-244-7711

CALGARY

Suite 4000, 421 7th Avenue SW
Calgary (Alberta) T2P 4K9
Tél. : 403-260-3500
Télééc. : 403-260-3501
Sans frais : 1-877-244-7711

TORONTO

Suite 5300, TD Bank Tower
Box 48, 66 Wellington Street West
Toronto (Ontario) M5K 1E6
Tél. : 416-362-1812
Télééc. : 416-868-0673
Sans frais : 1-877-244-7711

MONTRÉAL

Bureau 2500
1000, rue De La Gauchetière Ouest
Montréal (Québec) H3B 0A2
Tél. : 514-397-4100
Télééc. : 514-875-6246
Sans frais : 1-877-244-7711

QUÉBEC

500, Grande Allée Est, 9^e étage
Québec (Québec) G1R 2J7
Tél. : 418-521-3000
Télééc. : 418-521-3099
Sans frais : 1-877-244-7711

NEW YORK

55 West 46th Street Suite 2804
NEW YORK NY 10036
ÉTATS-UNIS
Tél. : 646-940-8970
Télééc. : 646-940-8972

LONDRES

125 Old Broad Street, 26th Floor
London EC2N 1AR
ROYAUME-UNI
Tél. : +44 (0)20 7786 5700
Télééc. : +44 (0)20 7786 5702



Panel 2 – Doing Business in Mexico



Doing business in Mexico

Francisco Andrés Gámez Garza, Partner, Corporate and M&A – Sánchez Devanny

Alfonso López-Lajud, Partner, Energy and Litigation – Sánchez Devanny

Abel Francisco Mejía-Cosenza, Partner, Tax – Sánchez Devanny

New Government: Major changes in National Policy

New Political Regime

Institutional left comes to power for first time

- Andres Manuel Lopez Obrador obtained an overwhelming victory;
 - Obtained victory through Morena left-leaning party;
 - Majority in both chambers of Congress, but not enough for unilateral constitutional changes
 - Period covers 2018-2024;

- Major economic policy changes
 - Review and revision of energy policy, slowdown of energy reform implemented in 2014.
 - Kickstart of Pemex as an oil-producing and refining powerhouse
 - Cancellation of major infrastructure projects (airport and special economic zones) for other major projects (Mayan Train & New Oil Refinery)
 - Major cuts in federal agencies budget and personnel
 - FULLY SUPPORTS NEW FOREIGN TRADE AGREEMENT WITH CANADA & US
 - Has regularly expressed support for foreign investment in Mexico.

- No radical legislation has been approved as of now;
 - There is some concern of potential introduction of inheritance tax; although official policy is that no such tax will be approved and there will not be any tax changes until 2021 (after mid-term elections).
 - Major changes have been carried on through administrative action.

New Political Regime

Institutional left comes to power for first time

- Focus on domestic issues, low international profile;
 - AMLO has not traveled abroad;
 - Major promotion agencies (*Promexico* and Tourism Council) have been reduced or shut down; participation in major international showcase events has been cancelled or minimized.
 - Initial positive rapport with President Trump, new tariffs and immigration will put relationship to the test.

- New business relationships and scenario
 - Traditional players have been relegated or denied major participation in shaping economic and industrial policy as well as in new major infrastructure projects.
 - Mexican economy has had worst economic scenario since 1994; other macroeconomic indicatives (amount of foreign investment and foreign exchange currency ratio) remain stable.
 - Potential radical legislation has been stalled or revised.

Labor Reform: The Real Impact on Companies

Main Drivers for the Labor Reform

- For many years, México has been in the international labor spotlight, as a country in which there is no respect of the right of freedom of association or the effective negotiation of collective bargaining by workers.
- Federal Labor Law contained minimum requirements for the registration of Unions and Collective Bargaining Agreements (“CBA’s”); situation that led to have a large number of unions and CBA’s with no real representation of the workers.
- The main purpose of many of these agreements was the protection of the workplace against external and aggressive unions. Before the Labor Reform, unions in Mexico could call for a strike, claiming the execution of a CBA, without showing employee representation.



98th Convention of the ILO

- ↪ On September 20th, 2018, Mexico ratified the 98th Convention of the ILO, regarding freedom of association and free collective bargaining rights (even though this convention has been in effect for other signatory countries since 1951). In general terms, the ratification of this convention will imply the following:
 - a) As an international treaty, Convention 98 of the ILO will have the same hierarchy as the Political Constitution;
 - b) Mexico will be mandated to enact and maintain legislation which protects workers rights to freely join or not join a union, or resign union affiliation, without employment retaliation (a common practice in Mexico);
 - c) Mexico will be required to pass legislation insuring freedom of association and that unions are free of any outside factor, preventing employer control.
- ↪ According to the ILO webpage, the Convention will have full effects as of November 23, 2019.

United States-Mexico-Canada Agreement

- On November 30, 2018, Mexico signed the new USMCA. Chapter 23 of the USMCA includes obligations for the three signatory countries, which will now become part of the international treaty, with potential commercial impact in case of non-compliance.
- Annex 23-A of the agreement provides the following labor obligations for Mexico:
 - a) Adopt and implement within local legislation and practices: i) freedom of association and collective bargaining, ii) eliminate all forms of child forced labor, iii) eliminate all forms of discrimination with a particular emphasis on the protection of women;
 - b) Guarantee the protection of immigrant workers;
 - c) Assure the compliance with labor provisions, by increasing inspections; and
 - d) Encourage dialogue to address differences related to the implementation of the Chapter commitments.
 - e) The creation of an independent institution that fosters conciliation and registers unions and CBAs.

United States-Mexico-Canada Agreement



- e) The election of union representatives should be done through personal, free, direct and secret voting.
- f) To register a CBA, the authority must verify that the company is already operating, that the employees know the agreement and that they agree to sign it.
- g) That the revision/update of a CBA should be agreed by the majority of the employees through a personal free, direct and secret voting.
- h) All CBAs should be public and therefore, its content should be available to all public.

Main Aspects of the Reform



- ↪ The employers are obligated to implement a protocol to prevent discrimination of gender, attend cases of violence, sexual and labor harassment.
- ↪ Additional protection in favor of pregnant workers and their social security rights.
- ↪ In case of an employee's death, beneficiaries in the employment agreement.
- ↪ Termination agreements without authority's intervention.
- ↪ Notice of termination will not be mandatory, but will create unfair termination will be presumed.
- ↪ Termination of managerial personal by filing severance before court.

Collective Matters

- ↪ Any intention or persuasion for employer-controlled associations, or to support any specific form of worker association in order to place them under their control, is prohibited.
- ↪ Broad classification of unions, that may result on an increase union formation and union campaign countrywide.
- ↪ Unions are prohibited to participate in simulation schemes and in acts of extortion with the purpose of receiving payments from employers.
- ↪ Union representatives can only be elected through personal, secret and free vote and cannot be elected for an indefinite term.



Collective Matters

- Employers are strictly prohibited from interfering with the employee's decision to affiliate or disaffiliate from a union. "Exclusion Clause" is prohibited.
- Unions should inform the employees about the administration of its assets every six months.
- Revision/updated of CBAs should be submitted to the free, secrete and personal vote of workers.
- An autonomous agency will register all CBAs and unions throughout the country: the Federal Conciliation and Labor Registry Center.
- Unions requesting the execution of a new CBA must obtain a "Representation Certificate" from the Federal Center, through the vote of at least 30% of the voting workers.
- Once the union obtains the Representation Certificate, the union has to obtain a majority vote of the employees authorizing the CBA.

Risk Scenarios

- Workers' discomfort with current union or with the company.
- Collective structure from external providers.
- On-site personnel hired by third parties (transportation, cafeteria, etc.).
- Promise of better employment conditions.
- Unilateral changes of employment conditions.
- Abuse of temporary workers.
- Profit sharing issues
- Direct involvement of international unions, NGOs and religious organizations
- Different unions and different union environment per working site.
- Weak union representation.

Suggested Actions

- ↪ Have an internal assessment of the collective structure/situation of the company.
- ↪ Assessment on a “protective” CBA.
- ↪ Identify positive and negative leadership within the workers.
- ↪ Empowering employees with a more “productive-oriented” mindset so they can be elected as representatives.
- ↪ Strict compliance of all labor and social security obligations.
- ↪ Improve recruitment and selection process of candidates.
- ↪ Open and permanent communication with workers and union.
- ↪ Training of supervisors and union delegates to better handle collective negotiation and union relationship.
- ↪ Transparency on union dues and any payment made to the union.
- ↪ Crisis protocol; continuity operation plan.

Doing Business in Mexico Dispute Resolution



Preliminary Takeaways

- Ongoing NAFTA Chapter 11 Investor-State Arbitrations, will **not** be disrupted or discontinued under USMCA Chapter 14.
- NAFTA is formally still in full force and effect. Once terminated, investors may file claims under NAFTA Chapter 11, within a **three-year period** after termination, provided that their investments were made while NAFTA was in force.
- USMCA completely eliminates investor-state arbitration between Canadian parties and US / Mexico.
- USMCA limits the type of disputes that may be subject to investor-state arbitration between US and Mexico parties, and forces investors to file claims in national courts first, and then wait 30 months before commencing arbitration.
- In case investment claims are part of a **covered sector** under the USMCA, investors may use full remedies available under the USMCA.

Preliminary Takeaways (continuation)

- Article 6 of Annex 14-E of USMCA defines “**covered government contract**” as:

“...a written agreement between a national authority of an Annex Party and a covered investment or investor of the other Annex Party, on which the covered investment or investor relies in establishing or acquiring a covered investment other than the written agreement itself, that grants rights to the covered investment or investor in a covered sector...”

- Also, said Article 6 of Annex 14-E names as “**covered sector**” activities, the following:

Oil and Natural Gas - Power Generation – Telecommunication Services – Transportation- Ownership or management of roads, railways, bridges, or canals

Legacy Investment Claims and Pending Claims

A “**legacy investment**” is defined in Article 6(a) of Annex 14-C as:

“an investment of an investor of another Party in the territory of the Party established or acquired between January 1, 1994, and the date of termination of NAFTA 1994, and in existence on the date of entry of force of this agreement”.

Said that, an investment must have been “established or acquired” when the NAFTA was in force but remain “in existence” on the date USMCA enters into force.

Article 14.1.- “**Investment**” means every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk.

Legacy Investment Claims and Pending Claims

An investment may include:

- a) an enterprise;
- b) shares, stock and other forms of equity participation in an enterprise;
- c) bonds, debentures, other debt instruments, and loans;
- d) futures, options, and other derivatives;
- e) turnkey, construction, management, production, concession, revenue-sharing, and other similar contracts;
- f) intellectual property rights;
- g) licenses, authorizations, permits, and similar rights conferred pursuant to a Party's law; and
- h) other tangible or intangible, movable or immovable property, and related property rights, such as liens, mortgages, pledges, and leases

Canadian Investments?



USMCA current text eliminates the possibility of future investor-state arbitration between US / Mexico and Canadian parties for investments made after termination of NAFTA.

Investor-State arbitration.- Article 14.2 of USMCA limits the scope of investor-state arbitration to Legacy Investment Claims and Pending Claims, Mexico-US Investment Disputes and Mexico-US Investment Disputes Related to Government Contracts.

State-to-state arbitration.- Canada may continue to bring suit before a special panel over alleged unfair trade practices by the US and/or Mexico, including anti-dumping and countervailing duties.

Canada – Mexico Investment Arbitration

- No consent for investment arbitration was included in USMCA for investments between Canada and Mexico.
- Investors seeking to bring investment claims are likely to rely on the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) rather than the USMCA, which offers similar protections accorded to investors under both NAFTA and USMCA.
- The CPTPP is a free trade agreement between Canada, Mexico and 9 other countries in the Asia-Pacific region: Australia, Brunei, Chile, Japan, Malaysia, New Zealand, Peru, Singapore and Vietnam. Once fully implemented, the 11 countries will form a trading bloc representing 495 million consumers and 13.5% of global GDP, providing both Canada and Mexico with preferential access to key markets in Asia and Latin America.
- On December 30, 2018 the CPTPP entered into force among the first 6 countries to ratify the agreement – Canada, Australia, Japan, Mexico, New Zealand, and Singapore. On January 2019, it entered into force for Vietnam.

Will the CPTPP be ratified before NAFTA's termination, and will it really provide Canadian and Mexican investors an effective tool for future investor-state arbitration?

Some recommendations...

- ▮ Know your counterparty
- ▮ Anticipate Legal Advice
- ▮ Document your transactions
- ▮ Include Penalties
- ▮ Securities
- ▮ Promissory Notes
- ▮ Select the proper venue / jurisdiction
- ▮ Arbitration Clause?



Tax Issues



Tax issues

- Only 3 major reforms:
 - (i) Elimination of VAT universal compensation;
 - (ii) Decree to Eliminate the Condonation of Federal Taxes;
 - (iii) Decree for Special Tax Incentive on corporate debt bonds and sale of public shares.

- Campaign promise to not raise taxes vs. Significant budget pressures.

- Emphasis on tax collection from multinational companies:
 - Heightened audits on related party transactions.
 - Recurrent use of substance over for doctrines.
 - Recurrent use of Tax Ombudsman Reconciliation Procedure for Corporate Audits

- Increased information received by Mexican tax authorities derived from Fatca, CRS, and other multilateral tax instruments.



Ciudad de México
T.+52 (55) 5029.8500

Monterrey
T.+52 (81) 8153.3900

Querétaro
T.+52 (442) 296.6400

www.sanchezdevanny.com

Abel Francisco Mejia Cosenza
Partner
amejia@sanchezdevanny.com

Alfonso López Lajud
Partner
alopez@sanchezdevanny.com

Jose Alberto Campos Vargas
Partner
jacampos@sanchezdevanny.com

Alfredo Kupfer
Partner
akupfer@sanchezdevanny.com

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