Kluwer Arbitration Blog

The USMCA/CUSMA/T-MEC's Entry into Force: Introducing a New Era in Regional ISDS with NAFTA 2.0

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On July 1, 2020, the United States – Mexico – Canada Agreement (USMCA) will enter into force. Although the media widely refers to the treaty by its American name, USMCA, it also carries two other names: Canada has adopted it as the Canada – United States – Mexico Agreement (CUSMA), while Mexico has settled on the title El Tratado entre México, Estados Unidos y Canadá (T-MEC). Regardless of which name is utilised, the trade deal serves as the successor to the North American Free Trade Agreement (NAFTA), which will officially terminate when the USMCA enters into force, although certain enumerated provisions will continue in force for a limited time period.

In anticipation of this milestone, we dedicate this week on the Blog to the USMCA and its origins, features, and goals. Through this series, we aim to provide insight into this new era of regional treaty law, including the innovations it heralds with respect to investor-State and State-State arbitration. To introduce the series, this post provides background concerning the rise of USMCA as NAFTA's successor and discusses its relationship to, among other topics, global investor-State dispute settlement ("ISDS") reform efforts. It then briefly introduces the posts that will feature as part of this week's series.

NAFTA to USMCA: How Did We Get Here?

When NAFTA entered into force in 1994, it was considered both remarkable and unremarkable in the same breath. NAFTA was lauded for the increased trade it facilitated across North America and its unprecedented economic benefits. In 1998, Daniel Griswold (former director of the Herbert A. Stiefel Center for Trade Policy Studies at the Cato Institute in Washington, DC) explained:

> Trade among the United States, Canada, and Mexico has flourished since the passage of NAFTA, benefiting American consumers and exporters.

> Since 1993, two-way trade with our NAFTA partners has increased by 44 percent, to $421 billion in 1996. That compares with a 33 percent increase in American trade with all other countries. Mexico has now become America's second largest market for exports, just ahead of Japan and behind only Canada.

To support investor confidence, Chapter 11 of NAFTA provided an ISDS mechanism. In 2001, Judge Charles N. Brower and Lee A. Steven explained:

> The only potentially unique aspect of NAFTA Chapter 11 is that the governments of two nations with developed economies agreed to enter into an investment protection treaty between themselves. The overwhelming majority of BITs to date have been North to South, between capital-exporting countries and capital-importing countries, and the private investors who actually have benefited from such treaties have been those from the North. (at pp. 193-94.)

Nearly twenty-five years of trade facilitation and numerous ISDS claims aided the NAFTA parties' understanding of the benefits and drawbacks of their trade deal. Despite its successful run, most commentators in recent years have agreed that the time had come for NAFTA's renegotiation and modernization.

In 2016, then-presidential candidate Donald Trump announced his intention to either renegotiate or terminate NAFTA should he become President. He vowed to revise NAFTA in a manner consistent with his "America First" ideology and applied aggressive import tariffs on Canadian and Mexican goods to influence renegotiation. From May 2017 to September 2018, Mexico, the United States and Canada embarked on a renegotiation and modernisation process through a series of negotiating rounds. In October 2018, the States completed the agreement and released a draft text of agreed provisions. The treaty covers a range of trade-related issues, and includes chapters on rules of origin, technical barriers to trade, intellectual property, competition policy, labour, the environment, and investment.

Mexico was the first to ratify USMCA in June 2019. Unexpectedly, on December 10, 2019, all three prospective USMCA States executed a "Protocol of Amendment" (Amendment). The 26-page Amendment included modifications to key elements of the USMCA, most importantly dispute settlement, labour and environmental provisions, intellectual property rights, and steel and aluminium requirements in the rules of origin for automobiles. Following this Amendment, the States followed their respective domestic ratification processes, with Mexico again as the first to ratify, and Canada as its final party on April 3, 2020.

USMCA: Providing New Balance for ISDS

Since the announcement of negotiations, our contributors have commented on the

shifting contents of and vision for USMCA's ISDS mechanism. At a policy level, our contributors have considered the interplay between USMCA negotiations and public policy, the possible impact on the North American energy industry, and the impact on parties participating in ongoing NAFTA arbitrations. Meanwhile, since the unveiling of USMCA's draft text, our commentators have focused on the substantive rights available to prospective claimants and the procedural means to assert them.

While Chapter 14 of USMCA provides an ISDS mechanism, it departs in many ways from Chapter 11 of NAFTA. Glaringly, Canada is not a party to the ISDS mechanism provided in Chapter 14. This means that ISDS claims cannot be asserted by Canadian investors, nor asserted against Canada. Canada's consent for legacy claims will expire three years from the termination of NAFTA (i.e., July 1, 2023).[1)] For many commentators, this is surprising: Canada remains committed to multilateral trade deals and continues to participate in ISDS through other trade agreements. Some speculate that Canada's opt-out may reflect Canada's mixed success with arbitrations involving American investors under NAFTA. Others cite Canada's perceived lack of bargaining power during USMCA negotiations and an ultimate decision simply to abstain.

ISDS survives for the benefit of American and Mexican investors only, and even then, with changes to the types of claims investors may pursue, and the procedural means to do so. Chapter 14 of USMCA (Investment) now includes a local litigation requirement as a prerequisite for ISDS claims. Once that requirement is exhausted (or 30 months have elapsed), claims may be asserted for: (1) direct (but not indirect or "creeping") expropriation (Annex 14-B (Expropriation), Article 2), (2) violations of national treatment (Article 14.4.1), or (3) violations of the USMCA's Most Favored Nation (MFN) provision (Article 14.5.1). There is a carve-out for MFN claims concerning "the establishment or acquisition of an investment."[2)] Chapter 14 also includes a novel asymmetrical fork-in-the-road provision that applies to American investors only. In many ways, USMCA reflects ideas currently circulating globally on ISDS reform.

Further substantive or procedural rights are also provided for claims concerning government contracts in several highly regulated sectors including energy, telecommunications, transportation, and infrastructure.[3)] Some commentators have referred to these sectors as "privileged" sectors under the USMCA. These provisions allow investors to pursue claims for violations of the minimum standard of treatment under customary international law, indirect expropriation, and the establishment or acquisition of an investment.[4)]

Placing the USMCA Within Broader Treaty Renegotiation and ISDS Reform Efforts

Most commentators accept that NAFTA needed modernization because commerce in the region has changed dramatically over the past quarter century. In this regard, some commentators have lauded USMCA for bringing North American regional trade

into the 21st century. USMCA allows for the free flow of cross-border data, seeks to prevent discriminatory trade barriers, and offers protections to online services to facilitate global competitiveness. Indeed, drawing on the assessment of some American businesses, USMCA is described as a step toward "transparency" and "predictability," while providing increased intellectual property protections, and sorely needed modern customs procedures. Accounting for these goals is a priority for many other treaties currently being renegotiated and modernized. For example, the WTO's General Agreement on Trade in Services (GATS) prioritizes liberalizing the digital sector, the Canada-Israel Free Trade Agreement (CIFTA) seeks to liberalize trade and the cross-border flow of goods, and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) Agreement offers enhanced and modern intellectual property rights.

With respect to ISDS, the differences between NAFTA's Chapter 11 and USMCA's Chapter 14 (and particularly Canada's non-participation in the ISDS mechanism) reflect concrete ISDS "evolution" for regional ISDS, and, perhaps, offers a template for future global trends. Optimistically speaking, the story of USMCA may demonstrate that evolution, and not death, is the answer to the modern ISDS debate.

Overview of This Week's Series

Each day this week, a different contributor will spotlight an aspect of USMCA from a variety of national and regional perspectives:

- On Tuesday, Barton Legum and Sean Stephenson will offer an obituary to memorialize NAFTA's Chapter 11 and its historic importance and legacy, as well as its imprint on USMCA's Chapter 14.
- On Wednesday, Dr. Devin Bray and Jason Czerwiec will examine Canada's position towards Chapter 14 of the USMCA and provide observations and implications for stakeholders affected by the upcoming changes to the North American investment-treaty regime.
- On Thursday, Mélida Hodgson will examine in detail the investor protections offered by USMCA's Chapter 14. In doing so, she will highlight its evolutionary aspects, political implications, and future complexities.
- On Friday, Aristeo Lopez will focus on USMCA's Chapter 17 (Financial Services). He will discuss the stages and elements for investor claims under this Chapter and offer comparisons to the approach previously provided in NAFTA for the arbitration of disputes concerning investments in the financial sector.
- On Saturday, Dr. Elizabeth Sheargold will provide an Australian perspective on USMCA. Her big-picture insights, gleaned through comparisons to the Australian experience, will contextualize the various choices adopted by the USMCA Parties within the modern ISDS debate.
- On Sunday, we will end the series by drawing focus to USMCA's Chapter 31 on State-State arbitration and provide some concluding remarks.

Through this series, we aim to provide insights into the unique features of USMCA's investor-State and State-State arbitration mechanisms, and place the agreement

within the context of a broader global discourse concerning treaty law and ISDS reform. We are proud to be able to mark this momentous occasion on the Blog with this series of posts by leading experts and practitioners from the region and beyond. We hope you enjoy the series!

For the full scope of our coverage of USMCA to date, click here.

References

↑1 USMCA, Annex 14-C (Legacy Investment Claims and Pending Claims), Article 6(a).

↑2 *Id.*, Annex 14-D (Mexico-U.S. Investment Disputes), Art. 14.D.3 (Submission of a Claim to Arbitration), Article 14.D.3 (Submission of a Claim to Arbitration), note 22.

↑3 *Id.*, Annex 14-E (Mexico-U.S. Investment Disputes Related to Covered Government Contracts), Article 6.

↑4 *Id.*

This entry was posted on Monday, June 22nd, 2020 at 8:00 am and is filed under Canada, International agreement, International arbitration, Investment agreements, Investment Arbitration, Investment protection, Investment Treaties, Mexico, NAFTA, United States, USMCA
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