
Kluwer Arbitration Blog

The USMCA/CUSMA/T-MEC's Entry into Force: Evolution, Innovation, and Reform

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Throughout this week, our contributors from around the globe have offered insights into the USMCA/CUSMA/T-MEC, which enters into force next week. Our contributors have contextualised USMCA against both regional and global developments. Many of them noted the link between USMCA and NAFTA, between USMCA and regional politics, and between USMCA and broader global trends related to investment treaty reform. Consistently, they engaged with the idea that USMCA is an “evolutionary,” and in some respects, “innovative” treaty. Today we pull these threads together to contextualise USMCA further by examining its additional dispute resolution features, to draw connections between USMCA and broader investor State dispute settlement (“ISDS”) reform efforts, and to offer forward-looking thoughts.

Chapter 31 of USMCA: Innovations to the State to State Dispute Settlement Framework

In addition to the unique features of the USMCA ISDS mechanism that have been highlighted by our contributors this week, USMCA also provides noteworthy innovations in State-to-State arbitration. [USMCA Chapter 31 \(Dispute Settlement\)](#) provides a mechanism that largely adopts the approach of [NAFTA Chapter 20](#), while also [addressing](#) some of its flaws, which many commentators [believe](#) led to its infrequent use.

The scope of dispute settlement under USMCA Chapter 31 is narrower than NAFTA's State-State dispute settlement framework. NAFTA Chapter 20 permitted panels to be convened to hear both violation complaints and nullification and impairment cases (non-violation cases) for all substantive NAFTA rights, except trade remedies and the labour and environment side agreements. Meanwhile, USMCA Chapter 31 denies panels the ability to hear violation cases for trade remedies, and it further excludes non-violation cases for claims under USMCA's chapters on labour, environment, digital trade, financial services, telecommunications, alongside a number of other chapters. Procedurally, once a Party identifies a dispute, consultation with technical

experts and the Free Trade Commission is required. Upon failure of such consultations, a binational panel may be convened to assist the Parties to resolve their dispute.

Chapter 31 further offers detailed rules and procedures to govern the establishment of a roster of panellists, their necessary qualifications, and how panellists are then selected from the roster to hear disputes. A key critique of NAFTA was the ability of a State to engage in “[panel blocking](#)”, employing its own failure to maintain an active and complete roster of candidates to prevent panel formation. This issue is resolved in USMCA through a commitment among the States to establish their rosters by the date USMCA enters into force (July 1, 2020). To protect from any future lapse in appointments, roster members maintain their position for a minimum of three years or until the Parties constitute a new roster. To this end, for example, in March this year the U.S. concluded its [open call](#) for applicants to the roster.

Once a panel is appointed, Chapter 31 provides detailed guidance on the conduct of proceedings, including requirements for evidentiary submissions, hearing format, e-filing, third-party participation, and the use of experts. This detailed guidance is unique to Chapter 31 and is not mirrored in Chapter 14’s ISDS mechanism. In large part, this detail was added to USMCA through the [December 2019 Amendment](#), which immediately preceded the Parties’ rapid and successive domestic ratification processes. Finally, Chapter 31 indicates processes for release and implementation of panel decisions, as well as the consequences of non-implementation of such decisions.

The nuances and details of Chapter 31 are welcome additions to USMCA and reflect a thoughtful evolution of NAFTA’s Chapter 20. However, many commentators question the efficiency of both the negotiating process and even of the dispute settlement mechanism itself. An obvious alternative path would have been to draw upon the dispute settlement provisions of the [Comprehensive and Progressive Agreement for Trans-Pacific Partnership](#) (CPTPP). Both Canada and Mexico are already parties to the CPTPP. CPTPP negotiations also took into account American input, as the U.S. was involved with Trans-Pacific Partnership (TPP) negotiations until President Donald Trump signed an executive order to [withdraw](#) prior to domestic ratification. The TPP provisions were negotiated to account for flaws in NAFTA Chapter 20 that were well-known to American, Mexican, and Canadian TPP negotiators. As explained by Jennifer Hillman the approach of the TPP dispute settlement system was “designed to be broader, deeper, faster, and more transparent than either the WTO’s Dispute Settlement Understanding or [NAFTA Chapter 20.]”¹⁾

Where Does USMCA Fall in the Spectrum of Broader Global ISDS Reform?

TPP is also relevant to USMCA’s position with respect to global ISDS reform discussions. Many will recall that the TPP’s [ISDS mechanism](#) and the “risks” it posed to State sovereignty were among the U.S.’ [reasons](#) for withdrawing from the TPP. This position aligned with the “[America First](#)” rhetoric, which inspired the American negotiating position in USMCA. Yet, USMCA remains evolutionary in that it does not dispense with ISDS altogether. As Dr. Sheargold explained in yesterday’s post, the

approach adopted in USMCA as between the U.S. and Canada is comparable to that adopted by Australia and the U.S. in their free trade agreement, where the exclusion of ISDS was justified – at least in part – by reference to the developed domestic legal systems of both States.

Compared to other more radical reform efforts, such as the European Commission’s [proposal](#) to implement a multilateral investment court, USMCA is not particularly [revolutionary](#) in its approach to *structuring* ISDS. It nonetheless incorporates [many of the substantive and procedural reforms](#) that differentiate new generation investment treaties from earlier models. As our contributors this week have noted, this includes various innovations concerning the scope and availability of ISDS itself. The treaty also imposes certain procedural safeguards for USMCA host States, including a requirement for would-be ISDS claimants to pursue local remedies for 30 months prior to filing their USMCA claim. Such innovations are reminiscent of reforms adopted in other contexts, including for example the inclusion in the 2015 Indian Model investment treaty of a [five-year recourse to domestic remedies requirement](#).

Where ISDS is provided, USMCA builds on the legacy of NAFTA and the broader context of modern ISDS reform efforts to endorse a number of procedural safeguards and innovations. USMCA contains, for instance, detailed guidance as to the transparency frameworks applicable to ISDS proceedings. USMCA does not adopt the [UNCITRAL Transparency Rules](#) by reference, but nonetheless contains many of the same disclosure requirements set out in those Rules and in some cases, [like other modern treaties](#), USMCA signals a willingness to go beyond the provisions on transparency contained in the UNCITRAL Rules. It imposes, for instance, obligations upon respondent States to make available to the public and the non-disputing USMCA State various documents associated with the proceeding (subject to certain safeguards). This includes the notice of intent, notice of arbitration, pleadings, memorials and briefs, minutes and transcripts of tribunal hearings and orders, awards, and decisions of the tribunal (Article 14.D.8). The USMCA further provides for the holding of open hearings and filing of *amicus curiae* submissions.

While USMCA provides for significant elements of procedural transparency for ISDS, it misses others. This includes certain [more specific elements of transparency](#), including for example transparency associated with third party funding arrangements (a topic currently under discussion in [UNCITRAL’s Working Group III](#)). USMCA nevertheless addresses other aspects of transparency even if indirectly. Article 14.D.6, for instance, governs the selection of arbitrators, including to stipulate that arbitrators shall comply with the [IBA Guidelines on Conflicts of Interest in International Arbitration](#) “or any supplemental guidelines or rules adopted by the Annex Parties”. It is therefore possible that additional guidance could be provided by the USMCA Parties for assessment of arbitrator conflicts, including in the event Mexico and the U.S. endorse the [recently-published Draft Code of Conduct for Adjudicators in ISDS](#).

USMCA also confronts the increasingly divisive issue of “[double hatting](#)”, where arbitrators also serve in other roles linked to ISDS proceedings (most commonly, as counsel). Would-be Chapter 14 arbitrators, once appointed, are prohibited from acting as counsel or in any other capacity in another pending USMCA Chapter 14 arbitration while the arbitrations in which they sit as arbitrators remain pending. Some critics

suggest that banning “double hatting” may, as a [side effect](#), [decrease diversity](#) among the pool of prospective arbitrators in ISDS proceedings, claiming that a ban effectively [limits](#) opportunities available to younger emerging arbitrators who are “transitional” in their practice and working to move to full-time arbitrator practices, while still acting as counsel.

There are no easy answers to the arbitrator diversity problem, but [commentators](#) agree that the system itself is only one piece of the puzzle. Counsel and their clients maintain decision-making power and should select (or at least consider) diverse candidates. [Important projects](#) are being developed in relation to diversity in ISDS more broadly, and stakeholders should continue to monitor appointment practices under USMCA to ensure appropriate diversity is achieved. Even broader ISDS reform efforts focused on diversity only can go so far. For example, the roster approached recently adopted by Comprehensive Economic and Trade Agreement between Canada, the European Union and its member states (CETA) [failed](#) to reflect diversity goals, that failure was [acknowledged](#), and improvement efforts are apparently underway. In this respect, the selection criteria of USMCA Article 14.D.6 are helpful. Arbitrators are not required to have any specific experience or training (e.g., in public international law and/or in international investment and trade law), thereby [creating avenues](#) for entry by diverse and/or emerging arbitrators who may provide complementary expertise, for example, in international commercial arbitration or in specific relevant industries.

USMCA is noticeably silent on a range of other matters, particularly when compared to the ISDS mechanisms developed in other new generation treaties. This includes on the issue of potential investor obligations, a topic [gaining increased traction](#) in other negotiation settings. While a corporate social responsibility clause is included in USMCA Article 14.17, the clause focusses upon the responsibilities of each USMCA party and is likely too permissive to result in a legal obligation on investors to make or operate their investment consistently with such standards. Further, while the ISDS Annex between the U.S. and Mexico refers in passing to possible “counterclaims” by respondent States (Article 14.D.7), it is largely structured to focus upon claims filed by investors against their host State and not *vice-versa*.

What’s Next?

Placing USMCA amongst these broader discussions on evolution and innovation highlights the many challenges associated with modern treaty negotiation and ISDS reform. Yet, USMCA’s entry into force remains a historic and encouraging development regionally and globally. As mentioned in the introductory post to this series, NAFTA, despite the unprecedented trade flows it heralded, needed modernization because global commerce has changed dramatically over the past quarter century. USMCA thus brings North American regional trade into the 21st century in a manner that, at the very least, takes into consideration emerging global trends in treaty law and ISDS.

While today in 2020 our focus is on NAFTA’s termination and legacy claims provisions,

soon it will be time to reconsider USMCA's efficacy and future. A sunset provision at Article 34.7 provides that the agreement is subject to review and renewal by mutual agreement after six years (in 2026). At that time, its Parties would need to agree to a further 16-year extension, and absent mutual assent, USMCA would expire in 2036. The six-year review deadline is promising as it may provide an opportunity to revisit the challenges and opportunities already hotly debated among commentators, some of which are also discussed in this week's series. We will continue to watch these North American developments closely in the months and years to come. For now, we thank you and our contributors again for helping us mark this momentous occasion on the Blog!

For the full scope of our coverage of USMCA to date, click [here](#).

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