

LEARN ABOUT THE IMPACT AND
THE RECOMMENDATIONS
FOR THE
AUTOMOTIVE SECTOR

UPDATE JUNE 2020

Automotive Sector.

A. Overview

The Rules of Origin of the automotive sector are found in *Chapter 4: Rules of Origin and Specific Rules of Origin* of the new agreement called United States - Mexico - Canada Agreement (USMCA).

The Agreement includes three side letters between the United States and Mexico, the first concerning Car Safety Standards. The second and third refer to the "national security" trade restrictions of Section 232. Canada also signed the same letters with the U.S.

In the first letter, Mexico and the U.S. reaffirm their commitment to strengthen North America, the automotive sector, and to actively promote and facilitate fair and reciprocal trade between the two countries. Therefore, Mexico will continue to recognize and accept the Federal Motor Vehicle Safety Standards (FMVSS), which is the U.S. regulatory system for automobiles.

The US - Mexico 232 Side Letter, and its Canadian counterpart, provide that Canada and Mexico will receive certain exemptions from possible restrictions on imports of automobiles or auto parts that may be imposed by the United States. It agrees to exclude:

- 2,600,000 passenger vehicles per year from each country.
- Light trucks imported from each country.
- Auto parts in the amount of \$32.4 billion for Canada and \$108 billion for Mexico.

The last pair of side letters stipulate that, if the United States imposes tariffs or restrictions on the importation of goods or services from Canada or Mexico under Section 232, there must be a 60-day period prior to execution during which the parties "shall attempt to negotiate an appropriate outcome based on industry dynamics and historical trade patterns. They provide that, if the measures taken are inconsistent with NAFTA, the USMCA or the World Trade Organization Agreement, Canada and Mexico may take equivalent retaliatory action, and retain WTO rights to challenge such measures.

According to the U.S. Department of Commerce (USTR), the new agreement will create more balanced and reciprocal trade. It points out that the updated rules of origin for passenger cars, light trucks and auto parts provide incentives for the incorporation of goods and materials of U.S. and North American origin.

The increase in regional value content encourages regional and U.S. manufacturing growth by requiring that 75% of automobile content be made in North America.

The new trade rules will generate higher wages by requiring that 40-45% of automobile content be made by workers earning at least \$16 per hour. Finally, they will encourage greater investment by auto companies in research and development in the region.

For the Secretariat of Economy (SE), the rules of origin strengthen regional value chains and increase incentives for the development of local suppliers.

- Light vehicles and vans:

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- 75% of its value must come from processes and inputs made in the region and 40% from high-wage areas in North America.
- Heavy vehicles:
 - 70% of its value must come from processes and inputs made in the region and 40% from high-wage areas in North America.
- Autoparts:
 - Between 65 and 75% of its value must come from processes and inputs made in the region.

The increase in the rule of origin will be gradual, starting on 1 January 2020 it will rise to 66%, with a deadline of 2023 to reach 75% of the Agreement.

The Protocol of Amendment to the Rules of Origin - Automotive establishes the following:

- Steel: 7 years after the entry into force of this agreement, steel shall be deemed to be originating, all manufacturing processes must occur in one or more of the Parties, except metallurgical processes involving refining of steel additives. Such processes include initial melting and mixing and continue through the coating stage.
 - This requirement does not apply to raw materials used in the steelmaking process, including scrap steel; iron ore; pig iron ore, reduced, processed or pelletized; or crude alloys.
- Aluminum: 10 years after the entry into force of this agreement, the Parties shall consider appropriate requirements of interest to all three countries for aluminum to be considered as originating.

The USMCA was signed on November 30, 2018, in Buenos Aires, Argentina, by the then President of Mexico, Enrique Peña Nieto; the Prime Minister of Canada, Justin Trudeau; and the President of the United States, Donald Trump. Once it enters into force, it will replace the North American Free Trade Agreement (NAFTA).

June 19, 2019, the full Senate of the Republic approved, with 114 votes in favor; 4 against, and 3 abstentions, the Treaty between Mexico, United States and Canada (USMCA).

In response to the demands of the Democrats in the U.S. House of Representatives and the American unions, the Protocol of Amendment was negotiated, these petitions revolved around 4 themes:

- a. protection of the environment;
- b. data protection for biological medicines;
- c. protection of labor rights; and
- d. monitoring and enforcement.

On December 10, 2019, the signing of the Protocol Modifying the Treaty between Mexico, the United States and Canada (USMCA) took place in Mexico City. This protocol reforms some of the disciplines originally agreed in the USMCA, including a provision recently proposed by the U.S., on rules of origin for the automotive and steel sectors.

The US was the last partner to notify its counterparts that it had completed the internal procedures necessary for the entry into force of the USMCA on 24 April 2020. Canada and Mexico did the same earlier this month.

The Protocol amending the USMCA provides that the agreement will enter into force on the first day of the third month after the last partner notifies the completion of its internal procedures. This deadline would be on July 1.

B. Background

From the beginning of the renegotiation of NAFTA to the Rule of Origin of the automotive sector was one of the complex issues, even at the end of the negotiation was one of the three points that delayed the closure of the Agreement.

At the end of 2017 USTR updated its objectives for the negotiation of the Agreement, where it stated:

- Access to Market:
 - Improve the United States' trade balance and reduce the trade deficit with the NAFTA countries
 - Increase transparency in import and export licensing.
 - Regulate import and export monopolies to avoid trade distortions
- Rules of Origin:
 - Update and strengthen the rules of origin, as necessary, to ensure that the benefits of NAFTA go to products genuinely produced in the United States and North America.
 - Ensure that rules of origin provide incentives for production in North America, specifically in the United States.

That is why U.S. negotiators during much of the negotiation process presented several proposals to tighten the rule of origin for the automotive sector, and close the gaps (encouraged by NAFTA) of low wages in auto and parts production.

At the beginning of the negotiation, the U.S. proposal provided for an increase in the percentage of regional content from 62.5 to 85%; wage requirements; a list of seven "essential" components including the engine, transmission, suspension and chassis, which together should account for 75% of regional content; 70% of the steel and aluminum used by vehicle manufacturers to come from North America; and elimination of the tracking rule.

The proposal was described as strict by the Mexican private sector, so transition periods were proposed both for the increase of the regional content of the rules of origin and for the percentage of the content of a vehicle manufactured with paid labor of US\$ 16.

In June 2018, the United States applied tariffs of 25% on imports of various steel products and 10% on various aluminum products. Canada and Mexico were not excluded from the application of these measures and retaliated against a number of products from the United States.

These measures strained the negotiations, especially when in May the U.S. Secretary of Commerce announced the initiation of the investigation against automobiles and auto parts based on Section 232. In view of such a scenario, a kind of "insurance" in case of the application of tariff measures by the U.S. began to be negotiated, seeking to respect current and future export capacity.

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C. USMCA

Chapter 4: Rules of Origin and Specific Rules of Origin consists of:

- Article 4.1: Definitions
- Article 4.2: Original goods
- Article 4.3: Entirely Obtained or Produced Goods
- Article 4.4: Treatment of recovered materials used in the production of a remanufactured good
- Article 4.5: Regional Content Value
- Article 4.6: Value of materials used in production
- Article 4.7: Adjustments to the Value of Materials
- Article 4.8: Intermediate Materials
- Article 4.9: Indirect Materials
- Article 4.10: Automotive Goods
- Article 4.11: Accumulation
- Article 4.12: Minimis
- Article 4.13: Goods and Fungible Materials
- Article 4.14: Accessories, Spare Parts, Tools or other Materials
- Article 4.15: Retail packaging and packaging materials
- Article 4.16: Containers and packaging materials for shipment
- Article 4.17: Set of goods, kits or composite goods
- Article 4.18: Transit and Transshipment
- Article 4.19: Non-qualifying transactions
 - Annex 4-A: Exceptions to the Minimis
 - Annex 4-B: Specific Rules of Origin
 - Appendix to Annex 4-B: Provisions Relating to the Rules of Origin for Automotive Goods.


It is important to review the appendix, as it sets out the deadlines for compliance with regionally valuable content, as well as the value of labor content.

Rule of Origin for light vehicles:

- Regional Value of Content (RVC) of 75%, under the Net Cost methodology, for cars and vans, applicable in 4 increments, through which the RVC must be adjusted, until reaching the agreed percentage.
- Work Content Value (WCV) of 40% for cars and 45% for trucks, applicable in 4 increments. The WCV is comprised of two components:
 - Materials and manufacturing costs (25% for cars and 30% for vans)
 - Research and Development (R&D), Information Technology services, and advanced engine, transmission or battery assembly operations, which account for 15% of the RVC.

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- At least 70% of the steel and aluminum must originate from the North American region. (to be fulfilled only by the shipowners).
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- Seven auto parts were identified as essential, which must originate in North America for the vehicle to be considered as originating.
- Three categories of auto parts were defined: essential, main and complementary, whose RVC was established between 75%, 70% or 65%, depending on the type of auto part. The RVC will also be increased by 4 increments.

 Rule of Origin for heavy vehicles:

- RVC of 70%, under the Net Cost method and applicable in 7 increments, through which the RVC must be adjusted, until the agreed percentage is reached.
- RVC of 45%, comprised of two components:
 - o Materials and manufacturing costs 30%.
 - o R&D, Information Technology services, and advanced engine, transmission or battery assembly operations, representing 15% of the WCV.
- At least 70% of the steel and aluminum must originate from the North American region. (to be fulfilled only by the shipowners).
-
- For auto parts, three categories were also defined: essential (must originate in North America), main and complementary, whose RVC was established between 70%, 60% or 65%, depending on the type of auto part, and the increase will be applicable in 7 stages.

 Vehicles not complying with the Rule of Origin:

- Up to 1,600,000 units will pay the Most Favored Nation (MFN) tariff which is 2.5% (in case the U.S. decides to increase the MFN tariff), complying with the rule of origin agreed in the NAFTA.
- Auto parts: up to 108 billion dollars of exports will face the MFN applied by the U.S. as of August 1, 2018, complying with the NAFTA rule of origin.

 Auto parts for light vehicles:

- o There are 3 categories.
 - Category 1: Essential Parts.
 - They will have to reach a maximum of 75% RVC or under the Transaction Value of 85%, in 4 increments.
 - Made in the region:

**TABLE A.1
CORE PARTS FOR PASSENGER VEHICLES AND LIGHT TRUCKS**

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HS 2012	DESCRIPTION
840731	Spark-Ignition Piston Engine for Vehicle Ex Railway Not Over 50 Cc
840732	Spark-Ignition Reciprocating Piston Engine Etc Nov 250Cc
840733	Spark-Ignition Reciprocating Piston Engine Etc >250 Nov1000Cc
840734	Spark-Ignition Reciprocating Piston Engine Etc > 1000 Cc
840820	Compression-Ignition Internal Combustion Piston Engine Etc
840991	Spark-Ignition Internal Combustion Piston Engine Parts Nesoi
840999	Spark-Ignition Reciprocating Internal Combustion Piston Engine Parts
850760	Lithium Ion Batteries
870600	Chassis W Engine for Trac, Motor Vehicle for Pass/Good & Special Purpose
870710	Bodies for Motor Cars/Vehicles for Transporting Persons
870790	Bodies for Road Tractors and Motor Vehicles (Pub Tran, Etc)
870840	Gear Boxes for Motor Vehicles
870850	Drive Axles with Differential for Motor Vehicles
870880	Suspension Shock Absorbers for Motor Vehicles
870894	Steering Wheels, Columns & Boxes for Motor Vehicles

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TABLE A.2
PARTS AND COMPONENTS FOR PASSENGER VEHICLES AND LIGHT TRUCKS

Column 1	Column 2
PARTS	COMPONENTS
ENGINE	Heads, Blocks, Crankshafts, Crankcases, Pistons, Rods, Head subassembly
TRANSMISSION	Transmission cases, Torque converters, Torque converter housings, Gears and gear blanks, Clutches, Valve body assembly
BODY AND CHASSIS	Major body panels, Secondary panels, Structural panels, Frames

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AXLE	Axle shafts, Axle housings, Axle hubs, Carriers, Differentials
SUSPENSION SYSTEM	Shock absorbers, Struts, Control arms, Sway bars, Knuckles, Coil springs, Leaf springs
STEERING SYSTEM	Steering columns, Steering gears/racks, Control units
ADVANCED BATTERY	Cells, Modules/arrays, Assembled packs

- Category 2: Main Parts.
 - They will have to reach a maximum of 70% RVC, or under the Transaction Value of 80%, in 4 increments.

**TABLE B
PRINCIPAL PARTS FOR PASSENGER VEHICLES AND LIGHT TRUCKS**

HS 2012	DESCRIPTION
401110	New Pneumatic Tires of Rubber, for Motor Cars
401120	New Pneumatic Tires of Rubber, for Buses or Trucks
401211	Retreaded Tires of Rubber, for Use on Motor Cars
401212	Retreaded Tires of Rubber, for Use on Trucks
401219	Retreaded Tires of Rubber, Nesoi
401310	Inner Tubes of Rubber for Mot Cars, Buses & Trucks
700711	toughened Safety Glass of Size a Shape for Vehicles Etc
700721	Laminated Safety Glass for Vehicles, Aircraft Etc.
700910	Rear-View Mirrors for Vehicles
841330	Fuel, Lub/Cooling Med Pumps for Internal Comb Piston Engine
841350	Hydraulic Fluid power Pumps
841391	Parts of hydraulic fluid power pumps
841430	Compressors Used In Refrigerating Equipment
841459	Fans, Nesoi (turbochargers and superchargers)
841480	Air/Gas Pumps, Compressors and Fans Etc, Nesoi
841520	Automotive Air Conditioners
841590	Parts, Nesoi, of Air Conditioning Machines
847989	Electronic brake systems incl. ABS and ESC systems
848210	Ball Bearings
848220	Tapered Roll Bearings, Including Cone & Roller Assemblies
848230	Spherical Roller Bearings
848240	Needle Roller Bearings
848250	Cylindrical Roller Bearing Nesoi
848280	Other Ball or Roll Bearings, Inc Comb Ball/Roll Bearings
848291	Balls, Needles and Rollers for Bearings
848310	Transmission Shafts (Inc Cam-& Crank-Shaft), Etc.
848320	Housed Bearings, Incorp Ball or Roller Bearings
848330	Bearing Housings; Plain Shaft Bearings
848340	Gears; Ball or Roller Screws; Gear Boxes, Etc
848350	Flywheels and Pulleys, Including Pulley Blocks

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848360	Clutches and Shaft Couplings (Incl. Universal Joints)
850132	Dc Motors & Generators W Output > 750W; N Over 75 Kw
850133	Dc Motors & Generators W Output > 75Kw; N Over 375Kw
850520	Electromagnetic couplings, clutches and brakes
850590	Other Electromagnets and permanent magnets, including parts
851140	Internal Combustion Engine Starter Motors
851150	Internal Combustion Engine Generators, Nesoi
851180	Elect Ignition/Start Equipment for Spark/Comp Engine; Generator Nesoi
851190	Pts Elect Ignition/Start Equip; Generators & Cut-Outs
853710	Controls Etc W Elect Appr for Elect Cont Nov 1000 V
870810	Bumpers and Parts, for Motor Vehicles
870821	Safety Seat Belts for Motor Vehicles
870829	Parts & Accessories of Bodies of Motor Vehicles, Nesoi
870830	Brakes and Servo-Breaks; Parts Thereof
870870	Road Wheels & Pts & Accessories for Motor Vehicles
870891	Radiators for Motor Vehicles
870892	Mufflers and Exhaust Pipes for Motor Vehicles
870893	Clutches and Parts Thereof for Motor Vehicles
870895	Safety Airbags with Inflator System; Parts Thereof
870899	Parts and Accessories of Motor Vehicles, Nesoi
940120	Seats of a Kind Used for Motor Vehicles
940190	Parts of Seats (Ex Medical, Barber, Dental Etc)

- Category 3: Complementary Parts.
 - They will have to reach a maximum of 65% RVC, or under the Transaction Value of 75%, in 4 increments.

**TABLE C
COMPLEMENTARY PARTS FOR PASSENGER VEHICLES AND LIGHT TRUCKS**

HS 2012	DESCRIPTION
400912	Pipe, Not Reinforced/Comb. W/ Materials W/ Fittings
400922	Pipes, Vulc Rub, Reinforced/Combo With Metal,W/ Fitting
400932	Pipe of Vul Rub, Reinforced W/ Text Only Mat,W/Fittings
400942	Pipe, Reinforced/Comb W/Other Textile Mat,W/Fittings
830120	Locks of a Kind Used On Motor Vehicles, Base Metal
842139	Catalytic converters
848120	Valves for Oleohydraulic or Pneumatic Transmissions
848130	Check Valves
848180	Taps Cocks Etc for Pipe Vat Inc Thermo Control Nesoi
850110	Electric Motors of an Output Not Exceeding 37.5 W
850120	Universal Ac/Dc Motors of an Output > 37.5 W

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850131	Dc Motors & Generators W Output N Over 750 W
850720	Lead-Acid Storage Batteries Nesoi
850730	Nickel-Cadmium Storage Batteries
850740	Nickel-Iron Storage Batteries
850750	Nickel-metal Hydride Batteries
850780	Storage Batteries Nesoi
851130	Distributors; Ignition Coils
851220	Elect Lighting/Visual Signaling Equipment Ex for Bicycles
851240	Windshield Wiper Defroster & Demister for Cycle/Motor Vehicle
851981	Sound Recording/Reproducing App Magnetic/Optical/Semiconductor Nesoi
853650	Elect Switches for Voltage Not Over 1000 V, Nesoi
853690	Elect Apparatus for Protect to Elect Circuit Nov 1000 V Nesoi
853910	Sealed Beam Electric Lamp Units
853921	Tungsten Halogen Electric Filament Lamps
854430	Insulated Wiring Sets for Vehicles Ships Aircraft
903180	Measuring & Checking Instrument, Appliances & Mach Nesoi
903289	Auto Regulating Ins & Appr Ex Thermostat, Mnstat, Etc

🚗 Auto parts for heavy vehicles:

- Two categories are made:
 - Category 1: Essential Parts.
 - The RVC will be 70% or below the Transaction Value of 80%, in two increments.

TABLE D
PRINCIPAL PARTS FOR HEAVY TRUCKS

HS 2012	DESCRIPTION
840731	Spark-Ignition Piston Engine for Vehicle Ex Railway Not Over 50 Cc
840732	Spark-Ignition Reciprocating Piston Engine Etc Nov 250Cc
840733	Spark-Ignition Reciprocating Piston Engine Etc >250 Nov1000Cc
840734	Spark-Ignition Reciprocating Piston Engine Etc > 1000 Cc
840820	Compression-Ignition Internal Combustion Piston Engine Etc
840991	Spark-Ignition Internal Combustion Piston Engine Parts Nesoi
840999	Spark-Ignition Reciprocating Internal Combustion Piston Engine Parts
841330	Fuel, Lub/Cooling Med Pumps for Internal Comb Piston Engine
841459	Fans, Nesoi (turbochargers and superchargers)
841480	Air/Gas Pumps, Compressors and Fans Etc, Nesoi
841520	Automotive Air Conditioners
848280	Other Ball or Roll Bearings, Inc Comb Ball/Roll Bearings
848310	Transmission Shafts (Inc Cam-& Crank-Shaft), Etc.

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848340	Gears; Ball or Roller Screws; Gear Boxes, Etc
848350	Flywheels and Pulleys, Including Pulley Blocks
850132	Dc Motors & Generators W Output > 750W; N Over 75 Kw
850133	Dc Motors & Generators W Output > 75Kw; N Over 375Kw
851140	Internal Combustion Engine Starter Motors
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870850	Drive Axles with Differential for Motor Vehicles
870870	Road Wheels & Pts & Accessories for Motor Vehicles
870880	Suspension Shock Absorbers for Motor Vehicles
870891	Radiators for Motor Vehicles
870892	Mufflers and Exhaust Pipes for Motor Vehicles
870893	Clutches and Parts Thereof for Motor Vehicles
870894	Steering Wheels, Columns & Boxes for Motor Vehicles
870895	Safety Airbags with Inflator System; Parts Thereof
870899	Parts and Accessories of Motor Vehicles, Nesoi
940120	Seats of a Kind Used for Motor Vehicles

- Category 2: Complementary Parts.
 - El The RVC of 60% or under the Transaction Value of 70%

TABLE E
COMPLEMENTARY PARTS FOR HEAVY TRUCKS

HS 2012	DESCRIPTION
841350	Hydraulic Fluid power Pumps
847989	Electronic brake systems incl. ABS and ESC systems
848210	Ball Bearings
848220	Tapered Roll Bearings, Including Cone & Roller Assemblies
848230	Spherical Roller Bearings
848240	Needle Roller Bearings
848250	Cylindrical Roller Bearing Nesoi
848320	Housed Bearings, Incorp Ball or Roller Bearings
848330	Bearing Housings; Plain Shaft Bearings
848360	Clutches and Shaft Couplings (Incl. Universal Joints)

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850520	Electromagnetic couplings, clutches and brakes
850590	Other Electromagnets and permanent magnets, including parts
850760	Lithium Ion Batteries
851180	Elect Ignition/Start Equipment for Spark/Comp Engine; Generator Nesoi
851190	Pts Elect Ignition/Start Equip; Generators & Cut-Outs

Additionally, the following chapters should be observed:

 **Customs and Trade Facilitation**

- It incorporates provisions on customs cooperation and enforcement, including:
 - Regional and bilateral cooperation, to improve coordination between customs and promote initiatives to detect and prevent customs offences.
 - Exchange of information to prevent customs crimes.
 - Verifications through collaboration between customs authorities to obtain documents and carry out visits to companies.

 **Investment:**

- It is divided in two sections:
 - The first contains the disciplines on the protection of foreign investment.
 - The second contains the investment arbitration mechanism (Investor-State)
- Investors in any sector may have recourse to an arbitration procedure in case of violations in the disciplines: National Treatment, Most Favored Nation Treatment, Direct Expropriation.
- The Investor-State dispute settlement mechanism does not apply to Canada.


 **Labor:**

- Specific provisions are included for Mexico on collective bargaining, which seek to guarantee this right.
- Cases of sustained or recurrent action or inaction in the application of labor law by a government will be subject to the dispute resolution mechanism.
- The Protocol of Amendment establishes that:
 - Language that made it difficult to prove that business partners were not committed to protecting workers from workplace violence was removed.
 - It creates a presumption that a labor violation affects trade and investment, so the other government must prove otherwise.
 - In order to ensure that the U.S. government will effectively monitor compliance with labor obligations in Mexico:
 - A committee is created to oversee the implementation of labor reform and compliance in Mexico.
 - There will be labor attachés in Mexico in order to have real information on labor practices.

- Rapid response mechanism for the settlement of labour disputes entering into force immediately. This mechanism provides for the establishment of panels of experts on labor matters in the event that a Party believes that a Covered Plant (Plant) is denying workers' rights relating to union elections and collective bargaining.
- It will apply to plants in the manufacturing, service and mining sectors. It will have a short time period established to issue a resolution.
- Sanctions may include the suspension of preferential tariff treatment for goods manufactured in the defendant company or the imposition of sanctions on goods manufactured or services provided by the defendant company.
- In cases where a company incurs at least two denials of duties, sanctions may include the suspension of preferential tariff treatment for such goods; the imposition of sanctions on such goods or services; or the denial of entry of such goods.

 Origin Procedures:

- The certificate of origin may be issued by the exporter, producer or importer.
- The format of the certificate is eliminated and certification is allowed on the invoice or on any commercial document, provided that minimum information is declared.
- In the event that importers fail to comply with the stipulations regarding the origin of the goods, each country will determine whether to apply a civil, criminal or administrative sanction.

 Intellectual Property:

- The authorities may detain goods suspected of being counterfeit on any entry or exit from the country.
- Implementation of measures against counterfeit goods and piracy on a commercial scale.

Fuente:

1. <https://www.gob.mx/tlcan/acciones-y-programas/resultados-de-la-modernizacion-del-acuerdo-comercial-entre-mexico-estados-unidos-y-canada?state=published>
2. <https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/united-states-mexico>
3. <https://www.whitecase.com/publications/alert/united-states-canada-and-mexico-announce-new-trilateral-trade-agreement-replace>
4. IQOM
5. Industria Nacional de Autopartes, A.C.



MARCANDO EL PASO

— EN EL CUMPLIMIENTO DEL —

COMERCIO EXTERIOR

Y ADUANAS



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