

LEARN ABOUT THE IMPACT AND
THE RECOMMENDATIONS
FOR THE
FOOTWEAR SECTOR

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Footwear Sector

The so-called United States - Mexico - Canada Agreement (USMCA) represents an agreement in principle that concludes the renegotiation of NAFTA, which began in August 2017. Although the USMCA has been described as a new trade agreement to replace the North American Free Trade Agreement (NAFTA), many of its chapters cover virtually the same issues, many of the provisions remain unchanged.

Although attention has focused on changes in the rules of origin for the automotive sector, which generates a large part of Mexico's exports to the United States (US), other branches of manufacturing activity also have changes aimed at increasing the regional content in their manufacture.

It establishes significant changes in the rules governing trade between the three countries, changes that involve an adjustment in the supply chains of several industries, including automotive, agriculture, textiles and clothing, alcoholic beverages, medical devices, and chemicals. As long as the regional content is met, products can be traded free of quotas and tariffs between the three partners.

The USMCA is an agreement comprising 34 chapters, 13 annexes and 13 parallel letters, which contain details of the new rules. It is expected to enter into force on July 1, 2020. In the meantime, NAFTA will continue to apply to trade between the three countries.

Among the important changes established by the USMCA, is the increase in the required level of regional content of automobiles and auto parts to export duty-free cars to the U.S. Canada also made concessions, by opening a part of its dairy market to U.S. imports. In the oil and gas industry, Canada will no longer be subject to the proportionality provisions in the energy chapter of NAFTA.

Overall, the USMCA appears to meet the objectives set by the U.S. government. Most importantly, it puts an end to the uncertainty caused. If ratified, the agreement will maintain the three linked economies for at least the next 16 years.

The specific rules of origin for footwear are contained in *Chapter 4: USMCA Rules of Origin and Specific Rules of Origin*. It is important to note that not all of the Specific Rules of Origin were updated, however, according to the Secretariat of Economy, the objective of the chapter was to modernize the rules of origin to make them compatible with more modern disciplines, which Mexico has already negotiated in other Agreements.

Specifically, some modifications were related to the following issues:

- De Minimis. Taking into account that global value chains have become an essential feature of our economic reality, in order to provide the necessary balance required by companies to access a global supply of inputs, and at the same time, encourage the use of components from the region, the provision on De Minimis was updated to increase the current percentage to 10%, which corresponds to that established with the rest of our trading partners.

- Games or Assortments. Also, taking into account that there is a trend towards presenting goods in game or assortment, where it has become an increasingly common marketing strategy, new provisions related to games and assortments were incorporated.
- Principle or Clause on "accumulation", which allows to recognize as original both the materials of the signatory countries and the processes carried out in any of their territories. With this, regional value chains are strengthened.

For the footwear industry, the new agreement is very similar to the previous one, according to the US Footwear Distributors Association. (FDRA). The FDRA has pushed in the past for more flexible rules of origin, which was not on the table in recent negotiations.

Nevertheless, it is important to review the Rules of Origin for each product, as well as changes in the methodology for calculating Regional Content Value (RCC).

The USMCA was signed on 30 November 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 United States-Mexico and Canada Agreement (USMCA).

In response to the demands of the Democrats in the U.S. House of Representatives and the American unions, the Modifying Protocol 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 of Amendment to the United States-Mexico-Canada Agreement (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 July 1.

A. 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: Goods Wholly Obtained or Produced
- Article 4.4: Treatment of Recovered Materials Used in the Production of Remanufactured Goods
- Article 4.5: Regional Content Value
- Article 4.6: Value of Materials Used in Production
- Article 4.7: Additional 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: De Minimis
- Article 4.13: Goods or Fungible Materials
- Article 4.14: Accessories, Spare Parts, Tools and Instructional Materials or Other Information
- Article 4.15: Packaging Materials and Retail Packaging
- Article 4.16: Packing Materials and Shipping Containers
- Article 4.17: Sets of Goods
- Article 4.18: Transit and Transshipment
- Article 4.19: Non-Origin Transactions
 - Annex 4-A: Exceptions to Article 4.12 De Minimis
 - Annex 4-B: Product Specific Rules of Origin
 - Appendix to Annex 4-B: Provisions Relating to the Rules of Origin Specific to Automotive Goods.


Article 4.5: Regional Content Value:

- 1. Except for paragraph 6, each Party shall provide that the regional content value of a good shall be calculated, at the option of the importer, exporter or producer of the good, under the transaction value method set out in paragraph 2 or the net cost method set out in paragraph 3.
- 2. Each Party shall provide that an importer, exporter or producer may calculate the regional content value of the good under the following transaction value method:
 - $VCR = (VT - VMNO) / VT \times 100$
 - In which:
 - VCR is the regional content value, expressed as a percentage;
 - VT is the transaction value of the goods, adjusted to exclude any costs incurred in the international shipment of the goods; and


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- 8. For the purposes of the net cost calculation set out in paragraph 3, the producer may:
 - (a) calculate the total cost incurred in respect of all goods produced by that producer, discounting any costs of sales promotion, marketing, after-sales services, royalties, shipping and packaging, as well as any ineligible financing costs included in the total cost of all such goods, and reasonably allocate the resulting net cost of those goods to the merchandise,
 - (b) calculate the total cost incurred in respect of all goods produced by that producer by reasonably allocating the total cost to the goods and discounting the costs of sales promotion, marketing, after-sales services, royalties, shipping and packaging, and ineligible financing costs, included in the portion of the total cost allocated to the goods; or
 - (c) to reasonably allocate each cost that is part of the total cost incurred with respect to the merchandise so that the sum of these costs does not include any costs for sales promotion, marketing, after-sales services, royalties, shipping and packaging, and ineligible financing costs,

provided that the allocation of such costs is consistent with the provisions on reasonable cost allocation set out in the Uniform Regulations

 Article 4.11: Accumulation:

- 1. Each Party shall provide that a good is originating if the good is produced in the territory of one or more of the Parties by one or more producers, provided that the good meets the requirements set out in Article 4.2 (Originating Goods) and all other applicable requirements of this Chapter.
- 2. Each Party shall provide that a good or material originating in one or more of the Parties shall be considered to be originating in the territory of another Party when used as material in the production of a good in the territory of another Party.
- 3. Each Party shall provide that production carried out on non-originating material in the territory of one or more of the Parties may contribute to the originating content of a good, whether or not such production was sufficient to confer originating status on the material itself.

 Article 4.12: De Minimis:

- Except as provided in Annex 4-A (Exceptions to Article 4.12 (De Minimis)), each Party shall provide that a good is an originating good if the value of all non-originating materials used in the production of the good that do not meet the applicable change in tariff classification requirement set out in Annex 4-B (Product Specific Rules of Origin) does not exceed 10 percent:
 - (a) from the transaction value of the goods adjusted to exclude any costs incurred in the international shipment of the goods or

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- (bof the total cost of the goods,
 - provided that the goods satisfy all other applicable requirements of this Chapter
- 2. If a good described in paragraph 1 is also subject to a value regional content requirement, the value of those non-originating materials shall be included in the value of the non-originating materials for the applicable value regional content requirement.
- 3. A good subject to a regional value content requirement shall not be required to satisfy the requirement if the value of all non-originating materials used in the production of the good does not exceed 10 percent of the transaction value of the good, adjusted to exclude any costs incurred in shipping the good internationally, or the total cost of the good, provided that the good satisfies all other applicable requirements of this Chapter.
- 4. Regarding a textile or clothing good, Article 6.1.2 through 6.1.3 applies instead of paragraph 1.

 Annex 4-B – Product Specific Rules of Origin:

Chapter 64 Footwear, gaiters and the like; parts of such articles

64.01 - 64.05	A change to heading 64.01 through 64.05 of any heading outside the group, other than that of subheading 6406.10, complying with a regional content of not less than 55 percent under the net cost method.
6406.10	A change to subheading 6406.10 from any other subheading, except from heading 64.01 through 64.05, complying with a regional content of not less than 55 percent under the net cost method.
6406.20 - 6406.90	A change to subheading 6406.20 through 6406.90 from any other chapter.

The current NAFTA ROE's for footwear are:


Chapter 64 Footwear, gaiters and the like; parts of such articles

64.01 a 64.05	A change to heading 64.01 through 64.05 of any heading outside the group, other than that of subheading 6406.10, complying with a regional content of not less than 55 percent under the net cost method.
6406.10	A change to subheading 6406.10 from any other subheading, except from heading 64.01 through 64.05,

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	complying with a regional content of not less than 55 percent under the net cost method.
6406.20 a 6406.99	A change to subheading 6406.20 through 6406.99 from any other chapter.

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 offences.
 - Verifications through collaboration between customs authorities to obtain documents and carry out visits to companies.
 - Establishment of a Customs Sub-Committee, which will address issues of potential or actual customs offences, as well as discuss joint initiatives on issues of mutual concern.

 **Public Sector Purchases:**

- The Mexico-Canada relationship will be governed by the provisions of the CPTPP once it enters into force.
- Disciplines are established between Mexico and the US, in particular:
 - The obligation to define purchasing requirements on the basis of objective and international criteria and not with the aim of creating unnecessary obstacles to trade between the Parties is maintained.
 - The obligation not to impose countervailing conditions on covered purchases, such as local content requirements, is maintained.
 - The power of entities to disqualify suppliers for matters such as bankruptcy, false declarations or disqualifications for poor performance in the performance of a government contract is recognized.

 **Investment:**

- It is divided into 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 states:

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- 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.
- Quick 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.

 Environment:

- Some harmful fisheries subsidies, mainly to vessels and operators involved in poaching and illegal fishing, are prohibited.
- Includes a commitment to prevent and reduce marine debris, promote sustainable forest management, and prevent commercial whaling.
- Intentional transnational trafficking in protected wildlife species is criminalized as a serious offence.
- Robust and modern mechanisms for public participation and environmental cooperation
- Disciplines that seek to improve the effectiveness of customs inspections of shipments containing wildlife at ports of entry.
- Disciplines are established to protect air quality, and ensure appropriate procedures for environmental impact assessments
- Cases of sustained or recurrent action or inaction in the enforcement of labor laws by a government will be subject to the dispute resolution mechanism.
- The Protocol of Amendment:
 - It creates a presumption that an environmental violation affects trade and investment, so the other government must prove otherwise.
 - The Montreal Protocol is covered.

- A commitment is added that all Parties will adopt, implement and maintain 7 multilateral environmental agreements, other agreements may be added to the list. Non-compliance with any of these agreements will be subject to the State-State dispute settlement mechanism, which could lead to the eventual adoption of retaliation.
- A committee is created to monitor the implementation of the obligations acquired in the agreements, as well as the recommendations. It will be the platform through which the American government will coordinate its support and financing of projects to implement the best practices in environmental matters.
- There will be environmental attachés in Mexico in order to have real information about regulations and practices.
- It adds a new customs verification mechanism to guarantee that only legally harvested and taken flora and fauna are traded through Mexico.
- A new North American Development Bank authorization and funding for EPA, loans under the Border Water Infrastructure Program to address pollution on the U.S.-Mexico border; and additional funds to the Trade Control Trust Fund to be used for focused environmental efforts.

 **Technical Barriers to Trade:**

- It incorporates provisions relating to the transparency of the processes of elaboration, adoption and application of the standards, technical regulations and conformity assessment procedures of the Parties.
- Provisions for the conclusion of mutual recognition agreements.

 **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:**

- Strengthen the system of protection of geographical indications.
- Disciplines are foreseen for well-known trademarks.
- The authorities may detain goods suspected of being counterfeited at any entry or exit to the country.
- Implementation of measures against counterfeit goods and piracy on a commercial scale.

 **Commercial Remedies:**

- Safeguards: an exclusion for partners subject to certain conditions (not being in the first 5 exporters) from the overall safeguard measures is maintained.
- Anti-dumping and subsidies: WTO rights are recognised in these areas. Additional rules were agreed to promote transparency.
- Combating circumvention: a cooperation mechanism is established to prevent the evasion of countervailing, anti-dumping and safeguard duties.

- Binational panels: the NAFTA Chapter XIX mechanism is maintained.

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