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NAFTA RENEGOTIATION STARTING — COMPANIES DOING BUSINESS IN THE UNITED STATES, CANADA, AND MEXICO SHOULD TAKE NOTICE

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The Office of the United States Trade Representative (USTR) has requested public comments on the Trump Administration's intent to renegotiate the North American Free Trade Agreement (NAFTA) with Mexico and Canada. Comments are due by no later than June 12, 2017. Additionally, USTR has set June 27, 2017 for a public hearing, at the U.S. International Trade Commission, on the Administration's renegotiation objectives. Requests to appear at the hearing likewise are due on June 12.

The Administration's decision to renegotiate the NAFTA follows the much-publicized events of the week of April 24, during which President Trump put forth a formal notice of U.S. withdrawal from NAFTA pursuant to Article 2205 of the Agreement. Strong opposition from U.S. agricultural interests, as well as urgent phone calls from President Nieto of Mexico and Prime Minister Trudeau of Canada, reportedly were decisive in reversing the President's course.

Background

On May 18, 2017, the newly confirmed U.S. Trade Representative (USTR) Robert Lighthizer formally notified Congress of the Trump Administration's intent to renegotiate the North American Free Trade Agreement (NAFTA) with Mexico and Canada. Ambassador Lighthizer' s notice triggered the 90-day Congressional consultation period required by the Bipartisan Congressional Trade Priorities and Accountability Act of 2015 (TPA Act). In particular, the TPA Act requires the President to give Congress written notice at least 90 calendar days before initiating trade negotiations with other countries. This period is designed to allow the Executive Branch and the Congress to consult fully regarding U.S. negotiating priorities, so they are on the same page.

USTR's notice does not itself contain specific details on what changes the Administration plans to make, but simply indicates its objective to "modernize the agreement" by implementing changes that support economic growth. Although USTR circulated a draft NAFTA renegotiation notice back in late March – setting forth detailed proposals for U.S. negotiating objectives – that draft was scrapped in favor of a more limited, straightforward notification that simply states that the Administration plans to initiate negotiations with Mexico and Canada. Congressional trade staffers say that there were concerns on Capitol Hill about certain proposed objectives in the March draft;

that others identified by Congress in the TPA Act were missing; and that others had been re-worded in ways that raised potential concerns for certain Members. We expect these concerns to be taken up with the Administration during the 90-day consultation period. Such consultations are not a formality, as the Administration needs Congress on board if it wants Congress to eventually approve its updated NAFTA agreement.

The Trump Administration has insisted that negotiations will conclude by the end of 2017. This timetable is ambitious, particularly since formal negotiation between the three NAFTA parties cannot commence until the end of August 2017, after the conclusion of the 90-day consultation period. While USTR could try to initiate "informal" negotiations in the interim in order to jump start the talks, this might produce a Congressional backlash, particularly since there remains disagreement about the appropriate negotiating objectives.

In the period leading up to the notification, Ambassador Lighthizer and Commerce Secretary Wilbur Ross met with the House Ways and Means and Senate Finance Committees, the House Congressional Oversight Group (COGs), and the Senate Advisory Group on Negotiations (SAGON) to brief them on the proposed notification. They are scheduled to hold further closed-door meetings with members of the Senate Finance and the House Ways and Means Committees.

House Ways and Means Committee Chairman Kevin Brady released the following statement in response to the Administration's official step towards negotiation:

"There is no question that NAFTA has been tremendously successful for American workers, farmers, and businesses. The United States enjoys a tremendous advantage through our NAFTA supply chain, for example, which allows us to partner with Canada and Mexico to create an integrated production base that improves our competitive edge against China and other competitors. However, it is time to update and improve this 20-year-old agreement to ensure that NAFTA continues to open more markets for American manufactured goods, agricultural products, and services and that it better reflects our needs in the 21st century."

Industry Impacts

President Trump has referred to NAFTA as one of the "worst" trade deals in history, and the Administration's threats to terminate the agreement have sent unsettling waves throughout various U.S. industries. The White House's decision to renegotiate NAFTA could result in a significant blow to the American agricultural industry, as Mexico and Canada are major markets for U.S. farm and food products. U.S. agriculture groups have urged the Administration to "do no harm" by maintaining tariffs at zero and to refrain from implementing polices that will disrupt trade. Specifically, they are emphasizing that an updated NAFTA should in no way undermine the preferential treatment bestowed to producers in North America under the agreement.

For their part, U.S. business groups, including the Business Roundtable, have stated that NAFTA could use some improvements and have welcomed renegotiation. For some stakeholders, the renegotiation of NAFTA presents an opportunity to address digital trade issues (e.g., cross-border data flows), state-owned enterprises, sanitary and phyto-sanitary rules, customs procedures, investment standards and dispute resolution, and financial services. Other interest groups, including the United Steelworkers, have insisted that labor and environmental protections should be incorporated in a new NAFTA. In particular, these groups have requested that the

Administration adopt a framework that will safeguard against labor and environmental violations and ensure timely remedies for such violations.

While the U.S. business community has been less vocal – perhaps fearing adverse publicity – many major U.S. companies have highly integrated North American supply chains. Accordingly, they could face major production disruptions, higher costs, and the loss of access to Mexican and Canadian export markets if the negotiations go awry.

What steps could the Trump Administration take?

There is considerable speculation surrounding the Trump Administration's approach and true objectives in renegotiating the Agreement. There are multiple potential scenarios. First, President Trump could use fast track/TPA to initiate a radical overhaul of the NAFTA. The Administration might take the view that this approach is authorized under Section 151 of the Trade Act of 1974, and this approach likely accords with the goals of Trump's Commerce and USTR teams. One goal of the Administration is to eliminate NAFTA Chapter 19's Binational Panel review of U.S. antidumping and countervailing duty (AD/CVD) decisions, which has been blamed for interfering with U.S. AD/CVD orders. Canada and Mexico have not taken a public position on this important, sensitive issue, which was the very last to be resolved in the U.S.-Canada FTA negotiations.

A second approach would be for the Administration to incorporate provisions of the Trans-Pacific Partnership (TPP) into the new NAFTA. This would facilitate cross-border data flows, and incorporate progressive environmental and labor protections not found in the original agreement. Such an approach would update and expand NAFTA, but would be open to anti-trade political attacks from Democrats and organized labor as "NAFTA on steroids."

Lastly, the Trump Administration could seek to negotiate a modestly updated NAFTA that the President could seek to implement without congressional approval. This would require less political lifting than the formally mentioned approaches, but such a moderate approach – likely not producing a wholesale rollback of NAFTA – could be inconsistent with the goals of some Trump campaign supporters and thus could carry political risk to the Administration.

The bottom line is that renegotiating NAFTA will present significant policy and political challenges for President Trump, as he will be forced to balance the competing and contradictory interests of his political base. The President won the 2016 election by cobbling together a unique coalition of, among others, (1) blue-collar workers from the Northern and Midwestern industrial states, who were drawn by his anti-trade and anti-immigration messages, and (2) rural voters, who opposed Obama-era regulations on the environment and land use, and who supported Trump's outspoken stances on social and cultural issues (e.g., gun control and abortion). However, U.S. farmers could be deeply harmed by trade restrictions, and are already being hurt by limits on immigrant labor. Mexico and Canada are huge export markets for U.S. agricultural products, and the loss of U.S. access could send U.S. exports and commodity prices into an even steeper decline. At the same time, Trump must meet the expectations of his blue-collar constituents who blame NAFTA for the loss of U.S. jobs and factories.

Finally, any "new NAFTA" requires striking a deal with Canada and Mexico, both of whom have highly capable trade negotiators with extensive experience dealing with U.S. trade demands and who understand the Administration's political pressure points. Mexico and Canada have political constraints of their own, and both countries have their own offensive agendas in the negotiations. While it is true that both run trade surpluses with the United States and stand to lose somewhat more economically if NAFTA is terminated, the reality is that trade wars do not have winners. There are only losers, as terminating NAFTA would cost exports and hundreds of thousands of jobs throughout North America, including in the United States.

In short, President Trump must find a deal that (1) can be negotiated with Canada and Mexico, (2) straddles the conflicting demands of his blue-collar and rural constituencies, and (3) can pass the Congress under the TPA procedures, if it is to achieve the ambitious revisions sought by the team being led by USTR Lighthizer and Secretary Ross, thereby requiring changes to U.S. law. This will not be easy.

Suggested Actions

Companies should monitor the NAFTA negotiations themselves or through trade counsel. It is also advisable for companies to participate actively, either individually or through trade associations, in the negotiations to ensure that their positions and interests are considered and taken into account.

Specifically, Companies interested in providing comments by June 12, 2017 on the Trump Administration's intent to renegotiate the NAFTA should start assessing their interests immediately.

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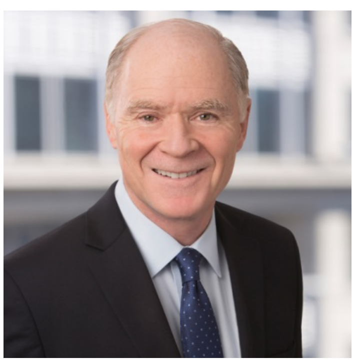

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