

# Intelligence MEMOS



From: Jon Johnson  
To: Global Affairs Canada and the European Parliament  
Date: January 02, 2019  
Re: **DOES THE USMCA COMPLY WITH WTO REQUIREMENTS?**

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In a recent [report](#), the European Parliamentary Research Service questions whether the new North American free trade agreement liberalizes “substantially all trade” among the USMCA parties as required by Article XXIV of GATT 1994, the WTO provision governing free trade areas.

The report also states that certain USMCA provisions risk being at odds with the prohibition of voluntary export restraints under the WTO Safeguards Agreement.

A Canada/US side letter to the USMCA provides that any tariffs applied to automotive goods by the US under Section 232 of the *Trade Expansion Act* of 1962 will not apply to annual imports from Canada of 2.6 million passenger vehicles, and imports from Canada of light trucks and certain volumes of automotive parts. Mexico and the US signed a similar side letter.

The side letters are not voluntary restraint agreements as they are undertakings by the US and not of Canada and Mexico. However, if the US decides to impose Section 232 tariffs on automotive goods from Canada and Mexico, trade in automotive goods among the USMCA countries will be subject to a major new trade barrier. While light trucks and certain volumes of passenger vehicles and parts will be exempt, the side letters do not exempt heavy trucks or specialty vehicles. The USMCA will not liberalize “substantially all trade” among the USMCA parties if the US imposes Section 232 tariffs on automotive goods because the side letters have the effect of setting caps on the growth of the Canadian and Mexican automotive industries.

The report also maintains that the USMCA regional sourcing provision for steel and aluminum “appears to be a local content requirement” that is difficult to justify under WTO national treatment and MFN obligations. Most vehicles will be considered originating and eligible for duty free treatment only if at least 70 percent of the steel and aluminum purchased by the producer originates in the US, Canada or Mexico.

While rules of origin in free trade agreements are content requirements, they do not offend WTO prohibitions because the required content can come from anywhere in the free trade area.

Rules of origin based on prescribed changes in tariff classification routinely require that certain materials must originate in the free trade area. The USMCA (and NAFTA) rule for rear-view mirrors requires that the glass used to make the mirror originate in a USMCA country. Subject only to a 10 percent *de minimis* provision, the rule prohibiting non-originating glass is absolute. The USMCA steel and aluminum rule provides for latitude of 30 percent.

However, this brings us back to the question of whether the USMCA meets the requirement of liberalizing “substantially all trade” among the USMCA parties. As the report points out, imports of steel and aluminum into the US from both Canada and Mexico are subject to Section 232 tariffs of 25 percent (steel) and 10 percent (aluminum). While steel purchased by a US vehicle producer from a supplier in Canada or Mexico counts towards satisfying the 70 percent originating content requirement, the 25 percent tariff will drive the producer to fulfilling its 70 percent requirement by purchasing steel only in the US.

If Section 232 tariffs are imposed on automotive goods, and so long as Section 232 tariffs continue to be imposed on steel and aluminum, the USMCA may be open to challenge as not liberalizing “substantially all trade” among the USMCA parties as WTO rules require.

However, it is debatable whether any WTO action would go beyond critical comments from the WTO working party constituted to examine the USMCA that will probably have no practical effect. However, the 70 percent steel and aluminum requirement demanded by the US negotiators, coupled with the cynical US decision to not exempt Canada and Mexico from the Section 232 tariffs imposed on these materials, has met with considerable opposition in Congress, as well as by organizations such as the US Chamber of Commerce. This glaring failure to liberalize trade could imperil the USMCA receiving the required congressional approval that it needs to go into effect.

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