

What is next for NAFTA?

The North American Free Trade Agreement (NAFTA) among the US, Canada and Mexico entered into force on 1 January 1994, and created one of the world's largest free trade areas. One of the first comprehensive free trade agreements worldwide, NAFTA set a valuable example for other free trade agreements for countries around the world.

Under NAFTA, import duties on all covered goods traded within the US, Canada and Mexico were gradually phased out and, as scheduled, on 1 January 2008, all remaining duties and quantitative restrictions were eliminated.

Products manufactured in any NAFTA country that meet the applicable rules of origin established under NAFTA may be considered "NAFTA originating" and thus can be imported into any NAFTA country without payment of duties. This has led to a high degree of integration in the industrial production chains of items that are manufactured and sold in the US, Canada and Mexico, and also for products that are exported from North America to the rest of the world.

Based on statements during the campaign and since the election, the incoming administration intends to pursue an aggressive series of amendments to

NAFTA or even the complete withdrawal from the agreement. While no concrete proposals for potential amendments have been put forward yet, we are including some thoughts on the various alternatives to amend NAFTA or to withdraw from the agreement entirely.

Established structure for amendments

One option for the incoming administration would be to take advantage of existing structures and procedures for proposing changes. While NAFTA itself has not been subject to substantial amendments since its entry into force, there are some examples of modifications to the agreement reflecting decisions reached by all three countries through the NAFTA Free Trade Commission.

NAFTA's Article 2001 establishes the Free Trade Commission, which is comprised of officials responsible for foreign trade from each NAFTA country (the US Trade Representative, Canada's Minister of International Trade and Mexico's Secretary of Economy). Its purpose is to supervise the implementation and interpretation of the agreement and solve any disputes from differences of interpretation.





The Free Trade Commission supervises the various committees and working groups established under NAFTA (i.e., those established under Annex 2001.2 including committees on trade in goods, agricultural trade and rules of origin, among others).

Throughout the years, the Free Trade Commission has adopted modifications to NAFTA, for instance liberalizing the rules of origin or amending procedures for binational panel reviews, which are then implemented through local legislation. The implementation requirements may vary by country. For example, in Mexico, in order for the modifications to enter into force the executive branch of the government, usually through the Ministry of Economy, publishes an "Accord in the Mexican Official Journal," which makes the amendments official. In the US, the proposed amendments follow the rulemaking process until the corresponding NAFTA implementing regulations are published in the Federal Register.

As such, there is an established structure under NAFTA that has acted as the vehicle for negotiations among the NAFTA countries and for implementing amendments to adjust the agreement. While the potential negotiations could be undertaken at the cabinet level and be performed directly between the representatives of the NAFTA parties, the Free Trade Commission could be a useful mechanism to discuss potential amendments.

Comprehensive negotiations

While the NAFTA Free Trade Commission has enacted modifications to the agreement, these have not included major changes or additions to the original text of the agreement. In fact, the Free Trade Commission is in charge of overseeing NAFTA's further elaboration, which may be interpreted as allowing the Free Trade Commission to enact more significant changes or even additions to the original text of the agreement.

If this is not the case, the NAFTA parties may, under NAFTA's Article 2202, agree on any modifications or additions to the agreement that will have to be subject to approval in accordance with the applicable legal procedures of each country.

Under the Article 2202 alternative, negotiations could be undertaken directly among the US, Canadian and Mexican governments without using the Free Trade Commission. If negotiations are performed under this alternative, any amendments made to NAFTA will likely have to follow the applicable legal procedures in each of the countries, which may lead to requiring domestic legislative approval and delay the implementation of potential amendments. In the United States, modifications to the agreement itself would likely involve amendment to existing legislation (for example, the North American Free Trade Agreement Implementation Act, as discussed below). This would require congressional action and presidential signature to take effect.

Withdrawal

Under Article 2205, any country may withdraw from NAFTA six months after it provides written notice of withdrawal to the other NAFTA countries. If one of the countries withdraws, the agreement would remain in force for the remaining countries.

Under US law, the President would likely have the sole power to issue such a notice, without requiring congressional approval or acquiescence. Although a trade agreement like NAFTA has not been terminated in more than 100 years in the United States, principles of US constitutional law suggest that the President's authority to terminate an executive agreement such as NAFTA is relatively unrestricted. For example, prior presidents have unilaterally terminated a mutual defense treaty with Taiwan and ended US accession to the Anti-Ballistic Missile Treaty. At the very least, even if the president issued an Article 2205 notice and a party brought a legal challenge, a US court would be unlikely to issue a ruling because the dispute would be considered a political question rather than a legal one.

Importantly, NAFTA was implemented in US law through the North American Free Trade Agreement Implementation Act of 1993. This nearly 200-page text made NAFTA-related changes to US law that would require further congressional action to change; in other words, a presidential withdrawal from NAFTA as an agreement among the three countries would not automatically repeal the implementation act as a matter of US law, there would need to be parallel action taken by Congress. The implications of this possible discontinuity between a terminated international agreement and existing domestic legal provisions could lead to uncertainty, especially in the short term.

Preparing for change

With amendment of NAFTA likely to be proposed early in the new Trump administration, business would be well-served by considering specific types of amendments that may be beneficial. For example, product-specific rules of origin may be changed that could impact qualification for duty-free treatment. NAFTA Article 303, which restricts drawback and use of duty deferral programs for goods traded among the NAFTA countries, has been identified by some companies as unfairly restricting trade. No process has yet been announced to allow business input into any proposals that the US may make to amend NAFTA, and as the time frame for any input may be short, businesses may be well advised to put together a NAFTA "wish list" that can be quickly shared if the opportunity arises.

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