



United States-Mexico-Canada Agreement (USMCA)

Center Forward Basics

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Overview

The United States-Mexico-Canada Agreement (USMCA), enacted in 2020 to replace NAFTA, aims to bolster trade and enhance relationships among North America's major economies. With 34 chapters and 12 side letters, the USMCA encompasses various components aimed at fostering regional cooperation and economic growth, including provisions on market access, intellectual property rights, environmental protection, labor standards, digital trade, and sectoral annexes. Notably, it prioritizes labor reforms in Mexico and targets environmental issues such as illegal wildlife trafficking and marine litter. Additionally, the agreement strengthens intellectual property rights and imposes stricter rules on the automobile industry. Dispute settlement mechanisms ensure compliance, while the sunset clause necessitates periodic reviews. As trade and investment between the U.S., Mexico, and Canada continue to flourish under the USMCA, ongoing collaboration among member nations remains crucial for maximizing its benefits and ensuring adaptability to evolving economic, social, and political landscapes, positioning the agreement as a cornerstone of North American economic cooperation for the foreseeable future.

What is the USMCA?

The United States-Mexico-Canada Agreement is a free trade agreement signed in 2018 to replace NAFTA. Its enforcement began in 2020. This agreement aims to facilitate trade and foster relationships between the three major economies in North America. Pieces of the USMCA are designed to build upon NAFTA, including key components such as market access, intellectual property rights (IPR), environmental protection, labor standards, digital trade, sectoral annexes, a dispute settlement process, and a sunset clause.

The USMCA has various components aimed at fostering regional cooperation and economic growth. It ensures duty-free access for most goods traded among the member nations while tackling non-tariff barriers to trade, such as restrictive licensing, permitting, and unwarranted technical – consumer safety, environmental, and national security – barriers to trade. Notably, it prioritizes labor standards by mandating reforms in Mexico to enhance collective bargaining rights and improve working conditions, thereby promoting fair competition and discouraging labor exploitation. Environmental protection is also a key focus, with provisions targeting issues like illegal wildlife trafficking and marine litter, alongside commitments to sustainable forestry practices. Additionally, the agreement strengthens intellectual property rights (IPR), addresses digital trade challenges, and imposes stricter requirements on the automobile industry, particularly regarding regional manufacturing and high-wage labor. Unlike NAFTA, the USMCA introduces a sunset clause every six years, necessitating periodic reviews for potential updates to ensure its relevance amid evolving economic and social landscapes.

The USMCA also contains sectoral annexes on chemical substances, pharmaceuticals, and cosmetics. These annexes are additional rights and obligations that only apply to defined sectors; Chapter 12 of the USMCA outlines annexes for chemical substances, cosmetic products, information and communication technology, energy performance standards, medical devices,

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In order to meet our challenges we need to put aside the partisan bickering that has gridlocked Washington and come together to find common sense solutions.

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and pharmaceuticals. The goal is to promote enhanced regulatory compatibility and trade between the three parties with respect to those sectors, while recognizing the regulatory authority of each party. These annexes commit to building on existing extensive regulatory cooperation on chemicals, pharmaceuticals, and cosmetics and identify areas of focus for future cooperation. For example, the Annex on Chemical Substances, which was not a part of NAFTA, creates a regulatory system for chemicals used to produce semiconductors, high-capacity batteries (HCBs), pesticides and fertilizers, and automotive goods. The Annex eliminates many trade barriers for these products and encourages continued efforts for a clean energy future in North America.

Chapter 31 of the USMCA establishes a dispute settlement mechanism between the member nations, known as state-to-state complaints. This section allows parties to bring claims about another party violating labor provisions of the agreement before a panel of arbitrators. The rulings passed down by these panels are final. State-to-state disputes can range from disputing domestic measures which other parties feel violate the USMCA to suspected failure to carry out the obligations of the agreement. Additionally, the USMCA Chapter 10 provides review and dispute settlement procedures in antidumping and countervailing duty matters. States are also able to raise disputes with investors. Under NAFTA, investors or investments of one NAFTA party had the ability to sue another NAFTA party for claims such as fair and equitable treatment, national treatment, and confiscation without full market value compensation. However, the USMCA terminated these investor-state dispute settlements (ISDS) and instead created a special ISDS regime for American or Mexican investors in the oil and gas, power generation, telecommunications, transportation, or infrastructure industries who are party to a “covered” government contract in addition to a restricted ISDS structure for other investors.

The USMCA retains most of NAFTA’s chapters, including the dispute settlement structure, but it makes notable changes to provisions for market access for automotive and agriculture products, rules on investment, government procurement, and IPR, as well as to provisions regarding labor and the environment.

Through these components, the USMCA is an effort to advance the economic and political relationships between the U.S., Mexico, and Canada. It goes beyond NAFTA regarding new provisions such as digital trade, state-owned enterprises, and currency misalignment. Advocates also hope the agreement will promote economic growth and prosperity across the region.

USMCA since 2020

During the era of NAFTA and now into the time of the USMCA, trade between the U.S., Mexico, and Canada has significantly increased. U.S. total merchandise exports to Mexico and Canada increased from \$165.1 billion to \$680.8 billion (312%), while merchandise imports increased from \$178.4 billion to \$891.3 billion (400%) between 1994 and 2022. In 2022, the services trade surplus with USMCA partners was \$26.0 billion. By comparison, the U.S. merchandise trade deficit in 2022 reached a low of \$210.6 billion.

Another large part of the American bilateral relationships with USMCA partners has been foreign direct investment (FDI). The build-up of economic relationships under the USMCA has fostered an environment for investing between the agreement’s parties. The U.S. is the largest single investor in Canada with FDI stock reaching \$438.8 billion in 2022, up from \$96.6 billion in 1997. Investment from the U.S. represents about half of the total stock of FDI in Canada from global investors. The U.S. was the largest destination for Canada’s total FDI in 2022, with a stock of \$683.8 billion, a significant increase from \$78.6 billion in 1997. Similarly, the U.S. is the largest source of FDI in Mexico. The stock of U.S. FDI in Mexico increased from \$24.1 billion in 1997 to \$130.3 billion in 2022. Mexican FDI in the United States, while substantially lower than U.S. investment in Mexico, has also increased rapidly under NAFTA/USMCA, from \$4.1 billion in 1997 to \$54.0 billion in 2022. This is especially important as companies navigate reducing their exposure to China and continue on- and near-shoring efforts. FDI between USMCA parties allows the three economies to become more integrated and less reliant on Chinese investments in Mexican, Canadian, and American businesses.

While the USMCA has fostered trade, disputes have arisen between its parties. All three countries have utilized the USMCA dispute settlement process since 2020. The U.S. has initiated disputes with Canada over Canada’s administration of fourteen of its dairy tariff-rate quotas (TRQs) which, according to the U.S. Trade Representative, “deny the ability of U.S. dairy

farmers, workers, and exporters to utilize the TRQs and realize the full benefit of the USMCA.” Under a unique Facility-Specific Rapid Response Labor Mechanism, the U.S. has raised concerns about labor conditions in Mexico. This dispute settlement mechanism provides for quick enforcement of workers’ rights to free association and collective bargaining. Conversely, Mexico and Canada brought and won a dispute against the U.S. claiming certain American rules of origin on automotive vehicles were inconsistent with the USMCA.

Multiple disputes are ongoing, including in the areas of genetically engineered corn, dairy, and labor concerns at the San Martín Mine in Mexico. Panels usually take between six months and a year to issue their final reports, so these disputes are expected to be settled before the review of the agreement next year.

Mexico has yet to issue secondary regulations to fully implement its IPR obligations under the USMCA. This includes patent enforcement mechanisms and regulatory data protection for pharmaceuticals. A timely marketing authorization process and transparent public procurement system would incentivize the development of more robust supply chains within North America.

The COVID-19 pandemic prompted the parties of the USMCA to establish a special committee to enable timely cooperation to fortify supply chains during emergencies. The Sub-Committee on Emergency Response under the USMCA North American Competitiveness Committee, established in February 2023, is charged with coordinating efforts to maintain regional trade flows during emergency situations like the pandemic.

Future of USMCA

As previously mentioned, the USMCA includes a sunset clause. This means the parties to the agreement must review and decide whether or not to renew it every six years. In 2026, six years after the agreement entered into force, the parties will hold their first joint review. At the end of the review, the parties can decide to renew the USMCA for another six years. If one of the parties does not agree to a renewal, a joint renewal will be held every year for ten years. If the agreement reaches its sixteenth anniversary in 2036 without the confirmation of an extension, the agreement will conclude.

The future of the USMCA holds significant promise for the continued prosperity and integration of North American economies. As globalization and technological advancements reshape global trade dynamics, the USMCA's provisions on digital trade, IPR, and labor and environmental standards position the agreement as a modern framework capable of navigating these complexities. Moreover, the focus on regional manufacturing in industries like automobiles underscores a commitment to bolstering domestic production and job creation. As the agreement’s fourth anniversary approaches in July, ongoing collaboration among the member nations will be essential to maximizing the benefits of the agreement, while periodic reviews under the sunset clause aim to ensure its adaptability to evolving economic, social, and political realities. As such, the USMCA is poised to remain a cornerstone of North American economic cooperation, fostering stability and growth in the region for years to come.

Links to Other Resources

- Brookings – [Developments in USMCA dispute settlements](#)
- Brookings – [Strengthening USMCA and North America’s economic cooperation](#)
- Congressional Research Service – [U.S.-Mexico-Canada \(USMCA\) Trade Agreement](#)
- CUSMA Secretariat – [Chapter 31 \(Dispute Settlement\) Disputes](#)
- Department of Commerce – [USMCA New York State Fact Sheet](#)
- Embassy of Mexico – [USMCA Sunset Clause Review and Term Extension](#)
- Federal Reserve Bank of Dallas – [Mexico awaits ‘nearshoring’ shift as China boosts its direct investment](#)
- United States Trade Representative – [Chapter 31 Disputes](#)

- United States Trade Representative – [United States-Canada-Mexico Agreement](#)