

What To Expect From A Trump Trade Policy: Part 2

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In a recent article, we discussed several steps that President-elect Trump may take to shake up U.S. trade policy. In this piece, we discuss one of his priority initiatives: the pledge to renegotiate, or withdraw from, the North American Free Trade Agreement to get a better deal for U.S. workers. If the Trump administration follows through on this pledge, any one of a number of scenarios may emerge — from an expanded and modernized agreement, implying offensive opportunities for companies to formulate a wish-list agenda for the negotiations, to substantial supply chain and commercial disruption, implying defensive concerns on the part of affected businesses. Given the range of potential outcomes, companies should proactively review their NAFTA positioning and become embedded in the negotiating process early on in order to further and/or safeguard their commercial interests.

Pledges to renegotiate NAFTA are a recurring theme in presidential campaigns. For example, as a presidential candidate in the 2008 primary season, Barack Obama promised to use the “hammer of a potential opt-out” as leverage to renegotiate the agreement's terms. The Obama administration shelved that idea after the election as trade policy took a back seat to the financial crisis and the push for Obamacare. But there are signs that this time may be different, as the president-elect has kept trade issues at the forefront in the post-election period.

If the Trump administration decides to seek renegotiation with Canada and Mexico, revisions and updates to NAFTA could be numerous. In one possible scenario, the changes could benefit a broad array of U.S. companies by substantially updating and expanding its reach.[1] For example:

- **Intellectual Property:** NAFTA's IP provisions are only slightly stronger than those adopted by all World Trade Organization members in 1995. A renegotiated NAFTA could include more robust IP protections, such as a minimum exclusivity period for biologics, which is 12 years under U.S. law but shorter under Canadian and Mexican law.[2] Other possible changes include digital rights management (i.e., to prevent circumvention of IP rights with respect to digital products), and limitations and exceptions for copyright (i.e., to protect news reporting, scholarship, research, etc.).
- **Digital Trade:** The internet was in its infancy when NAFTA was signed in 1992, and NAFTA does not include a chapter on the digital economy. Potentially, a renegotiated NAFTA could protect the free flow of information across borders, ban requirements that force U.S. businesses to locate ICT infrastructure abroad, and prohibit foreign governments from requiring disclosure of source code and encryption keys. This would help protect innovative U.S. producers of digital goods and services from unfair foreign practices and would set a high bar for



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other future negotiations. It is notable that Mexico was a strong ally of the United States in the negotiation of the electronic commerce chapter in the Trans-Pacific Partnership.

- **Anti-Corruption and Rule of Law:** Currently, NAFTA does not contain any provisions on anti-corruption and rule of law. A renegotiated NAFTA could include provisions on good governance, requiring the parties to effectively enforce anti-corruption laws and regulations, and also imposing transparency-related requirements.

However, a renegotiated NAFTA could also negatively impact U.S. companies, especially those with international supply chains or operations outside of the United States.[3] For example:

- **Rules of Origin:** Like other U.S. free trade agreements, NAFTA includes complicated “rules of origin” to determine whether a product imported from Canada or Mexico qualifies for duty-free treatment in the United States. The Trump administration may seek to tighten the NAFTA rules of origin by withdrawing duty-free treatment from goods made with inputs from third countries, such as China, which account for a significant share of the total value of the finished product. The potential for such changes should be of particular concern to the auto industry and other sectors with substantial Mexican or Canadian production facilities that use third-country inputs.
- **Investor-State Dispute Settlement:** NAFTA was one of the first free trade agreements to include investor-state dispute settlement (ISDS) provisions, which have since become a core part of the U.S. trade template — and one of the most controversial. Although Republican administrations have typically supported ISDS, the president-elect criticized the mechanism during the campaign. Thus, it is possible that the Trump administration will consider jettisoning ISDS from NAFTA. This would eliminate an important safeguard for U.S. companies with investments in Canada and Mexico — each of which may welcome the step, as they have both been the target of high-profile ISDS actions in the past.
- **New Provisions Targeting “Outsourced” Production:** The president-elect has threatened to impose additional taxes on U.S. companies that “outsource” U.S. production to foreign countries and then export their products back to the United States. It is unclear whether the Trump administration plans to use trade policy, tax policy, or the bully pulpit to accomplish this objective. However, to the extent that this policy is advanced via NAFTA, the impact on businesses could be profound.

Finally, some changes to NAFTA could be important for the effect that they have on future free trade agreements negotiated with countries outside North America, or in the event that an updated NAFTA is subsequently expanded to include additional parties. For example:

- **State-Owned Enterprises (SOEs):** NAFTA's provisions on SOEs are limited and do not reflect the full range of concerns about discriminatory preferences for SOEs that have come to the fore since NAFTA was signed. TPP would have included robust protections against unfair competition from SOEs, including provisions to combat

subsidies to SOE service suppliers. The Trump administration could push to add an SOE chapter to NAFTA with even stronger protections than those in TPP, given the absence from the NAFTA negotiations of parties with significant defensive concerns (unlike TPP).

- **Currency Manipulation:** The president-elect's pledge to instruct the Secretary of the Treasury to declare China a currency manipulator reflects the outsize role that currency has played in U.S. trade policy debates in recent years. Indeed, the lack of a sufficiently strong currency provision was one of the principal complaints of many TPP opponents. It is possible that Canada and Mexico would welcome the opportunity to add a strong currency provision to NAFTA, both for domestic political reasons and to establish a strong precedent for future negotiations with countries that are believed to manipulate their currencies to promote exports.

Several of these changes (e.g., ISDS, currency manipulation, provisions targeting “outsourced” production) would depart from traditional Republican trade orthodoxy, and congressional Republicans may not support them — although they would likely enjoy strong support from traditional trade skeptics in the Democratic Party. The fact that these ideas would even be on the table, however, is a reflection of the president-elect's unorthodox campaign and its unsettling effects on trade politics.

Canada and Mexico are undoubtedly already preparing their own demands for any negotiation, which may prove unacceptable to the United States. Mexico, for example, may push to expand NAFTA's “temporary entry” provisions to expand the availability of visas for Mexican and Canadian service suppliers in the U.S. market — a non-starter in U.S. trade politics since the completion of the Chile and Singapore FTAs in 2003. But if the three countries view the exercise as an opportunity to modernize NAFTA and increase the competitiveness of the North American market, the outcome could be an improved and greatly expanded agreement, which could serve as a template for future FTAs with other countries.

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[1] U.S. companies would be wise to look at provisions of the Trans-Pacific Partnership (TPP) for guidance, even though it remains controversial.

[2] See Ian F. Fergusson and Brock R. Williams, Congressional Research Service, “The Trans-Pacific Partnership (TPP): Key Provisions and Issues for Congress” (June 14, 2016) at pp. 49-50.

[3] By the same token, companies that compete against those harmed by these provisions stand to gain a competitive edge if they are introduced into NAFTA.