

# CLIENT ALERT

## Labor Provisions of the USMCA: What Multinational Employers Should Know

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The new United States Mexico Canada Agreement (USMCA), which replaced the 1994 North American Free Trade Agreement (NAFTA), became effective on July 1, 2020. Historically, free trade agreements like the NAFTA have been criticized for their lack of strong labor provisions to address low wages and inadequate labor standards that advocates argue support worker rights and improve economic growth in developing countries. The USMCA seeks to address those concerns. In fact, as a precondition to the passage of the USMCA, the U.S. Congress reopened the negotiations at the end of 2019 and amended the agreement to bolster Mexican workers' rights and to include stronger enforcement provisions like the Rapid Response Mechanism to hold companies in Mexico accountable for violating the rights of free association and collective bargaining.

### What is the Rapid Response Mechanism?

The Rapid Response Mechanism is perhaps the most novel aspect of the labor provisions of the USMCA. It applies between the U.S. and Mexico, and between Canada and Mexico, but not between the U.S. and Canada. Within the U.S., the Rapid Response Mechanism can be triggered when any person in the U.S. files a petition claiming the "denial of rights" at a "covered facility" in a "priority sector" in Mexico to the Interagency Labor Committee for Monitoring and Enforcement ("Interagency Labor Committee"), co-chaired by the U.S. Trade Representative and the Secretary of Labor. The Interagency Labor Committee can request that Mexico conduct a review to determine whether there is indeed a denial of rights, or. If Mexico does not agree to conduct a review, the Interagency Labor Committee may request a panel to be convened to conduct its own verification under the USMCA.

Denial of rights is defined as the denial of the right of free association and collective bargaining under Mexican legislation that complies with the USMCA. A covered facility is defined as a facility in a priority sector that (i) produces a good, or supplies a service, traded between the parties; or (2) produces a good, or supplies a service, that competes in the territory of a party with a good or service of the other party. Priority sectors are those that manufacture goods, supply services, or involve mining. Manufactured goods include, but are not limited to, aerospace products and components, auto and auto parts, cosmetic products, industrial baked goods, steel and aluminum, glass, pottery, plastics, forgings, and cement.

While the Rapid Response Mechanism is ongoing, the U.S. may suspend liquidation of imports from the covered facility. If a denial of rights has been found at a Mexican covered facility after the Rapid Response Mechanism has concluded, the U.S. may suspend the preferential treatment of goods manufactured at the covered facility, impose penalties on the covered facility, or deny entry of the goods from the covered facility if the covered facility had two prior denial of rights determinations.

### What is Mexico doing to implement its obligations under the USMCA?

Mexico's labor law reform, passed in May 2019 in response to the negotiations under the USMCA, drastically modified labor matters in Mexico, notably through the implementation of a new labor justice system and the creation of the Federal

Conciliation & Labor Registry Center (CFCRL), whose main tasks will be to: (i) supervise the proper conduct of collective affairs; and (ii) act as a conciliation authority before any judicial proceeding.

The CFCRL, once it is created and operating, will also be in charge of carrying out the internal investigation process that constitutes the first step of the Rapid Response Mechanism in Mexico. In the meantime, the Mexican Ministry of Labor and Social Welfare and the Federal Conciliation and Arbitration Board will carry out the internal investigation process.

Accordingly, even though the CFCRL does not yet exist, the Rapid Response Mechanism could still be triggered to enforce existing obligations in collective affairs, as the USMCA and its dispute mechanisms or proceedings are not contingent on the creation of government bodies or other domestic issues pursuant to the implementation of the Labor Law Reform by Mexico.

### **What are the other labor provisions in the USMCA?**

The USMCA contains an entire chapter on labor within its main agreement. The labor chapter, Chapter 23, requires that parties adopt and maintain laws consistent with the rights as stated in the International Labor Organization Declaration of Fundamental Principles and Rights at Work, which includes the freedom of association and recognition of the right to collective bargaining, the elimination of forced labor, the effective abolition of child labor, and the elimination of discrimination with respect to employment and occupation.

Specifically, each party shall prohibit importation of goods produced in whole or in part by forced or compulsory labor, including forced or compulsory child labor. The USMCA states that each party must prohibit discrimination on the basis of sex (including sexual harassment), pregnancy, sexual orientation, gender identity and caregiving responsibilities, although the U.S. is deemed to have fulfilled its obligations with respect to discrimination by virtue of Title VII of the U.S. Civil Rights Act of 1964.

Mexico, however, is required under the USMCA to implement specific labor reforms to ensure the right of workers to engage in collective bargaining and to organize. As mentioned above, many of these reforms have already been enacted with the new Mexican legislation that went into force in May 2019. As for other notable modifications, all existing collective bargaining agreements in Mexico also must be revised at least once during the four years after the legislation went into effect (by 2023), and unions will need to follow new requirements to negotiate collective bargaining agreements within work centers to ensure employees' accurate representation.

With respect to automobile production, the USMCA introduces the concept of Labor Value Content (LVC), which, along with a higher Regional Value Content threshold (75%, up from 62.5%), determines whether an automobile import qualifies for tariff-free treatment. The LVC rules require that at least 40% of a passenger car be made by workers earning at least \$16 an hour, with at least 25% of those high-wage workers be involved in materials and manufacturing. These new LVC rules will be fully phased in over three years.

### **How do those labor provisions in the USMCA affect multinational companies?**

One major goal of the USMCA is to effect changes in Mexico's labor rules. While a major reform of Mexico's labor legislation was implemented in May 2019 in anticipation of the USMCA becoming effective, many of the rules ensuring worker's freedom of association and collective bargaining are still being discussed in the Mexican legislation process. In addition, the Mexican labor law reform is still in its early implementation stage, meaning that years could pass before the new legislation be effectively and

fully enforced. Multinationals that relocated parts of their operations or manufacturing to Mexico to take advantage of NAFTA or otherwise have operations in Mexico are facing a changing landscape in terms of labor relations, and likely increased costs, over the next few years as Mexico updates its laws to comply with the labor provisions of the USMCA.

Multinationals should also keep an eye on the activities of the Interagency Labor Committee, which has been created as part of the U.S. Department of Labor. While the Interagency Labor Committee is tasked to receive petitions from private companies as part of the Rapid Response Mechanism discussed above, the legislation implementing the USMCA in the U.S. also grants the Interagency Labor Committee the power to monitor Mexico's compliance with the USMCA's labor requirements, including by creating a hotline for workers in any of the USMCA countries to report labor violations in Mexico. The enforcement actions triggered by these petitions and reports may lead to factory inspections, the loss of preferential tariff treatment or denial of imports of products.

### **What should employers be doing now that the USMCA is in effect?**

U.S. Customs and Border Protection has announced that, through the first six months of implementation, it will "show restraint" in its enforcement and will instead focus on supporting companies' efforts to comply. Despite this announcement, the above labor provisions described above, became fully enforceable immediately on day one.

- Employers should invest time and effort to understand the various labor provisions and the reporting and enforcement mechanisms built into the USMCA, especially if they or their competitors have operations in Mexico.
- Employers that have operations in Mexico should update their employment rules and agreements, if they have not done so already, to align with the new 2019 labor reforms in Mexico and to monitor upcoming labor changes.
- Companies that rely on suppliers with facilities in Mexico may consider methods to ensure that those suppliers are appropriately complying with Mexican labor laws.
- HR and labor relations professionals should review the terms of their collective bargaining agreements and policies relating to labor organizations to ensure compliance with the new rules under the USMCA and Mexican laws, as well as prepare training for managers and employees on the new requirements.
- Employers in the automobile industry (including downstream suppliers) will need to educate their employees who have oversight over operations and trade compliance on the LVC rules to maximize potential opportunities as automobile manufacturers in North America shift production over the next three years to qualify for preferential tariff treatment under the USMCA.

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