US & Multilateral Trade Policy Developments

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US Trade Policy Developments

Biden Administration Issues Proposed Rule to Increase Domestic Content Requirements Under Buy American Act

On July 30, the Federal Acquisition Regulatory Council (FAR Council) published a proposed rule that would increase domestic content requirements for federal government procurements that are subject to the Buy American Act (BAA), among other changes designed to strengthen enforcement of the BAA. The FAR Council is proposing these changes for public comment pursuant to President Biden's Executive Order of January 25, 2021 (EO 14005), which outlined the Biden administration's policy that US government procurement should "maximize the use of goods, products, and materials produced in, and services offered in, the United States." In addition to changing the regulatory definitions of "domestic" goods to require higher levels of US content, the proposed rule would establish more advantageous price preferences for domestic goods that the Federal government deems to be "critical." In so doing, it expressly seeks to link procurement policy to the Biden administration's ongoing initiative under EO 14017 to mitigate supply chain risks by promoting domestic production in critical sectors. This alert provides an overview of the Buy American Act and the FAR Council's proposed rule.

Background

The Buy American Act requires the federal government to buy domestic "articles, materials, and supplies" when they are acquired for public use, subject to exceptions for nonavailability of domestic products, unreasonable cost of domestic products, acquisitions subject to certain trade agreements, and situations where it would not be in the public interest to buy domestic products.[1] For purposes of the BAA, goods are domestic if they are "such unmanufactured articles, materials, and supplies as have been mined or produced in the United States" or "such manufactured articles, materials, and supplies as have been manufactured in the United States substantially all from articles, materials, or supplies mined, produced, or manufactured, as the case may be, in the United States."[2]

Domestic content thresholds under the BAA

The implementing regulations for the BAA are set out in the Federal Acquisition Regulation (FAR).[3] The FAR sets forth rules for determining whether solicited "construction material" or "end products" are "domestic" – that is, whether they were mined, produced, or manufactured in the United States, substantially all from components mined, produced, or manufactured in the United States. The FAR uses a two-part test to determine whether a manufactured end product or construction material is domestic:[4]

- The end product or construction material must be manufactured in the United States; and
- A certain percentage of all component parts (determined by the cost of the components) must also be mined, produced, or manufactured in the United States (a requirement known as the "component test" until early 2021, when it was redesignated the "domestic content test"). For an end product that does not consist wholly or predominantly of iron or steel or a combination of both, the cost of domestic components must exceed 55 percent of the cost of all components.[5] For an end product that consists wholly or predominantly of iron or steel or a combination of both, the cost of foreign iron and steel must constitute less than 5 percent of the cost of all the components.[6] The domestic content test is waived for acquisitions of commercially available off-the-shelf (COTS)

[1] *See generally* 41 U.S.C. §§ 10a-10d.

[2] 41 U.S.C. § 10a.

[3] 48 C.F.R. Part 25.

[4] 48 C.F.R. §§ 25.003 and 25.101(a).

[5] 48 C.F.R. § 25.003, 25.101(a)(2)(i), and 25.201(a)(2)(i).

[6] 48 C.F.R. § 25.105.

items, but not if they are iron or steel products (unless they are COTS fasteners).[7]

Price preferences for domestic goods under the BAA

The BAA does not prohibit the purchase of foreign end products or use of foreign construction material. Instead, it encourages the use of domestic end products and construction materials by imposing a "price preference" for such goods, applied when the procuring agency assesses the "reasonableness" of the cost of domestic offers.[8] Where a domestic offer is not the low offer, the price preference is applied by adding a specified percentage to the price of the foreign low offer, inclusive of duty.[9] The price of the domestic bid will be deemed reasonable if the bid price does not exceed the price of the low offer with the addition of the price preference.[10] Under the current FAR, large businesses offering domestic supplies receive a 20 percent price preference, and small businesses offering domestic supplies receive a 30 percent price preference.[11]

Trade agreements

Under the WTO Agreement on Government Procurement (GPA) and certain US free trade agreements, the United States has assumed obligations to afford non-discriminatory treatment to goods from participating foreign countries when it conducts procurements covered by the agreement. This obligation is implemented in US law through the Trade Agreements Act of 1979, which limits the Buy American Act's applicability by requiring US government procurements to treat as if they were domestic those materials originating in a country with which the United States has a covered trade agreement.[12]

Proposed rule to amend the FAR Buy American Act requirements

Increased domestic content thresholds

In EO 14005, President Biden directed the FAR Council to consider proposing regulations that would "[i]ncrease the numerical threshold for domestic content requirements for end products and construction materials[.]" Accordingly, the proposed rule would increase the domestic content threshold to 75 percent, from the current rate of 55 percent. The higher threshold would be phased in over several years, as follows:

- 60 percent (for items delivered through calendar year 2023)
- 65 percent (for items delivered in calendar years 2024 through 2028)
- 75 percent (for items delivered starting in calendar year 2029)

Under the proposed rule, a supplier holding a contract with a period of performance that spans the schedule of threshold increases will be required to comply with each increased threshold for the items in the year of delivery. For example, the rule states that a supplier awarded a contract in 2027 will have to comply with the 65 percent domestic content threshold initially, but in 2029 will have to supply products with 75 percent domestic content.

The proposed rule would establish a "fallback" threshold that would apply in instances where goods that meet the new, higher domestic content threshold are not available or are of unacceptable cost. In these circumstances, the proposed rule would allow for the acceptance of the former, lower domestic content threshold. For example, the proposed rule states that if a domestic end product exceeds the 60 percent domestic content threshold but is determined to be of unreasonable cost after application of the price preference, the government will treat an end product that is manufactured in the United States and exceeds 55 percent domestic content (but not 60 percent) as a

[7] 48 C.F.R. § 25.001(c)(1).

[8] 48 C.F.R. § 25.105.

[9] 48 C.F.R. § 25.105(b).

[10] 48 C.F.R. § 25.105(c).

[11] 48 C.F.R. § 25.105(b)(1) and (2).

[12] 19 U.S.C. § 2511(a).

domestic end product for purposes of the BAA. The fallback threshold would cease to apply one year after the domestic content threshold increases to 75 percent.

The thresholds set forth in the proposed rule would not apply to end products or construction materials that consist wholly or predominantly of iron or steel or a combination of both. Such items will continue to be classified as domestic only if the cost of foreign iron and steel constitutes "less than 5 percent of the cost of all the components used" in the end product or construction material. The fallback threshold described above also would not apply to such items.

Increased price preferences for "critical" products and components

In EO 14005, President Biden directed the FAR Council to consider proposing regulations that would "increase the price preferences for domestic end products and domestic construction materials." Accordingly, the proposed rule provides for a framework through which higher price preferences will be applied, but only for end products and construction materials deemed to be "critical" or made up of "critical components[.]" The list of critical products and components, and the level of additional price preference for such products, will be determined through future rulemaking.

The process for identifying critical items and components that are eligible for elevated price preferences will be informed by the quadrennial critical supply chain review instituted in President Biden's February 24, 2021 Executive Order on America's Supply Chains (EO 14017), as well as the Biden Administration's National COVID Strategy. EO 14017 directed federal agencies to review supply chain risks in six "critical" sectors (defense, public health, information technology, transportation, energy, and food production) by February 24, 2022. The Office of Management and Budget (OMB) will then lead a subsequent assessment "to further distill the list of products designated critical to those products for which procurement is likely to make a meaningful difference toward strengthening U.S. supply chains." The proposed rule states that, in addition to determining the list of critical products, this process will determine the level of enhanced price preference for each critical product – indicating that the levels may vary depending on the product at issue.

Once the list of critical products is established in the FAR, it will be published in the Federal Register for public comment "no less frequently than once every four years to reflect changes to the list."

Potential replacement of the "component test"

In EO 14005, President Biden directed the FAR Council to consider proposing regulations that would replace the "component test" (described above and now called the "domestic content test") with a test under which domestic content "is measured by the value that is added to the product through U.S.-based production or U.S. job-supporting economic activity," rather than the cost of components. The proposed rule does not seek to replace the "component test" at this time, and instead seeks public comments regarding "the strengths and shortcomings of the 'component test,' as currently structured," as well as "how domestic content might be better calculated to support America's workers and businesses[.]"

Public comment and hearing process

The FAR Council is seeking written comments on the proposed rule, with a comment deadline of September 28, 2021. Among other topics, the FAR Council is seeking comments on the following:

- Whether the commenters' products currently meet the higher domestic content thresholds envisioned by the proposed rule, and whether commenters would be willing and able to adjust their supply chains to meet the new thresholds;
- The utility of the proposed fallback threshold, including whether it would help companies adjust to the higher domestic content threshold or, alternatively, "delay the ability to increase Made in America content in Federal procurement;"

- Whether increased price preferences for critical items would be more, less, or equally effective as current preference levels at promoting domestic economic activity and strengthening domestic supply chains;
- Which items, if any, should receive an enhanced price preference, and what process OMB should use to determine such items;
- Whether and how the Federal government should incentivize vendors to supply products that exceed the minimum domestic content threshold by significant margins;
- Whether and how the current component test should be replaced by a "value added" calculation; and
- Whether the 2009 decision not to apply the component test to commercially available off the shelf (COTS) items should continue to apply.

The FAR Council and OMB's Made in America Office will hold a virtual public meeting on August 26, 2021, at which interested parties will have the opportunity to make presentations on these topics. In addition, the agencies have invited presenters to give feedback on other issues, including the interaction between trade agreements and the Buy American Act. Specifically, the proposed rule notes that under the Trade Agreements Act:

> "a purchase is treated as U.S.-made if it is mined, produced, or manufactured in the United States or substantially transformed in the United States, even if it is made of 100 percent foreign content. As a result, a substantially transformed U.S.-made product may have far less domestic content when compared to a domestic end product acquired under the Buy American statute."

The agencies "are seeking to understand more about the impact of the substantial transformation test and potential lost opportunities for American workers," and thus are inviting interested parties to comment on this topic at the public meeting.

Outlook

The changes contemplated by the proposed rule are significant, and would likely force some companies to alter their sourcing and manufacturing practices to continue benefiting from domestic preferences under the BAA. Though the administration is seeking public comments prior to implementing any changes, President Biden pledged when announcing the proposal that his administration will "make the biggest enforcement changes to the Buy American Act in 70 years," because the current domestic content thresholds are "not high enough" and new rules are needed to ensure domestic supply of critical products.[13] This is a strong indication that the rule will be adopted in some form. Companies therefore should begin considering how the proposed rule would impact their commercial interests, particularly if they operate in sectors that may be deemed "critical" for purposes of the rule.

Importantly, the domestic content thresholds and price preferences contemplated by the proposed rule would not apply to goods that are entitled to non-discriminatory treatment under the GPA and similar trade agreements. However, President Biden previously has expressed interested in renegotiating such agreements to facilitate further expansions of Buy American preferences, and the proposed rule seeks comments on whether such agreements, as implemented through US law, have resulted in "lost opportunities for American workers." This is a strong indication that the Biden administration will continue to study this issue and may undertake additional actions to enhance domestic preferences.

The proposed rule can be viewed here.

[13] "Remarks by President Biden on the Importance of American Manufacturing." *The White House*, July 28, 2021, https://www.whitehouse.gov/briefing-room/speeches-remarks/2021/07/28/remarks-by-president-biden-on-the-importance-of-american-manufacturing/

Senate Infrastructure Bill Seeks to Expand Domestic Content Requirements for Federally-Funded Infrastructure Projects and Government Procurement

On August 10, the US Senate approved the Infrastructure Investment and Jobs Act (H.R. 3684), which provides for $550 billion in new government spending to modernize and upgrade US core infrastructure including roads and bridges, ports and waterways, railroads, the electrical grid, and broadband. The legislation includes several provisions designed to maximize the use of domestic content in infrastructure projects that receive Federal financial assistance, and in Federal government procurements subject to the Buy American Act. The bill also would establish new domestic content requirements specific to government procurement of personal protective equipment (PPE). The Biden administration, which is undertaking its own regulatory initiatives to strengthen Buy American requirements, has welcomed the bill's "once-in-a-generation investment" in American infrastructure and the accompanying domestic content provisions, which the White House contends will "further the President's commitment to revitalizing the domestic industrial base."[14] The legislation will now be considered by the House of Representatives.

This alert provides an overview of the new domestic content requirements included in H.R. 3684.

Expansion of "Buy America" requirements for infrastructure projects

Several US statutes currently place domestic content restrictions on infrastructure projects that receive Federal funding and that non-Federal government agencies, such as state and local governments, carry out.[15] These statutes are commonly referred to as "Buy America" statutes, and are distinct from the requirements of the Buy American Act of 1933, which governs purchases made directly by the Federal government. Buy America statutes often involve funds administered by the US Department of Transportation and generally require the use of domestically-produced iron and steel and other manufactured goods unless the government grants a nationwide or project-specific waiver, though the precise nature of the restrictions and exceptions can vary depending on the statute and funds involved.

H.R. 3684 seeks to extend Buy America requirements to all programs that provide Federal financial assistance for infrastructure. The bill defines infrastructure as including, "at a minimum, the structures, facilities, and equipment for, in the United States":

- Roads, highways, and bridges;
- Public transportation;
- Dams, ports, harbors, and other maritime facilities;
- Intercity passenger and freight railroads;
- Freight and intermodal facilities;
- Airports;
- Water systems, including drinking water and wastewater systems;
- Electrical transmission facilities and systems;
- Utilities;

[14] "FACT SHEET: The Bipartisan Infrastructure Investment and Jobs Act Creates Good-Paying Jobs and Supports Workers." *The White House*, August 3, 2021, https://www.whitehouse.gov/briefing-room/statements-releases/2021/08/03/fact-sheet-the-bipartisan-infrastructure-investment-and-jobs-act-creates-good-paying-jobs-and-supports-workers/

[15] *See*, *e.g.,* 49 U.S.C. § 5323(j) (for projects funded by the Federal Transit Administration); 23 U.S.C. § 313 (for the Federal Highway Administration); 49 U.S.C. Chapters 244, 246, and § 24405 (for the Federal Railroad Administration); 49 U.S.C. §50101 (for the Federal Aviation Administration); and 49 U.S.C. § 24305 (for Amtrak).

- Broadband infrastructure; and
- Buildings and real property.

H.R. 3684 would require Federal agencies to identify all existing programs that provide Federal financial assistance for infrastructure, and to develop a list of any "deficient" programs. Deficient programs are defined as (1) those programs to which a "domestic content procurement preference," as that term is defined in the bill, does not currently apply;[16] or (2) those programs that are subject to Buy America waivers "of general applicability not limited to the use of specific products for use in a specific project." The bill would require agencies to publish a report identifying any "deficient programs" within 60 days of its enactment.

Within 180 days after enactment, H.R. 3684 would require each Federal agency to ensure that "none of the funds made available for a Federal financial assistance program for infrastructure, including each deficient program, may be obligated for a project unless all of the iron, steel, manufactured products, and construction materials used in the project are produced in the United States." For purposes of this requirement:

- Iron or steel products would be considered "produced in the United States" where "all manufacturing processes, from the initial melting stage through the application of coatings, occurred in the United States;"
- Construction materials would be considered "produced in the United States" where "all manufacturing processes for the construction material occurred in the United States;" and
- Manufactured products would be considered "produced in the United States" where (1) "the manufactured product was manufactured in the United States;" and (2) the cost of the components of the manufactured product that are mined, produced, or manufactured in the United States is greater than 55 percent of the total cost of all components of the manufactured product (unless another standard for determining the minimum amount of domestic content of the manufactured product has been established under applicable law or regulation).

The Buy America preference established by H.R. 3684 would apply only to the extent that an existing "domestic content procurement preference," as that term is defined in the bill, does not already apply to the program at issue.[17] Additionally, like the current statute, H.R. 3684 would permit Federal agencies to waive the application of the new preference where (1) the relevant products are not produced in the United States "in sufficient and reasonably available quantities or of a satisfactory quality;" (2) application of the preference would be inconsistent with the public interest; or (3) the inclusion of domestic products would increase the cost of the overall project by more than 25

[16] The bill defines the term ''domestic content procurement preference'' as a requirement that no amounts made available through a program for Federal financial assistance may be obligated for a project unless—

(A) all iron and steel used in the project are produced in the United States;

(B) the manufactured products used in the project are produced in the United States; or

(C) the construction materials used in the project are produced in the United States.

The bill defines the term "produced in the United States" to mean:

(A) in the case of iron or steel products, that all manufacturing processes, from the initial melting stage through the application of coatings, occurred in the United States;

(B) in the case of manufactured products, that—

(i) the manufactured product was manufactured in the United States; and

(ii) the cost of the components of the manufactured product that are mined, produced, or manufactured in the United States is greater than 55 percent of the total cost of all components of the manufactured product, unless another standard for determining the minimum amount of domestic content of the manufactured product has been established under applicable law or regulation; and

(C) in the case of construction materials, that all manufacturing processes for the construction material occurred in the United States.

[17] See Footnote 16.

percent. Existing Buy America statutes, such as those applicable to projects funded by the Federal Transit Administration, provide nearly identical exceptions.[18]

H.R. 3684 clarifies that the new Buy America preference is to be applied in a manner "consistent with United States obligations under international agreements." Relevant agreements to which the United States is a party include the WTO Agreement on Government Procurement (GPA) and certain US free trade agreements, in which the United States has assumed obligations to afford non-discriminatory treatment to goods from participating foreign countries when it conducts procurements covered by the agreement. The United States' schedule to the GPA exempts certain Buy America restrictions on mass transit and highway projects from the GPA's disciplines.[19] However, as noted above, H.R. 3684 contemplates the expansion of Buy America restrictions to a wide range of other projects that fall within the bill's definition of "infrastructure". The caveat that the new restrictions are to be applied consistent with US international obligations is likely intended to ensure that, where applying Buy America restrictions to a particular project would violate the GPA or another trade agreement, the application of the restrictions would be waived.

Buy American Act amendments and regulations

Distinct from the Buy America statutes, the Buy American Act requires the Federal government to buy domestic "articles, materials, and supplies" when they are acquired for public use, subject to exceptions for nonavailability of domestic products, unreasonable cost of domestic products, acquisitions subject to certain trade agreements, and situations where it would not be in the public interest to buy domestic products.[20] H.R. 3684 would amend the Buy American Act and require changes to its implementing regulations to increase the use of domestic content in federal procurement. These changes, described below, are again to be applied "in a manner consistent with United States obligations under international agreements," which would include the WTO GPA and US free trade agreements.[21]

New "melted and poured" standard for iron and steel products

The Buy American Act considers manufactured articles, materials, and supplies to be "domestic" if they "have been manufactured in the United States substantially all from articles, materials, or supplies mined, produced, or manufactured, as the case may be, in the United States."[22] The Federal Acquisition Regulation (FAR) implements this requirement in the form of a two-part test. For a manufactured end product or construction material to qualify as "domestic" under the FAR:[23]

- The end product or construction material "must be manufactured in the United States;" and
- A certain percentage of all component parts (determined by the cost of the components) must also be mined, produced, or manufactured in the United States. For an end product that does not consist wholly or predominantly of iron or steel or a combination of both, the cost of domestic components must exceed 55 percent of the cost of all components.[24] For an end product that consists wholly or predominantly of iron or steel or a combination of both, the cost of foreign iron and steel must constitute less than 5 percent of the cost of all the components.[25]

The Buy American Act, the Executive Orders implementing the Act, and the FAR do not define the term "manufacture." Judicial and other tribunals therefore have had to interpret whether particular activities constitute

[18] 49 U.S.C. § 5323(j)(2).

[19] United States Schedule to the GPA 2012, Annex 2 (WT/LET/950), at Note 5 (providing that "[f]or the state entities included in this Annex, this Agreement does not apply to restrictions attached to federal funds for mass transit and highway projects.")

[20] *See generally* 41 U.S.C. §§ 10a-10d.

[21] The Trade Agreements Act of 1979 (19 U.S.C. § 2511(a)) limits the Buy American Act's applicability by requiring US government procurements to treat as if they were domestic those materials originating in a country with which the United States has a covered trade agreement.

[22] 41 U.S.C. § 10a.

[23] 48 C.F.R. §§ 25.003 and 25.101(a).

[24] 48 C.F.R. § 25.003, 25.101(a)(2)(i), and 25.201(a)(2)(i).

[25] 48 C.F.R. § 25.105.

"manufacturing" in the United States for purposes of the two-part test, and in so doing have considered, of US processing that involved foreign-origin components, "whether there were 'substantial changes in physical character'; whether separate manufacturing stages were involved, or whether there was one continuous process; and whether the article is completed in the form required by the government."[26]

H.R. 3684 would amend the Buy American Act to specify what constitutes being "manufactured in the United States" in the case of iron and steel products. Specifically, it would deem manufactured articles, materials, and supplies of iron and steel "manufactured in the United States only if all manufacturing processes involved in the production of such iron and steel, from the initial melting stage through the application of coatings, occurs in the United States." To qualify as a "domestic" product eligible for Buy American preferences, an iron or steel product would have to satisfy this definition as well as the 95 percent domestic content threshold set forth in the FAR.

In addition to this new statutory standard for iron and steel products, H.R. 3684 would require the FAR Council (whose members include the Administrator for Federal Procurement Policy, the Secretary of Defense, the Administrator of National Aeronautics and Space, and the Administrator of General Services) to issue regulations that clarify the definition of "manufactured in the United States" in the case of other end products, including "guidelines to ensure that manufacturing processes involved in production of the end product occur domestically." The Far Council must issue such regulations within one year after the enactment of H.R. 3684.

Regulations and guidance on the Buy American Act

H.R. 3684 would further require the Office of Management and Budget (OMB) and the FAR Council to issue regulations or other guidance within one year concerning the enforcement of the Buy American Act. The regulations or guidance must include the following provisions, among others:

- "An increase to the price preferences for domestic end products and domestic construction materials." Regulations that the FAR Council recently proposed would increase price preferences for domestic goods under the Buy American Act, pursuant to President Biden's Executive Order of January 25, 2021. However, the proposed increases have not yet been adopted, and they would be limited to products that OMB deems to be "critical" in future rulemakings informed by the Biden administration's ongoing review of critical supply chains. Notably, H.R. 3684 does not expressly limit the required increase of price preferences to "critical" products.
- "Amending the definitions of 'domestic end product' and 'domestic construction material' to ensure that iron and steel products are, to the greatest extent possible, made with domestic components." As noted above, iron and steel products already are subject to a 95 percent domestic content threshold under the FAR. Additionally, if adopted, H.R. 3684 would couple this threshold with a new requirement that "all manufacturing processes" involved in production of the product occur in the United States, as described above. Nevertheless, H.R. 3684 requires further changes to the regulatory definition of domestic iron and steel products to promote the use of US content.

In addition to these changes, the bill would require OMB and the FAR Council to issue guidelines for Federal agencies detailing the circumstances in which certain exceptions to the Buy American Act are applicable (*e.g.*, because acquisition of domestic products is "inconsistent with the public interest" or because domestic products are not available.) These agencies must also issue guidelines to ensure that projects are not "disaggregated for purposes of avoiding the applicability of the requirements under the Buy American Act."

[26] For more information, see "Domestic Content Restrictions: The Buy American Act and Complementary Provisions of Federal Law," *Congressional Research Service*, September 12, 2016, https://crsreports.congress.gov/product/pdf/R/R43354, at p.4-5.

"Make PPE in America Act"

Entitled the Make PPE in America Act, legislation that H.R. 3684 incorporates seeks to foster a domestic PPE supply chain by providing "a strong and consistent demand signal from the Federal Government[.]" The bill requires that any contract for the procurement of PPE entered into by the Secretaries of Homeland Security, Health and Human Services, or Veterans Affairs ("covered Secretaries"):

(1) "be issued for a duration of at least 2 years, plus all option periods necessary," to incentivize investment in domestic production; and

(2) "be for personal protective equipment, including the materials and components thereof, that is grown, reprocessed, reused, or produced in the United States."

The legislation would permit the covered Secretaries to procure PPE from foreign sources that manufacture PPE using US components, but only "after maximizing to the extent feasible" domestic sources for the relevant items. In such circumstances, the covered Secretary may "maximize[] sources for [PPE] that is assembled outside the United States containing only materials and components that are grown, reprocessed, reused, or produced in the United States[.]" The bill would require the covered Secretary to certify every 120 days that procuring PPE from these alternative sources is necessary "to respond to the immediate needs of a public health emergency."

The government could waive this requirement to procure PPE from domestic sources (or, alternatively, from foreign sources that use US components) with respect to an item of PPE, or a component or material thereof:

(1) That is, or that includes, a material listed in section 25.104 of the FAR as one for which a non-availability determination has been made under the Buy American Act;[27] or

(2) As to which the covered Secretary determines "that a sufficient quantity of a satisfactory quality that is grown, reprocessed, reused, or produced in the United States cannot be procured as, and when, needed at United States market prices."

Importantly, H.R. 3684 anticipates conflicts between the legal requirement to procure domestic PPE and certain of the United States' obligations under the WTO GPA and other trade agreements. Accordingly, the bill directs the President or his designee to "take all necessary steps, including invoking the rights of the United States under Article III of the [WTO GPA] and the relevant exceptions of other relevant agreements to which the United States is a party, to ensure that the international obligations of the United States are consistent with the provisions of [the Make PPE in America Act]." Article III of the GPA 2012 sets forth security and general exceptions for certain measures that otherwise would be inconsistent with the Agreement, including (1) measures that a Party "considers necessary for the protection of its essential security interests relating to ... procurement indispensable for national security or for national defence purposes;" and (2) measures "necessary to protect human, animal or plant life or health," provided that they are not applied "in a manner that would constitute a means of arbitrary or unjustifiable discrimination between Parties where the same conditions prevail or a disguised restriction on international trade[.]"

Outlook

The Senate approved H.R. 3684 in a bipartisan vote of 69 to 30, and the White House has endorsed the legislation. According to House Speaker Nancy Pelosi (D-CA), the House will not take up H.R. 3684 until the Senate completes work on a separate, more controversial government spending bill that Democratic lawmakers intend to approve on a party-line vote using reconciliation procedures. This may delay House consideration of H.R. 3684 until at least late September, given that congressional committees have until September 15 to complete work on the reconciliation package. Nevertheless, there is a strong possibility that H.R. 3684 will become law. Companies therefore should

[27] This refers to a finding that a particular product is "not mined, produced, or manufactured in the United States in sufficient and reasonably available commercial quantities and of a satisfactory quality," in which case the Buy American Act does not apply to that product. 48 C.F.R. § 25.103(b).

consider how the domestic content requirements set forth in the bill, coupled with the Biden administration's ongoing initiative to strengthen enforcement of the Buy American Act, would affect their commercial interests.

House Republicans Introduce Bill to Renew 2015 Trade Promotion Authority Law and Establish New Negotiating Objectives for Pharmaceuticals

On July 27, Reps. John Joyce (R-PA) and Jim Banks (R-IN) introduced legislation that would establish new US trade negotiating objectives for the pharmaceutical sector, in the context of a broader renewal of the trade promotion authority ("TPA") statute that governs the negotiation and congressional approval of US trade agreements. The proposed objectives would apply to a wide range of pharmaceutical products, including biologics, as well as the active pharmaceutical ingredients (APIs) used to produce finished pharmaceuticals for animals and humans. US trade negotiating objectives for the pharmaceutical sector historically have focused on improving intellectual property protection in foreign countries to reflect the levels of protection provided under US law. The new bill, entitled the *International Pharmaceutical Supply Chain Security Agreement Act of 2021* (H.R. 4711), would direct US trade negotiators to pursue additional objectives designed to improve the security and efficiency of pharmaceutical supply chains, reflecting concerns brought on by the COVID-19 pandemic and certain policy responses thereto such as export restrictions. Aside from these new objectives, H.R. 4711 would renew without changes the TPA statute enacted by Congress in 2015. This alert provides an overview of the proposed legislation.

Background

Article I, Section 8 of the US Constitution gives Congress authority over the key levers of trade policy, including the power to impose duties and to otherwise "regulate Commerce with foreign Nations[.]" At the same time, the President has authority under Article II of the Constitution to conduct foreign affairs, including the power to negotiate international treaties with the advice and consent of the US Senate. Given this constitutional framework, the negotiation and implementation of US trade agreements requires cooperation and compromise between Congress and the Executive Branch.

Recognizing the constitutional framework and the need for the US government to credibly negotiate trade agreements with foreign nations, the Congress since 1974 has periodically enacted special, expedited procedures to consider trade agreements negotiated by the Executive Branch. Such legislation (previously referred to as "fast-track" and more recently "trade promotion authority") commits Congress to vote on bills implementing trade agreements within a fixed time period, with limited debate, without amendment, and subject to an up-or-down vote, once the President submits an implementing bill. These legislative procedures improve the likelihood that Congress will approve a trade agreement negotiated by the President, but they can be withdrawn if the President fails to adhere to the requisite statutory obligations, including negotiating objectives and congressional notification and consultation requirements. Congress enacted the most recent version of TPA, entitled the *Bipartisan Congressional Trade Priorities and Accountability Act*, in 2015 ("TPA 2015").[28] However, the law expired on July 1, 2021.

International Pharmaceutical Supply Chain Security Agreement Act of 2021 (H.R. 4711)

Reauthorization of TPA 2015

H.R. 4711 would reauthorize TPA 2015 through July 1, 2023, with an optional extension through July 1, 2026. The extension would occur if (1) the President requests the extension; and (2) neither House of Congress adopts a resolution before July 1, 2023 disapproving the extension. In practice, this means that:

- The President would be permitted to enter into (*i.e.*, sign) trade agreements with foreign countries before July 1, 2023 (or July 1, 2026, if the President receives an extension); and
- The expedited legislative procedures set forth in TPA 2015 would apply to implementing bills for trade agreements signed by the President within the above timeframes.

[28] 19 U.S.C. §§ 4201-4210

Aside from extending the duration of TPA and establishing new negotiating objectives for the pharmaceutical sector (described below), H.R. 4711 would not modify TPA 2015, which consists of (1) congressional objectives for trade agreements negotiated by the Executive Branch; (2) Executive-congressional notification and consultation requirements; and (3) the procedures for expedited congressional consideration of trade agreements.

New negotiating objectives for the pharmaceutical sector

H.R. 4711 would amend TPA 2015 by adding the following negotiating objectives relating to "trade in covered pharmaceutical products":[29]

- The objective regarding tariffs is to ensure that parties to US trade agreements "eliminate the imposition or re-imposition of tariffs on imports of [covered pharmaceuticals], particularly in the event of a declared emergency."
- The objectives regarding regulatory and technical barriers are:
  - To "reduce or eliminate regulatory and other technical barriers in the pharmaceutical sector;"
  - To ensure that parties promote "expedited approval" of pharmaceutical production facilities;
  - To ensure that parties promote the use of good regulatory practices and streamlined regulatory review and approval processes for pharmaceutical production;
  - To ensure that parties eliminate "duplicated actions and other barriers" to reduce the time for approval of pharmaceutical products and facilities; and
  - To ensure that parties will expand transparency and cooperation to ensure that regulatory processes are streamlined and harmonized among parties, to the maximum extent possible.
- The objective regarding export restraints is "to prohibit export restraints against parties to the agreement, particularly in the event of a declared emergency."
- The objectives regarding subsidies are:
  - To encourage the "coordinated provision" of subsidies that are not prohibited by WTO rules and are intended to incentivize manufacturing of covered pharmaceutical products, including "the provision of grants, loans, tax incentives, and guaranteed price and volume contracts;"
  - "[T]o explicitly permit, among parties to the agreement, the use of production subsidies to build pharmaceutical manufacturing capacity;"
  - To "affirm that subsidies provided by parties are not intended to be used primarily for export or to distort trade;" and to affirm the parties' commitments under the WTO Antidumping Agreement and the Agreement on Subsidies and Countervailing Measures; and
  - To encourage notification and consultation among parties regarding potential pharmaceutical manufacturing subsidies "to increase coordination and avoid creating conditions such as oversupply or market inefficiencies[.]"

[29] The bill defines "covered pharmaceutical products" as including:
- "An active pharmaceutical ingredient," *i.e.*, "any component that is intended to furnish pharmacological activity or other direct effect in the diagnosis, cure, mitigation, treatment, or prevention of disease, or to affect the structure or any function of the body of a human or animal," subject to certain exceptions; or
- "A drug (including a biological product)[.]" The term "drug" is not defined in the bill; "biological product" is given the definition set forth in the Public Health Service Act, i.e., "a virus, therapeutic serum, toxin, antitoxin, vaccine, blood, blood component or derivative, allergenic product, protein, or analogous product, or arsphenamine or derivative of arsphenamine (or any other trivalent organic arsenic compound), applicable to the prevention, treatment, or cure of a disease or condition of human beings."

- The objectives regarding government procurement are to provide reciprocal access to government procurements for pharmaceutical products among parties to the agreement; to facilitate the involvement of participant countries' companies in bids to supply such products; and to promote participation in the WTO Government Procurement Agreement.
- The objectives regarding trade in services are:
    - To obtain fair, open, and transparent access to supply chain services in the markets of the parties, such as distribution, logistics, and transportation services;
    - To ensure that any restrictions or regulatory requirements on such services are adopted and maintained in a transparent and efficient manner; and
    - To require parties to establish an internal process for identifying restrictions or regulatory requirements that could be waived in the event of a declared emergency.
- The objectives regarding transparency and trade facilitation are:
    - To obtain commitments to develop mechanisms to share information about supply chain constraints and coordinate approaches to minimize risks that could lead to supply chain failures; and
    - To obtain commitments that parties will fully implement their obligations under the WTO Trade Facilitation Agreement, to the extent they have not already done so.
- The objectives regarding enforcement of trade disciplines involving pharmaceuticals are to:
    - Ensure that benefits under the agreement can only be obtained by parties that are fully meeting their obligations;
    - Ensure that parties "will not bring a dispute under another agreement for actions that are consistent with the agreement";
    - Provide a dispute settlement mechanism comparable to that of the US-Mexico-Canada Agreement ("USMCA"); and
    - "[M]inimize the ability of parties to the agreement to undermine the effectiveness of the agreement by abusing exceptions," namely by requiring notification of a party's intent to rely on an exception and by limiting the duration for which parties may rely on an exception.

Outlook

The Biden administration and congressional Democrats have shown little interest in pursuing new TPA legislation this year, given President Biden's pledge to refrain from negotiating trade agreements until Congress has implemented his domestic policy agenda. Moreover, the vast majority of congressional Democrats opposed TPA 2015, and Biden administration officials have taken the view that any future TPA legislation should involve an overhaul of the law's negotiating objectives. At minimum, these stakeholders are likely to demand that any future TPA bill include updated negotiating objectives on labor and environmental protection, and perhaps on other issues such as investment protection, rules of origin, and intellectual property, reflecting the standards negotiated in the USMCA. For these reasons, it is highly unlikely that Congress will approve H.R. 4711 in its current form.

On the other hand, the negotiating objectives proposed in H.R. 4711 reflect the increasingly prevalent and bipartisan view that pharmaceutical supply chains should be made more secure and efficient in light of the COVID-19 pandemic. Such concerns prompted President Biden to order an interagency review of vulnerabilities in the pharmaceutical supply chain earlier this year, among other critical sectors. The Biden administration's review concluded that, in addition to providing financial and other incentives for domestic manufacturing of pharmaceuticals, the United States should cooperate with allied countries to secure supplies of critical products it cannot produce

domestically, as well as to align regulatory approaches.[30] The negotiating objectives set forth in H.R. 4711 reflect similar views, and are likely to inform future discussions in Congress regarding new TPA legislation.

The text of H.R. 4711 can be viewed here.

[30] "Building Resilient Supply Chains, Revitalizing American Manufacturing, and Fostering Broad-Based Growth: 100-Day Reviews under Executive Order 14017." *The White House*, June 2021, https://www.whitehouse.gov/wp-content/uploads/2021/06/100-day-supply-chain-review-report.pdf

Trade Remedies

US International Trade Commission Initiates Investigation Concerning Extension of Safeguard Action on Crystalline Silicon Photovoltaic Cells

On August 12, the US International Trade Commission published a Federal Register notice announcing the initiation of an investigation to determine whether to extend the United States' safeguard measure on imports of certain crystalline silicon photovoltaic (CSPV) cells (whether or not partially or fully assembled into other products). The Commission instituted the investigation in response to a petition filed on behalf of Auxin Solar Inc. and Suniva, Inc. on August 2, 2021, and a separate petition filed on behalf of Hanwha Q CELLS USA, Inc., LG Electronics USA, Inc., and Mission Solar Energy on August 4, 2021. The petitions seek the extension of the safeguard measure for an additional four years beyond its scheduled expiration date of February 6, 2022. An overview of the safeguard measure, the relief sought by the petitioners, and the investigation schedule is provided below.

Background

On January 23, 2018, President Donald Trump determined to impose a safeguard measure on imports of CSPV products for a period of four years. The safeguard measure consists of (1) a tariff-rate quota on imports of CSPV cells not partially or fully assembled into other products; and (2) an increase in duties on imports of CSPV modules. The measure took effect on February 7, 2018, and is currently scheduled to terminate on February 6, 2022. President Trump imposed the measure following a global safeguard investigation conducted by the Commission under Section 201 of the Trade Act of 1974.[31] In its investigation, the Commission determined that imports of the subject merchandise were being imported "in such increased quantities as to be a substantial cause of serious injury to the domestic industry" and recommended the imposition of remedies.[32]

Under the current CSPV safeguard measure, the first 2.5 gigawatts (GW) of covered CSPV cells imported each year (*i.e.*, the "in-quota quantity") are not subject to additional tariffs. Imports of covered CSPV cells in excess of the 2.5 GW quota, and all imports of covered CSPV modules, are subject to additional tariffs at the rates shown below.

Safeguard on CSPV Cells and Modules, as Modified by Proclamation 10101				
Period	**Year 1** 2/7/2018 – 2/6/2019	**Year 2** 2/7/2019 – 2/6/2020	**Year 3** 2/7/2020 – 2/6/2021	**Year 4** 2/7/2021 – 2/6/2022
Tariff on modules and out-of-quota cells	30%	25%	20%	18%
In-quota quantity (cells only)	2.5 GW	2.5 GW	2.5 GW	2.5 GW

President Trump modified the safeguard action in October 2020 to address concerns that the exclusion of bifacial solar panels from the remedy had undermined the effectiveness of the action. Bifacial panels initially were covered by the remedy, but the Office of the US Trade Representative later approved a request to exclude them during a formal exclusion request proceeding. In Proclamation 10101, President Trump terminated the exclusion of bifacial solar panels from the safeguard remedy, finding that the exclusion "impaired and is likely to continue to impair the effectiveness of the action…in light of the increased imports of competing products such exclusion entails[.]" Additionally, the Proclamation increased to 18% (from the previously-announced level of 15%) the safeguard tariff applicable to imports of CSPV modules, and to imports of CSPV cells in excess of the TRQ, during the fourth year of the safeguard action. The Proclamation stated that the tariff increase was necessary "to achieve the full remedial effect envisaged" for the safeguard action, in light of the alleged effects of the bifacial panels exclusion.

[31] 19 U.S.C. § 2251 *et seq.*

[32] *See* Crystalline Silicon Photovoltaic Cells (Whether or not Partially or Fully Assembled into Other Products), investigation No. TA-201-75, USITC Publication 4739, November 2017).

Legal framework for safeguard extensions

Pursuant to Section 203(e)(1)(A) of the Trade Act, an initial safeguard action imposed by the President may remain in effect for no more than 4 years.[33] The President may subsequently extend the action following an investigation and affirmative determination by the Commission in an extension proceeding under Section 204(c) of the Act, subject to the requirement that the total duration of a safeguard action, including any extensions thereof, may not exceed 8 years in the aggregate.[34]

Section 204(c) of the Act requires the Commission, upon request of the President or upon petition on behalf of the industry concerned, to "investigate to determine whether [the safeguard action imposed by the President] continues to be necessary to prevent or remedy serious injury and whether there is evidence that the industry is making a positive adjustment to import competition."[35] As part of its investigation, the Commission must hold a public hearing at which interested parties and consumers have the opportunity to present their views.[36] The Commission must issue a report on its investigation and determination no later than 60 days before the safeguard action is set to terminate, unless the President specifies a different date.[37]

If the Commission reaches an affirmative determination (or if the Commission is equally divided and the President considers the determination to be affirmative), the President may extend the safeguard action if he determines that (1) the action continues to be necessary to prevent or remedy the serious injury; and (2) there is evidence that the domestic industry is making a positive adjustment to import competition.[38]

Petitions for extension of the safeguard action

The petition filed on behalf of Hanwha Q CELLS USA, Inc., LG Electronics USA, Inc., and Mission Solar Energy states that "adverse market conditions faced by the industry during the last three years suggest that the safeguard will not effectuate its intended purpose within the current four-year safeguard period," and that "[w]ithout an extension of the remedy, planned investments in equipment and workforce, new capacity expansions and product innovation will have to be put on hold or may never come to fruition." Accordingly, the petition requests that the Commission "recommend extension of the safeguard measures for an additional four years at the highest possible duty rates on imports of out of quota CSPV cells and CSPV modules," as follows:

- Year 1 of the extension – tariff rate of 17%;
- Year 2 of the extension – tariff rate of 16%;
- Year 3 of the extension - tariff rate of 15%; and
- Year 4 of the extension – tariff rate of 14%.

In addition, these petitioners request that the Commission recommend increasing the TRQ level for cells above the current level of 2.5 GW. The petition states that "the increase in U.S. production of modules will result in the current TRQ quota level being reached," and therefore "an increase in TRQ level is required to allow U.S. CSPV module producers to continue to grow and thrive."

The petition filed on behalf of Auxin Solar Inc. and Suniva, Inc. states that "[h]indered by pre-safeguard stockpiling and the bifacial loophole, Legacy Producers such as Auxin Solar did not begin to receive certain key intended benefits of the remedy until Q4-2020[.]" Additionally, "[b]ecause of the large cell TRQ, Legacy Producers of CSPV

[33] 19 U.S.C. § 2253(e)(1)(A).

[34] 19 U.S.C. § 2253(e)(1)(B).

[35] 19 U.S.C. § 2254(c)(1).

[36] 19 U.S.C. § 2254(c)(2).

[37] 19 U.S.C. § 2254(c)(3).

[38] 19 U.S.C. § 2253(e)(1)(B)(i).

cells, such as Suniva, never received any of the intended benefits of the safeguard remedy." Accordingly, these petitioners seek the extension of the safeguard action "for up to four additional years, or until February 6, 2026, with only minimal liberalization of the tariff rates applicable to out-of-quota CSPV cells and CSPV modules[.]" These petitioners have requested that the in-quota volume for CSPV cells be maintained at the current level of 2.5 GW.

Next steps

The Commission's Federal Register notice sets forth the following schedule for the investigation:

- **Participation in the investigation and public service list.** Persons wishing to participate in the investigation as parties must file an entry of appearance with the Secretary to the Commission, as provided in § 201.11 of the Commission's rules, not later than 21 days after publication of the initiation notice in the Federal Register (*i.e.*, by September 2, 2021).
- **Public hearing.** The Commission will hold a hearing in connection with the investigation beginning at 9:30 a.m. on November 3, 2021. Information about the place and form of the hearing, including about how to participate in and/or view the hearing, will be posted on the Commission's website at https://www.usitc.gov/calendarpad/calendar.html. Requests to appear at the hearing should be filed in writing with the Secretary to the Commission on or before October 28, 2021.
- **Written submissions.** The deadline for filing prehearing briefs is October 27, 2021. Parties may also file written testimony in connection with their presentation at the hearing and posthearing briefs. The deadline for filing posthearing briefs is November 10, 2021. In addition, any person who has not entered an appearance as a party to the investigation may submit a written statement of information on or before November 10, 2021.

As noted above, the Commission must issue a report on its investigation and determination no later than 60 days before the safeguard action is set to terminate (*i.e.*, by December 8, 2021), unless the President specifies a different date.

The initiation notice can be viewed here.

US International Trade Commission Finds That Seamless Carbon and Alloy Steel Standard, Line, and Pressure Pipe from Korea, Russia, and Ukraine Injures US Industry

On August 2, 2021, the US International Trade Commission (ITC) determined that a US industry is materially injured by reason of imports of seamless carbon and alloy steel standard, line, and pressure pipe from Korea, Russia, and Ukraine that the US Department of Commerce (DOC) has determined is sold in the United States at less than fair value and subsidized by the governments of Korea and Russia. Chair Jason E. Kearns, Vice Chair Randolph J. Stayin, and Commissioners David S. Johanson, Rhonda K. Schmidtlein, and Amy A. Karpel voted in the affirmative. As a result of the ITC's affirmative determinations, DOC will issue antidumping duty orders on imports of these products from Korea, Russia, and Ukraine and countervailing duty orders on imports of these products from Korea and Russia.

In its antidumping and countervailing duty investigations, DOC determined that imports of the subject merchandise were sold in the United States at the following dumping margins and subsidy rates:

Country	Dumping Margin	Subsidy Rate
Russia	209.72%	48.38%
South Korea	4.44%	1.78%
Ukraine	23.75%	NA

The merchandise covered by the scope of these investigations is seamless carbon and alloy steel (other than stainless steel) pipes and redraw hollows, less than or equal to 16 inches (406.4 mm) in nominal outside diameter, regardless of wall-thickness, manufacturing process (*e.g.,* hot-finished or cold-drawn), end finish (*e.g.,* plain end,

beveled end, upset end, threaded, or threaded and coupled), or surface finish (*e.g.,* bare, lacquered or coated). Subject seamless standard, line, and pressure pipe are normally entered under Harmonized Tariff Schedule of the United States (HTSUS) subheadings 7304.19.1020, 7304.19.1030, 7304.19.1045, 7304.19.1060, 7304.19.5020, 7304.19.5050, 7304.31.6050, 7304.39.0016, 7304.39.0020, 7304.39.0024, 7304.39.0028, 7304.39.0032, 7304.39.0036, 7304.39.0040, 7304.39.0044, 7304.39.0048, 7304.39.0052, 7304.39.0056, 7304.39.0062, 7304.39.0068, 7304.39.0072, 7304.51.5005, 7304.51.5060, 7304.59.6000, 7304.59.8010, 7304.59.8015, 7304.59.8020, 7304.59.8025, 7304.59.8030, 7304.59.8035, 7304.59.8040, 7304.59.8045, 7304.59.8050, 7304.59.8055, 7304.59.8060, 7304.59.8065, and 7304.59.8070.

According to DOC, imports under the above-listed HTSUS subheadings in 2020 were valued at approximately $9.99 million (for Russia), $26.1 million (for Korea), and $25.5 million (for Ukraine).

The ITC's public report on these investiations will be availale by September 7, 2021.

US International Trade Commission Finds That Methionine from Japan and Spain Injures US Industry

On August 24, 2021, the US International Trade Commission (ITC) determined that a US industry is materially injured by reason of imports of methionine from Japan and Spain that the US Department of Commerce (DOC) has determined are sold in the United States at less than fair value. Chair Jason E. Kearns, Vice Chair Randolph J. Stayin, and Commissioners David S. Johanson, Rhonda K. Schmidtlein, and Amy A. Karpel voted in the affirmative. As a result of the ITC's affirmative determinations, DOC will issue antidumping duty orders on imports of this product from Japan and Spain.

In its antidumping investigations, DOC determined that imports of methionine from Japan and Spain were sold in the United States at dumping margins of 76.50 percent and 37.53 percent, respectively.

The merchandise covered by these investigations is methionine and dl-Hydroxy analogue of dl-methionine, also known as 2-Hydroxy 4-(Methylthio) Butanoic acid (HMTBa), regardless of purity, particle size, grade, or physical form. Methionine has the chemical formula $C_5 H_{11} NO_2 S$, liquid HMTBa has the chemical formula $C_5 H_{10} O_3 S$, and dry HMTBa has the chemical formula $(C_5 H_9 O_3 S)_2 Ca$. Subject merchandise also includes methionine processed in a third country including, but not limited to, refining, converting from liquid to dry or dry to liquid form, or any other processing that would not otherwise remove the merchandise from the scope of these investigations if performed in the country of manufacture of the in-scope methionine or dl-Hydroxy analogue of dl-methionine. The scope also includes methionine that is commingled (*i.e.,* mixed or combined) with methionine from sources not subject to these investigations. Only the subject component of such commingled products is covered by the scope of these investigations. Excluded from these investigations is United States Pharmacopoeia (USP) grade methionine.

Methionine is currently classified under subheadings 2930.40.0000 and 2930.90.4600 of the Harmonized Tariff Schedule of the United States (HTSUS). Methionine has the Chemical Abstracts Service (CAS) registry numbers 583-91-5, 4857-44-7, 59-51-8 and 922-50-9.

According to DOC, imports under HTSUS subheadings 2930.40.0000 and 2930.90.4600 were valued as follows in 2020: $52.1 million (for Japan) and $57 million (for Spain).

The ITC's public report on this investigation will be available by September 28, 2021.

Free Trade Agreements

Mexico Requests Consultations With United States Concerning Automotive Rules of Origin Under US-Mexico-Canada Agreement

On August 20, the Government of Mexico requested consultations with the United States under the US-Mexico-Canada Agreement (USMCA) "for the purpose of avoiding or settling a potential dispute" regarding the Agreement's rules of origin ("ROO") for automotive goods. The request alleges that the United States, through its interpretation of the ROO for automotive parts and finished vehicles, is "imposing certain requirements on motor vehicle producers that are inconsistent with the text of the USMCA and the Uniform Regulations." Specifically, Mexico contends that the USMCA's automotive ROO permit the use of "roll-up" methodologies, which allow materials that have acquired origin by meeting a regional value content (RVC) threshold to be considered fully originating when used as inputs in a subsequent manufactured product (*e.g.*, a finished vehicle). Such methodologies provide additional flexibility for producers of finished goods to satisfy the applicable ROO and therefore obtain preferential tariff treatment. However, the United States has taken the position that the USMCA provisions at issue do not permit the use of roll-up methodologies – a position consistent with its objective to limit the use of foreign content in the North American automotive supply chain.

The United States and Mexico have held informal consultations on this issue at the political and technical levels, but have failed to reach a consensus interpretation. Mexico is now requesting formal consultations under the USMCA's state-to-state dispute settlement mechanism to resolve the matter. If the two governments are unable to resolve the matter through formal consultations, an independent panel will convene in accordance with Chapter 31 of the USMCA to hear the dispute and potentially authorize the imposition of countermeasures, in the event that a violation is found. This alert provides an overview of the relevant USMCA provisions, Mexico's request for consultations, and the next steps in the dispute settlement process.

Background

Like the NAFTA, the USMCA provides that finished vehicles and parts thereof must contain a specified level of regional value content to be considered "originating" for purposes of the Agreement. Only originating vehicles and parts are eligible for duty-free treatment under the USMCA. The ROO for passenger vehicles, light trucks, and parts thereof are set forth in Article 3 of the Appendix to Annex 4-B of the USMCA (Automotive Appendix). As discussed in greater detail below, Article 3 provides separate ROO for vehicles and several distinct categories of parts, namely "core" parts (and groupings thereof), "principal" parts, and "complementary" parts.

RVC for passenger vehicles and light trucks (Article 3.1)

Whereas the NAFTA required that vehicles contain at least 62.5% RVC to be considered originating, the USMCA increases this requirement to 75% for passenger vehicles and light trucks (calculated using the "net cost" method).[39] This increase is being phased in over a three-year period as follows:

Date	RVC (net cost)
July 1, 2020	66%
July 1, 2021	69%
July 1, 2022	72%
July 1, 2023	75%

[39] Under the net cost method, RVC is calculated by subtracting the value of non-originating materials from the total net cost to produce the vehicle and dividing this figure by the vehicle's total net cost.

RVC for core parts, principal parts, and complementary parts (Articles 3.2-3.5)

Under the USMCA, the RVC requirements for parts for passenger vehicles and light trucks range from 65 to 75% net cost (or 75 to 85% under the "transaction value method"),[40] also to be phased in over a three-year period:

- "Core parts," including engines, bodies, gearboxes, and shock absorbers will be subject to a final RVC threshold of 75% net cost (85% transaction value).
- "Principal parts," including tires, mufflers, seats, and ball bearings will be subject to a final RVC threshold of 70% net cost (80% transaction value).
- "Complementary parts," including types of valves, batteries, and lamps will be subject to a final RVC threshold of 65% net cost (75% transaction value).

RVC and alternative calculation methodologies for "super-core" parts (Articles 3.7-3.9)

Table A.2 of the Automotive Appendix, reproduced below, identifies in Column 1 certain core parts to which special rules apply.

Column 1	Column 2
Parts	**Components**
Engine	Heads, Blocks, Crankshafts, Crankcases, Pistons, Rods, Head subassembly
Transmission	Transmission cases, Torque converters, Torque converter housings, Gears and gear blanks, Clutches, Valve body assembly
Body and Chassis	Major body panels, Secondary panels, Structural panels, Frames
Axle	Axle shafts, Axle housings, Axle hubs, Carriers, Differentials
Suspension System	Shock absorbers, Struts, Control arms, Sway bars, Knuckles, Coil springs, Leaf springs
Steering System	Steering columns, Steering gears/racks, Control units
Advanced Battery	Cells, Modules/arrays, Assembled packs

Article 3.7 of the Automotive Appendix provides that a passenger vehicle or light truck is originating only if the core parts listed in Column 1 above are originating. Generally, such parts are originating if they satisfy the 75% RVC threshold applicable to a "core part" under Article 3.2. However, Articles 3.8 and 3.9 provide certain alternative methodologies that producers may use when determining whether these parts are originating:

- Article 3.8 provides that, when calculating the RVC of a core part listed in Column 1, producers have the option to base the value of non-originating materials on (1) the value of *all non-originating materials* used in the production of the part; or (2) the value of any *non-originating components* that are used in the production of the part and are specifically listed in Column 2 of Table A.2. The latter option limits the universe of inputs that may count as non-originating content when determining the RVC of the core part.
- Article 3.9 provides that, instead of calculating the RVC for each of the core parts in Column 1 individually, producers may choose to treat all of the Column 1 parts as a single, "super-core" part for purposes of determining RVC. Where the producer chooses to treat these parts as a single super-core, it must sum the net cost of each part to determine total net cost of the super-core, and may base the value of non-originating materials on: (1) the sum of the value of all non-originating materials used in the production of the parts; or (2)

[40] Under the transaction value method, RVC is calculated by subtracting the value of non-originating materials from the transaction value of the good (i.e., the amount actually paid or payable for the good), and dividing this figure by the transaction value of the good.

the sum of the value of only those non-originating components (listed in Column 2) that are used in the production of the parts. If the RVC of the single, super-core part satisfies the 75% RVC threshold, "each Party shall provide that all [of the Column 1 parts comprising the super-core] are originating[.]"

Dispute over "roll-up" methodology and implications for RVC calculations

As discussed in more detail below, Mexico's interpretation of the automotive ROO would permit the use of "roll-up" methodologies for core parts listed in Table A.2, thus providing additional flexibility for vehicle producers to satisfy the ROO for finished vehicles. The implications of the roll-up methodology may be illustrated by the following, simplified example:

- For purposes of calculating the RVC of the core parts in Table A.2, Column 1 (*i.e.*, the engine, transmission, body and chassis, axle, suspension system, steering system, and battery), a vehicle producer chooses to treat such parts as a single "super-core" part in accordance with Article 3.9, rather than calculating RVC for each part individually;
- The vehicle producer determines that the super-core part, which has a total net cost of $20,000, is originating, because the value of non-originating materials across all of the core parts thereof is only $4,000 (thus satisfying the 75% RVC requirement of Article 3.2);
- For purposes of determining the RVC of the finished vehicle, the producer treats the entire $20,000 net cost of the super-core part as originating content. That is, rather than subtracting the value of non-originating materials ($4,000) from the net cost of the super-core part, the value of non-originating materials is "rolled up" into the net cost of the super-core part.

The United States reportedly has advanced a different interpretation of the relevant provisions of the automotive ROO. Under the United States' interpretation, the value of non-originating materials in the super-core part would not be treated as originating for purposes of determining the RVC of the finished vehicle. Rather, only the portion of the super-core part that is originating ($16,000, in the above example) would be counted as originating when determining the RVC of the finished vehicle. This interpretation discourages the use of core parts (and in turn, components thereof) that are deemed to originate outside the USMCA region.

Request for Consultations

Mexico's request for consultations concerns the United States' "application and interpretation" of Article 3 of the Automotive Appendix, as well as Article 4.5.4 of the USMCA, which sets forth general rules concerning RVC calculations under the Agreement. Mexico's request describes its own interpretations of these provisions, focusing primarily on those applicable to core parts:

Articles 3.8 and 3.9

According to Mexico, the "alternative calculation methodologies" provided for core parts in Articles 3.8 and 3.9 "can be applied in the overall passenger vehicle's or light truck's RVC calculation."

As noted above, Article 3.8 describes two permissible methodologies for calculating the RVC of the core parts in Table A.2, Column 1. The first methodology requires that the value of non-originating materials be based on the value of all non-originating materials used in the production of the part, whereas the second limits the universe of inputs that may count as non-originating to those components listed in Column 2. Mexico contends that "[t]he use of any of these methodologies is allowed to qualify the core parts as originating, *and subsequently, for purposes of calculating the origin of the vehicle*" (emphasis added).

Further, Mexico notes that Article 3.9 "provides an additional flexibility for a 'super-core part' that allows the calculation of the RVC of all core parts as they were a single auto part." Mexico indicates that the interpretation of this provision should be informed by Article 4.5.4 (Regional Value Content) of the USMCA, which states the following:

> Each Party shall provide that the value of non-originating materials used by the producer in the production of a good shall not, for the purposes of calculating the regional value content of the good under [Article 4.5.2 or 4.5.3], include the value of non-originating materials used to produce originating materials that are subsequently used in the production of the good.

In Mexico's view, Article 4.5.4 means that "once a material ('core-part') has qualified as originating and has been used in the production of a good, it must always be treated in the calculations as originating." Therefore, "if a 'super-core part' meets the RVC required percentage, *all the core parts comprising the 'super-core part' would be originating*" (emphasis added). Mexico asserts that the Uniform Regulations adopted by the USMCA Parties "develop and reiterate this principle[.]" Among other provisions, the request cites section 14(1) of the Uniform Regulations, which states in part that "[t]he value of non-originating materials used by the producer in the production of a passenger vehicle, light truck and parts thereof must not, for the purpose of calculating the regional value content of the good, include the value of non-originating materials used to produce originating materials that are subsequently used in the production of the good."

Article 3.7

Article 3.7 of the Automotive Appendix reads in the relevant part as follows:

> Each Party shall provide that a passenger vehicle or light truck is originating only if the parts under Column 1 of Table A.2…used in the production of a passenger vehicle or light truck are originating. Such a part is originating only if it satisfies the regional value content requirement in [Article 3.2], except for an advanced battery.

Mexico interprets this provision as "stipulat[ing] that once the core parts (materials) have satisfied the RVC percentage required in Article 3.2 of the [Appendix], such core parts are originating." Consequently, "for purposes of their use in the production of a subsequent good (vehicle), those core parts would be considered as originating" (emphasis added).

Taken together, Mexico's interpretations of Article 3 of the Automotive Appendix and Article 4.5.4 of the USMCA would permit the use of roll-up methodologies when determining how certain core parts factor into the RVC of a finished vehicle – a position that is at odds with the United States' interpretation.

Next steps

The automotive rules of origin were among the most complex and contentious issues addressed in the USMCA negotiation, given the tensions between the United States' goal of promoting domestic production and investment, on the one hand, and the desire of the other Parties to preserve the cost-competitiveness of the North American automotive industry and encourage North American production that results in originating content. The differences in interpretation between the United States and Mexico reflect these divergent priorities, as well as the consistency of the Biden administration's views on automotive trade with that of its predecessor.

In accordance with Article 31.6 of the USMCA, the two governments will have 75 days to resolve this matter through bilateral consultations, unless they agree on a different time period. If they fail to resolve the matter during the applicable timeframe, Mexico will be permitted to request the establishment of a dispute settlement panel to determine whether the United States' application of the relevant provisions is consistent with the terms of the Agreement. The process of arriving at a panel ruling would involve several procedural steps, including a panel composition process,[41] and the issuance of a panel report within prescribed time frames.[42] In total, the issuance of a

[41] In disputes involving two Parties, Panels will consist of five members (unless the Parties agree to a panel comprised of three members), selected from a pre-determined roster established by the Parties. The USMCA Parties established the Roster of Panelists for Chapter 31 Dispute Settlement Panels on July 2, 2020. *See* FTC Decision No. 1, Annex IV (July 2, 2020).

[42] The Panel must present an initial report to the disputing Parties no later than 150 days after the date of the appointment of the last panelist, except in "exceptional cases," in which the report may be delayed by an additional 30 days. USMCA Art. 31.17(1)-(2). The 30-day deadline may be altered if the disputing Parties agree. See also USMCA Arts. 31.18 and 31.19. The Panel reports must contain (1) "findings of fact"; (2)

final panel report would likely occur no earlier than 315 days after the date on which the request for consultations was submitted (i.e., on or after July 1, 2022).

Whether the dispute is resolved through consultations or a formal panel proceeding, it will have important implications for automotive supply chains, though these are likely to vary significantly depending on the individual circumstances of specific producers and suppliers. Importantly, the USMCA's Rules of Procedure allow a Panel to consider written views submitted by non-governmental entities during the course of the dispute, in addition to hearing the views of the disputing Party governments.[43] Producers and suppliers throughout the automotive supply chain should examine the implications of the Parties' competing interpretations of the USMCA and consider strategies to protect their commercial interests.

Mexico's request for consultations can be viewed **here**.

determinations as to whether the measure at issue is inconsistent with obligations in the Agreement, or a Party has otherwise failed to carry out its obligations in the Agreement; and (3) recommendations, if the disputing Parties have jointly requested them, for the resolution of the dispute. USMCA Art. 31.13.1.

[43] Article 20, USMCA Rules of Procedure for Chapter 31, available at https://ustr.gov/sites/default/files/files/agreements/usmca/AnnexIIIUSMCARulesProcedure.pdf