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WTO AND REGIONAL TRADE AGREEMENTS MONTHLY REPORT

May 2005

Due to the general nature of its contents, this newsletter is not and should not be regarded as legal advice.

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SUMMARY OF REPORTS

Special Report

USTR Publishes 2005 NTE Report on Foreign Trade Barriers

On March 30, 2005, the United States Trade Representative (USTR) published the National Trade Estimate (NTE) Report on Foreign Trade Barriers, which surveys significant trade barriers to U.S. exports. While addressing a wide array of issues, this year's report focuses on the protection and enforcement of intellectual property rights (IPR) and restrictions to services trade.

We highlight the NTE report's comments on the trade practices of major Asian trading partners China, Hong Kong, Indonesia, Japan, Korea, Malaysia, Philippines, Singapore and Thailand.

USTR Identifies Barriers to the Effectiveness of U.S. Telecommunications Trade Agreements

The United States Trade Representative (USTR) recently released its 2005 annual review concerning foreign compliance with U.S. telecommunications trade agreements, including with obligations in free trade agreements (FTAs) and the World Trade Organization (WTO).

The USTR report highlighted five common barriers that have impeded U.S. access to foreign telecommunications markets: (1) excessively high mobile termination rates; (2) restrictions on access to leased lines and to submarine cable capacity; (3) excessive regulatory requirements, including licensing fees; (4) burdensome testing and certification requirements; and (5) limits on technology choices.

Countries targeted for particular concern include China, Germany, India, Japan, Mexico, Peru, Singapore, Switzerland, among others. USTR also aims to expand market access and disciplines in the sector, as well as improve enforcement activity.

Commerce Secretary Gutierrez Provides Outlook on Administration's Trade Priorities

Department of Commerce (DOC) Secretary Carlos Gutierrez discussed the Administration's trade priorities in a recent speech to the Washington International Trade Association (WITA). Gutierrez provided an outlook on the Administration's objectives of pursuing free trade agreements (FTAs), further liberalization in the WTO Doha Round, further economic integration among NAFTA partners, passage of CAFTA through the Congress, and the protection of intellectual property rights. He also commented on the need for broader economic and structural reforms.

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United States

Department of Commerce Introduces New Monitoring Mechanism for Textile Imports and Initiates Safeguard Proceedings on Chinese Textile Imports; More Restraint Actions Expected

The growth in Chinese textile imports in the first quarter of 2005, and reactions from the U.S. government and industry indicate that safeguard actions and other trade restrictions affecting textile imports are on the rise.

The Department of Commerce (DOC) recently modified its monitoring mechanism for textile imports and started releasing preliminary import trade data this month. The release of preliminary data is expected to expedite the filing of antidumping and safeguard petitions against Chinese textile imports, and already has led to the launch of safeguard proceedings.

The U.S. government, through the DOC administered Committee on the Implementation of Textile Agreements (CITA) announced on April 4 that it would self-initiate safeguard proceedings on three Chinese textile products. In other developments, the Government Accountability Office (GAO) released a study urging more clear procedures on safeguard investigations, including for the "threat-based" claims pending before U.S. courts.

House Hearing Signals Frustrations with China Trade Policy; Pressure Mounts to Enact Legislation on China's Currency and Subsidies

At the House Ways and Means Committee hearing on April 14, 2005, Members of Congress made demands for a new approach to China trade policy, including to counteract the effects of China's fixed currency and government subsidies, and lack of compliance with WTO obligations. Pressure on the Administration is also high due to the record trade deficit (estimated in February 2005 at $61 billion), with China accounting for the largest portion. Nevertheless, witnesses from the Administration and private sector urged caution, and a focus on long-term solutions with China.

Meanwhile, legislation related to China's currency and subsidy practices are pending in both the House and Senate, and resisting action on these measures is becoming increasing difficult. Recently, an attempt to remove an amendment related to China's currency practices failed in the Senate, serving as a stark indicator of Senate support for action on China. Still, some Members have cautioned that the proposed measures would impose U.S. unilateral action in violation of its WTO obligations.

Concern over China has also spilled over into the effort to confirm U.S. Trade Representative nominee Representative Rob Portman (R-Ohio). Senator Evan Bayh (D-Indiana) intends to maintain a hold on Portman's nomination until the Senate votes on a bill Bayh is co-sponsoring that would allow the filing of countervailing duty cases against non-market economies like China.

United States Highlights

We also want to alert you to the following United States developments:

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- President Submits Official Request To Extend Trade Promotion Authority To Congress
- US Pledges Commitment To Ensuring WTO Accession And Restoring PNTR For Ukraine
- Senate Holds Confirmation Hearing for USTR Nominee Portman

Free Trade Agreements

Senate Finance Hearing Produces Little Firm Support For DR-CAFTA; Members Focus on Sugar, Labor and IPR Issues

The battle over the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) has begun with the start of Congressional hearings. On April 13, 2005, the Senate Finance Committee hearing produced little firm support for the agreement. Despite the best efforts of DR-CAFTA proponents including acting U.S. Trade Representative **Peter Allgeier**, several Senators including the Finance Committee's ranking Democrat **Max Baucus** (D-Montana) and several Republican members, expressed continued concerns about the implications of DR-CAFTA. Among the key concerns raised were the agreement's provisions on sugar, labor and access to essential drugs.

The day before the Senate Finance hearing, the Ambassadors of Costa Rica and the Dominican Republic spoke an event hosted by the Washington International Trade Association. They reiterated their countries' position that ratification of the agreement would bring economic benefits and help consolidate democracy in the region.

The Administration continues to rely on cabinet secretaries to press the case for DR-CAFTA. On April 11, 2005, Secretary of Agriculture **Mike Johanns** stated that passage of DR-CAFTA would not only secure benefits for U.S. farmers, but would help solidify support for U.S. positions in the WTO Doha Round.

Contentious House Hearing Amidst New Announcements of Opposition/Support for CAFTA

Congressional focus on the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) shifted to the House on April 21, 2005, with a hearing before the Ways and Means Committee.

At the hearing, tempered flared as Committee Democrats decried the lack of consultation with Congress during the negotiations, and attacked the labor and environment provisions. Armed with similar testimony from last week's Senate Finance hearing, Acting U.S. Trade Representative **Peter Allgeier** defended DR-CAFTA, asserting that the agreement that will benefit all parties.

President Bush waded into the DR-CAFTA debate, and in a statement on April 20, 2005, urged Congress to move quickly to adopt the agreement. The President's message, however, failed to gain much traction on the Hill. Moreover, some Members urged the President to take a more active role. Meanwhile, two Montana legislators have come out in opposition to

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the agreement. In addition, several former cabinet officials have entered the debate, issuing a letter supporting the agreement.

The timing of a vote seems uncertain as House Speaker **Dennis Hastert** (R-Illinois) stated that the Memorial Day recess in late May might not be enough time to complete work, despite previous predications by House Republicans, including Ways and Means Chairman **Bill Thomas** (R-California) *(Please see related report this edition).*

Battle Over Labor Provisions DR-CAFTA Intensifies; Ways and Means Chairman Thomas Anticipates Vote by May

The battle over passage of the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) has turned recently to labor issues. Pro and anti-DR-CAFTA forces have released a series of reports about the region's efforts to reform labor practices and enforce existing labor laws.

Trade ministers from the region paid a visit to Washington on April 5, 2005, to rally support for DR-CAFTA. The ministers defended their laws during their visit to Congress, and pledged enhanced enforcement in an action plan on labor. Democrats, led by Sander Levin (D-Michigan), continue to criticize the countries for failing to meet core International Labor Organization (ILO) standards.

In related developments, House Ways and Means Chairman Bill Thomas (R-California) has pledged to bring DR-CAFTA to a vote in the House before the Memorial Day recess in late May. The pledge comes as informal vote counts show supporters of DR-CAFTA short 30 to 40 votes in the House.

US-Andean FTA Achieves Some Progress in Latest Round; Substantial Differences Remain as June "Deadline" Approaches

Upon the conclusion of the eighth round of the US-Andean FTA negotiations on March 21, 2005, negotiators indicated that major differences remain in a number of areas including agriculture and rules-related issues.

The latest round addressed agriculture tariff and quota liberalization, rules of origin, safeguards for agricultural and other goods, extending intellectual property and investment protection, telecommunications services, among other issues. Less attention was paid during this round to industrial market access and services issues.

Negotiators have moved the target date for concluding negotiations to June 2005 (initial deadline was January 2005). The next round of talks are scheduled for Lima, Peru on April 18-22, 2005.

Free Trade Agreements Highlights

We also want to alert you to the following FTA development:

- US And Thailand Hold Third Round Of Negotiations On FTA

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US-European Union

USTR Publishes Annual Report On EU Trade Barriers To US Exports

On March 30, 2005, the United States Trade Representative (USTR) published the 2005 National Trade Estimate (NTE) Report on Foreign Trade Barriers. The report examines the trade practices of the 61 largest US export markets, listing the most significant barriers to US exports of goods and services, US foreign direct investment, and intellectual property rights (IPR) protection.

With regard to the European Union, the report notes that:

- US exporters continue to face "chronic" barriers, of which a number have already been highlighted in previous NTE reports;

- The EU enlargement has resulted in new barriers due to the application of EU tariff, non-tariff, and services-related measures by the new Member States, while existing problems surrounding the lack of uniformity and transparency of the EU customs administration have become more prominent;

- The EU's policy of subsidizing the development, production, and marketing of large civil aircraft (LCA) has a distorting effect;

- Other barriers result from restrictive regulatory approaches that do not reflect a sound assessment of the actual risks posed by the goods in question and that rely on ill-defined concepts of precaution, such as wine restrictions and agricultural biotechnology; and

- A number of emerging EU policies may threaten to disrupt trade in the future, such as the proposed EU regulation on registration, evaluation, and authorization of chemical products (REACH).

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US EU Highlights

We also want to alert you to the following US-EU developments:

- Commission Proposes Sanctions In Retaliation For US Failure To Repeal Byrd Amendment; Amendment Supporters In Congress Issue Letter Opposing Repeal
- US And EU Fail To Resolve Dispute On Subsidization Of Boeing And Airbus By Set Deadline
- WTO Establishes Dispute Settlement Panel To Judge On EU Customs Regime; USTR Requests Comments
- WTO Establishes Dispute Settlement Panel To Rule On US Jobs Act; USTR Requests Comments

US-Latin America

FTAA

GAO Issues Report on FTAA Progress

The latest GAO report on the FTAA negotiations analyzes last year's meetings, developments and failures of the negotiations. The lack of agreement between the United States and Brazil is the key obstacle. The most contentious issues are market access, agriculture, intellectual property rights, government procurement, services and investment.

The report emphasizes three main factors that weakened the negotiations: i) differences between United States and Brazil and its principal allies, ii) the focus on other negotiating forums and iii) unsuccessful negotiation mechanisms.

The report concludes that there are some positive signs of progress for this year. These signs include i) meetings between U.S. and Brazilian officials during the first months of the year, ii) WTO developments, iii) the 2005 Summit of the Americas, and iv) the recognition by FTAA partners that the process is worth pursuing.

NAFTA

Mexican Senate Approves Modifications to NAFTA Rules of Origin

On March 16, 2005, the Mexican Senate approved several modifications to Annex 401 of the North American Free Trade Agreement (NAFTA) on Rules of Origin (ROO), known as the "Track I" NAFTA ROO package. The modifications eliminate and/or create rules of origin within NAFTA Annex 401, including chapters 84 and 85 of Mexico's Harmonized Tariff Schedule.

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Multilateral

Responses to USTR Request on WTO Doha Round Negotiations Generally Positive, But Anxieties Toward Trade Liberalization More Apparent

U.S. industry associations, companies and other interested parties provided mostly supportive views in response to the U.S. Trade Representative's (USTR) most recent request for public comments on the WTO Doha Round negotiations. Many respondents see a real chance for realizing improved market-access if the Round concludes by next year.

Most of the comments submitted on agriculture, non-agriculture market access ("NAMA") and services still favor an ambitious agenda on improving market-access and trade disciplines. Agricultural interests comprised the majority of the respondents, and provided mixed views toward removing U.S. trade barriers and domestic support. Many industrial and manufacturing groups support WTO negotiations, but expressed concern about growing U.S. trade imbalances with China in particular – and some sought maintaining U.S. tariff protection.

In addition, respondents provided perspectives on other areas of negotiation, including rules-related issues (e.g. disciplines on antidumping and subsidies), trade facilitation and dispute settlement. The comments were particularly divided over reform of antidumping and other trade remedies.

WTO Panel Rules On EC Regulations Governing Geographical Indications

On March 15, 2005, a WTO Panel released a mixed decision in the challenge by the United States and Australia to EC rules governing so-called "geographical indications" (GIs). GIs identify a product with a particular region, such as Florida oranges, Parma ham, or Darjeeling tea.

The Panel ruled that the EC Regulation on GIs violated the national treatment obligations of the EC under the WTO *Agreement on Trade-Related Aspects of Intellectual Property Rights* (TRIPS), largely because it accorded national treatment only on a reciprocal basis. However, the Panel rejected the portion of the complaint based on the trademarks provisions of TRIPS. Although the Regulation was found to violate WTO trademarks disciplines, it was nevertheless saved as a "limited exception" to trademark rights.

WTO Appellate Body Rules On US Federal Law Prohibiting Internet Gambling

On April 7, 2005, the WTO Appellate Body ruled that U.S. federal law prohibiting Internet gambling violates the obligations of the United States under the WTO General Agreement on Trade in Services (GATS). The Appellate Body upheld a complaint by Antigua that the U.S. laws were inconsistent with the market access commitments of the United States for services trade.

The United States had invoked the exception in the GATS for laws "necessary to protect public morals or to maintain public order", and the Appellate Body agreed that the U.S. measures could be provisionally justified under this provision. However, the United States failed to demonstrate that its measures were not applied in a discriminatory manner, given

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evidence of a separate U.S. law that exempted domestic service suppliers - but not foreign service suppliers - from the ban on internet betting services for horse racing.

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REPORTS IN DETAIL

SPECIAL REPORT

USTR Publishes 2005 NTE Report on Foreign Trade Barriers

SUMMARY

On April 1, 2005, the United States Trade Representative (USTR) published the National Trade Estimate (NTE) Report on Foreign Trade Barriers, which surveys significant trade barriers to U.S. exports. While addressing a wide array of issues, this year's report focuses on the protection and enforcement of intellectual property rights (IPR) and restrictions to services trade.

We highlight the NTE report's comments on the trade practices of major Asian trading partners China, Hong Kong, Indonesia, Japan, Korea, Malaysia, Philippines, Singapore and Thailand.

ANALYSIS

On April 1, 2005, the United States Trade Representative (USTR) published the 2004 National Trade Estimate (NTE) Report on Foreign Trade Barriers. The annual report, as required by the Omnibus Trade and Competitiveness Act of 1988 (the 1988 Trade Act), is an inventory of the most significant foreign barriers to U.S. exports of goods and services, foreign direct investment by U.S. persons, and protection of intellectual property rights (IPR).

The 2005 NTE report classifies foreign trade barriers into ten different categories, covering all governmental measures and policies, whether consistent or inconsistent with international trading rules, that restrict, prevent, or impede the international exchange of goods and services. These categories include:

- Import policies
- Standards, testing, labeling, and certification
- Government procurement
- Export subsidies
- Lack of intellectual property protection
- Services barriers
- Investment barriers
- Anticompetitive practices with trade effects tolerated by foreign governments
- Trade restrictions affecting electronic commerce

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- Other barriers

The report examines the trade practices of 56 countries, which are the largest export markets for the US. We summarize below the report's findings on trade barriers of major Asian trading partners China, Hong Kong, Indonesia, Japan, Korea, Malaysia, Philippines, Singapore and Thailand.

China

The NTE offers a mixed assessment of China's trade performance in 2004. While complimenting steps China has taken in areas such as tariff reduction, trading rights and tax policy, the report raised a number of concerns in the areas of agriculture, industrial policy, services and intellectual property rights (IPR). Specific issues raised in the NTE include:

- ***Tariff classification and tariff valuation*** remain inconsistently applied across China. Importers have reported that Chinese customs officials continue to use "reference price" lists, rather than relying on actual transaction values. In the software sector, officials are still applying royalties and other fees inappropriately. Chinese customs has also reportedly valuated various forms of digital media incorrectly, subjecting the imports to additional fees.

- ***Non-tariff and regulatory barriers*** remain a significant obstacle to accessing the Chinese market, particularly in the service sector. Foreign firms face high entry barriers, including excessive capitalization requirements, and branching restrictions. Restrictions on branching continue despite China's elimination of geographic restrictions on foreign service providers. Express delivery continues to face a weight restriction of 500 grams, although recent proposals have suggested reducing this limit to 350 grams.

- The development of ***China-only technical standards*** presents a significant obstacle to U.S. exports. Obtaining the necessary testing of goods is often a slow and cumbersome process, with theft of intellectual property during standards testing commonplace. Importers have also reported that testing and certification procedures are not transparent, and also may involve officials from rival firms. The lack of coordination among China's various standards bodies further compounds the difficulty in obtaining needed approvals.

- Despite some positive steps taken by China in 2004, ***IPR protection*** remains seriously inadequate. Losses due to the piracy of copyrighted materials are estimated at US$3.0 billion annually. In 2004, China enacted changes to its criminal laws, with an aim to facilitate prosecution of those infringing IPR. Notwithstanding the amendment, enforcement is still lackluster. The US continues to monitor China under Section 301 of the Trade Act, and could impose trade sanctions or pursue WTO dispute settlement due to China's failure to combat adequately IPR violations.

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Hong Kong, Special Administrative Region

The NTE report provides a generally favorable report of Hong Kong's policies with respect to IPR enforcement, a long-standing source of friction between Hong Kong and the US. The report noted that Hong Kong has begun to make use of its organized crime laws to pursue networks of copyright violators. Pharmaceutical companies in the US have also expressed concern about the repackaging of counterfeit drugs that are then exported abroad.

Indonesia

Indonesia's new President Yudhoyono has pledged to pursue reforms based on open markets and free trade in an attempt to reassert Indonesia's stature in the region. The tsunami of December 2004 has had a profound human effect on the residents of Sumatra, however the long-term economic implications of the disaster remain unclear. A lack of regulatory transparency and high rates of corruption remain the core barriers to trade and investment in Indonesia. Trade related concerns cited in the NTE include:

- The imposition of ***bans on the imports of rice, sugar and salt*** during harvests in 2004.

- Continued high tariffs on agricultural commodities and other sensitive goods such as alcohol and automotive products.

- De-facto ***quantitative restrictions*** on certain agricultural imports such as meat and poultry, and mandatory labeling.

- Rampant ***copyright and patent infringement*** continue unabated despite passage of additional IPR laws in 2001. A lack of understanding among law enforcement and judicial officers, combined with a poor prosecution record has rendered the Indonesian justice system an ineffective deterrent against IPR violations.

- ***Barriers to services trade*** remain high in some sectors, notably distribution, financial, accounting, banking, and telecommunications. Corruption further deters foreign service providers from entering Indonesia.

Japan

In June 2001, President Bush and Prime Minister Koizumi established the Regulatory Reform and Competition Policy Initiative, which works to, *inter alia*, facilitate regulatory reforms related to trade. Through this mechanism, the US has been able to make recommendations to open further the Japanese market for U.S. exports. The NTE reiterates several ongoing U.S. requests to Japan for regulatory reform in various sectors including the telecommunications, energy, information technology, medical devices and financial services.

With respect to import barriers, the NTE expressed several concerns:

- Serious ***restrictions on U.S. agricultural*** remain in the form of tariff rate quotas (TRQs), domestic use requirements for corn and potatoes, and sanitary and phytosanitary measures with respect to beef and pork. Japan imposed a ban on

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imports of U.S. beef after the discovery of a single case of BSE in Washington State.

- ***Government procurement*** practices in Japan continue to deny effective entry of U.S. computer equipment, construction, architecture, and engineering services. The US has pushed Japan to confront problems of rigged bidding in major public works projects.

- Despite a strong ***IPR protection*** regime, Japan's patent administration system is slow to render final judgment in patent litigation. In addition, Japan needs to take steps to tighten use of copyrighted materials via the Internet.

- Legal and regulatory barriers in the ***service sector***, notably insurance, accounting, legal, and medical, continue to prevent effective entry into the Japanese market by U.S. firms. The insurance sector is the most heavily regulated, with domestic firms enjoying regulatory and tax advantages over foreign competitors. The US is monitoring efforts by Japan to privatize the Postal System and its insurance operations. New insurance products introduced by Japan Post in 2004 have resulted in renewed criticisms of barriers to Japan's insurance sector.

Beyond general regulatory concerns, the NTE reviewed sector specific obstacles. The aerospace, auto and auto parts, civil aviation, electric utilities, paper, and sea transport sectors are all cited as sectors with barriers to U.S. exports.

Korea

Korea continues to use a combination of non-tariff barriers and domestic supports to protect several sectors from foreign import competition. On the non-tariff barrier front, the development of "Korea-only" technical standards persists as a major barrier to trade. The government-owned Korea Development Bank continues to serve as the government's chief mechanism for providing preferential support to favored industries. In addition, the NTE raised several other areas of concern:

- The US continues to monitor ***IPR enforcement*** in Korea, despite passage of new laws in 2004. Online piracy remains a serious concern, and Korea has pledged to take legislative action to strengthen protections for copyright holders. The US continues to urge Korea to impose stiffer criminal penalties on IPR violators.

- Korea maintains a "negative list" approach to the ***service sector***, and has done little to liberalize sensitive sectors such as advertising, cable TV, accounting and legal services. Furthermore, IMF mandated reforms in the banking and financial sectors as a result of the Asian financial crisis have not been completely implemented and suffer from a lack of regulatory transparency.

- Despite record auto imports by Korea, access to the Korean market remains highly limited owing to ***technical standards and domestic tax laws***.

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Malaysia

- ***IPR protection*** and enforcement is of increasing concern, with the Philippines having few successful cases of prosecution and imprisonment. A lack of legislation and enforcement resources has resulted in increasing rates of piracy of optical media such as CDs and DVDs. In 2004, the US government named the Philippines to its Special 301 Priority Watch List for the fourth year running.

- ***High tariffs*** remain Malaysia's preferred tool for preventing the entry of foreign goods as Malaysia's average effective tariff rate remains close to 19%. Motor vehicles and textiles have been targeted for protection by high tariffs and NTBs. In addition, Malaysian auto producers continue to enjoy rebates on excise taxes.

- ***Piracy of optical media*** such as CDs and DVDs remains a serious concern. Optical media pirated in Malaysia has been found in several countries throughout the Asia-Pacific region. While its government has made headway in reducing the judicial backlog of infringement cases through prosecutions, imprisonments and fines, much work remains in educating the general public about IPR to the businesses that own them.

- The ***service sector*** remains highly protected and Malaysia has yet to offer much liberalization in the context of the Doha Round. In some sectors, such as legal services, foreign entities may not provide services of any kind. In other sectors, such as accounting, banking and engineering, foreign companies are required to partner or affiliate with Malaysian firms. Most affiliate agreements require government licenses and investment by foreign companies in the Malaysian service sector is restricted.

- ***Transparency*** of government decision-making and procedures remains an issue on government software procurement and procurement projects. While Malaysia has not signed the WTO Government Procurement Agreement, its public policy objectives encourage greater participation of ethnic Malays into the economy, keeping out foreign competition.

Philippines

Corruption and a lack of regulatory transparency continue to undermine trade with the Philippines. The NTE also raises concerns of backsliding on commitments in the area of tariff reduction and IPR enforcement. The report also criticizes the Philippines for various trade deterring policies:

- In 2004 the Philippine Tariff Commission ***increased tariffs*** in several sensitive sectors, and slowed reductions in other sectors. While the increased tariffs remain within the Philippines bound tariff commitments under the WTO, the increasing protectionist sentiment is concerning. Tariffs in the agricultural and automotive sectors continue to remain high.

- ***IPR protection*** and enforcement is of increasing concern, with the Philippines having few successful cases of prosecution and imprisonment. A lack of

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legislation and enforcement resources has resulted in increasing rates of piracy of optical media such as CDs and DVDs. In 2004, the US government named the Philippines to its Special 301 Priority Watch List for the fourth year running.

- Restrictions in the ***services sector*** are pervasive, with financial services, insurance, and banking sectors restricted in terms of foreign competition. Compounding this is a series of investment restrictions in the services and manufacturing sectors.

- The ***Philippine Customs Department remains corrupt*** as periodic procedural irregularities continue to occur. Contrary to a 2001 Philippine law, continued private sector involvement in the valuation of imports and inconsistent applications of rules are still practiced and remain as important US trade issues.

Singapore

The NTE sounded a generally positive note about access for exports into Singapore, reflecting the benefits resulting from the entry into force of the U.S.-Singapore Free Trade Agreement. Tariffs on U.S. exports have been eliminated, and previous barriers to the telecommunications sector have been overcome through the FTA. Nevertheless, the main barriers in Singapore's economy remain in the service sector. Foreign audiovisual ad media service provides are effectively shut out of the market, and the use of direct-to-home satellite television remains prohibited. In addition, foreign entities are prohibited from owning majority stake in domestic free-to air broadcasting, cable and newspaper firms, and the directors and executive officers of audiovisual service providers are generally required to be citizens of Singapore.

In other developments, IPR enforcement in Singapore has improved, however the absence of criminal penalties for the use of unlicensed software remains a problem. Singapore, in its FTA agreement with the US, has pledged to close this loophole in its criminal law. Transshipment of pirated goods through Singapore's ports, particularly with software, optical and music media, has yet to be addressed meaningfully as Singapore still does not collect information on this trade.

Thailand

While the US and Thailand continue negotiations toward an FTA, a number of trade barriers remain burdensome for U.S. companies, including:

- The ***complicated tariff regime and the high tariff structure***. The highest rates apply to imports of agricultural products, autos and auto parts, alcoholic beverages, textiles and some electrical appliances.

- The overall ***agricultural import policy*** aimed at protecting domestic producers and impeding U.S. market access.

- The ***tax administration***, which is complicated and not transparent, and the ***customs valuation authority***, which tends to be non-transparent and often arbitrary and irregular. These last two barriers are acute in the automotive sector.

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- The required ***sanitary and phytosanitary (SPS) standards*** on testing, labeling, and certification permits for all imports of food and pharmaceutical products.

- The barriers in the ***services sectors*** toward telecommunications, legal, financial, construction, architecture, engineering, and accounting services.

- ***Discriminatory and non-transparent government policies***, especially regarding government procurement. The government protects several government firms from foreign competition, retains authority to set price ceilings for a number of products, and uses control review mechanisms that are non-transparent.

- ***Corruption in the Thai Customs*** department remains a serious problem. The department also has incentives for revenue maximization versus compliance with legal requirements.

- High-level of ***IPR piracy***.

OUTLOOK

The 2005 NTE report highlights the major barriers U.S. exporters face in key markets in Asia and abroad. The congressionally mandated report provides USTR and Members of Congress with a list of concerns on which to focus as the Administration pursues its competitive liberalization strategy, including through FTA and WTO negotiations, among other trade initiatives. In some cases, failure to resolve issues raised in the report results in WTO disputes, or other actions.

USTR Identifies Barriers to the Effectiveness of U.S. Telecommunications Trade Agreements

SUMMARY

The United States Trade Representative (USTR) recently released its 2005 annual review concerning foreign compliance with U.S. telecommunications trade agreements, including with obligations in free trade agreements (FTAs) and the World Trade Organization (WTO).

The USTR report highlighted five common barriers that have impeded U.S. access to foreign telecommunications markets: (1) excessively high mobile termination rates; (2) restrictions on access to leased lines and to submarine cable capacity; (3) excessive regulatory requirements, including licensing fees; (4) burdensome testing and certification requirements; and (5) limits on technology choices.

Countries targeted for particular concern include China, Germany, India, Japan, Mexico, Peru, Singapore, Switzerland, among others. USTR also aims to expand market access and disciplines in the sector, as well as improve enforcement activity.

ANALYSIS

On March 31, 2005, the United States Trade Representative (USTR) issued its annual review of the operation and effectiveness of U.S. telecommunications trade agreements, as

required under Section 1377 of the Omnibus Trade and Competitiveness Act of 1988 (19 U.S.C. § 3106). This review was based, among other things, upon the input provided by comments and reply comments submitted by twenty-two parties in relation to trading partners' compliance with obligations in free trade agreement (FTA) and the World Trade Organization (WTO).

I. USTR Section 1377 Report Identifies Key Barriers and Target Countries

USTR highlighted five common barriers that have impeded U.S. access to foreign telecommunications markets:

(1) excessively high mobile termination rates;

(2) restrictions on access to leased lines and to submarine cable capacity;

(3) excessive regulatory requirements, including licensing fees;

(4) burdensome testing and certification requirements; and

(5) limits on technology choices.

While the five concerns that USTR identified are not necessarily new, their persistence warranted inclusion in this year's report.

USTR further indicated an intent to monitor developments in a number of specific countries, with particular attention paid to anticipated regulatory decisions that should address certain of these concerns. Should such decisions not be forthcoming as expected, USTR stands ready to take additional actions including WTO dispute settlement proceedings. Countries of particular concern for one or more of these issues include China, Germany, India, Japan, Mexico, Peru, Singapore and Switzerland.

II. Barriers Commonly Identified in Key Markets

We discuss below five common barriers in key markets. We also highlight other barriers raised in the Section 1377 report.

A. Excessively High Mobile Termination Rates

Given that the number of global mobile subscribers now exceeds that of wireline networks, the high cost of completing calls on mobile networks in foreign countries has assumed even greater importance. While USTR noted a general trend towards reduction of mobile termination rates and heightened awareness by regulators in certain countries, such as France and Australia, efforts in other countries – including Germany, Switzerland, Mexico, Peru and Japan — continue to lag.

Part of the underlying problem may be attributable to reliance on a "calling party pays" (CPP) rate system, where effective competition as a check on excessive rates is less likely to occur and a greater imperative for regulatory intervention is present. To complicate matters further, Mexico, which currently utilizes a "receiving party pays" (RPP) rate system, is considering a shift to a CPP rate system for long-distance calls. While acknowledging that countries should have the discretion to choose between RPP and CPP systems, and the Mexican regulator's pledge to intervene if such a switch occurs and negotiations between fixed and mobile operators do not produce cost-based rates, USTR nonetheless expressed the

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concern that long lead times and delays associated with such negotiations and any subsequent regulatory intervention could at least temporarily result in new termination charges adding tens of millions of dollars to the price of U.S. phone calls placed to mobile phone subscribers in Mexico. USTR intends to monitor these developments closely and is fully prepared to engage Mexican authorities to minimize any adverse impact of such a change.

B. Restrictions on Access to Leased Lines and to Submarine Cable Capacity

USTR identified a number of possible impediments adversely affecting reasonable and nondiscriminatory access to leased lines and submarine cable capacity that could result in excessive pricing and lengthy provisioning times. Germany and India are of particular concern in this regard, although USTR also identified certain issues involving Singapore as well.

The main concern in the case of Germany is whether the new telecommunications law provides the regulator with sufficient enforcement measures to control abusive practices on the part of the dominant operator, such as a refusal to guarantee provisioning times in private contracts or unwillingness to offer competitors access to specific lease line products (i.e., partial private lines or ISDN lines) that it uses itself.

With regard to India, USTR had noted continuing complaints about access to and use of submarine cable capacity under the control of the dominant international carrier. That operator's refusal to permit interconnection and to activate additional capacity has resulted in artificial shortages of bandwidth into and out of India as well as price inflation, hampering the provision of robust global telecommunications services. The concerns in the case of Singapore relate to the presence of interconnection arrangements that have hampered competition by either requiring the purchase of bundled service with unnecessary features or the assembly of individual network elements in an inefficient manner.

C. Excessive Regulatory Requirements, Including Licensing Fees

In recent years, the imposition of excessive regulatory requirements has given rise to newer types of market access barriers in the form of high licensing fees, high capitalization requirements, restrictions on resale and restrictions on the entities with whom a foreign licensee can partner. Such practices would appear to be contrary to the requirements of Article VI of the WTO General Agreement on Trade in Services (GATS), which require that measures of general application in sectors where specific service commitments have been undertaken should be administered in a reasonable, objective and impartial manner, neither unnecessarily restricting service supply nor imposing greater burdens than absolutely necessary for service quality assurance. Moreover, many WTO Members have adopted the "Reference Paper" disciplines on anti-competitive practices, which addresses certain regulatory requirements. Countries engaging in questionable practices here include India, Colombia, and China.

D. Burdensome Testing and Certification Requirements

Both Mexico and Korea were identified as potentially imposing excessively burdensome testing requirements for telecommunications equipment. In the case of Mexico, the concern was that new requirements would be imposed prior to the adoption of accompanying safeguards that would allow testing to be conducted in the U.S. or Canada.

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The situation in Korea has improved to the extent that Korea has now indicated that it would be prepared to permit telecommunications equipment testing to occur in countries with whom it has established bilateral arrangements, which USTR intends to pursue as a matter of priority. Moreover, Korea and the United States are reportedly in discussions to launch negotiations on an FTA later this year; if launched, this requirement should become less onerous.

E. Limitations on Technology Choices

The mandatory imposition of certain technical standards can also limit technology choice and impede effective market access. In the case of China, the most recent manifestation of this relates to the terms and conditions for new mobile wireless licenses in the 2 GHz band, and the likelihood that licenses will be awarded in a manner that advantages China's home grown 3G standard, TD-SCDMA. USTR continues to monitor the situation as China has yet to implement fully the new standard.

In related developments, Korea has recently awarded three licenses for a broadband wireless service where it has required that all licensees use a single standard selected by the Korean government, with the effect of limiting the scope of technology that can be marketed in Korea. Even though Korea has selected an international standard in this regard rather than an indigenous one, the manner of its implementation still leaves scope for restricting the ability of U.S. and other firms with proven technologies to compete in this dynamic market. USTR intends to continue to urge Korea to instead consider reliance on international voluntary standards that can be applied in a flexible and technology neutral manner, and which do not effectively serve as barriers to U.S. telecommunications technologies entering the Korean market.

F. Other Issues: Interconnection Charges in Mexico and Japan, Allocation of Mobile Frequencies in Japan

USTR identified two country specific sets of issues warranting special attention. In the case of Mexico, persistently high "off-net" interconnection charges by the national operator had resulted in interconnection charges to regions not yet open to competition that were as much as six times higher than other interconnection rates in Mexico. (USTR has already succeeded in similar complaints at the WTO against excessive interconnection charges by Mexico's dominant operator Telmex, and might make take further action.)

In the case of Japan, additional concerns addressed apparent unjustified wireline interconnection rate increases over a three-year period and a lack of transparency in the allocation of new frequencies to mobile wireless providers. These wireline interconnection rate increases represent a development not present in any other OECD country, and have the effect of constituting an exclusionary price squeeze on its competitors seeking such interconnection. The source of this problem is the Japanese regulator's prior acquiescence in allowing the national operator to recover non-traffic sensitive costs via per minute interconnection charges. While the regulator has committed to eliminate this practice in the future, it has afforded a five-year transition period for this to occur.

Also of concern is the fact that the Japanese regulator still has not formalized procedures for allocating additional wireless mobile spectrum, leading to concerns that

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spectrum allocation practices in Japan will continue to favor incumbents (who have yet to exhaust their existing assignments) over possible new entrants. Given the high concentration of Japan's mobile wireless market (the top three operators have close to 100% market share), it is more important than ever that new spectrum assignments be conducted in a transparent and impartial manner and with an eye towards promotion of additional competition.

III. Anticipated Regulatory Actions

USTR identified a number of key regulatory actions that its trade partners were expected to take during the course of this year to address certain of these problems. USTR intends to monitor such regulatory deliberations quite closely, including the following:

- Peru's consideration of the implementation of cost-oriented mobile interconnection rates.
- Germany's completion of its market analysis studies concerning the possible presence/implications of an operator possessing Significant Market Power with respect to mobile termination rates.
- Mexico's consideration of a new mobile interconnection rate system.
- Japan's allocation of new spectrum for mobile operators.
- China's completion of its new telecommunication law and assignment of spectrum for new mobile services.

OUTLOOK

As many of these concerns, both general and specific, have been carried over from prior years' annual reviews, an increased emphasis on the part of USTR in encouraging appropriate regulatory intervention can be expected. Particularly troublesome, according to Acting U.S. Trade Representative Peter F. Allgeier, is the "the tepid commitment [that] some of our trade partners have shown to competition in the telecommunications sector", singling out China, India and Japan as specific examples where "national operators are already competing on a global level, but remain protected at home by relatively closed markets."

In this regard, Mr. Allgeier also reaffirmed the U.S.'s unwavering commitment to "work[ing] vigorously to strengthen and enforce our trade rights in these countries and elsewhere." Presumably, USTR will pursue a dual approach to fulfill these objectives: (1) negotiate further market-access and regulatory disciplines in ongoing and future WTO/GATS and FTA talks; and (2) initiate disputes against trading partners if they fail to meet existing WTO or FTA obligations in the sector.

* * *

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Commerce Secretary Gutierrez Provides Outlook on Administration's Trade Priorities

SUMMARY

Department of Commerce (DOC) Secretary Carlos Gutierrez discussed the Administration's trade priorities in a recent speech to the Washington International Trade Association (WITA). Gutierrez provided an outlook on the Administration's objectives of pursuing free trade agreements (FTAs), further liberalization in the WTO Doha Round, further economic integration among NAFTA partners, passage of CAFTA through the Congress, and the protection of intellectual property rights. He also commented on the need for broader economic and structural reforms.

ANALYSIS

On March 29, 2005, the newly appointed Secretary of Commerce, Carlos Gutierrez, addressed the Washington International Trade Association (WITA) on the Administration's trade priorities. The event was Secretary Gutierrez' first opportunity to meet with the international trade community in Washington D.C. Secretary Gutierrez was sworn into office on February 2, 2005 after serving as the chief executive officer of Kellogg Company.

I. Need for Reform of Broader Economic Issues; Dealing with the Trade Deficit

Secretary Gutierrez began his comments by setting out the broader economic context for his remarks. He pointed out that the US has the fastest growing economy of the developed world. While the U.S. global domestic product[1] grew 4.4 percent last year, the economies of most of America's trading partners, including Canada, France, Germany, Italy, Japan or the United Kingdom grew between 2.5 and 2.6 percent. In this context, he pointed out that US has added 262,000 jobs the previous month, and 3 million jobs since May 2003.

To keep the economy vibrant and growing, the President set out an aggressive agenda of economic reforms, Gutierrez said. For example, he cited the need for regulatory and legal reform, commenting that it was "terrible" that many businesses were more worried about getting sued than about growing their business. A "very important first step" was taken when the Congress passed the Lawsuit Abuse Reduction Act;[2] and the President seeks to expand these legal reforms.

Other structural issues in need of reform include rising health care costs and energy costs (aimed at reducing U.S. reliance on foreign oil and developing new sources of energy for the future). Finally, Secretary Gutierrez addressed the need for social security reform, pointing out that unless action was taken, social security as we knew it today would not be

[1] Secretary Gutierrez referred to GDP as "the number [he] likes the most as an economic indicator"

[2] Generally perceived to limit the availability of class action lawsuits by limiting the choice of law options in civil tort cases to residency, place of accident or defendant's place of business. In addition, the Act made sanctions against attorneys or parties who file frivolous lawsuits mandatory (used to be discretionary), dispensed with safe harbor provisions (which allowed parties to avoid sanctions by giving them 21 days to withdraw a frivolous suit after a motion for sanction was filed), and expanded sanctions for harassing conduct during discovery.

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there for our children. To illustrate how severe the situation is, Gutierrez pointed out that the "social security fund" referred to in the media, was empty and unfunded.

In response to a question from the audience, Secretary Gutierrez discussed the trade deficit. He noted that while U.S. exports rose over 12% last year, US imports grew by 18%. The key to reducing the trade deficit, he said, would be to reduce the 6% gap between the two, which would be difficult due to the fact that the U.S. economy, the biggest in the world, was growing faster than the smaller economies of U.S. trade partners (like the European Union and Japan), which were growing slower. Due to this dynamic, it is easier for foreign firms to increase their exports to the US, than it is for U.S. companies to increase their exports. The solution, said Secretary Gutierrez, was to continue opening up foreign markets, supporting exports, and ensuring that U.S. exporters are competing on a leveled playing field.

II. NAFTA Has Had Positive Effects on North America

Secretary Gutierrez commented on the recently launched "Security and Prosperity Partnership of North America."[3] He said that ensuring the security of borders was "a first and foremost" goal, but that the NAFTA partners did not want to hinder the free flow of goods, wanting the "trade doors" to remain open. He acknowledged that finding the balance between the two goals was "the tricky part."[4] Gutierrez praised the economic effects of NAFTA on the economies of Canada, Mexico, and the US. He pointed out that each NAFTA country has grown "considerably faster" than it did prior to NAFTA. Secretary Gutierrez narrowed in on Mexico, pointing out that Mexico has "the best economic numbers they've had in three to four decades."

III. U.S. – Chile FTA a Success

Secretary Gutierrez praised the effects of the US-Chile free trade agreement, which entered into force in January 1, 2004. He pointed out that U.S. exports increased 32% in the first six months of the year, growing from $1.28 to $1.70 billion, reversing a downward trend in U.S. market share in the Chilean economy. Discussing particular sectors, Gutierrez pointed to an 11% increase in agricultural exports, 67% increase in construction equipment exports, 28% increase in medical equipment exports, and 76% increase in paper exports.

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[3] Initiative launched by President George W. Bush of the US, President Vincente Fox of Mexico, and Prime Minister Paul Martin of Canada during their trilateral meeting in Waco, Texas, on March 23, 2005. As part of the efforts to protect North America from external and internal threats, and to streamline legitimate cross-border trade and travel, the countries will implement common border-security strategies, enhance infrastructure protection, implement a common approach to emergency response, implement improvements to aviation and maritime security, enhance intelligence partnerships, combat transnational threats, and implement a border-facilitation strategy.

Similarly, to improve competitiveness and enhance the quality of life, the partnership participants will pursue regulatory cooperation maintaining high health and safety standards. The countries will also promote sectoral cooperation in energy, transportation, financial services, technology and other areas. Other initiatives include reducing the costs of trade and enhancing environmental stewardship. Ministerial-level working groups will be established to set goals and identify concrete steps. Within 90 days, the ministers will issue initial reports. Thereafter, the groups will report semi-annually.

[4] A similar problem of finding a balance between security and open borders plagues US post-9/11 visa policies. For more details, please see *WC Trade Alert--Administration and Business Community Struggle Over U.S. Visa Policies and Their Impact on Trade – February 17, 2005*.

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IV. CAFTA-DR Passage an Immediate Priority

Secretary Gutierrez emphasized that the Bush Administration will pay "considerable attention" to passage of CAFTA-DR in the Congress.[5] He emphasized the benefits of CAFTA-DR, citing the recent US Chamber of Commerce study showing that CAFTA-DR would increase sales by eight key U.S. states by more than $3 billion annually.[6] Gutierrez pointed out that CAFTA-DR would level the playing field for U.S. exporters to Central America, because 80% of CAFTA region products already come to the US duty-free under various preferential programs. After CAFTA-DR comes in force, U.S. exporters would benefit from similar preferential access to Central American markets. The sectors benefiting most would be agriculture,[7] information technology, agricultural and construction equipment, paper products, medical and scientific equipment and pharmaceuticals.

According to Secretary Gutierrez, CAFTA-DR would create the second biggest U.S. export market after Mexico and the 13th largest export market in the world. In this context, Gutierrez pointed out that trade with CAFTA-DR countries already exceeded U.S. trade with Australia or Brazil and the new export market would surpass Russia, India and Indonesia combined.

Finally, Secretary Gutierrez highlighted the development aspect of engaging Central America in a free trade agreement with the US. He referred to "three of the countries" as "young", "not still fully stable", "sensitive" or "fragile" democracies, and said they were looking forward to the US to "help them prosper." US support for CAFTA would, in his view, be symbolic in what the US feels about trade and broader cooperation with its neighbors, and with the rest of the world.

V. US Will Remain Fully Engaged in Doha Round

Secretary Gutierrez emphasized that the Bush Administration was committed to a strong multilateral system and to completing the Doha Round. He indicated that improving market access for industrial products and services are two priority areas of concern for the US. Discussing industrial products, he stressed that trade negotiations require "give and take," and that for other countries to be making demands of the US, they also must allow U.S. exporters to gain a fair share, and must address both tariff and non-tariff barriers. In regards to services, he pointed out that some of America's most competitive and innovative companies were in the services sector. While he acknowledged it had been more difficult to achieve results in this sector, the US is determined to "keep the pressure on."

[5] Free Trade Agreement between the US, Guatemala, Costa Rica, El Salvador, Honduras, Nicaragua, and the Dominican Republic. The Agreement was signed on May 28, 2004, and August 5, 2004, and has since then been approved by Guatemala, El Salvador and Honduras.

[6] The study covered such states as California, Florida, Louisiana, New York, New Jersey, North Carolina, and Texas. For more details on US Chamber of Commerce predictions on CAFTA-DR effect on Florida, please see http://www.uschamber.com/ publications/reports/0410_intl_cafta.htm

[7] Secretary Gutierrez cited an American Farm Bureau Federation estimate suggesting a possible increase in annual agricultural sales by $1.5 billion.

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VI. IP Violations a "Big Concern"

Gutierrez narrowed in on IP violations as a particular problem for U.S. businesses abroad. He said the protection of brands, patents, technology, and ability to differentiate products was very important to U.S. businesses and that the US would encourage understanding among its partners.

Without making a reference to particular countries, he mentioned "markets" where statistics showed that 90% of software, videos, or music are counterfeit. "In the long haul," he admonished, "this is not acceptable and a major risk to our business." He cited the example of his former employer, Kellogg Company, as having encountered problems with enforcing its IP rights in Chinese courts after facing counterfeit competition only three months after Kellogg entered the market in 1996.

Secretary also commented on the STOP Initiative,[8] aimed at stopping counterfeiters and pirated goods. The program includes a hotline for business to help protect their products, and promotes cooperation between U.S. Customs and businesses to block goods violating U.S. IP laws at the border. Gutierrez emphasized IP violations are a "major problem" and vowed to protect America's creativity and innovations from theft and piracy.

VII. Bush Administration Will Make Sure That Free Trade is Win-Win for the US

In his closing remarks, Secretary Gutierrez stated that the Bush Administration would ensure that trade continues to be a win-win for the US. He pointed out that when recent and anticipated trade agreements are fully in effect, liberalization will eliminate up to $8.3 billion[9] in cost disadvantages that impede U.S. exports.

Notwithstanding its free trade stance, the Administration is "passionately committed" to ensuring that American companies and workers enjoy the full value of their trade agreements, and will prosecute any violations. If the competition is fair, the Secretary insisted, the US will be able to compete because it has the best companies and workers in the world.

[8] The Strategy Targeting Organized Piracy (STOP!) program, officially announced in October 2004, is a joint program of the United States Trade Representative, Department of Commerce, the Justice Department, and Department of Homeland Security (specifically, US Customs and Border Protection - CBP). STOP! involves a number of steps benefiting innovators and manufacturers who have been hurt by the sale of pirated and counterfeit goods, including a hotline providing one-stop-shop for businesses to protect their IP rights in the US and abroad, notification system for trademark recipients that they can register their trademarks with CBP to ensure effective enforcement at borders, enabling copyright registration with CBP prior to its registration with US Copyright Office, implementation of new procedures and risk assessment that will allow DHS and CBP to better identify firms routinely trafficking in fake goods, conducting post-entry audits to verify that importers are authorized to use trademarks and copyrights, applying specialized technologies and techniques developed to combat terror to fight IP violations, as well as seeking new legislation to empower US District Courts to issue injunctions against pirated and counterfeited goods entering US at any port (currently, a US District Court can issue an injunction targeting only the ports within its district), and others. For more information on STOP! Please see: http://www.export.gov/stop_fakes_gov/

[9] According to Secretary Gutierrez, $6.4 billion has already been lifted, and $1.9 billion is at stake in the negotiations currently underway.

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Secretary Gutierrez ended his comments by quoting President Bush: "*Free and open trade creates new jobs and new incomes. It lifts the lives of all our people, applying the power of the markets to the needs of the poor*". He added: "*Our mission, as stewards of democratic, free market capitalism, is to transform our world by introducing opportunity, lifting lives, and helping to build the institutions that bring stability, order and fully functioning societies.*"

VIII. Response to Questions on Export Strategy, Specific Trade Problems, Visa Policy and Other Issues

Export Strategy

Responding to a question, Secretary Gutierrez explained that pursuant to a new major export development strategy, the Commerce Department has categorized its trade partners into two groups: (1) those with whom a free trade agreement is in place, or negotiated (FTA group); and (2) other important trade partners. With respect to the first grouping, DOC would launch a policy aimed at educating American companies about the trade agreements, and how they can be used to enter those markets. In regards to the second grouping, the Administration would also monitor and counteract trade barriers in the "non-FTA" group of key trade partners.

Medical Device Exports to Japan

Secretary Gutierrez received a question from a representative of the medical device industry, who pointed out that the industry has lost its $3 billion trade surplus five years ago. Now, the industry faces a $3 billion trade deficit caused by TBT-type[10] restrictions imposed by the Japanese Health Ministry. According to Japanese government, it will take over two years to address the backlog of over 500 applications to allow the equipment into Japan. Secretary Gutierrez noted that Japan as a huge economy, although is not easy to penetrate, can bring great results for companies that do manage to penetrate it. He added that while progress often took longer than the companies would like it to, the DOC would not ignore the problem, and would continue to work to resolve it. He commented generally that problems of American companies were the problems of the Department.

Africa Is On the Agenda

In response to a question about the role of Africa in U.S. trade strategy, Secretary Gutierrez commented that the Bush Administration seeks to sign FTAs with six countries in Africa,[11] including Botswana, "one of the fastest growing economies in the world."

[10] Technical Barriers to Trade – types of regulations, such as quality, health or technical standards, which, when used improperly and in contravention of the WTO Technical Barriers to Trade Agreement, can constitute discriminatory and non-tariff barriers impeding free trade.

[11] While Secretary Gutierrez did not elaborate, he most likely referred to the US-South African Customs Union, including South Africa, Namibia, Botswana, Swaziland, and Lesotho, under negotiations since 2003. The negotiations are currently focused on the more controversial issues, including investment, services, government procurement, and intellectual property rights. The last significant meeting took place in July 21, 2004 in Paris, and the subsequent meeting has been postponed. The original December 2004 deadline for the FTA has been scrapped, and the officials on both sides expressed hope that the agreement would be concluded by fall 2007. The sixth African country referred to by Secretary Gutierrez might have been Egypt. While no FTA talks with Egypt have begun yet, in December 2004 US announced a program of "Qualified Industrial

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Referring to Africa as a "very important trading area", Secretary Gutierrez said "Africa is on the agenda," setting it in the context of the Administration's efforts to open up markets in all regions.

Facilitating Visas and Security Objectives

In response to a question on visa policies, Secretary Gutierrez acknowledged the conflict between the Administration's post 9/11 policy of securing U.S. borders, and wanting to facilitate the visits of executives from foreign countries. Secretary Gutierrez also recognized tourism was an "important part of the whole visa process." He noted that since becoming the Secretary of Commerce, he had several meetings in an attempt to strike the balance, and to designate areas where progress could be made without compromising security on the one hand, and the free flow of goods on the other. In general, Secretary said the problem was "well recognized" and "dealt with on a daily basis."

OUTLOOK

Secretary Gutierrez's speech seems to indicate that no major changes with respect to the Bush Administration's trade policies should be anticipated. While some suggestions were made in the past that the US has focused too much on bilateral free trade agreements, Secretary Gutierrez's comments should be interpreted as support for continuation of the U.S. "competitive liberalization" approach.[12] Thus, it appears that the US will continue to negotiate trade agreements at the bilateral, regional and multilateral levels.

Gutierrez is also in a prominent role to articulate trade policy given the departure of USTR Robert Zoellick. Moreover, the role of USTR has been vacant (nonetheless, Peter Allgeier is serving as Acting USTR) due to the somewhat later-than-expected appointment of Robert Portman, a Member of Congress from Ohio, and a member of the House Ways and Means Committee. Thus, Secretary Gutierrez' is reportedly taking on key responsibilities in trade policy, including to lobby for the passage of CAFTA-DR through Congress.

In regards to the CAFTA-DR, Secretary Gutierrez' speech confirms that the Administration is determined to place a high priority on passage of the agreement. The Senate Finance Committee and the House Committee on Ways and Means have scheduled hearings on CAFTA-DR on April 13th and 21st, respectively. During those hearings, Members of Congress are expected to voice their numerous concerns on expanding sugar quotas, labor standards in Central America, textiles, intellectual property, and other issues. In fact, supporters reportedly aim to put the agreement up for a vote before the end of May. Moreover, the Administration considers the vote on CAFTA-DR as a litmus test of U.S. support for advancing international trade in general.

Zones", which was to be a first step leading towards an FTA with Egypt. According to sources, US and Egypt have established "technical groups" studying and identifying the possible chapters of a future FTA.

[12] In addition to the seven bilateral FTAs already in place - with Israel (1985), Mexico and Canada (NAFTA, 1994), Jordan (2001), Chile (2004), Singapore (2004), Morocco (2005), Australia (2005)], and the two FTAs with Bahrain and DR-CAFTA FTAs already concluded, but waiting Congressional approval, USTR is currently negotiating FTAs with the South African Customs Union, the Andean Pact,[12] Panama, Thailand, Oman, and the United Arab Emirates. There has also been discussion of possible FTA negotiations with Egypt and South Korea. Other candidate FTA partners include Taiwan, Malaysia, the Philippines, Qatar, and Kuwait, as well as Tunisia, Yemen, and Sri Lanka.

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UNITED STATES

Department of Commerce Introduces New Monitoring Mechanism for Textile Imports and Initiates Safeguard Proceedings on Chinese Textile Imports; More Restraint Actions Expected

SUMMARY

The growth in Chinese textile imports in the first quarter of 2005, and reactions from the U.S. government and industry indicate that safeguard actions and other trade restrictions affecting textile imports are on the rise.

The Department of Commerce (DOC) recently modified its monitoring mechanism for textile imports and started releasing preliminary import trade data this month. The release of preliminary data is expected to expedite the filing of antidumping and safeguard petitions against Chinese textile imports, and already has led to the launch of safeguard proceedings.

The U.S. government, through the DOC administered Committee on the Implementation of Textile Agreements (CITA) announced on April 4 that it would self-initiate safeguard proceedings on three Chinese textile products. In other developments, the Government Accountability Office (GAO) released a study urging more clear procedures on safeguard investigations, including for the "threat-based" claims pending before U.S. courts.

ANALYSIS

I. DOC Announces New Textile Import Monitoring Mechanism

Commerce Secretary Carlos M. Gutierrez announced on March 21, 2005, that the DOC will begin releasing preliminary data on U.S. textile and apparel imports, starting in April. The preliminary data should allow decision makers to more quickly analyze the impact of those imports on the U.S. market. Moreover, it is believed the faster release of data might result in more active filings of antidumping and safeguard petitions.

Gutierrez's decision was prompted in part by a letter from Senator Elizabeth Dole (R-North Carolina) dated March 7, which urged the DOC to expedite the release of import statistics. Senator Dole's state of North Carolina has significant textile manufacturing, but is facing a rapid decline in the industry due to import competition and other factors.

The DOC's new approach will provide more timely access to preliminary textile and apparel import data (aggregated by categories of products). The Bureau of Customs and Border Protection will post the data every two weeks, starting the first week of April with data from the first quarter of 2005. The new schedule represents a significantly faster release of data than under the current system. Presently, the data for a given month are not available until six weeks after the month ends. Commerce will also continue to release official data with a six-week lag time. For example, the DOC issued final data for January on March 11, 2005.

The preliminary data will be posted on a website maintained by the Department's International Trade Administration Office of Textiles and Apparel at http://otexa.ita.doc.gov

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II. Early Release of Data and Possible Effects of China Textile Safeguard

The DOC's expedited release of data is of significant interest to the U.S. textile manufacturing industry, which is seeking to invoke safeguard actions to limit imports from China. The industry has alleged that as a result of the WTO Agreement on Textiles and Clothing (ATC) which ended global textile quotas in January 2005 – the surge in Chinese imports in the first quarter of 2005 have already caused significant harm and must be restrained.

The safeguard procedures applicable to Chinese textiles is unique due to its WTO Accession Agreements which allows WTO Members to restrict imports of Chinese textiles and apparel on lesser standards than under the WTO Safeguards Agreement, until December 31, 2008 (Paragraph 242 of the Working Party Report on China). Once consultations are initiated, China must agree to limit imports to no greater than 7.5 percent above recent trade levels (for the past 12 months) if those imports are alleged to cause "market disruption" and impede trade. The "market disruption" standard is lesser than the injury standards in the WTO Safeguards Agreement applicable to other Members.

The expedited release of textile import data should enable the U.S. industry to file trade remedy petitions more actively and with less delays. The industry has already filed 12 petitions last autumn requesting the imposition of safeguards based on the "threat" that imports from China would increase once U.S. import quotas are removed on January 1, 2005. It is estimated that of the $12 billion in textile imports that are potentially subject to safeguards, the 12 threat-based actions constitute 11 percent of this total. Consideration of those so-called "threat-based" petitions, however, has been delayed by a lawsuit filed by U.S. apparel importers and retailers. These groups have argued that the petitions are based on the mere "threat" of market disruption due to the expected surge in imports, rather than on evidence of actual market disruption as required by law.

III. Bush Administration Self-Initiates Safeguards on Chinese Textiles

On April 4, the inter-agency Committee for the Implementation of Textile Agreements (CITA) announced that it will self-initiate safeguard proceedings to investigate whether imports of Chinese shirts, trousers and underwear have contributed to the "disruption" of the U.S. market. (As noted above, CITA's decision whether to impose a safeguard will be based on the lesser "market disruption" standards of the China-specific textile safeguard, and not the injury standards of the WTO Safeguard Agreement.)

According to the DOC's release on April 4 of preliminary import data, since January 1, 2005, imports of Chinese cotton shirts and blouses, cotton trousers, and cotton and man-made underwear rose significantly over the same quarter last year as noted in the table below.

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Product	Category	Growth rate of Chinese imports since Jan 1 2005 (Approximate)
Cotton Knit Shirts and Blouses	338/339	1,250%
Cotton Trousers	347/348	1,500%
Cotton and Man-Made Fiber Underwear	352/362	300%

CITA will soon publish a Federal Register notices seeking relevant public comments regarding each product subject to the safeguard proceedings. After 30 days from the deadline for the submission of comments, CITA has up to 60 days to render a final determination. If CITA determines that Chinese textile and apparel are disrupting the U.S. market, CITA will request consultations with China to easing or avoiding such market disruption.

Once the U.S. government requests consultations with China, consultations are to be held within 30 days. If the parties do not reach a "mutually satisfactory solution" within 90 days, then the US can impose restraints (in the form of quotas or other measures) typically until December 31 of the same year. The import restraint measures are to last no longer than one year.

IV. Recent Reactions from U.S. Industry and Members of Congress

We discuss below initial reactions by industry groups and Members of Congress to the DOC's new monitoring mechanism, the Administration's safeguard petitions and related issues.

A. US Representatives Robin Hayes and Patrick Henry

Representative Hayes (R-North Carolina), a major supporter of the textile manufacturing industry, noted that the new data supports allegations that Chinese textile imports "are choking our domestic textile industry." She also commented that, "Self-initiating of safeguards by Commerce is the quickest way to protect our domestic textile industry from these imports."

Likewise, Representative McHenry (R-North Carolina) supports her view and remarked that the Administration's recent self-initiation of safeguards shows it "is willing to enforce the written agreements."

B. National Council of Textile Organizations (NCTO)

The NCTO, the main coordinating body among textile manufacturers welcomed the DOC's new approach as a "welcome step." NCTO alleges that according to Chinese export statistics, exports of textiles in January 2005 has already increased 546% on average in many product categories, compared to January 2004. Moreover, NCTO asserts that 12,000 jobs

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have already been lost in January 2005 alone. NCTO supported the initiation of the safeguards, but asserts more must be done to protect jobs.

C. American Manufacturing Trade Action Coalition (AMTAC)

The AMTAC, which includes textile and other manufacturing industries, supports the DOC's new monitoring mechanism and the initiation of safeguards. AMTAC asserted that the data will demonstrate "dramatic increases in U.S. imports of textile and apparel products from China. This data will help to prove the industry's claim that China is disrupting the U.S. market." Therefore, AMTAC called on the government to act quickly in imposing safeguards on China to limit job loss in the manufacturing sector.

In addition, on April 6, AMTAC, NCTO, the National Textile Association, the National Cotton Council, the UNITE HERE union and other textile organizations announced they will file an undisclosed number of petitions requesting safeguards to limit Chinese textile imports covering the above-mentioned cotton and man-made products.

D. National Retail Federation

In contrast, the National Retail Federation (NRF) – the world's largest retail association, opposes the safeguards and asserted that import restraint measures "simply are not warranted." The NRF believes the latest Chinese import numbers demonstrate a shift in textile imports among countries, and not a shift from U.S. manufacturing to imports. It also noted the base numbers used to determine import levels were artificially low because quotas were in place under the Multi-Fiber Agreement until January 1, 2005. NRF also indicated it would lead the retail industry in filing submissions to CITA arguing against imposing safeguards.

V. China Warns It Might Retaliate Against Safeguards

In response to the proposed safeguards against Chinese textile exports by its trading partners, China has warned that such measures could be inconsistent with Paragraph 242 of the Working Party Report on China (and possibly Paragraph 16 of the Protocol of Accession). China also warned it might impose retaliate by imposing countermeasures against the imports of countries invoking inconsistent safeguards.

VI. GAO Urges Clarification of Textile Safeguard Procedures

The Government Accountability Office on April 4, 2005, released a study urging improvement in the procedures implementing the China-specific textile safeguard. Among its findings, the GAO noted that the procedures for invoking these safeguards have not been effective due to various administrative and other delays.

Although the DOC is making strides to post import data more rapidly, the GAO also recommended that the DOC take actions to make production data more transparent and accessible for industry sectors at risk of disruptive import surges. Apparently, about 20 percent of production data on textile and apparel product categories is unavailable, which prevents equal access by industry sectors to file for safeguard protections.

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The GAO also suggested that if the courts allow the filed "threat-based" cases to proceed, CITA should clarify its procedures for these cases. GAO noted that current CITA procedures do not specify under what circumstances the threat-based petition requests would be considered.

The GAO's full study can be found at: http://www.gao.gov/cgi-bin/getrpt?GAO-05-323.

OUTLOOK

The DOC's preliminary data for the first quarter of 2005 comes as no great surprise as significant growth in Chinese textile imports has been expected. Coupled with the Bush Administration's announcement of safeguard proceedings on three products, there are strong indicators that the struggle over Chinese textile imports is just beginning.

Apparently, the expedited release of preliminary data starting this month is already being used to support new petitions based on estimated and actual import surges – as seen with CITA's announcement on April 4 to self-initiate safeguard proceedings. Industry groups including the NCTO and AMCTO are already gearing to initiate more petitions based on this data. Moreover, the data might be used to support the already-filed threat-based petitions, if the legal issues surrounding the petitions are resolved.

The recent U.S. government "self-initiation" of safeguard proceedings has probably preempted inevitable industry petitions on these products. Reportedly, the decision is linked to the Bush Administration's efforts to lobby support among Members of Congress sensitive to textile issues, to vote in favor of the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA).

In any event, more petitions are likely to be filed in the coming months by the textile industry and possibly the U.S. government – against China, and perhaps other exporters that expand their market share in the United States. The battle will only get more political as US-China trade is linked to passage of DR-CAFTA, and other issues.

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House Hearing Signals Frustrations with China Trade Policy; Pressure Mounts to Enact Legislation on China's Currency and Subsidies

SUMMARY

At the House Ways and Means Committee hearing on April 14, 2005, Members of Congress made demands for a new approach to China trade policy, including to counteract the effects of China's fixed currency and government subsidies, and lack of compliance with WTO obligations. Pressure on the Administration is also high due to the record trade deficit (estimated in February 2005 at $61 billion), with China accounting for the largest portion. Nevertheless, witnesses from the Administration and private sector urged caution, and a focus on long-term solutions with China.

Meanwhile, legislation related to China's currency and subsidy practices are pending in both the House and Senate, and resisting action on these measures is becoming increasing difficult. Recently, an attempt to remove an amendment related to China's currency practices failed in the Senate, serving as a stark indicator of Senate support for action on China. Still, some Members have cautioned that the proposed measures would impose U.S. unilateral action in violation of its WTO obligations.

Concern over China has also spilled over into the effort to confirm U.S. Trade Representative nominee Representative Rob Portman (R-Ohio). Senator Evan Bayh (D-Indiana) intends to maintain a hold on Portman's nomination until the Senate votes on a bill Bayh is co-sponsoring that would allow the filing of countervailing duty cases against non-market economies like China.

ANALYSIS

The number of bills in Congress related to China's economic policies, specifically currency and subsidies, continues to increase. Some legislative action on these bills has occurred, and pressure for further action is growing. In addition, the nomination of Representative Robert Portman for USTR has become embroiled in Congressional concern over China. We review here China-related trade legislation and the outlook for action on US-China trade policy.

I. Currency Policy and Subsidy Practices Major Targets of Legislation

A. H.R. 1575 / S. 295: 27.5% Penalties on Chinese Imports Due to Fixed Currency

Sponsored by Senators **Charles Schumer** (D-New York) and **Lindsey Graham** (R-S. Carolina), S. 295 would impose a 27.5% tariff on all imports from China if the Chinese government fails to move away from a fixed exchange rate within 180 days of the bill's enactment. Introduced in the 108th Congress by Senator Schumer, this bill has gained traction in the Senate. On April 7, 2005, Senators Schumer and Lindsey offered the bill as an amendment to the annual Foreign Affairs Authorization bill (S.600). A motion to table (remove) the amendment failed 33-67.

In exchange for withdrawing the amendment from the Foreign Affairs Authorization bill, Senators Schumer and Graham have been assured a vote before the August recess (by

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July 27) on their proposed legislation (S.295) as a stand-alone bill. Senators Graham and Schumer have also agreed to refrain from offering their amendment to any other legislation for the remainder of this session of Congress.

Prospects for the bill's passage in the Senate remain unclear. Senate Finance staff have indicated that they may not be able to prevent the bill's passage, owing to mounting concerns over China's trade surplus with the US. A procedural tactic could prevent Senate consideration of the bill. Under the US constitution, measures related to revenue (including imposition of tariffs) must originate in the House. Under Congressional rules, the Speaker of the House could put a hold on further consideration of S. 295 until the House first considers a similar measure. A House version of the Schumer-Graham bill (H.R. 1575) has already been introduced.

B. H.R. 1216 / S. 593: Allowing CVD Cases Against Non-Market Economies

Introduced by Senators **Evan Bayh** (D-Indiana) and **Susan Collins** (R-Maine), the Stop Overseas Subsidies Act of 2005 (S. 593) would allow the imposition of countervailing duties (CVD) against non-market economies including China, in order to counteract possible effects from government subsidies. Under a 1986 court ruling, the Department of Commerce has declined to accept CVD petitions against non-market economies (NMEs) due to the difficulty in assessing potential government subsidies in NMEs.

In an attempt to advance the legislation, Senator Bayh has placed a hold on the nomination of Representative Robert Portman as USTR. Senator Bayh is demanding a vote on S. 593 before releasing his hold on the Portman nomination. Senator Collins, among many other Senators, has expressed opposition to Senator Bayh's tactics. The Senate Republican leadership has responded by scheduling a confirmation hearing for Representative Portman on April 21, 2005, and intends to apply further pressure on Bayh to rescind the hold.

Meanwhile in the House, Representative **Phil English** (R-Pennsylvania) has introduced a House version of the Bayh-Collins bill (H.R. 1216).

Industry reaction to the Bayh-Collins-English bill has been supportive. Groups including the National Association of Manufacturers, the Committee on Pipe and Tube Imports, and the American Forest and Paper Association have expressed support for allowing CVD claims against NMEs.

C. H.R. 1498: Chinese Currency Manipulation a Prohibited Subsidy

On April 7, 2005, Representatives **Duncan Hunter** (R-California) and **Tim Ryan** (D-Ohio) introduced a bill that would declare exchange-rate manipulation a prohibited export subsidy under U.S. trade remedy law (HR 1498). In addition, the bill would require the International Trade Commission (ITC) to consider exchange-rate manipulation in any case brought under the China-specific safeguard (Section 421). The bill also would require that the Department of Defense not purchase Chinese imports that the ITC determines to be disrupting the U.S. market. Similar to the Schumer-Graham legislation, some of these measures would raise concerns of WTO inconsistency, as they would impose discriminatory action against Chinese goods.

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No hearings have yet been scheduled on the Hunter-Ryan bill. However, sources have suggested that elements of the Hunter-Ryan bill could become part of a possible omnibus China trade bill. The House Republican leadership is considering an omnibus China trade bill to garner support for passage of the Dominican Republic-Central American Free Trade Agreement (DR-CAFTA).

II. House Ways and Means Holds Hearing on US-China Economic Relations

On April 14, 2005, the House Ways and Means Committee held a hearing to discuss current issues in US-China economic relations. China's currency practices and trade barriers dominated the hearing, with practically all Members of Congress at the hearing calling for immediate attention to addressing problems in China trade relations.

A. Members of Congress Critical of Administration's China Trade Policy

Chairman **Bill Thomas** (R-California) offered caution with respect to extreme solutions proposed in Congress. For instance, Chairman Thomas noted his preference that China move towards a flexible exchange rate, but expressed concern about the state of China's banking system and the consequences of moving too quickly to a liberal currency regime. Mr. Thomas also inquired about what steps would need to be taken to reduce China's impact on the U.S. trade deficit.

Representative **Charles Rangel** (D-New York) sought clarification on U.S. trade policy with China because in his opinion, it has failed. He also does not believe that passage of CAFTA-DR will be enough to change an ineffective China trade policy.

Representative **Clay Shaw** (R-Florida) noted how U.S. exports to China in 2004 increased by 35 percent while Chinese imports grew 36 percent. He observed that the EU exports more to China, and inquired why EU visa policies allow quicker turnaround times than U.S. visa policies, which possibly enables the EU to gain additional market share in China. Mr. Shaw agreed the China currency issue requires resolution but cautioned that the issue cannot be pushed too hard, lest it prove another Asian financial market crisis as in 1997.

Representative **Benjamin Cardin** (D-Maryland) asserted that since China's WTO accession in 2001, the US has not engaged China aggressively enough to enforce China's WTO obligations. He emphasized that clear White House direction is needed to control the escalating U.S. trade deficit, especially with China. Mr. Cardin also called for WTO action on reducing China's piracy of $2.5 billion worth of goods produced there each year. In addition, Cardin urged for the launch of safeguard investigations on textile imports.

Representative **Bernard Sanders** (I-Vermont) made another push for his legislation that would repeal Permanent Normal Trade Relations (PNTR) with China because, in his opinion, free trade policies are ineffective. Similar to Mr. Rangel, Mr. Sanders called for a new direction in trade policy towards China, as well as free trade agreements across the board, but did not specify what changes should be made. Mr. Sanders observed that it would be difficult for U.S. labor and companies to compete with China in the long run due to wage disparities, which will continue so long as labor unions are illegal in China. He cited that from 1989-2004, the US lost 1.5 million jobs and experienced real wage reductions at the lower end of the economic scale due to PNTR. Mr. Cardin also felt the US should bring more trade cases to the WTO to better enforce China's obligations.

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Similarly, Representative **Sander Levin** (D-Michigan) asserted that U.S. trade with China is not complementary. He cited as examples that Sections 421 and 301 have not been used actively, and that the WTO dispute settlement process has not been used effectively.

B. Administration Officials Insist Actions Being Taken to Address China Trade Concerns; Emphasize Long-Term Relationship

Witnesses from USTR, the White House and Congressional Budget Office at the hearing tried to address concerns and impress upon Members that the Administration is working to deal with existing bilateral trade irritants.

Charles Freeman, Assistant USTR for China, highlighted the benefits of trade with China (e.g., the US has doubled exports to China during 2001 to 2004, to $35 billion annually), while also stating that USTR has worked to resolve several trade issues. Mr. Freeman indicated that the US wants China to enforce WTO IPR laws as a priority, and noted that USTR is having a Special 301 out of cycle IPR review later in April. Moreover, USTR stands ready to pursue WTO action should China not improve enforcement of IPR. Freeman also noted ongoing technical cooperation between U.S. and Chinese officials on the currency issue, as well as non-tariff barriers such as licensing and the use of sanitary and phyto-sanitary measures.

Congressman **Dave Camp** (R-Michigan) expressed concern to Freeman that U.S. automobile manufacturers are losing market share and jobs to China due to counterfeit auto parts. Freeman agreed that China's legal regime is not adequate, and China needs to improve its structural and legislative environment to enforce IPR laws. He noted that the US Customs is using USTR's STOP initiative to partner with U.S. manufacturers on reducing foreign IPR violations.

Dr. Kristen Forbes, a member of the President's Council of Economic Advisors, testified about the broader macroeconomic implications of trade with China. Forbes noted that China's economic growth as the single most important factor in reducing global poverty since the 1980's. As the fifth largest U.S. export market, China also helped to maintain global economic stability during 2000 to 2004.

Dr. Forbes attempted to downplay the significance of the U.S. trade deficit with China. She noted that imports from China have expanded while at the same time diminishing from other Asian countries, especially Japan. Thus, she noted that China's relative share of the U.S. trade deficit has not increased significantly since 1997.

Dr. Forbes advised that constructive dialogue rather than rhetoric, accomplishes more toward resolving problems like China's pegged currency. Likewise, she asserted that short-term fixes are not conducive to enhancing long-term U.S. economic competitiveness. In fact, imposing punitive tariffs would raise U.S. consumer goods prices, and could raise the general costs of conducting business.

Dr. Douglas Holtz-Eakin, Director of the Congressional Budget Office, observed that China is not the root cause of U.S. manufacturing losses or the trade deficit. Rather, he pointed out that manufacturing productivity in the US remains robust and the sector has generally maintained its share of GDP over the past forty years. Holtz-Eaken also stated that

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revaluation of the yuan would have a lower than anticipated impact on prices and trade, and that U.S. retaliatory trade policies against China might violate WTO obligations.

C. Private Sector Witnesses Express Mixed Views on China Trade and Compliance

U.S. industry representatives testified on their experiences with US-China trade, including: **Mr. Richard Wilkey**, President, Fisher-Barton Co. (on behalf of the National Association of Manufacturers); **Mr. Jay Berman**, CEO Emeritus, International Federation of Phonogram Industries (on behalf of the Recording Industry Association of America); **Mr. Robert Weil II**, Chairman and CEO, Weil Brothers Cotton Company, and Vice President, National Cotton Council; **Mr. Myron Brilliant**, Vice President for East Asia, US Chamber of Commerce; **Mr. Alex Gregory**, President and CEO, YKK Corporation of America; **Mr. Robert Stevenson**, CEO, Eastman Machine Company; and **Mr. David Spence**, Managing Director for Regulatory Affairs Legal Department, Federal Express Corporation.

Mr. **Richard Wilkey** of Fisher-Barton Co. noted that U.S. health care and litigation costs are major factors eroding U.S. competitiveness. Likewise, China should not be blamed as the scapegoat for the trade imbalance and other U.S. economic shortcomings. Wilkey also remarked that wage disadvantages with China could be overcome through innovation and technology. Nevertheless, he urged support of H.R.1216 and S.593 to allow countervailing duty action against China.

Mr. **Jay Berman** of the International Federation of Phonogram Industries acknowledged that China imposes administrative sanctions and fines for piracy violations, but piracy remains a profitable business. The challenge for the US is to get China to satisfy its IPR enforcement obligations. Moreover, Chinese government censorship of imported U.S. recorded products acts as an NTB.

Mr. **Robert Weil II** of Weil Brothers Cotton Company stated that China dominates the world cotton industry. He urged the U.S. government to improve opportunities for U.S. manufacturers to enter into contracts in China, and to address China's product quality issues that over-penalize U.S. cotton.

Mr. **Myron Brilliant** of the US Chamber of Commerce indicated that China's currency should move toward a floating rate, but in a way that would not shock international financial markets. He also advised against unilateral punitive measures like tariffs. Among other concerns, he pointed out that U.S. companies are still waiting for greater transparency and full implementation of distribution rights in China. Moreover, concerns remain over the new Chinese government procurement law.

Mr. **Alex Gregory** of YKK Corporation noted that while the US remains a formidable economic power, outsourcing to China and increased textile imports has resulted in U.S. job losses. Moreover, the labor wage disparity will continue to make it difficult for U.S. companies to remain competitive.

Mr. **Robert Stevenson** of Eastman Machine Company pointed out that trademark infringement by quasi-governmental Chinese manufacturers has hurts his company's quality reputation as all of its products have been pirated.

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Mr. **David Spence** of FedEx highlighted the growing air shipment trade with China, and urged the US to pursue ongoing engagement with Beijing to expand free trade.

OUTLOOK

Pressure to enact legislation forcing a change in US-China economic relations continues to grow in Congress. Members of Congress, along with certain trade groups, continue to point to the loss of manufacturing jobs, coupled with the expanding U.S. trade deficit as evidence that trade with China is far from fair.

Among the more controversial proposed legislation, the Schumer-Graham bill continues to gain support despite its severe penalties and apparent WTO inconsistency. The fact that it survived a motion to table is evidence of Congress' growing impatience with China, and willingness to act. Some Democrats have also called for a radical overhaul of U.S. trade policy toward China, including the revocation of PNTR status. Whatever the outcome, Congressional staff have indicated that further legislative action on China-related bills may be unavoidable in the coming months.

Notwithstanding the pressure arising from China trade imbalances, Administration officials have expressed opposition to imposing tariff penalties, and other extreme measures. Rather, they have urged caution, as the outcome of China's movement away from a fixed currency rate is uncertain. Nevertheless, the Administration is expected to take a stronger stand to address certain Chinese trade frictions. For example, Chinese textile imports have increased significantly since the lifting of global quotas in January 2005. Safeguards on textiles are inevitable, as are other possible trade remedies. Moreover, the Administration's efforts to pass the DR-CAFTA in the coming months will likely require major trade-offs, including support for an omnibus China bill targeted at restraining certain Chinese imports.

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United States Highlights

President Submits Official Request To Extend Trade Promotion Authority To Congress

On March 30, 2005, President George W. Bush submitted a letter to the U.S. Congress requesting extension of Trade Promotion Authority (TPA) for two years. Consistent with section 2103(c)(2) of the Trade Act of 2002, Bush also enclosed a report on the trade negotiations that were conducted since the renewal of TPA in August 2002.[13]

Signed August 6, 2002, the legislation authorizes "trade authorities procedures" to apply to bills that implement trade agreements that the President enters into before July 1, 2005. The Act also provides for extension of the procedures to include agreements concluded before July 1, 2007, if the President so requests in a report submitted to the Congress by April 1, 2005.

The Congressional Committees with jurisdiction over international trade (the House Ways and Means and Senate Finance) will soon act to either issue a resolution disapproving the President's request, or to discharge such a resolution. (If the resolution is not discharged, either Chamber of Congress can vote to disapprove TPA extension by a majority vote). Most observers believe the President's request will be approved and TPA will not expire until July 2007.

US Pledges Commitment To Ensuring WTO Accession And Restoring PNTR For Ukraine

On April 4, 2005, President George W. Bush met with the President of Ukraine Viktor Yushchenko in Washington, DC. At the end of the meeting, both parties issued a joint statement, pledging to cooperate on ensuring Ukraine's accession to the World Trade Organization (WTO). Bush particularly noted that the US was committed to concluding its bilateral WTO accession negotiations with Ukraine by the end of 2005.

The US further expressed its support for the immediate elimination of the trade restrictions under the Jackson-Vanik amendment for Ukraine. Passed in 1974, this amendment denies Permanent Normal Trade Relations (PNTR) to former Soviet republics.

Senate Holds Confirmation Hearing for USTR Nominee Portman

On April 21, 2005, the Senate Finance Committee held a confirmation hearing for U.S. Trade Representative (USTR) nominee Representative Rob Portman (R-Ohio). During the hearing, Portman vowed to work to open markets for US exporters, with a particular focus on Doha Development Round at the World Trade Organization (WTO). Portman also pledged to conduct a thorough review of USTR efforts at reviewing China's compliance with its WTO obligations, particularly with respect to intellectual property rights infringement, among other matters.

[13] http://www.ustr.gov/assets/Document_Library/Reports_Publications/2005/2005_TPA_Report/asset_upload_file834_7514.pdf.

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Senators appearing at the hearing spoke positively about Representative Portman. Both Senator Charles Grassley (R-Iowa) and Max Baucus (D-Montana) urged quick confirmation of Representative Portman. Under questioning, Senators urged Portman, if confirmed, to focus on US trade relations with China, improving access to commercially significant markets, and working on resolving the softwood lumber dispute with Canada.

During the hearing, Senator Grassley stated that he would hold a committee vote on the Portman nomination on April 26, 2005. Representative Portman's nomination is expected to pass easily in the Senate.

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Free Trade Agreements

Senate Finance Hearing Produces Little Firm Support For DR-CAFTA; Members Focus on Sugar, Labor and IPR Issues

SUMMARY

The battle over the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) has begun with the start of Congressional hearings. On April 13, 2005, the Senate Finance Committee hearing produced little firm support for the agreement. Despite the best efforts of DR-CAFTA proponents including acting U.S. Trade Representative **Peter Allgeier**, several Senators including the Finance Committee's ranking Democrat **Max Baucus** (D-Montana) and several Republican members, expressed continued concerns about the implications of DR-CAFTA. Among the key concerns raised were the agreement's provisions on sugar, labor and access to essential drugs.

The day before the Senate Finance hearing, the Ambassadors of Costa Rica and the Dominican Republic spoke an event hosted by the Washington International Trade Association. They reiterated their countries' position that ratification of the agreement would bring economic benefits and help consolidate democracy in the region.

The Administration continues to rely on cabinet secretaries to press the case for DR-CAFTA. On April 11, 2005, Secretary of Agriculture **Mike Johanns** stated that passage of DR-CAFTA would not only secure benefits for U.S. farmers, but would help solidify support for U.S. positions in the WTO Doha Round.

ANALYSIS

Senators from both parties expressed concerns over sugar, labor, intellectual property, the trade deficit, among other issues. The Administration has countered by expounding on the benefits to U.S. agriculture and on intangible benefits, such as U.S. credibility with trading partners. We review here some important developments in the fight to win passage of DR-CAFTA:

I. Senate Finance Holds First Hearing on CAFTA, Doubts Over Sugar Figure Prominently

On April 13, 2005, the Senate Finance Committee kicked off congressional review of the Dr-CAFTA. Several Senators from both parties expressed concerns over the agreement's provisions on improving access for sugar imports, labor standards in Central America, and access to pharmaceuticals. Only the Committee Chairman **Charles Grassley** (R-Iowa) expressed firm commitment for the agreement, stating that it would expand market access for the agriculture and service sectors.

A. Expansion of Sugar Imports Sets Dangerous Precedent Says Conrad and Crepo

The bulk of concern expressed during the hearing related to the DR-CAFTA's provisions relating to sugar. Senators **Kent Conrad** (D-N. Dakota) and **Michael Crepo** (R-Idaho) were most vocal in there criticism of the agreement. Senator Conrad argued that the

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inclusion of sugar in DR-CAFTA sets a dangerous precedent for future agreements, particularly those with the Andean Region and Thailand. Conrad added that if the U.S. administration were to grant Andean countries and Thailand similar increased quotas for sugar exports to the US, the price of sugar in the US could collapse, with dire consequences for farmers.

Jack Roney, Director of Economics for the American Sugar Alliance joined in the criticism of DR-CAFTA's sugar provisions. In his testimony, Roney argued that the Farm Act of 2002 did not provide sufficient cushion to allow for increased imports from Central America, the Andean region and Thailand, and that inclusion of sugar in bilateral trade agreements could undermine the future of the sugar program.

Acting USTR Allgeier responded to criticisms of DR-CAFTA sugar provisions by noting that the agreement contains a compensation mechanism that would allow the US to limit imports of sugar. Allgeier further noted that the compensation mechanism can be triggered at any time and requires the US to provide adequate compensation either in the form of payments or additional trade benefits. Senator Baucus expressed doubts about the compensation mechanism, saying that the lack of a clear trigger for its use would mean that farmers would be beholden to political action.

B. Baucus Criticizes Administration's Lack of Leadership

Finance Committee ranking member Senator Baucus, in addition to expressing concerns about sugar, focused his remarks and questions on the Administration's handling of DR-CAFTA. Baucus queried Allgeier about the number of events President Bush has attended or hosted in support of the agreement. Baucus, citing the President's fervent cross-country push on social security, suggested that if the President were truly interested in passage of DR-CAFTA, he would be making a similar cross-country effort to promote the accord.

C. More Strict IPR Provisions Could Undermine Countries' Health Care Systems

Another major criticism of DR-CAFTA raised during the Senate hearing was the potential impact of the agreement arising from greater protections for the pharmaceutical sector. Senator **Ron Wyden** (D-Oregon), in a series of questions, argued that the agreement's protection of patents and clinical test data would stifle the development of generic drugs in the region, and could result in increased costs to the health care systems of Central America. Allgeier responded that the agreement in no way modifies the rights of parties under the TRIPs provisions of the World Trade Organization.

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D. Bingaman Expresses Concerns Over Labor and Immigration

Senator **Jeff Bingaman** (D-New Mexico) led Democrats in raising issues regarding labor standards in DR-CAFTA countries. Going beyond current rhetoric regarding the DR-CAFTA countries' compliance with International Labor Organization standards, Bingaman expressed concerns about the potential immigration effects of the agreement. He argued that enhanced market access to Central America could displace the region's farmers, and drive them to seek economic opportunities elsewhere, namely the United States.

II. DR-CAFTA Ambassadors Attempt to Assuage Concerns on Labor; Religious Leader Expresses Opposition

On April 12, 2005, the Washington International Trade Association hosted a panel discussion featuring the **H.E. Tomas Duenas,** Costa Rican Ambassador to the United States, and **H.E. Flavio Espinal,** Dominican Ambassador to the United States, and moderated by Assistant USTR for the Americas, Ms. Regina Vargo. Both the Ambassadors focused their remarks on the importance of DR-CAFTA to consolidate economic growth in the region. Ambassador Espinal also discussed at some length steps that the Dominican Republic has undertaken to strengthen enforcement of labor laws.

Also speaking at the event was Bishop of San Marcos, **Alvaro Ramazzini.** The Bishop argued that any benefits that Central American countries may accrue under DR-CAFTA would not flow to the region's workers. He also argued that the economic dislocation that the agreement would cause would further aggravate existing poverty levels. In related developments, Costa Rican Presidential candidate **Otton Solis**, speaking at a forum hosted by the Inter-American Dialogue, advanced similar arguments on the lack of benefits of DR-CAFTA to his country's labor force.

III. Secretary Johanns Promotes Agriculture Benefits of DR-CAFTA

On April 11, 2005, Secretary of Agriculture **Mike Johanns** addressed a meeting of agriculture groups supporting DR-CAFTA. Secretary Johanns, joined by USTR agriculture negotiator **Allen Johnson**, promoted the market access opportunities that DR-CAFTA would afford to U.S. agriculture. In themes similar to those raised by Senator Grassley at the Senate Finance hearings, Johanns and Johnson stressed that 99% of U.S. agricultural exports would receive duty free treatment upon entry into force of the agreement. In his opening statement at the Finance hearing, Senator Grassley went to great lengths to point out states that would benefit from the agricultural provisions of DR-CAFTA.

In addition to the benefits that would accrue to the U.S. agriculture sector, Johnson also stated that passage of DR-CAFTA would increase U.S. credibility in the Doha round. Describing DR-CAFTA and the WTO talks as "inextricability linked," Johnson stated that the US risked being marginalized in multilateral trade talks if it was unable to deliver in a regional free trade accord.

OUTLOOK

DR-CAFTA's formal introduction in Congress was less than positive. The Senate Finance hearing served as a rallying cry for opponents more than it served as a forum for those trumpeting the agreement. Leading up to the hearing, a number of Members of

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Congress added their voices in opposition to the agreement. Senators **Byron Dorgan** (D-N. Dakota) and **Lindsey Graham** (R-S. Carolina) have organized the "CAFTA Action Caucus," which aims to defeat the agreement in the Senate. On the House side, Representative **Sherrod Brown** (D-Ohio) has also joined those opposing the agreement.

DR-CAFTA supporters are increasingly concerned about the lack of leadership in Congress for passing DR-CAFTA, unlike the experience with previous FTAs. Senator Grassley was the only senator at the Senate Finance hearing to offer whole-hearted support of the accord. Senator Baucus, a usually reliable free-trade ally, remains undecided, as does a number of key Democrats in both the House and Senate. Senator Grassley has conceded that winning approval for DR-CAFTA in the Senate Finance committee may be a tougher proposition than first anticipated. Pro-DR-CAFTA advocates have admitted that without Democratic support, passage of DR-CAFTA will be impossible.

DR-CAFTA opponents continue to advance their longstanding criticism, and have refined their arguments. Rather than criticizing the amount of increased sugar imports permitted under DR-CAFTA, opponents argue that including sugar sets a dangerous precedent in view of ongoing negotiations with the Andean region and Thailand. Democrats have also modified their arguments on labor, arguing that, in addition to the lack of effective labor standards, the benefits of the accord will not accrue to the region's workers.

Given the skeptical attitudes in the Senate Finance Committee towards DR-CAFTA, it is expected that next week's hearing on April 21 in the House Ways and Means Committee will be even more contentious. The House has usually been the primary battleground for support on trade issues, and the fight over DR-CAFTA could turn the tide against free trade – or at least, the current approach to FTAs.

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Contentious House Hearing Amidst New Announcements of Opposition/Support for CAFTA

SUMMARY

Congressional focus on the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) shifted to the House on April 21, 2005, with a hearing before the Ways and Means Committee.

At the hearing, tempered flared as Committee Democrats decried the lack of consultation with Congress during the negotiations, and attacked the labor and environment provisions. Armed with similar testimony from last week's Senate Finance hearing, Acting U.S. Trade Representative **Peter Allgeier** defended DR-CAFTA, asserting that the agreement that will benefit all parties.

President Bush waded into the DR-CAFTA debate, and in a statement on April 20, 2005, urged Congress to move quickly to adopt the agreement. The President's message, however, failed to gain much traction on the Hill. Moreover, some Members urged the President to take a more active role. Meanwhile, two Montana legislators have come out in opposition to the agreement. In addition, several former cabinet officials have entered the debate, issuing a letter supporting the agreement.

The timing of a vote seems uncertain as House Speaker **Dennis Hastert** (R-Illinois) stated that the Memorial Day recess in late May might not be enough time to complete work, despite previous predications by House Republicans, including Ways and Means Chairman **Bill Thomas** (R-California) *(Please see related report this edition).*

ANALYSIS

Congressional debate on DR-CAFTA has become more acute after the recent hearings by both Chambers. Members of Congress have been articulating their formal positions in support or disapproval of the agreement. Meanwhile, the House Ways and Means Committee has conducted its first full inquiry into the agreement.

I. House Ways and Means Holds DR-CAFTA Hearing, Concerns Over Labor and Environment Dominate

On April 21, 2005, the House Ways and Means Committee held its first formal hearing on the DR-CAFTA. The acrimonious hearing featured recurring themes in the DR-CAFTA debate, including concerns over sugar, textiles, labor and the environment, intellectual property and other issues.

(We will provide a more detailed coverage of the Ways and Means hearing in a separate report.)

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A. Rangel Accuses Thomas, Administration of Shutting Out Democrats

The Ways and Means hearing on DR-CAFTA opened with a tense exchange between Ranking Member **Charles Rangel** (D-New York) and Chairman Thomas over how the Republican leadership has been handling Congressional consideration of DR-CAFTA. Rangel accused both Thomas and the White House of shutting out Democrats from strategy meetings aimed at garnering support on the Hill for the agreement. In addition, Rangel also lashed out at the Administration for failing to work with Democrats to resolve areas of concern, including on labor and environment provisions. Thomas countered that Democrats have participated in meetings of the Congressional Oversight Group on trade, and that USTR has reached out to Democrats.

B. Levin Demands Release of Critical Labor Study

Representative **Sander Levin** (D-Michigan) criticized the Department of Labor (DoL) for failing to release the results of a study on labor laws in Central America. The study, prepared by the International Labor Rights Fund (ILRF) at DoL's request, is believed to contradict assertions made by the Bush administration that existing laws in DR-CAFTA countries meet core international labor standards. In response, Allgeier cited a study by the International Labor Organization (ILO), which demonstrates that labor laws in DR-CAFTA do meet international standards.

The DoL report, according to sources, remains confidential because of ILRF's unwillingness to approve its release. Levin stated at the hearing that if the DoL does not act soon to release the report, he would seek a privilege resolution in the House to have the report made public.

C. Democrats Accuse USTR of Double Standards in DR-CAFTA

Committee Democrats repeatedly attacked the alleged double standards contained in DR-CAFTA. Representative **Ben Cardin** (D-Maryland), ranking member on the Trade Subcommittee, argued that while USTR was content with the "enforce existing laws" provisions with respect to labor and environment, USTR had no problem asking DR-CAFTA countries to change their laws with respect to intellectual property rights.

Following on this argument were questions from Representative Fortney Stark (D-California), who expressed concern over the patent protection provisions. Stark argued that if implemented, Central American countries would find it difficult to introduce generic drugs into the market. Allgeier defended the provisions, stating that nothing in DR-CAFTA would allow the parties more flexible provisions on patent protection in response to health emergencies.

II. Members of Congress Form Coalition to Defeat DR-CAFTA, Several Members Announce Opposition

The contentious Ways and Means hearing coincides with recent announcements by Members of Congress opposing DR-CAFTA. The announcements, made on the eve of the Ways and Means hearing were part of the launch of a new coalition opposing DR-CAFTA.

Since April 13, 2005, the following Members of Congress have announced their intention to oppose the agreement:

Senate	House of Representatives		
Conrad Burns (R-Montana)	Sherrod Brown (D-Ohio)	Dale Kildee (D-Michigan)	Hilda Solis (D-California)
Larry Craig (R-Idaho)	Joseph Crowley (D-New York)	Charlie Norwood (R-Georgia)	Bart Stupak (D-Michigan)
Saxy Chambliss (R-Georgia)	Marcy Kaptur (D-Ohio)	Denny Rehberg (R-Montana)	

Perhaps the most significant among the recent defections against CAFTA is the loss of deputy Democratic Whip Representative **Joseph Crowley** (D-New York). Combined with the quiet opposition to DR-CAFTA being mounted by House Minority Leader Nancy Pelosi (D-California), Democrats may find it increasingly difficult to support the agreement. Press releases from those announcing their opposition cite concerns over labor and sugar, among other provisions.

III. Democrat Jefferson, Former Ag Secretaries Announce Support for DR-CAFTA

On April 18, 2005, Representative **William Jefferson** (D-Louisiana) announced his intention to support DR-CAFTA. Jefferson, a frequent supporter of trade agreements, cited potential benefits to the port of New Orleans as a key factor in supporting DR-CAFTA. Jefferson's announcement makes him the most senior House Democrat to support the agreement. However, his staff has made clear that he will not assist pro-DR-CAFTA forces to lobby fellow members of Congress.

On April 19, 2005, six former Secretaries of Agriculture from both parties issued a letter to Congress urging support for DR-CAFTA. The letter expounded the benefits that will accrue to U.S. farmers and described a vote against DR-CAFTA as a vote for "continued one-way trade." The letter also argues that U.S. credibility at the WTO would be damaged if DR-CAFTA were defeated.

OUTLOOK

DR-CAFTA's introduction in the House was even more problematic than in the Senate. The tone of the House Ways and Means hearing was tense and sometimes hostile, with Committee Democrats targeting their anger at both Chairman Thomas and the Administration. Apparently, Acting USTR Allgeier and other witnesses were unable to persuade most Members of the potential benefits of DR-CAFTA. At this stage, pro-CAFTA lobbyists believe that they will need 25 Democrats in the House to ensure passage of the accord. To date, only two Democrats have offered their support. Moreover, given that Democratic Whip **Steny Hoyer** (D-Maryland) will likely oppose the agreement and rally others against it, the prospects for the agreement appear grim – but not hopeless.

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President Bush appears to remain disengaged from the DR-CAFTA debate, despite his recent letter of support. During a speech before the Hispanic Chamber of Commerce, an organization supporting the agreement, President Bush made only passing reference to DR-CAFTA. The President's leadership will be crucial to passing DR-CAFTA, and to shore up support for future trade initiatives.

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Battle Over Labor Provisions DR-CAFTA Intensifies; Ways and Means Chairman Thomas Anticipates Vote by May

SUMMARY

The battle over passage of the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) has turned recently to labor issues. Pro and anti-DR-CAFTA forces have released a series of reports about the region's efforts to reform labor practices and enforce existing labor laws.

Trade ministers from the region paid a visit to Washington on April 5, 2005, to rally support for DR-CAFTA. The ministers defended their laws during their visit to Congress, and pledged enhanced enforcement in an action plan on labor. Democrats, led by Sander Levin (D-Michigan), continue to criticize the countries for failing to meet core International Labor Organization (ILO) standards.

In related developments, House Ways and Means Chairman Bill Thomas (R-California) has pledged to bring DR-CAFTA to a vote in the House before the Memorial Day recess in late May. The pledge comes as informal vote counts show supporters of DR-CAFTA short 30 to 40 votes in the House.

ANALYSIS

I. House Democrats Continue Criticism of Labor Standards in DR-CAFTA Countries

On April 4, 2005, Democrats on the House Ways and Means Committee dispatched a letter to acting US Trade Representative (USTR) Peter Allgeier complaining that Central American countries have not taken meaningful steps to remedy deficiencies identified by the International Labor Organization (ILO) in 2003.

The letter, signed by Representatives Ben Cardin (D-Maryland), and Charles Rangel (D-New York), cites a number of concerns, including onerous strike requirements in Costa Rica, anti-union discrimination in El Salvador, and restrictions on union leadership in Guatemala. The letter urged USTR to submit evidence on what steps DR-CAFTA countries have taken to improve their labor regimes.

II. AFL-CIO Assails DR-CAFTA Labor Provisions and Current Labor Practices

On the same day that Democrats wrote to USTR expressing its concerns, the AFL-CIO published a report outlining its opposition to DR-CAFTA. In arguing for a rejection of DR-CAFTA, the AFL-CIO cites ILO and State Department reports, which criticize Central American countries for failing to afford workers basic protections, and for interfering in union activities. The report, *The Real Record on Workers' Rights in Central America*, links DR-CAFTA to the record of the North America Free Trade Agreement (NAFTA). The report claims, for example, that the "enforce your own laws" provisions of NAFTA have failed to increase the welfare and labor conditions of workers in Mexico.

The AFL-CIO report further asserts that adoption of DR-CAFTA would be a step backwards from existing requirements in U.S. preference programs (e.g. Generalized System

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of Preferences and the Caribbean Basin Initiative). The report argues that, under present law, the US can withhold benefits from those countries that fail to meet core ILO standards. Under DR-CAFTA, however, such an option would not be available.

III. DR-CAFTA Trade Ministers Issue Action Plan on Labor; Pay Visit to Capitol Hill

On April 5, 2005, trade ministers from Central America and the Dominican Republic visited Washington to rally support for the agreement. Ministers also met with key Members of Congress.

The ministers on the occasion of the visit released an action plan aimed at improving enforcement of their labor laws. The release of the action plan was timely, and came just a day after House Democrats wrote to USTR demanding evidence that countries party to the DR-CAFTA have or are taking steps to address concerns raised by the ILO in 2003.

The action plan outlines steps that DR-CAFTA countries will take to ensure better enforcement of existing labor laws within six key areas of concern. Additionally, the action plan outlines steps already taken by the countries, including provision of greater resources and capacity building in resolution of labor disputes. The action plan was developed in concert with the Inter-American Development Bank.

OUTLOOK

House Ways and Means Chairman Thomas, along with Deputy Secretary of State Robert Zoellick have urged the scheduling of a vote on DR-CAFTA before the end of May. The push for a quick vote comes as DR-CAFTA supporters acknowledge that, at present, they lack the votes to pass the measure in the House. Nevertheless, both Chairman Thomas and Senate Finance Chairman Charles Grassley (R-Iowa) have stated that President Bush will play an active role in convincing Members of Congress to support the agreement. Presumably, they perceive that an early vote on CAFTA would stand a better chance than allowing opposition to increase.

The lack of votes in support of DR-CAFTA already has some Congressional staffers talking about concessions to certain key interest groups. Members of Florida's Congressional delegation, for example, have indicated that they would support DR-CAFTA in exchange for protections in future agreements, or for support of their priority interests during the reauthorization of the Farm Bill in 2007. Notwithstanding, House Trade Subcommittee Chairman Clay Shaw (R-Florida) has opposed providing additional concessions to sugar interest groups, arguing that the current agreement sufficiently protects sugar. In other developments, some Members of Congress have insisted that the Bush Administration initiate safeguards on Chinese textile imports, among other concessions, in exchange for their support.

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US-Andean FTA Achieves Some Progress in Latest Round; Substantial Differences Remain as June "Deadline" Approaches

SUMMARY

Upon the conclusion of the eighth round of the US-Andean FTA negotiations on March 21, 2005, negotiators indicated that major differences remain in a number of areas including agriculture and rules-related issues.

The latest round addressed agriculture tariff and quota liberalization, rules of origin, safeguards for agricultural and other goods, extending intellectual property and investment protection, telecommunications services, among other issues. Less attention was paid during this round to industrial market access and services issues.

Negotiators have moved the target date for concluding negotiations to June 2005 (initial deadline was January 2005). The next round of talks are scheduled for Lima, Peru on April 18-22, 2005.

ANALYSIS

I. Significant Differences Remain in US-Andean FTA Negotiations

Assistant U.S. Trade Representative (USTR) Regina Vargo and negotiations from Colombia, Peru and Ecuador have indicated that the recent round of talks narrowed some differences, but significant work remains in many areas of the agreement.

A. Agriculture: Significant Work Left in Market Access and Rules

Agriculture negotiations between the US and the three Andean countries are proving to be particularly difficult given the many sensitive issues in bilateral trade. The US has been holding bilateral negotiations with each of the three countries.

1. Market Access: Many Unresolved Tariff and Quotas; Price Bands

Ms. Vargo has signaled that the negotiations are at a preliminary stage with respect to market access issues. An issue of priority for the US is the removal of price bands for sensitive commodities. Ecuador has offered to remove some oilseed related products from the band, but so far has resisted making additional concessions on other products including soybeans, soybean meal, soy oil, white and yellow corn, rice, African palm oil, barley, sugar, chicken, pork and powdered milk.

The US and Ecuador held talks on March 9-10, and narrowed some differences regarding the treatment of certain agricultural commodities and whether they would be subject to tariff rate quotas. However, differences remain on the duration of quota phase-outs, growth rates, safeguards and market access.

The US and Peru held talks on March 16-17, which were focused on treatment of sensitive agricultural products. Peru submitted a proposal on dairy products and sugar, seeking a limited quota with a 3% annual increase. Peru also raised again its proposal for a CAFTA-like approach on longer transition periods for certain products, of up to 20 years.

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Nonetheless, Peru faces considerable resistance as Chile only obtained a maximum phase-out period of 12 years for very limited items.

The US and Colombia held talks from March 21-22, and discussion focused on key products in bilateral trade. The US presented a proposal on market access for corn, wheat, barley, and other cereals. Colombia, in turn, made an offer on rice and put forth a technical document on the substitution of local varieties of beans. Colombia also sought market access in tobacco through a request of a quota and the ratification of the ATPDEA. The next round will cover products including tropical fruits, vegetables, aromatic herbs and ethanol. Another key product is cotton. Overall, Colombia seems optimistic regarding the progress of the talks.

The treatment of the highly controversial issue of sugar remains on the table, as Andean countries are keen to gain improved access. The prospects, however, are uncertain and the sector might be excluded from an eventual agreement.

2. Safeguards: Disagreement Over "Snapbacks"

Ms. Vargo indicated the US would be open to allowing for safeguards on sensitive commodities. However, the U.S. opposes the current safeguard proposals put forth by Andean countries utilizing tariff "snapbacks" (which would raise tariffs higher as commodity prices drop). Safeguards are intended as transition measures as tariffs and quotas are eliminated, and would be triggered when the global commodity price of a particular product reaches a threshold amount. However, with snapbacks – various other factors such as drought and oil prices may affect the price of a particular product. Thus, the U.S. feels that the current Andean safeguard proposals would provide excessive protection.

B. Industrial Goods: Not a Major Focus of Recent Round

Reportedly, much work remains to conclude negotiations in industrial market access, which was not a main topic of discussion in this round. The previous rounds achieved progress in sectors including chemicals, heavy equipment, and medical and scientific equipment.

For example, Colombia's market access offers to the US can be found at: http://www.coltrade.org/fta/mao.asp.

C. Services: Telecommunications/E-Commerce Close to Agreement

According to Ms. Vargo, negotiators are close to concluding an agreement on telecommunications and electronic commerce. However, Andean countries are urging the inclusion of mobile telephony in the accord. The U.S. objects to the Andean approach of including the sector within telecommunications services, asserting that it is not the dominant technology. The U.S. is also concerned about the precedence for such treatment in future FTAs.

In other developments, negotiators discussed a Colombian draft proposal on commercial agency services, among other issues.

D. Investment: Major Hurdles Remain

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Investment also remains a major obstacle, especially since Andean countries do not yet have a common position. Current proposals contain numerous brackets indicating the lack of agreement. Thus far, some proposals suggest extending to Andean investors MFN treatment that each U.S. state offers to investors of other U.S. states. Moreover, it has not been settled whether the investment protection would be constitutional in each participating country.

Provisions granting investor-state dispute rights are also still on the table. (In the U.S.-Australia FTA, Australia denied these benefits to the U.S. to offset the exclusion of sugar. However, investor-state rights were a high priority in the U.S.-CAFTA-DR agreement.)

E. Intellectual Property Rights: Extension of IP Protection Provisions Unresolved

Negotiators discussed extending protection and improvement in enforcement of intellectual property rights. Reportedly, disagreements remain on biodiversity (Andean priority), and data exclusivity for patent drugs (U.S. priority).

In general, U.S. industries seek extending protection beyond the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) in FTA negotiations. Andean countries, on the other hand, seek greater flexibility on compulsory licensing and the ability to introduce generic drugs. For example, Andean countries are resisting U.S. demands on data exclusivity of clinical test data. Since developing independent research is costly, generic companies rely on the test data of the brand-name companies to register generic brands. Securing data exclusivity on such test data would delay generic manufacturers from registering generic drugs until the end of such period; in fact, brand-name companies in some developing countries rely more heavily on data exclusivity as a source of ensuring profits than on the patent system itself.

F. Rules of Origin: Automotive Rules Agreed; Pending for Other Products

Negotiators reached an agreement on automotive rules of origin, but discussions will continue for other products. For the automotive sector, negotiators agreed to use a net cost rule to determine regional content, and to incorporate a roll up or down approach to determine whether a part can be counted towards the regional content. However, they did not agree on what percentage of a car must be produced in the region to gain the FTA benefits. (The net cost approach is also unique to certain U.S. agreements like NAFTA, and not transaction value – the common approach in most other regional agreements.)

Also, negotiators agreed to develop more flexible rules with respect to incorporation of parts with higher technological development from third countries, and not produced in the Andean region. Nevertheless, there is no agreement on the threshold that would determine when components not totally produced in the region would have enough regional content to be deemed as originating in the region.

G. Textiles: Customs Facilitation, Safeguards and New Products

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Negotiators agreed in principle to link customs cooperation and verification procedures as part of the textiles chapter. Work remains, nonetheless, on how to coordinate customs cooperation among the countries.

In other developments, the U.S. offered flexibility in accepting Andean proposals on textile safeguards that would suspend tariff reductions in certain circumstances. Similarly, the U.S. supports a mechanism that would account for the effects of import surges on the domestic market. During the talks, textile negotiators also developed a proposal to offer more favorable treatment for products of fine animal fibers, which covers alpaca, vicuna, llama or guanaco.

H. Technology Transfer: Facilitating Research Exchanges

In regards to technology transfer, Ecuador offered a proposal that would facilitate the exchange of government laboratory researchers. The US State Department will review the recent proposal.

I. Labor and Environment: Peer Review and ILO Standards

The US accepted the Andean proposal to have an independent panels review countries' compliance with environment and labor standards. Although Chile and the CAFTA-DR agreements also took a similar approach, the Andean countries consider it an achievement in light of the increasing pressure by U.S. domestic interests to enforce labor and environment standards with trade sanctions. Rather, non-compliance in these areas would be in form of fines or other penalties. The Andean countries also insist on abiding by labor standards as defined by the International Labor Organization (ILO) rather than alternate U.S.-proposed criteria.

II. CAFTA-DR Implications on the US Andean FTA: Labor and Other Issues

The current battle over passing legislation of the CAFTA-DR agreement is expected to have implications for the U.S.-Andean and other FTA negotiations. Many Members of Congress are concerned about enforcement of labor and environmental provisions, as well as access for sugar and textile imports, among other issues.

In regards to labor issues, House Democrats and labor groups like the AFL-CIO have expressed opposition to the CAFTA-DR based on their view that the labor provisions in the agreement are inadequate. In response, trade and labor ministers from the Central American countries unveiled an action plan on April 5 aimed at strengthening labor law compliance.

The CAFTA-DR action plan identifies six key areas for actions targeted at improving workers' rights:

- Labor law implementation with respect to freedom of association and trade union formation and issues related to inspection and compliance;
- Labor ministries' budget and personnel needs;
- Improving the judicial system;

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- Protections against discrimination;
- Taking action against the worst forms of child labor; and
- Promoting a culture of compliance.

A ***key learning*** from the CAFTA-DR experience would be to leverage the existing legal framework in the individual countries, for a joint-effort to seek technical assistance in the area of labor protection reforms.

Thus far, it is unclear whether the Andean countries are developing a similar proposal. Nonetheless, an effort to demonstrate goodwill in labor compliance could have positive effects on whether the U.S. Congress would approve the FTA.

III. Ninth Round of Talks Scheduled for April; More Rounds Expected

The ninth round nine of FTA negotiation has been scheduled for April 18-22, 2005 in Peru. At least two additional rounds are expected in order to conclude the agreement. Negotiators also intend to hold meetings between major rounds in order to advance negotiations.

Some of the potential issues for discussion in the upcoming round include:

- The US proposal on rice and tobacco, and possibly meats (bovine and pork);
- Market access for dairy products and cotton;
- Debate over the inclusion of mobile telecommunications; and
- How the U.S.-Andean FTA might co-exist with other regional trade accords, such as the Andean Community (CAN). In particular, Bolivia and Venezuela are both parties to the CAN but are not included in the U.S.-Andean FTA (although Bolivia might join at a later stage).

OUTLOOK

Although initially targeted to conclude by January 2005, and now June 2005, the negotiations of the U.S.-Andean FTA might extend further due to the many remaining differences among the parties. Among the most sensitive issues remaining include treatment of sensitive agricultural products, safeguard mechanisms for agriculture and textiles, investment and intellectual property protection, and of course, the enforcement of labor and environment standards. Not surprisingly, in a press conference on March 18, Ecuadorian Minister of Foreign Trade, Ivonne Baki, expressed doubts regarding whether the parties will be able to conclude negotiations by June.

Even if the FTA negotiations are concluded this year, the agreement is likely to face serious obstacles in Congress, and might not be brought to a vote until 2006. The prospects for the U.S.-Andean FTA are also tied to the fate of the DR-CAFTA, which is facing

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considerable resistance from Members of Congress and the sugar, textile and labor/environmental groups, among others.

Nevertheless, strong support exists to conclude the FTA this year – given the significant market-access and other benefits. A U.S.-Andean FTA could also encourage progress in the long-stalled FTAA talks, and possibly add momentum to the WTO Doha Round.

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Free Trade Agreements Highlights

US And Thailand Hold Third Round Of Negotiations On FTA

From April 4-8, 2005 the U.S. and Thailand held a third round of negotiations on a bilateral Free Trade Agreement (FTA), during which they:

- exchanged additional data and information on each other's positions on specific issues;
- agreed to collaborate on multiple trade capacity building projects in the areas as customs, services, and telecommunications; and
- agreed to collaborate on programs aimed at improving the access of Thailand's small and medium-sized enterprises (SMEs) to financing, information technology, and business planning services.

The fourth negotiating round will take place in July 2005, in the US.

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US-EUROPEAN UNION

USTR Publishes Annual Report On EU Trade Barriers To US Exports

SUMMARY

On March 30, 2005, the United States Trade Representative (USTR) published the 2005 National Trade Estimate (NTE) Report on Foreign Trade Barriers. The report examines the trade practices of the 61 largest US export markets, listing the most significant barriers to US exports of goods and services, US foreign direct investment, and intellectual property rights (IPR) protection.

With regard to the European Union, the report notes that:

- US exporters continue to face "chronic" barriers, of which a number have already been highlighted in previous NTE reports;
- The EU enlargement has resulted in new barriers due to the application of EU tariff, non-tariff, and services-related measures by the new Member States, while existing problems surrounding the lack of uniformity and transparency of the EU customs administration have become more prominent;
- The EU's policy of subsidizing the development, production, and marketing of large civil aircraft (LCA) has a distorting effect;
- Other barriers result from restrictive regulatory approaches that do not reflect a sound assessment of the actual risks posed by the goods in question and that rely on ill-defined concepts of precaution, such as wine restrictions and agricultural biotechnology; and
- A number of emerging EU policies may threaten to disrupt trade in the future, such as the proposed EU regulation on registration, evaluation, and authorization of chemical products (REACH).

ANALYSIS

On March 30, 2005, the United States Trade Representative (USTR) published the 2005 National Trade Estimate (NTE) Report on Foreign Trade Barriers.[14] *(Please see related report this edition)* The annual report, required by the Omnibus Trade and Competitiveness Act of 1988 (the 1988 Trade Act), is an inventory of the most significant foreign barriers to US exports of goods and services, foreign direct investment by US persons, and protection of intellectual property rights (IPR). In particular, the report examines the trade practices of the 61 largest US export markets, classifying the trade barriers into different categories that cover all governmental measures and policies, whether consistent or inconsistent with international trading rules, that restrict, prevent, or impede the international exchange of goods and

[14]http://www.ustr.gov/assets/Document_Library/Reports_Publications/2005/2005_NTE_Report/asset_upload_file383_7446.pdf

services. We summarize below the section of the report analyzing the barriers existing in the European Union.[15]

I. ***Import policies*** **–** in general, these include tariffs and other import charges, quantitative restrictions, import licensing, and customs barriers. With regard to the EU, the report lists the following as US concerns:

1. Customs administration procedures: there is (i) a lack of uniformity between the EU Member States' customs administrations procedures, (ii) an absence of EU-wide administrative management of customs operations, and (iii) an absence of tribunals and procedures that would provide for a prompt review and EU-wide correction of administrative actions relating to customs matters. The impact of these deficiencies has grown after the EU enlargement on May 1, 2004. It is worth noting that in March 2005 a WTO panel was established, pursuant to a request by the US, to decide whether the EU was in breach of its WTO obligations in relation to these alleged customs-related violations.

2. Import regime for rice: on September 1, 2004, the EU implemented a new import regime for rice, replacing the former "margin of preference" (MOP) mechanism with fixed tariffs on brown rice. As a result, the US risked losing its market access for brown rice in Europe. However, on February 28, 2005 both parties concluded an agreement that ensures market access for US brown rice exports.

3. EU enlargement: the US is concerned about (i) the new Member States' application of the EU's tariff, non-tariff, and services related barriers and (ii) their compliance with the terms of trade agreements to which the EU is bound, (iii) the uncertainty about how the EU will adjust import and tariff-rate quotas on EU imports of agricultural and fish products, and (iv) the extension of EU antidumping and countervailing duty orders to the new Member States.

4. Restrictions affecting US wine exports: for almost 20 years, US wines have been imported into the EU on the basis of derogations from several EU wine regulations. Negotiations on a bilateral EU-US wine agreement that would increase access for US wines to the EU market are still ongoing. In March 2004, the EU enforced a new wine labeling regulation that imposes additional restrictions,[16] and amendments to this regulation have so far failed to address key US industry concerns.

5. Whey protein tariff reclassification: the EU has recently approved a tariff classification for whey protein isolate (WPI) that has substantially reduced access for US WPI exports to the EU market.

[15] http://www.ustr.gov/assets/Document_Library/Reports_Publications/2005/2005_NTE_Report/asset_upload_file446_7468.pdf

[16] Commission Regulation No. 753/2002

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6. Bananas: agreements to resolve the US-EU dispute regarding trade in bananas require the EU to institute a new import regime by January 1, 2006. The US is concerned, however, that any new regime should uphold the EU's multilateral commitment to maintain total market access for non-preferential banana suppliers.

7. Market access for pharmaceuticals: the EU's national governments place various price, volume and access controls on medicines, causing market access problems for US exporters.

8. Uranium imports: EU import quotas could restrict US exports of enriched uranium and possible downstream goods such as nuclear fuel and nuclear rods and assemblies. The US is also concerned about whether nuclear agreements that the EU is currently negotiating with Russia will comply with the WTO rules on import quotas and transparency.

II. ***Standards, testing, labeling, and certification*** – among others, these include the restrictive application of Sanitary and Phytosanitary (SPS) and environmental measures; and non-acceptance of US manufacturers' self-certification of conformity to foreign product standards:

1. Standardization: certain problems continue to restrict market access, such as (i) delays in the development of EU standards and legislation, (ii) inconsistent implementation of legislation by the EU Member States, and (iii) and an overlap between Directives pertaining to specific product areas. There are also concerns regarding the respective procedures, responsibilities, and transparency in the Member States, the European Commission, and the European standards bodies.

2. Agricultural biotechnology ("GMOs", genetically modified organisms): since 1998 there has been a *de facto* moratorium in the EU on approvals of new biotechnology products. Also, several Member States have imposed marketing bans on some biotechnology products despite existing EU approvals. A WTO panel, requested by the US, Canada and Argentina, should decide in the next few months whether that moratorium is in breach of the EU's WTO obligations.

3. Barriers affecting trade in livestock products: various EU measures restrict US exports of cattle, beef, poultry, and animal by-products, such as EC Directives 96/22 ("the Hormone Directive") and 1774/2002 (on animal by-products).

4. Emerging regulatory barriers: the US is concerned about the ongoing development of Directives on (i) wood packaging material (WPM); (ii) the registration, evaluation, and authorization of chemical products (REACH); (iii) cosmetics; (iv) waste electrical and electronic equipment (WEEE) and hazardous substances in electrical and electronic equipment

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(RoHS); (v) batteries; (vi) energy using products (EuP); (vii) medical devices; and (viii) the emissions of greenhouse gases.

5. Barriers affecting vitamins and health food products

III. ***Government procurement –*** (i) the EU continues to discriminate in the utilities sector, (ii) US companies are not eligible to participate in the assistance programs that the EU provides to candidate countries for EU membership, and (iii) the fact that Member States have their own national practices regarding government procurement creates additional barriers such as pro-EU bias, excessive bureaucracy and/or limited transparency.

IV. ***Export subsidies*** – government support for Airbus by France, Germany, Spain and the United Kingdom provides significant benefits for Airbus in comparison with its US competitors. The report also lists specific measures by the governments of Belgium, France, and Spain to support Airbus suppliers, as well as measures by the governments of France and the UK to support producers of aircraft engines. The EU and the US have resumed bilateral negotiations in relation to this dispute, but it is likely that the US will request the establishment of a WTO panel to rule on the consistency of EU subsidy programs to Airbus, if they fail to reach an agreement.

V. ***Intellectual property rights (IPR) protection*** – the report mentions US concerns about (i) the high patent and maintenance fees in the EU, (ii) the inconsistency of the EU system for the protection of geographical indications (GIs) for agricultural products and foodstuffs (but not wine) with the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), and (iii) the failure of some EU Member States to fully implement the TRIPS agreement and the EU regulations. In relation to geographical indications, a recent WTO panel has ruled that the EC system is inconsistent with the TRIPS Agreement and GATT 1994 because it requires foreign governments to adopt EC-style GI protection in order to obtain registration of their GIs in the EC, and also because it requires foreign governments to act as intermediaries in processing applications and objections to registration and in running product inspection systems. The EC will need to amend its GI system to deal with this part of the Panel's conclusions. However, the Panel did not find that the requirement for product inspections in itself was inconsistent with any WTO obligation. Concerning the relationship between GIs and prior trademarks such as that between the Czech GI "Budejovické pivo" and the US-owned trademark "Budweiser", the Panel found that although the EC's system can protect GIs even where they are similar to prior trademarks, the system, on its face, has sufficient limitations to constitute a permissible exception to the trademark owners' rights. This part of the EC's GI system does not require amendment. However, the Panel rejected the EC's view that GIs may prevail over prior trademark owner's rights simply because they are GIs.

VI. ***Services barriers*** – these include, for example, limitations on financial services, data flow regulation, and restrictions on the use of foreign data processing. In particular, the report lists the following as US concerns:

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1. EU enlargement: the US is currently consulting with the European Commission to evaluate (i) possible adverse consequences of the EU enlargement for US trade in services and (ii) potential EU compensation to the US.

2. Television without Frontiers Directive: some EU Member States have implemented legislation that hinders the free flow of television programs because of their origin or language. Also, some countries have a film quota system in place ensuring EU-made films are shown on a constant basis.

3. Postal services: postal monopolies in many EU Member States restrict market access for US postal services and create unfair conditions of competition.

4. Professional services: the report focuses on barriers in the EU Member States for accounting and auditing services, architectural services, and insurance services. Significant variations between the EU Member States requirements for foreign lawyers and accountants who intend to practice in the EU can complicate market access.

5. Commercial air services: the US currently has bilateral open skies agreements with the individual EU Member States, and in the absence of a broader comprehensive agreement with the EU as a whole, it will continue to seek more liberalized arrangements with the individual EU countries. The report particularly mentions barriers in Ireland and the UK.

6. Telecommunications market access: liberalization and harmonization of the telecommunications sector has been uneven in the EU, and technical and administrative problems in some countries continue to restrict operators' access to the market. In France, Italy, Austria and Portugal, among others, the implementation of existing EU legislation is impeded by complicated procedures. In Germany, Greece, Spain, Italy, Ireland, Austria, Finland, and Sweden, the existing telecoms operators have systematically hampered slowed the entrance of competition through lengthy if often unsuccessful appeals of their national regulators' decisions.

VII. ***Investment barriers*** **–**Although free movement of capital is an EU responsibility under the 1993 Maastricht Treaty, investment barriers continue to exist in certain EU Member States. They include (i) restrictions on foreign equity participation; (ii) local export performance requirements; and (iii) restrictions on repatriation of profits. The report particularly mentions ownership restrictions and reciprocity provisions, creating barriers in a wide range of sectors, such as maritime transport and financial services.

VIII. ***Electronic commerce*** - there are no significant barriers to electronic commerce in the EU, although the EU regulations regarding exports of personal data from the EU

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could be burdensome for US companies. Also, potential problems can be caused by the so-called Brussels Regulation, which allows consumers to sue companies in the court of their country of residence.

IX. ***Other barriers –*** these include agricultural subsidies and wood industry subsidies.

OUTLOOK

A day after the release of the NTE report, Democrats of the US House of Representatives sent a letter to President George W. Bush, demanding that the Administration increase its efforts to ensure the enforcement of the US trade agreements. Among other things, they urged USTR to request WTO consultations regarding the EU's alleged unfair subsidization of Airbus.

Besides the NTE report, USTR on March 31, 2005 released the annual "Section 1377 Review" of foreign compliance with telecommunications trade agreements.[17] *(Please see related report this edition)* Thirty days after the NTE report, USTR will also publish the "Special 301" annual report on the adequacy and effectiveness of intellectual property rights (IPR) protection in trading partners. The information gathered in the NTE-report plays a key role in the preparation of both these reports.

[17] http://www.ustr.gov/assets/Trade_Sectors/Services/Telecom/Section_1377/asset_upload_file959_7529.pdf

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US-EU Highlights

Commission Proposes Sanctions In Retaliation For US Failure To Repeal Byrd Amendment; Amendment Supporters In Congress Issue Letter Opposing Repeal

On March 31, 2005, the European Commission proposed to impose retaliatory sanctions for the US's non-compliance with the 2002 WTO ruling that found the US Continued Dumping and Subsidy Offset Act of 2000 ("Byrd Amendment" or "CDSOA") inconsistent with WTO rules.[18] In particular, the EU will establish, as of May 1, 2005, an extra *ad valorem* duty of 15 % on a range of US imports such as paper, agricultural, textile and machinery products.

In a first reaction, USTR spokesman Richard Mills said that the US was disappointed with the EU's decision.[19] He added that USTR was working with the US Congress to comply with the WTO decision and repeal the Byrd amendment. However, on April 7, 2005, Senators Mike DeWine (R-Ohio) and Robert Byrd (D-W. Virginia) published a letter to House and Senate colleagues arguing against a repeal. The letter describes the retaliation as "tiny", and urges USTR to negotiate acceptance of the Byrd Amendment at the WTO.

US And EU Fail To Resolve Dispute On Subsidization Of Boeing And Airbus By Set Deadline

On April 8, 2005, USTR announced that the US and the EU had failed to conclude negotiations to resolve the dispute regarding their alleged unfair subsidization of Airbus and Boeing by the deadline of April 11, 2005.[20] Launched with the signing of the "EU-US Agreement on Terms for Negotiation to end Subsidies for Large Civil Aircraft (LCA)" on January 11, 2005,[21] these negotiations aim to eliminate all subsidies to LCA producers. USTR claims that in spite of this agreement, there continue to be differences within the EU about whether the negotiations should aim to eliminate launch aid for LCA producers.

USTR stated that they are prepared to continue the negotiations on the basis of the January 11 agreement, but warned that the US would return to WTO dispute settlement if the EU provided additional subsidies to Airbus. In the meantime, a spokesperson for the French Ministry of Foreign Affairs on April 12 said that France is currently considering a request from Airbus to provide launch aid for its A 350-model.[22]

[18] http://europa.eu.int/comm/trade/issues/respectrules/dispute/pr310305_en.htm

[19] http://www.ustr.gov/Document_Library/Spokesperson_Statements/Statement_from_USTR_Spokesman_Richard_Mills_Regarding_Announcement_by_Canada_EU_of_Retaliation_in_Byrd_Amendment_Dispute.html

[20] http://www.ustr.gov/Document_Library/Spokesperson_Statements/USTR_Spokesman_Richard_Mills_Statement_On_the_Status_of_U.S.-EU_Large_Civil_Aircraft_Subsidy-Litigation_Talks.html

[21] http://europa.eu.int/comm/trade/issues/respectrules/dispute/pr110105_agr_en.htm

[22] http://www.info-france-usa.org/news/briefing/us120405.asp

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WTO Establishes Dispute Settlement Panel To Judge On EU Customs Regime; USTR Requests Comments

On April 11, 2005, USTR announced in the Federal Register (70 FR 18448) that on March 21, 2005 the WTO Dispute Settlement Body (DSB) had established a dispute settlement panel to determine whether certain aspects of the EU customs regime are illegal under WTO rules. The US had formally requested the establishment of a panel on January 13, 2005, arguing that (i) the lack of uniformity of the EU customs administration, coupled with (ii) the lack of procedures for prompt EU-wide review, constitute a trade barrier to US exports, and particularly for small to mid-size businesses in the agriculture and high-technology sectors.[23] The EU has insisted however that its customs rules ensure a uniform treatment of imports across the EU.

Once appointed, the WTO Panel should normally issue its decision within six months. The full panel proceedings, which could include an appeal, could take between six to twelve months, or longer.

USTR is requesting written comments from the public on the issues raised in the dispute, to be submitted by May 2, 2005.

WTO Establishes Dispute Settlement Panel To Rule On US Jobs Act; USTR Requests Comments

On April 11, 2005, USTR announced in the Federal Register (70 FR 18446) that the WTO DSB has established a dispute settlement panel on the WTO consistency of the American Jobs Creation Act ("the Jobs Act"). This measure, as signed by President George W. Bush on October 22, 2004, was adopted in response to a January 2002 WTO ruling that the corporate tax cuts provided to US companies under the Foreign Sales Corporation/Extraterritorial Income (FSC/ETI) tax bill were an illegal subsidy.

Despite the adoption of the Jobs Act repealing the FSC/ETI legislation, the European Communities (EC) requested the establishment of the panel on January 25, 2005, challenging the legality of:

- the two-year transition period to repeal the Act, during which US firms would continue to receive FSC tax benefits; and
- the "grandfathering" provision that allows companies with permanent contracts in effect after September 17, 2003 to continue to receive FSC benefits beyond 2006.

Once appointed, the WTO Panel should normally issue its decision within six months. In certain cases as with this dispute, the Panel will expedite these procedures and issue its findings within 90 days. If the panel agrees with the EC's claims, the EC can seek once again compensation or suspension of concessions (e.g. possible list of sanctions arising from the residual FSC/ETI benefits. The full panel proceedings, which could include an appeal, could take between six to twelve months, or longer.

[23] WT/DS315/8

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USTR is requesting written comments from the public on the issues raised in the dispute, to be submitted by May 2, 2005.

US-LATIN AMERICA

FTAA

GAO Issues Report on FTAA Progress

SUMMARY

The latest GAO report on the FTAA negotiations analyzes last year's meetings, developments and failures of the negotiations. The lack of agreement between the United States and Brazil is the key obstacle. The most contentious issues are market access, agriculture, intellectual property rights, government procurement, services and investment.

The report emphasizes three main factors that weakened the negotiations: i) differences between United States and Brazil and its principal allies, ii) the focus on other negotiating forums and iii) unsuccessful negotiation mechanisms.

The report concludes that there are some positive signs of progress for this year. These signs include i) meetings between U.S. and Brazilian officials during the first months of the year, ii) WTO developments, iii) the 2005 Summit of the Americas, and iv) the recognition by FTAA partners that the process is worth pursuing.

ANALYSIS

On April 18th, the United States Government Accountability Office ("GAO") released a report, issued on March 18th, which analyzes the development of the FTAA negotiations.

The report provides a history of the negotiations, focusing mainly on developments between the November 2002 Quito ministerial to the November 2003 Miami ministerial, and 2004 developments. Between those meetings, explains the report, FTAA negotiators made progress on the technical aspects of the agreement, including the exchange of market access offers and some request for improvement of these offers. However, growing differences between the United States, Brazil, and many other countries over the scope and depth of obligations in the FTAA slowed down progress.

We highlight below the key issues raised in the report.

I. Countries Fail to Agree on Roadmap for Negotiations

Areas of conflict that contributed to the slow down of the negotiations noted in the report include:

- The failure of Brazil and Argentina to submit initial market access offers by the February 2003 deadline on services, investment and government procurement;

- The U.S. long-standing insistence that negotiations on certain agricultural subsidies and trade remedies be conducted within the WTO, not the FTAA;

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- The Brazilian complaint that the U.S. market access offer for Brazil and its MERCOSUR partners was poor in consumer and agricultural products.

Moreover, the United States rejected Brazil's vision of a scaled-back and rebalanced FTAA. This proposal, known as "FTAA-lite" called for: i) bilateral FTAA negotiations to focus primarily on market access for good and services; ii) regional FTAA negotiations on rules for several issues not covered by the WTO, including competition policy and dispute settlement; and iii) leaving six of the original nine issues out of the FTAA altogether and moving them to the WTO Doha Round negotiations.

The failure of the September 2003 WTO ministerial at Cancun further complicated FTAA talks.

Leading up to the Miami ministerial, states the report, FTAA ministers recognized the need for flexibility and for political guidance to avoid a breakdown in the negotiations. At Miami, countries agreed on a new negotiating structure, which gives each country the flexibility to decide, according to its needs, sensitivities, objectives, and capabilities, whether to assume commitments beyond the common set which will be applicable to all 34 countries.[24] Subsequent talks failed to define this new structure. Formal FTAA talks have yet to resume since an inconclusive February 2004 meeting. As a result, the scheduled conclusion of the FTAA in January 2005 passed without an agreement.

II. U.S.-Brazil Disagreements, Other Negotiating Priorities and Failed Negotiating Mechanisms Impede FTAA Progress

The report identifies three main factors that have inhibited progress in FTAA talks:

- ***U.S.-Brazil disagreements:*** Underlying differences remain between the United States and Brazil and their respective allies on the depth of rights and obligations on key issues continue. The most conflictive points are market access, agriculture and Intellectual Property Rights (IPR).

- ***Focus on other negotiating forums:*** Negotiations in other forums were given priority over the FTAA.[25] Participants turned to negotiations in forums such as WTO talks and subregional and bilateral efforts. In particular, WTO Doha Round and regional negotiations (US–Andean Nations, MERCOSUR–EU).

- ***Failed negotiating mechanisms:*** Two mechanisms intended to facilitate compromise, the U.S.-Brazil co-chairmanship and the two-tier structure, have thus far failed to do so. The report concludes that both mechanisms complicated negotiations.

[24] Known as the "Two tiered or two track agreement". The "lower tier" covers all nine areas previously under negotiation. The "upper tier" covers country participation, issue coverage and specific obligations, worked only by the participating countries.

[25] In part, because the United States and Brazil deemed that progress there was more possible and could eventually enhance prospects for a mutually advantageous FTAA.

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III. GAO Identifies Key Factors for Future FTAA Progress

The GAO report identifies three key issues that would lead to further development in FTAA negotiations.

- ***Break U.S.-Brazil impasse:*** First, the will to break the U.S.-Brazil impasse is necessary. USTR Zoellick and Brazil's Foreign Minister Amorim met during the first months of 2005 to analyze the possibility of renewing FTAA talks. As a result, they made some progress in bridging their differences concerning the scope of the FTAA's common set of obligations.

- ***Use WTO progress and 2005 Summit to restart negotiations:*** The second key issue mentioned by the report is that the WTO Framework Agreement and the 2005 Summit of Americas may provide a better basis for restarting FTAA talks. The WTO framework adopted in July 2004 resulted in somewhat clearer commitments regarding further disciplining agricultural subsidies and other issues; the November 2005 Summit of the Americas in Argentina could generate forward momentum for the FTAA.

- ***Countries expect gains from FTAA***: The third positive factor mentioned in the report, based on opinions of participating countries' contacted officials, is that the underlying motivation remains strong among many participants. Many experts and officials believe that the FTAA is an idea that is still worth pursuing and are hopeful for re-engagement later in 2005. Two important reasons of optimism for further FTAA development, according to the report, is that ideas that originally motivated pursuit of an FTAA remain valid and that many officials continue anticipating gains from concluding an FTAA.

OUTLOOK

FTAA countries missed the original deadline for the entering into force of the hemispheric bloc, January 2005, and the year 2004 was marked by general pessimism regarding the FTAA. In 2005, meetings between officials of the major countries, United States and Brazil, have indicated that negotiations might resume.

It is unclear how countries will deal with sensitive areas such as market access, agriculture, intellectual property rights, government procurement, services and investment.

FTAA progress requires strong political will from the major players to break the deadlocked negotiations, particularly the Brazilian and U.S. administrations. The Lula administration in Brazil continues to insist that the FTAA is not one of Brazil's priorities. Instead, Brazil will focus on South America, particularly MERCOSUR. The Bush administration is focused on garnering congressional support for the Central America-Dominican Republic-U.S. FTA, and has thus far not spent much political capital on reviving the FTAA talks. Despite the current state of negotiations, countries have invested much time and effort in the FTAA process, and the GAO study indicates that FTAA countries believe the process still is worth pursuing.

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NAFTA

Mexican Senate Approves Modifications to NAFTA Rules of Origin

SUMMARY

On March 16, 2005, the Mexican Senate approved several modifications to Annex 401 of the North American Free Trade Agreement (NAFTA) on Rules of Origin (ROO), known as the "Track I" NAFTA ROO package. The modifications eliminate and/or create rules of origin within NAFTA Annex 401, including chapters 84 and 85 of Mexico's Harmonized Tariff Schedule.

ANALYSIS

I. Mexican Senate Approves Modifications to NAFTA Rules of Origin

On March 16, 2005, the Mexican Senate approved several modifications to Annex 401 of the North American Free Trade Agreement (NAFTA) on Rules of Origin (ROO). Mexico is the last one of the three NAFTA partners to approve the amendments to the Track I NAFTA ROO package. *(Please see W&C February 2005 Report).*

Canada and the United States agreed to the amendments to Track I NAFTA ROO and these entered into force on January 1, 2005. The modifications are the result of ongoing efforts carried out by the NAFTA Working Group on Rules of Origin to liberalize the rules to stimulate trade and improve regional competitiveness. The ROO modifications aim to make it easier for manufacturers to meet the NAFTA ROO and to qualify for duty-free treatment under NAFTA.

The amendments liberalize NAFTA ROO applicable to tea, spices, carragennan (a product used in the food industry), seasonings, precious metals, speed drive controllers and their printed circuit assemblies, loudspeakers, household appliances, thermostats, toys, and parts for various equipment and machinery such as cathode ray tubes and batteries. We highlight below the modifications to Chapters 84 and 85 that Mexico approved.

Speed drive controllers

Chapter 85, 8504.40.bb:

Eliminate rule of origin applicable to tariff item 8504.40.bb and replace it with the following new rule of origin:

8504.40.bb A change to tariff item 8504.40.bb from any other subheading.

Printed circuit assemblies

Chapter 85, 8504.90.aa:

Add the following rule of origin applicable to tariff item 8504.90.aa:

8504.90.aa A change to tariff item 8504.90.aa from any other tariff item.

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Household appliances

Chapter 84, 8414.51:

Eliminate rule of origin applicable to subheading 8414.40-8414.80 and replace it with the following new rules:

8414.40 A change to subheading 8414.40 from any other heading; or a change to subheading 8414.40 within subheading 8414.90, whether or not there is also a change from any other heading, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8414.51 A change to subheading 8414.51 from any other subheading.

8414.59-8414.80 A change to subheading 8414.59 through 8414.80 from any other heading; or a change to subheading 8414.59 through 8414.80 from subheading 8414.90, whether or not there is also a change from any other heading, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

Chapter 85, 8509.10-8509.80:

Eliminate rule of origin applicable to subheading 8509.10-8509.40 and 8509.80 and replace it with the following new rules:

8509.10-8509.30 A change to subheading 8509.10 through 8509.30 from any other subheading aside from the group, except from heading 85.01 or tariff item 8509.90.aa; or a change to subheading 8509.10 through 8509.30 within heading 85.01 or tariff item 8509.90.aa, whether or not there is also a change from any other subheading aside from the group, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8509.40-8509.80 A change to subheading 8509.40 through 8509.80 from any other subheading, including another subheading within that group.

Chapter 85, 8516.10-8516.80:

Eliminate rule of origin applicable to subheading 8516.10-8516.80 and replace it with the following new rule of origin:

8516.10-8516.80 A change to subheading 8516.10 through 8516.80 from any other subheading, including another subheading within that group.

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Loudspeakers

Chapter 85, 8518.10-8518.21, 8518.22, 8518.29and 8518.90:

Eliminate rule of origin applicable to subheading 8518.10-8518.21, 8518.22, 8518.29 and 8518.90 and replace it with the following new rules:

8518.10 - 8518.29 A change to subheading 8518.10 through 8518.29 from any other heading; or a change to a good within subheading 8518.10 through 8518.29 from any other good from that subheading or from any other subheading within heading 85.18, including another subheading within that group, whether or not there is also a change from any other heading, provided there is a regional value content of not less than:

(a) 30 percent where the transaction value method is used, or
(b) 25 percent where the net cost method is used.

8518.90 A change to subheading 8518.90 from any other heading; or a change to subheading 8518.90 from any other subheading within heading 85.18, whether or not there is also a change from any other heading, provided there is a regional value content of not less than:

(a) 30 percent where the transaction value method is used, or
(b) 25 percent where the net cost method is used.

Parts

Chapter 84:

Eliminate rule of origin applicable to subheading 8473.30 and replace it with the following new rule of origin:

8473.30 A change to subheading 8473.30 from any other heading; or no required change in tariff classification to subheading 8473.30, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

Chapter 85:

Eliminate rule of origin applicable to subheading 8504.90, 8505.90, 8506.90, 8507.90, 8509.90, 8511.90, 8514.90, 8516.90, 8517.90, 8529.10,8529.90, 8530.90, 8531.90, 8532.90 and 8533.90, heading 85.38 (subheading 8538.10-8538.90), subheading 8540.91, 8540.99 and 8543.90 and replace it with the following new rules:

8504.90 A change to subheading 8504.90 from any other heading; or no required change in tariff classification to subheading 8504.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or

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(b) 50 percent where the net cost method is used.

8505.90 A change to subheading 8505.90 from any other heading; or no required change in tariff classification to subheading 8505.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8506.90 A change to subheading 8506.90 from any other heading, except from tariff line 8548.10.aa; or no required change in tariff classification to subheading 8506.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8507.90 A change to subheading 8507.90 from any other heading, except from tariff line 8548.10.aa or no required change in tariff classification to subheading 8507.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8509.90 A change to subheading 8509.90 from any other heading; or no required change in tariff classification to subheading 8509.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8511.90 A change to subheading 8511.90 from any other heading; or no required change in tariff classification to subheading 8511.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8514.90 A change to subheading 8514.90 from any other heading; or no required change in tariff classification to subheading 8514.90, provided there is a regional value content of not less than a:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8516.90 A change to subheading 8516.90 from any other heading; or no required change in tariff classification to subheading 8516.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

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8517.90 A change to subheading 8517.90 from any other heading; or no required change in tariff classification to subheading 8517.90 provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8529.10 A change to subheading 8529.10 from any other heading; or no required change in tariff classification to subheading 8529.10, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8529.90 A change to subheading 8529.90 from any other heading; or no required change in tariff classification to subheading 8529.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8530.90 A change to subheading 8530.90 from any other heading; or no required change in tariff classification to subheading 8530.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8531.90 A change to subheading 8531.90 from any other heading; or no required change in tariff classification to subheading 8531.90 provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8532.90 A change to subheading 8532.90 from any other heading; or no required change in tariff classification to subheading 8532.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8533.90 A change to subheading 8533.90 from any other heading; or no required change in tariff classification to subheading 8533.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

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8538.10-8538.90 A change to subheading 8538.10 through 8538.90 from any other heading; or a change to subheading 8538.10 through 8538.90 from any other subheading within that group, whether or not there is also a change from any other heading, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8540.91 A change to subheading 8540.91 from any other heading; or no required change in tariff classification to subheading 8540.91, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8540.99 A change to subheading 8540.99 from any other heading; or no required change in tariff classification to subheading 8540.99, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

8543.90 A change to subheading 8543.90 from any other heading; or no required change in tariff classification to subheading 8543.90, provided there is a regional value content of not less than:

(a) 60 percent where the transaction value method is used, or
(b) 50 percent where the net cost method is used.

OUTLOOK

The Mexican Senate's approval of the modifications to NAFTA Annex 401 was expected.

The NAFTA Working Group on Rules of Origin formed by representatives of the United States, Canada and Mexico developed the Track I NAFTA ROO package. Industry chambers and representatives were consulted about the modifications.

The NAFTA Working Group on Rules of Origin continues to work to reach consensus among the parties to identify further modifications to NAFTA ROO to stimulate trade and improve regional competitiveness. It is now negotiating the Track II proposals to be implemented as of January 1, 2006. The working group will continue to evaluate the Track I and Track II proposals.

The modifications to NAFTA Annex 401 will enter into effect once they are published in the *Diario Official*.

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MULTILATERAL

Responses to USTR Request on WTO Doha Round Negotiations Generally Positive, But Anxieties Toward Trade Liberalization More Apparent

SUMMARY

U.S. industry associations, companies and other interested parties provided mostly supportive views in response to the U.S. Trade Representative's (USTR) most recent request for public comments on the WTO Doha Round negotiations. Many respondents see a real chance for realizing improved market-access if the Round concludes by next year.

Most of the comments submitted on agriculture, non-agriculture market access ("NAMA") and services still favor an ambitious agenda on improving market-access and trade disciplines. Agricultural interests comprised the majority of the respondents, and provided mixed views toward removing U.S. trade barriers and domestic support. Many industrial and manufacturing groups support WTO negotiations, but expressed concern about growing U.S. trade imbalances with China in particular – and some sought maintaining U.S. tariff protection.

In addition, respondents provided perspectives on other areas of negotiation, including rules-related issues (e.g. disciplines on antidumping and subsidies), trade facilitation and dispute settlement. The comments were particularly divided over reform of antidumping and other trade remedies.

ANALYSIS

We summarize below comments submitted to the USTR Trade Policy Staff Committee (TPSC) in response to a recent Federal Register notice seeking comments on the Doha Round.[26] The comments represent U.S. companies, industry groups, foreign companies and other interested parties.

I. General Support for Non-Agricultural Market Access Negotiations; Some Resistance to Removal of U.S. Tariffs

The following industries submitted comments to USTR regarding NAMA negotiations on tariffs and non-tariff barriers ("NTBs"):

A. General Comments

The National Association of Manufactures (NAM) supports liberalization without exclusions and stated that negotiations should be as comprehensive as possible. NAM targeted 23 trading partners (20 developing, 3 developed) for substantial tariff reductions;

[26] *Federal Register*, Vol. 69, No. 236: Public Comments Regarding the WTO Doha Develoment Agenda (DDA) and the WTO Dispute Settlement Understanding (DSU) Negotiations, 9 December 2004. (Comments due 31 January 2005.)

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these account for 96 percent of duties assessed on U.S. exports of industrial goods.[27] NAM noted that the average developed country tariff is at 3 percent, while the average developing country tariff is at 17 percent. In addition, NAM supports the use of both a formula approach (non-linear with higher tariffs being cut more sharply) and sectoral negotiations involving a critical mass of countries.

The Emergency Committee for American Trade (ECAT) supports ambitious reduction of tariff and non-tariff barriers, including full tariff elimination by a date certain, and zero-for-zero initiatives in key sectors supported by a critical mass of countries. Among the sectors cited include: information technology, energy, chemicals, toys, environmental products, medical and scientific equipment, forest products, fish, gems and jewelry (most were identified as part of APEC discussions).

Consumers for World Trade (CWT) also supports zero tariffs on all goods, by a date certain and the immediate elimination of tariffs on goods not produced in the import market. CWT also identified key sectors for tariff reduction including food and agriculture, textiles, apparel and footwear. CWT noted that fully half of all duties collected by the U.S. government are in the textile, apparel and footwear categories (HTS chapters 50 to 65), or about $9.5 billion in 2001.

B. Electronics and IT Sector

The Electronic Industries Alliance (EIA), the National Electrical Manufacturers Association (NEMA), the Consumer Electronics Association (CEA) and the American Electronics Association (AeA) support ambitious sectoral initiatives including elimination of global tariffs and NTBs in the hi-tech sector.

For example, EIA, AeA and NEMA called for the expansion of the Information Technology Agreement (ITA), and complete elimination of tariffs in the electronics sector (e.g. zero-for-zero tariff initiatives). EIA noted, nevertheless, that some of its member companies have concerns with the treatment of certain products – and would communicate their concerns separately.

Toshiba America Consumer Products called for the elimination of duties on smaller, older technology televisions and harmonization of duties on all TVs to a maximum of 3.9 percent.

C. Automotive

[27] NAM recommends targeting the following countries: EU, Japan and New Zealand (99% of duties assessed among developed countries on U.S. exports); and China, Brazil, Korea, India, Thailand, Taiwan, Malaysia, Colombia, Egypt, Argentina, Venezuela, the Philippines, Peru, the United Arab Emirates, Pakistan, Nigeria, South Africa, Indonesia, Ecuador and Panama (95 percent of duties assessed by developing countries on U.S. exports). NAM notes the US is currently negotiating FTAs with seven out of the 20 developing countries and thus some barriers might be reduced earlier.

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Toyota Motor North America[28] seeks the reduction of global automotive tariffs and NTBs, and noted that barriers in developed and developing countries impede potential plans to exports its vehicles from the US. Toyota also urged the US to support inclusion of the auto sector in the "zero for zero" tariff initiative, including vehicles, auto parts and components. In addition, Toyota called for greater harmony in national customs procedures.

D. Steel and Metals

Steel and metals industries appear more protectionist in their views, including their support for maintaining existing U.S. tariffs in the sector. The Timken Company (a manufacturer of bearings and other steel products) and International Steel Group both seek reductions in global tariff rates and NTBs on steel products. However, Timken requests USTR to maintain tariffs on bearings. Likewise, Titanium Metals Corporation recommended that its products (Chapters 8108.20 and 8108.90) should be off of the Doha agenda altogether due to a shrinking U.S. titanium processing industry and national security interests.

E. Paper and Forestry Products

The American Forest and Paper Association (AFPA) and Hallmark Cards, Inc. support deep reductions or complete elimination of global tariffs in forest products. (Hallmark also supported similar objectives for toy products.) Hallmark identified key markets for reductions, and primarily developing countries which tend to have higher or no bound rates. AFPA also supports the elimination of NTBs, and is a proponent of zero-for-zero sectoral agreements as a principal negotiating strategy.

F. Kitchenware

The Cookware Manufacturers Association (CMA) and Meyer Corporation (a medium-sized aluminum and stainless steel cookware manufacturer) support the removal of tariffs and NTBs, including U.S. tariffs on these products. CMA and Meyer identified as priority markets China, the EU, Japan, Canada and Australia, where tariffs range up to 15 percent. CMA also noted with concern the considerable trade imbalance with China, which maintains tariffs of 12-15 percent.

On the contrary, Libby Inc., a manufacturer of low-value glassware and tableware, believes that a strict formula approach to tariff reductions ignores the special needs of its import-sensitive products, and requests reasonable phase-in periods to adjust to these reductions.

G. Healthcare, Medical and Chemical Products

[28] Although TMNA's parent company is in Japan, Toyota indicates that its U.S. operations account for over 31,000 U.S. workers and represent the fourth largest auto manufacturer in the US.

The Advanced Technology Medical Association (AdvaMed) and Bayer Corporation[29] favor the elimination of global tariffs and NTBs in the health sector, including on medical technology products. Bayer and Shrieve Chemical Products identified a number of chemical and medical products where they sought tariff reductions.

AdvaMed and other associations including PhRMA and NEMA support a broad health care sectoral initiative that would reduce barriers in the sector. The associations note that the elimination of trade barriers on their products would be consistent with the Doha Round's focus on improved access to health care, especially for developing country members.

H. Plastics

The Society of Plastics Industry (SPI) supports the reduction of tariffs and elimination of NTBs to restore the industry's export competitiveness. SPI expressed concern that its former trade surplus of $894 million in 2000 has turned into a considerable deficit of $3.3 billion in 2003.

I. Textile, Apparel and Footwear

Domestic textile and footwear manufacturers generally oppose further U.S. tariff reductions due to import competition from China in particular. Galey & Lord, a producer of cotton twill fabric and demin, urged maintaining tariffs on textile and apparel products and safeguard actions against Chinese imports. Nevertheless, it would support a comprehensive tariff harmonization initiative based on current U.S. duty rates, while reducing some tariff peaks.

The Rubber and Plastic Footwear Association (RPFA) also maintains that its industry is import sensitive and urged USTR to retain current tariffs on products of the domestic rubber footwear industry. RPFA also believes that China would be the main beneficiary of any tariff reductions.

J. General Manufacturing

The Association of Equipment Manufacturers (AEM), the Outdoor Power Equipment Industry (OPEI represents manufacturers of lawn and garden maintenance products) and Penn United Technology (a medium-sized tooling manufacturer) support trade liberalization and the significant reduction or elimination of global tariffs and NTBs. As demonstrated by NAFTA and the Uruguay Round, OPEI indicated that the elimination of foreign tariffs has provided significant economic benefits to its sector. OPEI also favors a sectoral tariff initiative covering outdoor power equipment.

II. Majority of Comments Focused on Agriculture Negotiations

Most U.S. industry comments to USTR were in relation to the Doha Round agriculture negotiations. The comments addressed the three pillars of the agriculture

[29] Bayer Corporation is the U.S. holding company of German-headquarted Bayer Group. Bayer notes it employs 23,300 in North America with sales of approximately $10 billion in 2003, including export products.

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negotiations (*i.e.*, market access, export subsidies, and domestic support) and related issues concerning development.

A. Expanding Market Access (Pillar One)

1. Wide Support for Tariff Reductions

Several entities were very supportive of the U.S. focus on improving market access through tariff reductions. *See, e.g.*, Comments of the California Raisin Marketing Board, National Fisheries Institute, Distilled Spirits Council of the United States, National Potato Council. The Emergency Committee for American Trade (ECAT) recommended that no product be exempted from market access commitments and the Consumers for World Trade (CWT) advocated zero tariffs for all agricultural products.

Companies specifically requested that the US negotiate improved access to foreign markets for the following products: fruits and vegetables (California Farm Bureau Federation), flowers (Floral Trade Council), sorbitol and mannitol (SPI Polyols, Inc.), frozen potatoes (ConAgra Foods), vegetable and fruit juices (Juice Products Association), cookies (Pepperidge Farm), crop protection chemicals (CropLife America), cherries (California Cherry Advisory Board), grape juice and grape products (Welch Foods Inc.) and potatoes (National Potato Council).

The American Sugar Alliance recommended that negotiations focus on applied rates rather than bound rates and that the US should not make commitments unless it receives reciprocal commitments from other WTO Members. The Grocery Manufacturers of America (GMA) advocated the creation of tariff escalation principles in addition to improved market access.

The Juice Products Association opposes reductions in U.S. duties on imports of oranges, grapefruits, lemons and grape juice and the Florida Fruit & Vegetable Association opposes U.S. tariff reductions on import-sensitive fruit and vegetable products. The American Dehydrated Onion and Garlic Association opposes reduction in U.S. tariffs for dehydrated onions and garlic.

2. Conversion of Tariffs to Ad Valorem Equivalents ("AVEs")

The Sweetners Users Association recommends using world prices to convert tariffs to AVEs. However, the Florida Fruit & Vegetable Association cautioned that the US should not rush to develop a conversion formula. The Distilled Spirits Council of the United States (DISCUS) argued that the conversion to AVEs should only be temporary for U.S. distilled spirits, because U.S. companies export higher value products and would be disadvantaged by a permanent AVE approach.

3. Reduction/Expansion of Tariff Rate Quotas

Several companies commented that in-quota and over-quota tariffs should be reduced, in-quota volume should be expanded, or that tariffs should be eliminated for in-quota shipments. *See* Comments of the Sweetners Users Association, American Sugar Alliance, International Dairy Foods Association, National Potato Council.

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4. Support for Sectoral or Product-Specific Initiatives

Several companies commented that tariffs should be reduced on at least a sectoral basis so benefits can be experienced for trade in all products. *See* Comments of Emergency Committee for American Trade, California Farm Bureau Federation, American Sugar Alliance, CropLife America.

5. Debate Over Special Agriculture Safeguards

The Sweetners Users Association opposes a special agricultural safeguard because it affects the predictability of agricultural trade and the American Sugar Alliance questioned why a special safeguard is only available for developing countries. The American Sugar Alliance argued that a special safeguard should be available in the US for sugar. The Floral Trade Council also argued that a special safeguard is needed to address perishable and cyclical products. The Florida Fruit & Vegetable Association argued that a special safeguard should be available for sensitive products.

6. Disciplines on State Trading Enterprises ("STEs")

The American Sugar Alliance argued that the US should negotiate principles on import STEs. ECAT also supports U.S. efforts to counter the trade-distorting effects of agricultural STEs.

B. Call for Elimination of Export Subsidies (Pillar Two)

Many companies agreed that the negotiations should focus on the elimination of export subsidies. *See* Comments of the Sweetners Users Association, Emergency Committee for American Trade, California Farm Bureau Federation, Floral Trade Council, Grocery Manufacturers of America, International Dairy Foods Association, California Cherry Advisory Board. The American Oilseed Coalition also argues that differential export taxes should be eliminated as an export subsidy.

The American Oilseed Coalition also argued that food aid should not only be permitted in grant form and that food aid should still include commodities and products.

C. Reductions in Domestic Support (Pillar Three)

Several companies support the reduction of trade-distorting domestic support. *See, e.g.*, Comments of ECAT, National Fisheries Institute, International Dairy Foods Association (IDFA). Cargill, Incorporated cautioned that the US should consider its economic condition and not push for domestic supports the country will not be able to afford.

1. Amber, Blue and Green Boxes

(a) Amber Box & Blue Box

GMA argued that amber box subsidies are the most trade-distorting domestic supports and it advocated clear disciplines and caps on blue box subsidies. The IDFA warned that the new blue box may just shift some subsidies from the amber box to the blue box and that blue box standards should be clarified.

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(b) Green Box

The California Farm Bureau Federation supports adding greater transparency to green box principles. The Floral Trade Council argued all domestic subsidies except green box subsidies should be eliminated and the IDFA argued all domestic supports should move towards the green box. The Sustainable Agriculture Coalition expressed concern that the green box supports should continue to include U.S. provisions for land conservation and research and development.

2. Product or Sector-Specific Initiatives

Several companies commented that real reform would not be possible unless the negotiations on trade-distorting domestic support address product- or sectoral-specific reductions. *See* Comments of California Farm Bureau Federation, California Cling Peach Board, California Cling Peach Board, Florida Fruit & Vegetable Association, Welch Foods Inc. Some companies explained that this approach may need to result in caps on product-specific supports. *See* Comments of Sweetners Users Association. The American Sugar Alliance also argued that a sector-specific approach to sugar is necessary to address related subsidies such as the support for ethanol production.

3. Formula for Reduction of Domestic Support

The Sweetners Users Association recommended that WTO Members negotiate a reduction methodology that uses the years 2000-2003 as a base period because countries had implemented their Uruguay Round commitments by that period. The Association fears that using data beyond 2003 may result in some manipulation because countries have not yet submitted that data to the WTO.

D. Special and Differential Treatment ("S&D") and Designation of Developing Countries

Cargill, Incorporated recommended that countries emphasize the developmental benefits of liberalization and greater competition, and that S&D should focus on capacity building rather than creating exemptions. The American Oilseed Coalition commented that most future growth in demand will be in developing countries; thus, those countries must undertake substantial improvements in market access. The National Fisheries Institute supports increased levels of trade adjustment assistance.

The American Sugar Alliance objects to the number of S&D provisions in the July Package. *See also* Comments of the International Dairy Foods Association.

In addition, several entities commented that some countries have are inappropriately designated themselves as developing countries with developing agriculture sectors, or that there are insufficient distinctions between developing countries, and that criteria should be imposed to designate countries as developing countries. *See, e.g.*, Comments of California Farm Bureau Federation, California Raisin Marketing Board, California Raisin Marketing Board, American Sugar Alliance, Floral Trade Council, Grocery Manufacturers of America, American Oilseed Coalition, Welch Foods Inc., National Potato Council. The Floral Trade Council objects to SDT for countries with developed flower industries.

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E. Special & Sensitive Products

The California Farm Bureau Federation recommends that longer phase out periods be permitted for U.S. peaches and apricots due to global subsidized overproduction. The California Cling Peach Board advocates tariff-sensitive treatment for U.S. canned peaches, canned fruit mixtures and frozen peaches. The American Sugar Alliance argued that sugar should receive sensitive product status and it argued that duty-free and quota-free access for least developed countries should not apply to sugar. The Florida Fruit & Vegetable Association argued Florida's fruit and vegetable products should be designated sensitive products and that these products should be exempt from tariff escalation.

The Grocery Manufacturers of America advocated increased access to foreign markets for sensitive products. In addition, the International Dairy Foods Association argued there should be a limit to the number of products a country can designate as sensitive. *See also* Comments of the American Oilseed Coalition, Distilled Spirits Council of the United States.

F. Geographic Indications

The Grocery Manufacturers of America is opposed to a more formalized system of registration for Geographic Indications ("GIs"). The International Dairy Foods Association opposes extending the GI system to foods.

G. Other Agriculture-Related Issues

The Floral Trade Council argued that flowers should be addressed through a sectoral initiative so negotiators could also address standards on chemicals and pesticides, and IP enforcement on royalties.

III. Comments on Services Negotiations Reflect Ambition and Skepticism

A. General Comments

ECAT suggested that key priorities in services include: increase market-access across all sectors, promote pro-competitive and non-discriminatory regulations, more transparency in the rule-making process, allow business personnel "easy access to visas" and commencing negotiation of government procurement commitments under the General Agreement on Trade in Services (GATS), among other objectives.

B. Energy Services

NEMA supports energy services liberalization, especially to allow electricity suppliers to expand their services abroad.

C. Maritime Services

The American Waterways Operators (AWO) urged USTR to maintain the Jones Act and related statutes (requiring vessels transporting goods between American ports to be

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owned, crewed and built in the US), and not to make any commitments on maritime transport services as part of Doha Round negotiations.

D. Engineering Services (and Mode 4 Temporary Entry)

The American Engineering Association (AEA) opposed any commitments in "Mode 4" that would designate a certain number of H1-B, L-1 or other foreign worker visas, and any commitments that would encourage business process-off shoring services.

E. Telecommunications Services

BellSouth urged USTR to ensure compliance with the WTO "Reference Paper" on anti-competitive practices, seek improved commitments in telecommunications services, and ensure the independence of national telecommunications regulatory agencies.

IV. Other Doha Round Negotiations and Issues

A. Trade Facilitation

NAM urged support for trade facilitation, citing that customs delays create significant barriers to industries' real-time, global business models. NAM also indicated that many barriers could be addressed through the establishment of "uniform, simplified procedures."

ECAT noted that trade facilitation negotiations should aim to produce "tangible progress" in reducing customs clearance times and costs, and build upon the work of APEC working groups. Among the areas targeted by APEC: (i) transparency; (ii) simplification in processing of goods, with special programs for major shippers; (iii) modernization and automation including paperless transactions; and (iv) more effective dispute resolution including expediting right to appeal rulings.

AeA called for harmonization and simplification of customs procedures, including the adoption of the World Customs Organization (WCO) Revised Kyoto Convention (RKC).

B. Rules Negotiations: Antidumping and Subsidy Disciplines

ECAT suggested that U.S. priorities should include: (i) greater transparency in operation of trade remedy rules; (ii) increased recognition of commercial business practices as normal and not unfair pricing behavior (e.g. cyclical agricultural products); (iii) fairness in calculation of trade remedies; and (iv) better account of public interest considerations.

CWT emphasized the need for reform of antidumping and countervailing duty rules, including to prohibit "false methods of calculation such as zeroing." CWT attacked the "Byrd Amendment" as weakening antidumping disciplines. CWT also urged that the AD Agreement should mandate consideration of consumers and downstream industries (i.e. the "greater public interest"), and not only those of petitioning domestic industries.

NAM urged caution to ensure that negotiations do not diminish the effectiveness of existing trade remedy measures.

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Timken, Libbey and the Specialty Steel Industry of North America (SSINA) urged U.S. negotiators to oppose all proposals that would modify the AD agreement that would make it more difficult to impose remedies or limit relief. Likewise, the International Steel Group criticized WTO bodies for their faulty interpretation of antidumping and safeguard provisions. It urged the US to oppose proposals that would weaken trade remedy rules, including on the lesser duty rule, public interest test, and raising de minimis levels.

In addition, the Committee to Support U.S. Trade Laws (CSUSTL) and the Law Offices of Steward and Stewart both provided detailed submissions urging USTR to defend U.S. trade remedy laws.

C. Dispute Settlement

ECAT believed that the WTO dispute settlement mechanism has been, "on balance… a very effective mechanism in enforcing rights." It noted, for example, that the US has raised more complaints than any other Member and prevailed (or settled favorably) in a majority of the cases filed.

ECAT and NAM suggested the dispute mechanism would benefit from greater transparency, including public access to documents and hearings.

Timken, SSINA and the International Steel Group expressed concern that WTO dispute bodies have gone beyond their mandate and created rules not found within the WTO Agreements. These groups also urged that panelists hearing trade remedy cases should have expertise in these issues.

D. Government Procurement

ECAT expressed disappointment that negotiations on transparency in government procurement were not included in the July 2004 framework agreement. ECAT urged the US to expand membership of the Government Procurement Agreement (GPA) to include key markets like China, India, Brazil and acceding countries Russia and Vietnam.

OUTLOOK

Negotiations in the WTO Doha Round are proceeding towards a critical stage as many WTO Members including the United States aim to conclude negotiations by the end of 2006. It appears that most comments to USTR recognize that real progress in WTO negotiations is within reach, and urged USTR to support an ambitious agenda of reducing barriers in key U.S. trading partners.

U.S. industry comments indicate wide support for an ambitious agenda, but growing skepticism among some industry groups is apparent, including the manufacturing, agriculture and services sectors. Some of these groups that once enjoyed favorable trade balances are now facing serious deficits. U.S. industry groups are also reluctant to allow too much flexibility to developing countries, given that some are much more competitive exporters than others – including China in industrial products and Brazil in agricultural products.

Some groups urged USTR to take a more defensive position in areas like trade remedy rules, elimination of tariffs in import sensitive sectors and facilitating temporary

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workers. The US is under industry and Congressional pressure not to alter its positions. The US is isolated in its position towards trade remedy disciplines, and a lack of movement could complicate other negotiations.

USTR and other U.S. agencies involved in Doha Round negotiations will take account of these comments as they formulate their negotiating positions. The more than forty comments (see list below) provide useful insight on industry perspectives, but do not fully represent various U.S. interests. For example, non-governmental organizations and service industries did not provide many comments as part of this request, but have presented their views through other channels.

In general, USTR is keen to support an ambitious liberalization agenda. Notwithstanding, its negotiating positions will come under greater scrutiny as Doha Round negotiations enter a final stage.

This report was based on public comments from the following industries:

1. Sweetner Users Association
2. Cargill
3. Emergency Committee for American Trade (ECAT)
4. California Farm Bureau
5. Consumers for World Trade
6. Bell South
7. Western Growers Association
8. Electronic Industries Alliance
9. American Electronics Association (AeA)
10. National Association of Manufacturers (NAM)
11. California Cling Peach Board
12. TIMET
13. Timken Company
14. Libbeys
15. Outdoor Power Equipment Institute
16. California Raisin Marketing Board
17. Society of the Plastics Industry, Inc.
18. American Chemical Council
19. American Sugar Alliance
20. Floral Trade Council
21. National Fisheries Institute
22. Rubber and Plastic FootwearManufacturers
23. SPI Polyols, Inc.
24. American Engineering Association
25. Penn United Technology, Inc.
26. Golden Associates, Inc.
27. National Electronics Manufacturers Association (NEMA)
28. Gayley & Lord
29. ConAgra Foods
30. International Trademark Association
31. Juice Products Association
32. Florida Fruit and Vegetable Association

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33. Grocery Manufacturers Association
34. International Dairy Foods Association (IDFA)
35. Toyota Motors N.A. Inc.
36. American Waterways Operators
37. Distilled Spirits Council (DISCUS)
38. California Cherry Advisory Board
39. Welch Foods Inc.
40. CropLife America
41. Sustainable Agriculture Coalition
42. American Oilseed Coalition
43. Pepperidge Farm
44. American Dehydrated Onion and Garlic Association

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WTO Panel Rules On EC Regulations Governing Geographical Indications

SUMMARY

On March 15, 2005, a WTO Panel released a mixed decision in the challenge by the United States and Australia to EC rules governing so-called "geographical indications" (GIs). GIs identify a product with a particular region, such as Florida oranges, Parma ham, or Darjeeling tea.

The Panel ruled that the EC Regulation on GIs violated the national treatment obligations of the EC under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), largely because it accorded national treatment only on a reciprocal basis. However, the Panel rejected the portion of the complaint based on the trademarks provisions of TRIPS. Although the Regulation was found to violate WTO trademarks disciplines, it was nevertheless saved as a "limited exception" to trademark rights.

ANALYSIS

I. WTO Panel Releases Mixed Decision On EC Rules Governing Geographical Indications

On March 15, 2005, a WTO Panel released a decision on European Communities - Protection of Trademarks and Geographical Indications for Agricultural Products and Foodstuffs, following a challenge by the United States and Australia.[30] It is the first time that a WTO Panel has ruled on the intellectual property rights of Geographical Indications ("GIs"), which the TRIPS Agreement defines as "indications which identify a good as originating in the territory of a Member, or a region or locality in that territory, where a given quality, reputation or other characteristic of the good is essentially attributable to its geographical origin." The intellectual property rights that are - or should be - accorded to GIs has long been one of the most difficult and contentious issues in the WTO, particularly in the ongoing trade negotiations.

The Panel's report was divided into two main parts: national treatment and trademarks. Under the national treatment disciplines of TRIPS, each WTO Member is required to accord to the nationals of other Members "treatment no less favorable than that it accords to its own nationals with regard to the protection of intellectual property." Under the challenged EC Regulation, the availability of protection within the EC for GIs located in third countries was contingent on the third country giving "guarantees identical or equivalent" to the EC. The Panel rejected the notion that national treatment obligations can be conditioned on reciprocity, and had little difficultly in finding these provisions of the EC measure to be WTO-inconsistent. The Panel's national treatment analysis is sound, and is consistent with the broad, purposeful approach that has been taken by earlier Panels.

However, the Panel's ruling on trademarks is questionable. The EC Regulation confers a positive right to use a GI that, in certain circumstances, prevents a trademark owner from exercising its trademark rights against a registered GI. The Panel agreed that the Regulation violated the exclusive trademark rights provided for in TRIPS with respect to the

[30] WT/DS174/R

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"coexistence of GIs with prior trademarks." However, the Panel ruled that the EC measure could be justified as a "limited exception" to the rights conferred by trademark. Therefore, this portion of the EC Regulation was ultimately upheld.

In determining the scope of the "limited exceptions" permitted by TRIPS, the Panel adopted the test enunciated by the 2000 *Canada - Pharmaceuticals* Panel that the "exception must be narrow and permit only a small diminution of rights." Although the Panel correctly articulated the test, its application of the law to the EC measure raises doubts. The Panel stressed that the EC Regulation curtailed the rights of the trademark owner with respect to certain goods, third parties, and signs, but not "all goods", "all third parties" and "all signs." However, the fact that the EC Regulation does not apply in "all" situations does not necessarily lead to the conclusion that the infringement of trademark is "limited." The EC's violation of the rights enjoyed by prior trademarks was arguably not "narrow", or limited to a "small diminution of rights."

One of the difficulties faced by the complainants in this case was the manner in which the Panel characterized the scope of the EC Regulation. The Panel found that the EC measure applied in relatively narrow circumstances, and this was the basis for its subsequent ruling that the EC's violation of trademark was "limited." The Panel's determinations on the scope of the EC law will be considered as findings of fact, which will complicate any appeal that may be made by the United States and Australia. A successful appeal may need to be premised on the argument that even if the EC law only applies in the manner determined by the Panel, the violation of trademark nevertheless goes beyond the "small diminution of rights" permitted under the Agreement.

II. Panel rules That EC Rules Violate National Treatment Obligations Under WTO

A. Availability Of Intellectual Property Protection: "Equivalence And Reciprocity" Conditions Violate National Treatment Obligations

The impugned EC Regulation contained two sets of procedures for the registration of GIs for agricultural products and foodstuffs, depending on whether the names of the geographical areas were located inside or outside the EC. The Panel agreed with the complainants that the availability of protection within the EC for GIs located in third countries was contingent on the third country giving "guarantees identical or equivalent" to the EC, and the willingness of the third country to provide protection "equivalent" to that available in the EC. Indeed, the Panel quoted a statement by the EC to the TRIPS Council that "the EC register on GIs for foodstuffs does not allow the registration of a foreign GI unless it is determined that a third country has an equivalent or reciprocal system of GI protection." The Regulation also provided that the European Commission could determine whether a third country "satisfies the equivalence conditions."

Article 3.1 of TRIPS provides in part that each WTO Member must accord to the nationals of other Members "treatment no less favorable than that it accords to its own nationals with regard to the protection of intellection property." The Panel noted that this obligation applied to "nationals" and not products. It also stated that this provision required the "effective equality of opportunities" between EC nationals and the nationals of other WTO Members with regard to the protection of intellectual property rights.

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Applying this test, the Panel found that the EC Regulation modified the effective equality of opportunities to obtain intellectual property protection in two ways. First, GI protection was unavailable under the Regulation for geographical areas in third countries that the Commission had not recognized as providing equivalent protection. Second, GI protection could become available under the Regulation if the third country either entered into an international agreement with the EC, or satisfied the "equivalence conditions." In the view of the Panel, both of these conditions represented a significant "additional hurdle" in obtaining GI protection that did not apply to geographical areas located within the EC. The Panel added that the "significance of the hurdle" was reflected in the fact that no third country had either entered into such an agreement, or satisfied the equivalence conditions.

The Panel examined what it called the "fundamental thrust and effect" of the Regulation and concluded that the equivalence and reciprocity conditions "modify the effective equality of opportunities" to the detriment of those wishing to obtain intellectual property protection in respect of geographical areas in third countries. The Panel said that this was constituted less favorable treatment. The Panel also pointed to the close link between nationality, on the one hand, and residence and establishment, on the other.

Therefore, with respect to the equivalence and reciprocity conditions, the Panel concluded that the EC Regulation accorded to nationals of other Members treatment less favorable than that it accorded to EC nationals, in violation of Article 3.1 of TRIPS.

B. Violation Of GATT National Treatment Obligations: EC Regulation "Formally Discriminates" Against Imports

The Panel also found that the Regulation violated the national treatment obligations of the EC under GATT Article III:4, which provides that imported products "shall be accorded treatment no less favorable than that accorded to like products of national origin."

The Panel reaffirmed that the protection of names of products from other WTO Members was contingent on satisfaction of certain conditions of equivalence and reciprocity that did not apply to the names of products from the EC. Therefore, the Panel concluded that the Regulation "formally discriminates" between imported products and EC like products, in breach of GATT Article III:4.

C. Application Procedures: "Extra Hurdles" Are WTO-Inconsistent

The Panel found that the application procedures for GI protection also breached the obligations of the EC under Article 3.1 of TRIPS and Article III:4 of GATT.

Under the Regulation, any application relating to a GI within the EC may be filed directly with an EC member State. However, an application relating to a GI located in a third country cannot be filed directly, but must be filed with its own government. If that third country government considers that the requirements of the EC Regulation have been met, it forwards the application to the European Commission. The Panel noted that under EC law, each EC member State was obligated to establish application procedures for the purpose of the Regulation, to examine applications for GI registration, and, if the application were justified, to forward it to the Commission. By contrast, a third country government is of course under no obligation under EC law to examine an application or to transmit it to the EC.

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The Panel said that applicants for GIs in third countries thus faced an "extra hurdle" that applicants in the EC did not face. Each such "extra hurdle", according to the Panel, "significantly reduces the opportunities available to the nationals of other WTO Members in the acquisition of rights under the Regulation below those available" to EC nationals. Therefore, the Regulation accorded to the nationals of other WTO Members treatment less favorable than that accorded to EC nationals, inconsistently with TRIPS Article 3.1.

D. EC Defence Of "Necessity" Rejected

The Panel found that insofar as the Regulation required examination and transmission of applications by third country governments, it accorded less favorable treatment to imported products than to like domestic products, in violation of GATT Article III:4. The Panel rejected the EC argument that its measure was justified under GATT Article XX(d) as "necessary" to secure compliance with GATT-consistent laws. The EC had argued that the requirements of examination and transmission of applications by third country governments secured compliance with the Regulation. However, Article XX(d) only applies to measures that are necessary to secure compliance with GATT-*consistent laws*. As the Panel had already found the Regulation to be GATT-*inconsistent*, the EC could not avail itself of the defence under Article XX(d). The Panel also stated that "it is not clear to what extent examination by governments, including third country governments, contributes to securing compliance with the conditions for registration."

E. Objection And Inspection Procedures Also Violate National Treatment Obligations

The Panel found that the procedures relating to the verification and transmission of objections were also WTO-inconsistent. EC nationals have a direct means to object to a registration, while non-EC nationals have to file an objection with the authorities of the third country. The Panel ruled that objectors in third countries faced another "extra hurdle" in ensuring that the authorities in their own countries forward the objection to the Commission. The Regulation therefore accorded to the nationals of other Members less favorable treatment than the EC's own nationals, inconsistently with Article 3.1 of TRIPS.

The EC Regulation also requires EC member States to ensure that inspection structures are in place. One of the conditions for the registration of GIs located outside the EC is a declaration by the third country government that inspection structures have been established. If the third country government does not establish such inspection procedures, the GI located outside the EC cannot be registered with the Commission.

The Panel said that applicants for GIs in third countries therefore did not have a right to the availability of protection and application procedures provided to applicants for GIs located within the EC. This "extra hurdle" accorded less favorable treatment to nationals of other WTO Members, in violation of the obligations of the EC under Article 3.1 of TRIPS.

The inspection procedures were also inconsistent with the GATT. The Panel recalled that non-registration of GIs would lead to a "failure of the products from those third countries to obtain the benefits of registration" set out in the Regulation. Therefore, the Regulation accorded less favorable treatment to imported products than to like domestic products, inconsistently with GATT Article III:4.

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The Panel rejected the EC's argument that the Regulation's provision on inspection could be justified under GATT Article XX(d), largely for the same reasons noted above. Article XX(d) related to securing compliance with GATT-consistent laws, but the Regulation had already been found to be GATT-inconsistent. The Panel also found that the Regulation could not be considered as "necessary" under Article XX(d), because GATT-consistent measures were available to secure compliance. The Panel noted that in other areas, such as technical regulations, exporters may have inspections conducted either by notified bodies within the EC, or by bodies located outside the EC through mutual recognition agreements. By contrast, the EC Regulation on GIs required the participation of governments. The Panel stated that the EC had not explained "what aspect of GI protection distinguishes it from these other areas and makes it necessary to require government participation".

III. Panel Rules That EC Rules Do Not Violate Trademark Disciplines Under WTO

A. Provisional Violation Of Trademark Disciplines Of TRIPS

The complainants argued that the EC Regulation violated Article 16.1 of TRIPS because it did not ensure that a trademark owner may prevent uses of GIs that would result in a likelihood of confusion with a prior trademark. Article 16.1 provides that the owner of a registered trademark has the exclusive right to prevent all third parties not having the owner's consent from using identical or similar signs for goods "which are identical or similar to those in respect of which the trademark is registered where such use would result in a likelihood of confusion."

The Panel made a number of critical threshold determinations as to the relatively narrow scope of the impugned provision. It found that:

- The provision required GI registration to be refused where it would be "liable to mislead the consumer as to the true identity of the product." The Panel stressed that, "[t]his is limited to liability to mislead as to a single issue, and not with respect to anything else."

- The provision prohibited registration "in light of a trade mark's reputation and renown and the length of time it has been used." Thus, as the Panel noted, the scope of the provision was "limited to a subset of trademarks which, as a minimum, excludes trademarks with no reputation, renown, or use." It did not prevent the registration of a GI on the basis that its use would affect any prior trademark "outside that subset."

- The standard in the provision that registration would "mislead the consumer as to the true identity of the product" was "intended to apply to a narrower set of circumstances than the trademark owner's right to prevent use that would result in a likelihood of confusion."

Turning to Article 16.1, the Panel ruled that "Members are required to make available to trademark owners a right against certain uses, including uses as a GI" and the Regulation "limits the availability of that right".

B. EC Violation Of Trademark Upheld As "Limited Exception"

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The Panel accepted the EC's argument that this portion of the Regulation could be justified as an exception under Article 17 of TRIPS. Article 17 provides that "Members may provide limited exceptions to the rights conferred by a trademark, such as fair use of descriptive terms, provided that such exceptions take account of the legitimate interests of the owner of the trademark and of third parties." The Panel considered this defence within the context of what it called the "regime of coexistence" between GIs and prior trademarks.

The Panel noted that the term "limited exceptions" in TRIPS Article 17 "emphasizes that the exception must be narrow and permit only a small diminution of rights." In the view of the Panel, there were a number of reasons why the EC Regulation met this test. The Panel stated that "it curtails the trademark owner's right in respect of certain goods but not all goods identical or similar to those in respect of which the trademark is registered." It curtailed the trademark owner's right against certain third parties, but not "all third parties." It similarly "curtails the trademark owner's right in respect of certain signs", although not "all signs identical or similar to the one protected as a trademark."

Thus, the Panel concluded that "not only may the trademark continue to be used, but that the trademark owner's right to prevent confusing uses is unaffected except with respect to the use of a GI as entered in the GI register in accordance with its registration." The Panel said that the scope of the EC regulation fell "far short" of that which had been claimed by the United States and Australia. Therefore, the Regulation constituted a "limited exception" within the meaning of Article 17 of the TRIPS Agreement. The Panel also ruled that the Regulation took account of the legitimate interests of trademark owners and third parties, including consumers.

Thus, the Panel ruled that although the Regulation was inconsistent with Article 16.1, it was justified as an exception under Article 17. Therefore, the WTO-consistency of this portion of the Regulation was upheld.

C. Other Issues

On a number of other claims raised by the United States and Australia, the Panel either exercised judicial economy, found that a prima facie case had not been made, or rejected the claims.

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WTO Appellate Body Rules On US Federal Law Prohibiting Internet Gambling

SUMMARY

On April 7, 2005, the WTO Appellate Body ruled that U.S. federal law prohibiting internet gambling violates the obligations of the United States under the WTO General Agreement on Trade in Services (GATS). The Appellate Body upheld a complaint by Antigua that the U.S. laws were inconsistent with the market access commitments of the United States for services trade.

The United States had invoked the exception in the GATS for laws "necessary to protect public morals or to maintain public order", and the Appellate Body agreed that the U.S. measures could be provisionally justified under this provision. However, the United States failed to demonstrate that its measures were not applied in a discriminatory manner, given evidence of a separate U.S. law that exempted domestic service suppliers - but not foreign service suppliers - from the ban on internet betting services for horse racing.

ANALYSIS

On April 7, 2005, the WTO Appellate Body released a decision in the dispute regarding United States Measures Affecting the Cross-Border Supply of Gambling and Betting Services (DS285). This highly contentious, politicized dispute marks the first time that the "public morals" defence has been invoked. The Appellate Body's ruling is a short-term victory for Antigua, as U.S. laws prohibiting internet gambling have been found to be WTO-inconsistent. However, it is a long-term victory for the United States, given the nature of the Appellate Body's reasoning and relatively minimal changes that will be required for the United States to comply with the decision.

The Appellate Body agreed that the challenged U.S. measures could be considered as "necessary to protect public morals or to maintain public order", which was a critically important ruling for the United States. In order to implement the Appellate Body's ruling, the United States need only remedy the discriminatory application of the law, which results from a separate statute that appeared to permit domestic service suppliers to use the internet for gambling on horse racing. If the United States ensures that its laws apply equally to domestic and foreign service suppliers, then the U.S. prohibition against internet gambling will be WTO-consistent. By ensuring equal application of the law, the United States will be able to comply with the Appellate Body's rulings without amending any of the three statutes challenged by Antigua, or opening its market to foreign internet service suppliers.

The exception for "public morals" has been part of the multilateral trading system since its inclusion in the original GATT in 1947. The fact that it has never been invoked before now likely reflects the reluctance of many countries to override objective trade rules with something as subjective as "public morals." However, its invocation by the United States in this case was entirely legitimate. The United States put before the Panel evidence of serious social problems caused by internet gambling, including money laundering, fraud, compulsive gambling and underage gambling, as well as the unique regulatory challenges posed by the internet.

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The current dispute is reminiscent of the earlier - and equally controversial - *U.S. - Shrimp* case (1997-2001). In that dispute, a U.S. law protecting sea turtles was found to be "provisionally justified" as a measure related to conservation, but was nevertheless ruled to be WTO-inconsistent because of the discriminatory manner in which the law was applied. The United States eliminated the discriminatory application, and the U.S. measure was later upheld by both a compliance panel and the Appellate Body. The same scenario may well play out in *U.S. - Gambling*. By eliminating the discriminatory application in the one identified area of horse racing, U.S. laws against internet gambling may ultimately be upheld as WTO-consistent.

I. Scope of Challenged U.S. Laws: "Total Prohibition" Not a "Measure"

In its Panel Request, Antigua had identified the "total prohibition" on the cross-border supply of gambling and betting services as the "effect" of various U.S. federal and state laws.

The Appellate Body ruled that the "total prohibition" was not a "measure" for the purposes of WTO dispute settlement. It stated that a complaint had to be brought against the measure that was "the source of the alleged effects." As Antigua had not demonstrated such a source, the Appellate Body found that the "total prohibition" could not be considered as a "measure" that could be challenged.

The Appellate Body also rejected Antigua's challenges to a number of state gambling laws. Although the Panel had followed what the Appellate Body described as a "trail of footnote references" to state measures, the Appellate Body concluded that Antigua had failed to connect the state laws to the relevant provisions of the GATS. Therefore, the Appellate Body ruled that Antigua had failed to establish a prima facie case of inconsistency of the state laws. On this basis, the Appellate Body overturned the finding of the Panel that several state laws had violated the GATS.

This left three federal laws within the terms of reference: the Wire Act, the Travel Act, and the Illegal Gambling Business Act. The Wire Act prohibits the use of wire communications (including the internet) in interstate foreign bets or wagers. The Travel Act prohibits the use any facility (including the internet) in interstate or foreign commerce with the intent of carrying on any unlawful activity. The Act defines "unlawful activity" to include gambling in violation of state laws. The Illegal Gambling Business Act prohibits anyone from conducting, financing, managing or supervising an "illegal gambling business", i.e. a gambling business that violates state law.

II. Scheduling "Specific Commitments" for Trade in Services

Under the GATS, each WTO Member sets out in a separate schedule - similar to a tariff schedule - the sector-specific commitments it has undertaken for trade in services. Under the terms of the treaty, Members" schedules of specific commitments are "an integral part" of the GATS.

This part of the dispute turned on the interpretation of the scope of specific commitments set out in the U.S. Services Schedule. The case related exclusively to the cross-border supply of services, i.e., the so-called "mode 1" of GATS.

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Excluding "Sporting" Services Did Not Exclude Betting and Gambling Services

The U.S. Services Schedule does not include the words "gambling and betting services." However, the United States undertook a full commitment - i.e., with no market access limitations - under the subheading of "Other Recreational Services (except sporting)." The United States argued that by excluding "sporting" services from its GATS Schedule, it had excluded gambling and betting services from the scope of the U.S. specific commitments. The Appellate Body rejected the U.S. position on this issue.

The Appellate Body endorsed the ruling it made in the 1998 case of *EC - Computer Equipment* that "while each Schedule represents the tariff commitments made by one Member, they represent a common agreement among *all* Members [original emphasis]." The Appellate Body found this to be equally applicable to GATS schedules. Thus, the Appellate Body said that in ascertaining the meaning of a concession in a Schedule, it was necessary to identify "the *common intention* of Members [original emphasis]."

The Panel had examined a variety of dictionary definitions of the word "sporting", an approach that the Appellate Body faulted as "too mechanical", particularly as the range of meanings included the meanings advanced by both of the disputing parties. Indeed, the Appellate Body found that the application of general rules of interpretation left the meaning of "other recreational services (except sporting)" ambiguous. Therefore, the Appellate Body said that it was necessary to have recourse to supplementary means of interpretation, as provided for in the *Vienna Convention on the Law of Treaties.*

The supplementary means of interpretation relied upon by the Appellate Body included two documents prepared by the GATT Secretariat during the Uruguay Round:

- the 1993 Scheduling Guidelines which, as the title suggests, provided guidance on the scheduling of specific services commitments; and
- the 1991 Services Sectoral Classification List ("W/120"), which provided a breakdown of service sectors and sub-sectors, based on the U.N. provisional Central Product Classification list ("CPC"). The Appellate Body described the CPC as exhaustive of all goods and services, and noted that its categories were mutually exclusive - a given good or service could only be classified in one CPC category, to the exclusion of all others.

The Appellate Body said that these two documents "provided a common language and structure which, although not obligatory, was widely used and relied upon." Therefore, unless otherwise indicated in the GATS Schedule, "Members were assumed to have relied upon W/120 and the corresponding CPC references."

This finding was critical to the disposition of the appeal on this issue. The U.S. reference to "Other Recreational Services (except sporting)" corresponded to a CPC sub-sector called "Sporting and other recreational services." This CPC category, in turn, included "gambling and betting services." Therefore, the Appellate Body ruled that the relevant entry in the U.S. Services Schedule had to be read as including gambling and betting services.

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III. U.S. Federal Laws Found to Violate U.S. Market Access Commitments

A. Applicable GATS Disciplines

GATS Article XVI:1 provides that each Member "shall accord services and service suppliers of any other Member treatment no less favourable than that provided for" under its Schedule. This general rule is given more specific content in Article XVI:2. Article XVI:2(a) provides that in sectors for which market-access commitments have been undertaken, Members may not, among other things, maintain "limitations on the number of service suppliers...in the form of numerical quotas..." Article XVI:2(c) similarly prohibits "limitations on the total number of service operations or on the total quantity of service output expressed in terms of designated numerical units in the form of quotas...."

B. U.S. Limitations on Market Access for Gambling Services: "None"

In the U.S. Services Schedule, under the column designated "limitations on market access" for "other recreational services (except sporting)", the United States had inscribed "None." Thus, as the Appellate Body found, the United States had "undertaken to provide full market access" for these services.

Nevertheless, the United States argued that its laws on internet gambling did not fall within the scope of the disciplines of Article XVI:2, because its measures did not establish any "numerical units" or "quotas." The Appellate Body rejected this argument, ruling that a prohibition on the remote supply of betting services was both a "limitation on the number of services suppliers" and a "limitation on the total number of service operations or the total quantity of service output." In the view of the Appellate Body, "limitations amounting to a zero quota are quantitative limitations."

Therefore, the Appellate Body ruled that the Wire Act, the Travel Act and the Illegal Gambling Business Act were inconsistent with the market access obligations of the United States under Articles XVI:1 and XVI:2(a) and (c) of the GATS.

IV. U.S. Public Morals Defense Rejected: Discriminatory Application

A. Applicable Defence: A Three-part Test

Article XIV(a) of the GATS permits WTO Members to take measures "necessary to protect public morals or to maintain public order." Any Member invoking this provision needs to satisfy three tests. The challenged measure must:

- relate to "public morals" or the maintenance of "public order", which in turn requires what the Appellate Body described as a "sufficient nexus between the measure and the interest protected";
- be "necessary", in that there is no reasonably-available, WTO-consistent alternative; and
- meet the conditions of the so-called "chapeau", or opening paragraph of Article XIV, i.e., the measure must not be "applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination

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> between countries where like conditions prevail, or a disguised restriction on trade in services."

The U.S. prohibition on internet gambling met the first two parts of the test, but failed the third condition, as discussed below.

B. Defining "Public Morals and Public Order"

The Panel had defined "public morals" in part as "standards of right and wrong conduct maintained by or on behalf of a community or nation." The Panel referred to the evidence led by the United States that the three federal statutes in question had been adopted to address concerns such as money laundering, organized crime, fraud, underage gambling and pathological gambling. On this basis, the Panel found that the U.S. measures were designed to protect public morals and/or to maintain public order within the meaning of Article XIV(a).

On appeal, Antigua challenged the Panel's finding on what the Appellate Body said was the "rather limited ground" that the Panel had failed to determine whether the U.S. concerns met the standard set out in the footnote to this provision (that the public order exception could be invoked only where "a genuine and sufficiently serious threat is posed to one of the fundamental interests of society"). The Appellate Body found that there was no basis to conclude that the Panel failed to assess whether this standard had been satisfied.

Accordingly, the Appellate Body affirmed that the three U.S. laws fell within the scope of "public morals and/or public order" within the meaning of Article XIV(a).

C. Appellate Body Reverses Panel on "Necessity" Requirement

The Appellate Body stressed that in determining whether a measure was "necessary", there needed to be a "weighing and balancing" and comparison of measures, "taking into account the interests or values at stake", in order to determine "whether another, WTO-consistent measure is 'reasonably available'."

The Panel had attached great importance to the fact that the United States declined Antigua's offer to consult with Antigua on these issues. In the view of the Panel, by "rejecting Antigua's invitation to engage in bilateral or multilateral consultations and/or negotiations, the United States failed to pursue in good faith a course of action that could have been used by it to explore the possibility of finding a reasonably available WTO-consistent alternative." Thus, the Panel concluded that the U.S. measures could not be considered as "necessary" under Article XIV(a).

The Appellate Body overturned the Panel on this issue, finding that a mere failure to consult was an insufficient basis on which to find that the U.S. measures were not "necessary." The Appellate Body said that the Panel's "necessity" analysis was "flawed because it did not focus on an alternative measure that was reasonably available to the United States to achieve the stated objectives regarding the protection of public morals or the maintenance of public order." Engaging in consultations with Antigua "was not an appropriate alternative for the Panel to consider because consultations are by definition a process, the results of which are uncertain and therefore not capable of comparison with the measures at issue in this case." Therefore, the Appellate Body reversed the Panel's finding

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that because the United States did not enter into consultations with Antigua, its measures could not be considered as "necessary."

The Appellate Body then ruled that the United States had made a prima facie case of "necessity", and Antigua had failed to identify a reasonably alternative measure. The Appellate Body noted the Panel had recognized that the United States had "legitimate specific concerns with respect to money laundering, fraud, health and underage gambling that are specific to the remote supply of gambling and betting services", which suggested to the Panel that such measures were indeed "necessary" within the meaning of Article XIV(a). The Appellate Body said that the Panel acknowledged that, "but for" the U.S. alleged refusal to negotiate with Antigua, the Panel would have found the U.S. laws to be "necessary." As the Appellate Body found that the Panel erred in finding that consultations constituted a measure reasonably available to the United States, and as Antigua had raised no other measure that could be considered as an alternative to the prohibition on remote gambling, the Appellate Body found the U.S. laws to be "necessary" within the meaning of Article XIV(a).

D. U.S. Failed to Demonstrate That Its Measures Did Not Constitute "Arbitrary or Unjustifiable Discrimination"

As the U.S. measures had been found to be "provisionally justified" under Article XIV(a), the Appellate Body still needed to assess whether the measures were applied in a discriminatory way, contrary to the requirements of the so-called "chapeau" of this provision.

The Appellate Body pointed to a federal statute that appeared to permit wagering for horse racing over the telephone and the internet for domestic service suppliers (although the two sides differed on the meaning of the statute). The Appellate Body said that the U.S. measures therefore did not meet the tests set out in the chapeau to Article XIV. It ruled that the United States "did not demonstrate that the prohibition embodied in the measures at issue applies to both foreign and domestic suppliers of remote gambling services." The Appellate Body was careful to note that it was not making a finding as to whether the horseracing statute did, in fact, permit domestic suppliers to provide certain remote betting services that would otherwise be prohibited by the Wire Act, the Travel Act, or the Illegal Gambling Business Act. However, the United States had not demonstrated that the prohibitions in the three challenged statutes were applied to both foreign and domestic service suppliers of remote betting for horse racing. For this reason, the Appellate Body concluded that the United States had not established that its measures met the conditions of the chapeau.

Accordingly, the U.S. invocation of the Article XIV defence was rejected, and its measures were found to be WTO-inconsistent.

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