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Japan External Trade Organization
WTO and Regional Trade Agreements Monthly Report

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Summary of Reports

United States

United States Continues Export Control Regime Enforcement

On June 29, 2006, the Washington International Trade Association (WITA) hosted a panel on "U.S. Trade Security and Export Controls." Stephen Brosnan, State Department Directorate of Defense Trade Controls, and Bernie Kritzer, Director of the Office of National Security and Technology Controls at the U.S. Department of Commerce Bureau of Industry and Security (BIS), provided a brief overview of the U.S. export controls regime. We review here their assessments.

USITC Releases Report on Recent Trends in U.S. Services Trade

On June 23, 2006, the United States International Trade Commission (USITC) released its 2006 Annual Report on "Recent Trends in U.S. Services Trade." The report contains figures for U.S. cross-border trade in services for 2004, the most recent year for which such statistics are available. According to the report, the U.S. service sector accounted for 83 percent of gross domestic product (GDP) and 85 percent of private sector employment in 2004, with U.S. service firms "preeminent in global services trade" and experiencing a 13 percent growth in sales of services abroad by foreign-based affiliates of U.S. firms in 2003. Cross-border services trade accounted for 22 percent of total U.S. cross-border trade volume and generated a $47.8 billion surplus in 2004. The report also highlights services trade with China and tariff rate equivalents (TREs) for barriers to trade and investment in commercial banking services in 50 countries.

The 2006 Annual Report on "Recent Trends in U.S. Services Trade" is available at: http://www.usitc.gov/ind_econ_ana/research_ana/pres_cong/index.htm

Senate Finance Committee Examines Vietnam's PNTR Status

On July 12, 2006, the Senate Finance Committee held a hearing to discuss granting Vietnam Permanent Normal Trade Relations (PNTR) as part of its accession to the World Trade Organization (WTO). The committee heard **on-the-record** oral testimony from panelists representing government and business interests on **S. 3495** "A bill to authorize the extension of nondiscriminatory treatment (normal trade relations treatment) to the products of Vietnam." We review below this testimony and the discussion between the Committee and the hearing witnesses.

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The full text of the witnesses' statements is available on the Finance Committee website at: http://www.senate.gov/~finance/sitepages/hearing071206.htm.

United States and Mexico Strike NAFTA Sugar Agreement

On July 27, 2006, the U.S. Department of Agriculture (USDA) announced that U.S. and Mexican trade officials have negotiated the terms of an agreement that end the 12-year-old dispute over U.S.-Mexico trade in sugar. The conflict involved U.S. quota restrictions on Mexican sugar imports and Mexican duties on U.S. imports of High Fructose Corn Syrup (HFCS). The agreement follows the United States and Mexico's agreement to a deadline for Mexico to comply with a World Trade Organization (WTO) ruling (DS308, *Mexico–Tax Measures on Soft Drinks and Other Beverages*) that a Mexican tax on soft drinks and other beverages with non-sugar sweeteners was inconsistent with WTO rules.

United States Highlights

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

- Senate Finance Committee Approves Vietnam PNTR Bill
- Senate Passes Legislation Extending Sanctions on Burma for Three More Years
- AFBF President Calls for One-Year Extension of Farm Bill
- Japan Eases U.S. Beef Ban After Concluding Meatpacking Facility Inspections
- CIT: Byrd Amendment 'Support Provision' Violates First Amendment
- COAC Seeks Appointment Nominees, Holds Open Meeting on Customs Issues
- Sens. Grassley and Baucus Introduce Customs and Trade Facilitation Bill
- Senate Finance Committee Requests Written Comments on Miscellaneous Tariff Measures
- OEE Seeks Passage of EAA and Further Compliance of U.S. Export Control Regime
- President Bush Nominates New Asst. Secretary for Commerce
- DOC Proposes Rule to Tighten Defense-Related Exports to China, Loosen Controls on High-Technology Exports; Negative Reaction by U.S. Industry
- USTR Susan Schwab's Briefing to ABCDoha on U.S. Trade Agenda
- "Patriot Corporations" Act Grants Preferential Federal Contracting, Tax Preferences to Certain Firms

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- USTR Announces Results of 2005 Annual GSP Review
- U.S. and Canada Sign Lumber Agreement, Builds on April 27 Version

Free Trade Agreements

House Ways and Means Committee Holds Hearing on U.S.-Peru FTA

On July 12, 2006, the House Ways and Means Committee held a hearing on the U.S.-Peru Free Trade Agreement (FTA), the "Peru Trade Promotion Agreement" (PTPA). The hearing included **on-the-record** oral testimony from government and business representatives. We review below this testimony and the discussion between the Committee and witnesses.

The full text of the witnesses' statements is available on the Committee website at: http://waysandmeans.house.gov/hearings.asp?formmode=detail&hearing=491

U.S. and Korean Negotiators End Second Round of FTA Talks A Day Early

On July 14, 2006, U.S. and Korean negotiators ended a day early the second round of five-day talks on the U.S.-Korea (KORUS) Free Trade Agreement (FTA) in Seoul. South Korea ended the final day of negotiations after the U.S. delegation suspended working group meetings on trade remedies and services, two areas that Korea has prioritized. The United States suspended the meetings after Korea informed the U.S. delegation that it intended to implement without further discussion a "positive list" reimbursement system for pharmaceutical products. The United States argues that this system would discriminate against U.S. and other foreign pharmaceutical firms that wish to sell their products in the Korean market. Despite the impasse over pharmaceuticals, negotiators made some progress in agriculture, automobiles, tariff elimination for industrial goods, and services and investments. The parties plan to meet in the United States September 4-8 for a third round of talks but have not yet designated a city.

U.S. and Malaysia Complete Second Round of FTA Negotiations

On July 17, 2006, U.S. and Malaysian officials met in Washington, D.C. for the second round of formal bilateral Free Trade Agreement (FTA) negotiations. Officials from the Office of the United States Trade Representative (USTR) conducted discussions with their Malaysian counterparts in several areas including government procurement and pharmaceuticals. After the Washington talks, there will be three more rounds of negotiations to be tentatively held on September 17, October 30 and December 11, 2006.

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Free Trade Agreements Highlights

We want to alert you to the following Free Trade Agreements developments:

- Senate Finance Approves Peru FTA in “Mock Markup”
- USTR Official Discusses KORUS Second Round
- U.S. Implements U.S.-Bahrain FTA as of August 1, 2006
- Senate Finance Committee Delays Vote on Draft Peru FTA Legislation During “Mock Markup,” Approves Amendment on Beef
- USTR Official and Cambodian Commerce Minister Discuss Bilateral TIFA, TRADE Act
- House Passes Oman FTA 221-205 Along Partisan Lines; Labor, Port Security Issues Narrow Margin of Victory
- Deputy USTR Discusses U.S.-Asian Trade Agenda Before House International Relations Committee
- House Ways and Means Approves Peru Agreement in “Mock Markup”
- USTR Commends Omani Labor Reforms as FTA Vote Looms
- U.S. to Sign TIFA with Cambodia; USTR Announces ASEAN TIFA Close to Completion
- U.S. and Colombia Finalize FTA Text; Bush Administration to Announce Intent to Sign Agreement
- House Members Demand Proof of Korea’s Open Auto Markets Before USTR Cuts Tariffs in FTA Negotiations
- DR-CAFTA Takes Effect in Guatemala

Multilateral

Doha: What’s Next?

Entrenched positions prevented World Trade Organization (WTO) Members from reaching an agreement on agricultural and non-agricultural market access (NAMA) modalities at the June 27-30, 2006 Doha Round negotiations. Discussions between the Group of Six (G-6) nations – Australia, Brazil, the European Union, India, Japan and the United States – did not result in any substantive agreement that could serve as a basis for discussion with the other Member’s trade ministers. The meeting’s failure did not surprise observers, and some participants noted that negotiations never really started.

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A July 1 formal meeting of the Trade Negotiating Committee (TNC) mandated that WTO Director-General Pascal Lamy hold intensive consultations with the G-6 nations to break the deadlock. There is a sense of urgency among Members to reach a consensus on modalities as soon as possible in order to complete Doha Round negotiations by the end of 2006. However, some Members have begun to express skepticism about the feasibility of this timeframe. If Members fail to meet this deadline, the round's future would grow uncertain, and it is unclear whether Members would be able to muster the political will necessary to revive the stalled negotiations.

U.S. Services Coalition Releases Summary of Revised U.S. Services Offer

On July 11, 2006, the Coalition of Services Industries (CSI) released a summary of the United States' revised World Trade Organization (WTO) services offer. The summary outlines the U.S. offer including new commitments in research and development (R&D) and technical testing and analysis services, online games services, physical well-being services, and a number of small service activities categorized as "other business services." The new U.S. offer also includes revisions to legal services and computer and related services (CRS) commitments. Under the timeframe established at the December 2005 WTO Ministerial Conference in Hong Kong, all WTO Members must submit their revised services offers by July 31, 2006. We will send a detailed report of the new U.S. services offer once its full text is available. We include here the CSI summary's full text.

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Multilateral Highlights

We want to alert you to the following Multilateral developments:

- Lamy Suspends Doha Round After Last-Minute Talks Collapse
- Mexico, Argentina Initiate WTO Compliance Proceedings in US OCTG Case
- U.S. Becomes Focus of Two New WTO Panels: Gambling and Shrimp
- Religious Freedom Clouds Vietnam PNTR Consideration; WTO Pushes for October Accession
- U.S. Requests Panel Selection in Airbus-Boeing Dispute
- WTO Members Continue to Point Fingers While WTO Services Chair Calls for "Major Improvements" to Revised Offers
- WTO Director-General Pascal Lamy Welcomes WTO Agreement on Regional Trade Agreements
- Japanese Prime Minister, Cabinet Ministers Promise Cooperation to Conclude Doha by End-2006; Lamy Holds "Confessionals" In Effort to Determine Members' "Bottom-Line" Positions on Doha
- U.S. and Mexico Agree to WTO Ruling Compliance Date on Soft Drink Tax
- Tension Grows Between U.S. and Russia On WTO Accession; Lead to Failure in Reaching Agreement, Negotiations to Continue Through Fall
- U.S. Banks Worried About U.S. Concessions in Potential Russia WTO Accession Deal

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Reports in Detail

United States

United States Continues Export Control Regime Enforcement

Summary

On June 29, 2006, the Washington International Trade Association (WITA) hosted a panel on "U.S. Trade Security and Export Controls." Stephen Brosnan, State Department Directorate of Defense Trade Controls, and Bernie Kritzer, Director of the Office of National Security and Technology Controls at the U.S. Department of Commerce Bureau of Industry and Security (BIS), provided a brief overview of the U.S. export controls regime. We review here their assessments.

Analysis

On June 29, 2006, WITA hosted a panel on "U.S. Trade Security and Export Controls." U.S. State and Commerce Department officials provided their views on the U.S. export control regime and the major policy issues on which the Administration is currently focused.

- **Stephen Brosnan, State Department Directorate of Defense Trade Controls,** explained that four entities administer export controls over goods and commodities from the United States: the State Department (State), the Department of Commerce (DOC), the Department of Defense (DOD), and the U.S. Congress. The Department of State regulates the export of items that have military or space applications while the Department of Commerce regulates the export of items and information that have civil applications and "dual-use" items with civil and military applications. The Department of Defense reviews both State and Commerce export licenses for national security concerns. The U.S. Congress is a key participant in the U.S. export control regime because it has jurisdiction over U.S. export control laws. In this context, according to Brosnan, an "export" is: (i) a defense article[1] or technological data transmitted outside the United States or (ii) the disclosure, by any means, of physical or intangible articles (i.e., faxes, technical data) to a foreign national. State officials first ensure that the article in question is eligible for export, and that access to the exported article by the

[1] In general, a defense article is an item developed for a military application that does not have a predominant civilian application. Unless an exemption applies, a license must be obtained before any defense article is exported to a foreign country or provided to a foreign national.

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prospective end user is not prohibited under U.S. law. According to Brosnan, there are two major policy issues on which the Administration is currently focused : (i) U.S. arms embargoes to Libya and Venezuela; and (ii) the Administration's disagreement with possible lifting of the European Union's embargo on arms to China. Brosnan said that the State Department will soon remove Libya from a U.S. list of state sponsors of terrorism. The Administration has announced a possible arms embargo for Venezuela. The U.S. is pressuring the EU to not lift its arms embargo to China. Last year EU officials sought to replace the ban with a tightened code of conduct on arms exports to ensure weapon sales to China did not increase overall.

- **Bernie Kritzer, Director of the Office of National Security and Technology Controls at the Bureau of Industry and Security (BIS) of the U.S. Department of Commerce**, stated that BIS enforces and implements U.S. export control regulations concerning the export of "dual-use" goods and technologies (those having both civil and military applications), as well as exclusively civil application items. The items subject to the BIS' jurisdiction are listed on the Commerce Control List ("CCL"), which is found in the Export Administration Regulations.[2] According to Kritzer, whether a license is required to export or reexport an item on the CCL is determined by examining the precise classification of the item, the destination of the item, and the end-user. BIS also maintains the Denied Persons List and the Entities List, which identify specific persons and entities to which exports are not permitted without the prior approval of BIS. BIS also deals with "deemed export controls" on the release of technology or source codes to foreign nationals in the United States or abroad. In this regard, the Administration seeks to maintain national security while permitting business and researchers to employ foreign nationals who play a key role in their operations. BIS also conducts pre-license (PLC) and post-shipment verification (PSVs) checks to: (i) establish the *bona fides* of the end user and (ii) ensure that these technologies arrive at their intended destination and are used for the purposes stated in the export license. According to Brenan, BIS has no discretionary role and it operates with a legal mandate that implements closely the provisions established under various international treaties and control regimes (*e.g.,* the Wassenaar Agreement and the Missile Technology Control Regime).

[2] The CCL covers items such as electronics, computers, telecommunications and information security; lasers and sensors; navigation and avionics materials; marine-related materials; propulsion systems, certain space vehicles, and related equipment. And materials, chemicals, microorganisms, and toxins. The CCL index is located at http://www.access.gpo.gov/bis/ear/ear_data.html.

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Outlook

Both Administration officials stressed that the U.S. export control regime will continue to respond to global security concerns while allowing for “legitimate trade.” Brosnan and Kritzer denied that the regime is a cause for the U.S. soaring deficit, as some observers have suggested.

In recent years, and due to changes in technology and the ongoing “War on Terror,” export control emphasis has shifted to high technology exports and “deemed exports.” To reflect these changes, the Administration constantly updates its computer and microprocessor regulations and periodically issues controls on sensitive items, such as night vision and thermal imaging equipment, which did not exist before.

Last year, BIS processed 17,681 export licenses. BIS approved 14,962 licenses worth US$38.4 billion and denied 2,474 worth US$2.2 billion (of total U.S. exports of US$804 billion). According to BIS’ 2005 annual report, China was the destination for the largest number of approved licenses. BIS approved 1,303 licenses for exports to China, worth more than US$2.4 billion; 31 percent of these were for “deemed exports” licenses. China continues to be one of the largest foreign markets for controlled items as well. In 2005, nearly 10 percent of all licenses were for Chinese end-users.

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USITC Releases Report on Recent Trends in U.S. Services Trade

Summary

On June 23, 2006, the United States International Trade Commission (USITC) released its 2006 Annual Report on "Recent Trends in U.S. Services Trade." The report contains figures for U.S. cross-border trade in services for 2004, the most recent year for which such statistics are available. According to the report, the U.S. service sector accounted for 83 percent of gross domestic product (GDP) and 85 percent of private sector employment in 2004, with U.S. service firms "preeminent in global services trade" and experiencing a 13 percent growth in sales of services abroad by foreign-based affiliates of U.S. firms in 2003. Cross-border services trade accounted for 22 percent of total U.S. cross-border trade volume and generated a $47.8 billion surplus in 2004. The report also highlights services trade with China and tariff rate equivalents (TREs) for barriers to trade and investment in commercial banking services in 50 countries.

The 2006 Annual Report on "Recent Trends in U.S. Services Trade" is available at: http://www.usitc.gov/ind_econ_ana/research_ana/pres_cong/index.htm

Analysis

On June 23, 2006, the USITC released its 2006 Annual Report on "Recent Trends in U.S. Services Trade." The report contains figures for U.S. cross-border trade in services for 2004, the most recent year for which such statistics are available. The USITC compiles the report annually but did not publish a report in 2005. The 2006 report presents a statistical overview of U.S. trade in services and analyzes five service industries: air transportation, banking and securities, education, insurance, and legal services. It examines cross-border exports, imports, and trade balances; services provided to U.S. and foreign consumers by multinational firms' overseas affiliates; and the competitive conditions affecting the global market for these services. The report also contains a chapter on U.S. services trade with China and a special topic chapter that estimates TREs for barriers to trade and investment in commercial banking services in 50 countries.

I. General Figures

According to the report, the U.S. services sector accounted for 83 percent of GDP and 85 percent of private sector employment in 2004. U.S. services firms were "preeminent in global services trade" and experienced a 13 percent growth in sales of services abroad by foreign-based affiliates of U.S. firms in 2003. Cross-border services trade accounted for 22 percent of total U.S. cross-border trade volume and

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generated a $47.8 billion surplus in 2004. The report also notes that in recent years, the value of services transactions through affiliates abroad has exceeded the value transacted through cross-border trade, reflecting continuing, although uneven, services trade and investment liberalization that "encourages the globalization of service firms." In 2003, sales by foreign-based affiliates of U.S. firms reached $477.5 billion, and U.S. cross-border exports totaled $291.5 billion.

The report notes that in 2004, "U.S. services exports and imports experienced exceptionally rapid growth" due in large part to the recovery of travel-related services following the September 11, 2001 terrorist attacks.[3] U.S. exports of private services totaled $323 billion, while U.S. imports totaled $258 billion, "resulting in a trade surplus of approximately $65 billion," a surplus which was 2 percent smaller than the $67-billion surplus in 2003. The report notes that exports increased by 11 percent during 2004 with the bulk of export growth in 2004 attributable to growth in five categories: (i) passenger fares; (ii) other transportation; (iii) travel; (iv) financial services; and (v) royalties and license fees.[4] U.S. services imports grew by 15 percent in 2004, stemming from growth in: (i) other transportation; (ii) travel; (iii) royalties and license fees; and (iv) passenger fares (8 percent).[5]

The report states that in 2003, sales by foreign-based affiliates of U.S. companies increased by 13 percent to approximately $477 billion. U.S.-owned affiliates in the insurance industry accounted for 17 percent of total affiliate sales, and the finance, broadcasting and telecommunications, wholesale trade, transportation and warehousing, and publishing industries also accounted for large shares of total affiliate sales. According to the report, the largest host-country markets for U.S.-firms' foreign affiliates were the United Kingdom, Japan, Canada, Germany and France. The report also notes that European countries accounted for approximately 56 percent of U.S. firms' affiliate sales in 2003. Purchases from majority-owned, U.S.-based affiliates of foreign firms totaled $381 billion with services purchased from U.S.-based insurance affiliates accounting for 22 percent of such purchases, the largest single-industry share; other important purchasers included firms in the transportation and warehousing, utilities and finance sectors.[6]

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3 *Recent Trends in U.S. Services Trade: 2006 Annual Report*, U.S. International Trade Commission, June 2006, Washington DC, p. 2-1

4 *Id.* at 2-2 – 2-3

5 *Id.* at 2-3

6 *Id.* at 2-5

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II. Air Transportation Services

USITC determined that between 1999-2004, U.S. air transportation services exports grew at a compound annual growth rate of approximately 3 percent, while imports grew by 4 percent. The report notes that "the trade deficit during this period reflects the greater number of U.S. citizens that travel on foreign airlines, relative to foreign citizens that travel on U.S. airlines."[7] The report also states that in dollar terms, the U.S. market accounts for 40 percent of the global airline industry, and that Europe and the Asia-Pacific region account for 28 and 24 percent, respectively. The report highlights the "difficult operating environment" that airlines around the world have faced over the past several years; the global airline industry lost $18 billion in 2001, $13 billion in 2002, $6.6 billion in 2003, and $4.8 billion in 2004. Such large-scale losses particularly affected the U.S. air transportation market, with five of the largest U.S. carriers declaring bankruptcy in 2005. The report notes that high oil prices, persistent overcapacity, weak global macroeconomic conditions, and a steep decline in passenger traffic following September 11, 2001 all contributed to the industry's financial difficulties.[8]

III. Banking and Securities Services

The report states that in 2004 U.S. cross-border financial services exports grew 13 percent to $27.4 billion and imports grew 14 percent to reach $11.2 billion. USITC notes that increased foreign purchases of U.S. bonds, financial management services, and credit card services contributed to the rise in exports; the rise in services imports is due to U.S. investors' increased trading in foreign markets, a response that USITC attributes to a lack of significant growth in U.S. equity markets in 2004.[9] The report also notes that the largest markets for U.S. financial services exports in 2004 were the United Kingdom ($4.2 billion in purchases), Bermuda ($1.3 billion), Canada ($1.2 billion), France ($897 million) and Japan ($875 million). The largest suppliers of financial services imports into the United States were the United Kingdom ($1.4 billion in sales), Japan ($284 million), France ($264 million), Hong Kong ($227 million) and Canada ($226 million).

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7 *Recent Trends in U.S. Services Trade: 2006 Annual Report*, U.S. International Trade Commission, June 2006, Washington DC, p. 3-1

8 *Id.* at 3-3 – 3-4

9 *Id.* at 4-1

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IV. Education Services

USITC reports that in 2004, U.S. education services exports totaled $13.5 billion and imports amounted to $3.5 billion, resulting in a $10-billion trade surplus. The report notes that the principal U.S. export markets for education services were India (12 percent of all exports), China (9 percent), Korea (8 percent), Japan (7 percent), and Canada (5 percent). The report also states that in 2003 one-quarter of foreign students studying abroad chose to study at colleges and universities in the United States, the largest overall market worldwide.[10]

V. Insurance Services

The report states that between 1999-2004, U.S. cross-border exports of insurance services grew at a annual compound growth rate of 15 percent to $6.1 billion and imports grew 26 percent to $29.9 billion. USITC notes that the majority of cross-border trade in insurance services reflects reinsurance transactions, with the trade deficit during the 1999-2004 period reflecting non-U.S. companies' dominance in the reinsurance sector. The report states that in 2004, the largest U.S. export markets for insurance services were the United Kingdom ($1.3 billion), Germany ($809 million), Canada ($715 million), Bermuda ($466 million), and Japan ($401 million). The report also notes that in 2004, the largest source of U.S. insurance services imports was Bermuda ($12.4 billion in U.S. insurance imports) followed by the United Kingdom ($3.5 billion), Switzerland ($3.1 billion), and Germany ($2.9 billion). Sales of services by insurance carriers' U.S.-owned affiliates in foreign markets totaled $80.4 billion in 2003, with non-life insurance accounting for $43.8 billion in sales and life insurance accounting for $31.2 billion. The report states that sales by U.S.-owned affiliates were largest in Japan followed by the United Kingdom and Latin America and other Western hemisphere countries.[11]

VI. Legal Services

USITC determined that U.S. cross-border exports of legal services increased to $3.9 billion in 2004, and that imports declined to $754 million, producing a trade surplus of $3.2 billion. The report notes that U.S. exports increased 19 percent in 2004 and imports grew at a 6 percent annual compound rate during the same period. The report also identifies the United Kingdom ($711 million), Japan ($658 million), Canada ($340 million), Germany ($312 million) and France ($287 million) as the largest U.S. export markets for

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[10] *Recent Trends in U.S. Services Trade: 2006 Annual Report*, U.S. International Trade Commission, June 2006, Washington DC, pp. 5-1 – 5-4

[11] *Id.* at 6-1 – 6-2

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legal services. According to the report, in 2003, sales of legal services by U.S.-owned affiliates in foreign markets totaled $1.1 billion, and U.S. purchases from U.S.-based legal affiliates of foreign companies totaled $24 million. [12]

VII. U.S. Services Trade with China

The USITC found that bilateral merchandise trade drove growth in services trade between the United States and China, and that many of the services traded involve intermediary functions that facilitate product, payment and information flows between producers and consumers. According to the report, the largest amount of cross-border trade occurred in freight transport and port services. As part of its 2001 accession agreement to the World Trade Organization (WTO), China agreed to open selected services sectors to foreign trade and investment, including the air transport, banking, education and insurance services sectors. U.S. industry representatives, however, consider China's implementation of these commitments uneven. They report continued barriers to trade and investment including "high capitalization requirements to establish businesses, burdensome licensing and operating requirements, and ambiguous regulations and procedures."[13]

The report states that for the first time China became one of the top ten export markets for U.S. cross-border trade in services, having received $7.2 billion worth of services exports from the United States in 2004. USITC notes, however, that this still only accounts for 2.2 percent of U.S. service exports worldwide. In 2004, U.S. services exports to China grew by 20.4 percent, the highest annual growth rate in U.S. cross-border services exports to China since 2000. Overall, U.S. cross-border services imports from China reached $5.6 billion. The report also states that the provision of financial, telecom, education, and other business services exports accounted for the largest segment of U.S. cross-border exports to China, totaling $3.4 billion.

VIII. Measurement of Non-Tariff Impediments to Trade in Commercial Banking Services

USITC notes that "trade negotiations increasingly focus on the removal of non-tariff measures (NTMs), which restrict the cross-border flow of goods, services, and investment capital," and that "it is often difficult for trade policymakers to perceive the benefits of agreements that remove NTMs."[14] Thus the USITC is

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[12] *Recent Trends in U.S. Services Trade: 2006 Annual Report*, U.S. International Trade Commission, June 2006, Washington DC, pp. 7-1 – 7-4

[13] *Id.* at 8-1

[14] *Id.* at 9-1

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developing methodologies to quantify NTMs in goods and services and assess their economic impact through the development of baseline tariff rate equivalents (TREs) for existing NTMs.[15] Based on this methodology, the report estimates baseline TREs for NTMs on selected commercial banking services across 50 developed and developing countries and identifies several EU member states as having the smallest TREs and several Latin American countries as having the largest. USITC plans to use benchmark TRE estimates as a basis for assessing progress made through bilateral and multilateral trade agreements in liberalizing services trade regimes.

Outlook

The USITC report details a healthy trade in services between the United States and other major global economies, including China, an increasingly important marketplace. The surplus in U.S. trade in services contrasts with its trade deficit in goods and reflects the continuously expanding role of the services sector in the United States economy. A successful conclusion to the WTO Doha Round services negotiations would open more markets for U.S. service providers and likely expand the U.S. trade surplus even further. As USITC noted, several non-tariff barriers (NTBs) and NTMs prevent U.S. services providers from efficiently working in and with other economies. USITC along with other government bodies, including the Office of the United States Trade Representative (USTR), will likely focus on these NTBs and NTMs in bilateral negotiations in an attempt to liberalize foreign markets for the benefit of U.S. services providers.

15 TREs express the percentage increase in a product's or service's price due to trade restriction.

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Senate Finance Committee Examines Vietnam's PNTR Status

Summary

On July 12, 2006, the Senate Finance Committee held a hearing to discuss granting Vietnam Permanent Normal Trade Relations (PNTR) as part of its accession to the World Trade Organization (WTO). The committee heard **on-the-record** oral testimony from panelists representing government and business interests on **S. 3495** "A bill to authorize the extension of nondiscriminatory treatment (normal trade relations treatment) to the products of Vietnam." We review below this testimony and the discussion between the Committee and the hearing witnesses.

The full text of the witnesses' statements is available on the Finance Committee website at: http://www.senate.gov/~finance/sitepages/hearing071206.htm.

Analysis

On July 12, 2006, the Senate Finance Committee held a hearing to discuss granting Vietnam PNTR as part of its WTO accession. The committee heard **on-the-record** oral testimony from panelists representing government and business interests on **S. 3495** "A bill to authorize the extension of nondiscriminatory treatment (normal trade relations treatment) to the products of Vietnam."

- **Senator Charles Grassley (R-IA), Chairman of the Senate Finance Committee,** stated that if the United States does not extend PNTR to Vietnam, WTO Rules mandate that the United States will be unable to "enjoy the market access benefits of the bilateral agreement with Vietnam" or to "realize significant reductions in [Vietnamese] duties on U.S. exports of beef, pork, soybean, fruit, and dairy products, among others." He stated that "Vietnam will also provide significant market access opportunities across the entire services spectrum…. [K]ey areas include banking, insurance, telecommunications, energy, express delivery, distribution, and computer and related services." He also opined that the "commercial merits of Vietnam's accession to the World Trade Organization are amply demonstrated" but added that "concerns have been raised that Vietnam does not adequately protect human rights and religious and political freedoms." Grassley also stated that he received "a letter of support from the U.S.-Vietnam WTO Coalition… signed by a number of respected Democrats and Republicans who urge Congress to extend permanent normal trade relations to Vietnam as soon as possible." Signatories include Madeleine Albright, James Baker III, Warren Christopher, Henry Kissinger, Robert Rubin, and Colin Powell.

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- **Senator Max Baucus (D-MT), Ranking Committee Member and S. 3495 sponsor** stated that granting Vietnam PNTR will allow Vietnam to "reduce to 15 percent or less its tariffs on agriculture goods that affect three-quarters of U.S. farm exports, …cut tariffs to 15 percent or less for 94 percent of U.S. exports, … [and] permit U.S. banks, insurance companies, and distribution companies to establish 100 percent foreign-owned subsidiaries immediately or within a few short years." He added that "Vietnam will eliminate BSE-related restrictions on all beef products and recognize the equivalency of U.S. food safety inspections." Calling Vietnam's WTO accession "a big deal," Baucus opined that it "is a big commercial win for the United States [because] …it is the most economically-significant trade initiative in some years [and therefore] commands broad political support in both chambers of Congress." Baucus stated that "to get the benefit of Vietnam's accession, we must come together to grant Vietnam PNTR," and that "the time is now, before other countries - like China - beat us to the punch by benefiting first from Vietnam's market-opening commitments." Baucus also warned that if Congress does not grant PNTR to Vietnam by the end of July it will be difficult to address the issue until after November's mid-term elections. He urged Deputy United States Trade Representative (USTR) Karan Bhatia to send a message to the Bush Administration to "get engaged" to ensure the measure's July passage.

- **Karan Bhatia, Deputy United States Trade Representative (USTR),** testified on behalf of the Bush Administration in strong support of S. 3495, arguing that "WTO accession for Vietnam will benefit the United States economically, will promote reform in Vietnam, and will support broader American interests in Vietnam and in Southeast Asia as a whole." He described the U.S.-Vietnam bilateral agreement and stated that "Vietnam's bilateral market access agreement with the United States builds on the progress we have achieved over the past five years and promises even greater access to one of Southeast Asia's most dynamic economies." Bhatia stated that "Vietnam has committed to the elimination or phase out of all WTO-prohibited industrial subsidies and agricultural export subsidies." He also noted that the Administration achieved two significant results in the bilateral agreement: (i) Vietnam has confirmed that its state-owned and state-controlled enterprises will make purchases and sales in international trade based on commercial considerations; and (ii) Vietnam agreed that the United States can continue to use special "Non-market Economy" calculation methodologies in antidumping cases "until the Department determines that Vietnam has become a market economy or the year 2018, whichever comes first." Bhatia opined that "Vietnam has worked hard to prepare for WTO membership" and "has enacted over 80 new laws and regulations to bring its trade regime into consistency with international norms, … momentous changes for a country with

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no previous record for transparency in its legislative and regulatory processes." Bhatia urged the Senate to consider the bill before the summer recess in August.

- **Eric John, Deputy Assistant Secretary, Bureau of East Asian and Pacific Affairs, U.S. Department of State**, stated that "Vietnam's accession to the World Trade Organization comes in the context of a remarkable transformation that has been underway in Vietnam for some time." He added that "for Vietnam, WTO accession – and PNTR status - is only the latest chapter in a long story of change and opening to the world that continues to be written," opining that WTO accession and PNTR will "keep Vietnam committed to the very positive course." John noted that "there are some remaining areas that are of concern to the Administration [including] continuing deficiencies in Vietnam with respect to human rights and restrictions on the ability of Vietnamese to freely practice their religious beliefs." He stated, however, that "overall, reports of violations have sharply declined in number while evidence of positive developments has multiplied" and added that the Administration would continue to work with Vietnam to ensure that these concerns are addressed.

- **Jon Caspers, Former President, National Pork Producers Council (NPPC)**, stated that the NPPC "strongly supports Vietnam's accession to the WTO," and that "U.S. pork exports have benefited from virtually all recent trade agreements, and the agreement with Vietnam will be no different." According to Caspers, Vietnam's WTO accession will mean that its tariffs on key pork and pork products will be reduced by 50 percent over five years, its tariffs on pork variety meats will be immediately cut from the Most Favored Nation (MFN) level of 20 percent to 15 percent, and its tariffs on processed pork products will be reduced from 20 percent to 10 percent over five years. He also stated that "Vietnam has agreed to recognize the U.S. meat inspection system as equivalent to its own meat inspection system [and] has also agreed to implement the WTO Agreement on sanitary and phytosanitary measures upon accession." Caspers added that "to realize the benefits of this WTO agreement, the United States does not have to reciprocate anything other than to grant the same normal trading rights to Vietnam on a permanent basis that the U.S. grants to virtually all of its trading partners and to all 150 WTO member countries."

- **Jeffrey Shafer, Vice Chairman, Citigroup Global Markets**, congratulated U.S. and Vietnamese negotiators for achieving a comprehensive WTO accession agreement "that will provide broad market access across a range of U.S. goods and services." He added that Citigroup "believes that the agreement is a good one in this respect, that it will be an important step in securing broader U.S. national interests and that it will contribute to economic modernization and growth in emerging markets such as Vietnam." Shafer also stated that "liberalization through WTO accession and PNTR

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will promote development of Vietnam's financial sector." He added that "reducing barriers to trade, ensuring the protection of legal rights, WTO accession and PNTR for Vietnam will be by far the most important event that has taken place since the resumption of bilateral relations," and it "will provide U.S. companies with the certainty and protections they need to invest for the long-term in Vietnam."

Outlook

Congressional passage of legislation granting PNTR with Vietnam and enabling it to accede to the WTO should not prove problematic. However, the timing of consideration of the bill remains uncertain. Sources note that Congress will likely have to wait to address Vietnam PNTR until after it considers the formal implementing legislation for the U.S.- Oman Free Trade Agreement (FTA) and perhaps also the U.S.-Peru FTA. Congress will likely consider the Oman and Peru agreements before considering Vietnam's PNTR status because that legislation preceded the Vietnam PNTR legislation in Congress. Thus, USTR's push for summer Congressional consideration of the PNTR legislation might be too ambitious, with Congress instead focusing on Vietnam following the congressional recess for the November mid-term elections. If this is the case, Vietnam will accede to the WTO in late 2006 or early 2007. On the other hand, the Bush Administration's active engagement with Congress on the Vietnam issue might hasten the legislation's approval and vault it ahead of the FTA legislation. In November 2006, President Bush will attend the annual Asia Pacific Economic Cooperation (APEC) leaders meeting in Hanoi, and the Administration might ask Congress to approve the bill before that time to avoid arriving there empty-handed. Vietnam hopes to complete its accession to the WTO by the APEC summit, and PNTR's passage would send a strong message of U.S. support for Vietnam's joining the global trade body. Whether congressional leadership will eschew traditional scheduling procedures and comply with the Administration's wishes remains unclear.

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United States and Mexico Strike NAFTA Sugar Agreement

Summary

On July 27, 2006, the U.S. Department of Agriculture (USDA) announced that U.S. and Mexican trade officials have negotiated the terms of an agreement that end the 12-year-old dispute over U.S.-Mexico trade in sugar. The conflict involved U.S. quota restrictions on Mexican sugar imports and Mexican duties on U.S. imports of High Fructose Corn Syrup (HFCS). The agreement follows the United States and Mexico's agreement to a deadline for Mexico to comply with a World Trade Organization (WTO) ruling (DS308, *Mexico–Tax Measures on Soft Drinks and Other Beverages*) that a Mexican tax on soft drinks and other beverages with non-sugar sweeteners was inconsistent with WTO rules.

Analysis

I. United States and Mexico Reach Agreement on NAFTA Sugar

On July 27, 2006, the U.S. Department of Agriculture (USDA) announced that U.S. and Mexican government trade officials had negotiated an agreement to end the 12-year-old dispute over U.S.-Mexico sugar trade. This dispute centered on U.S. quota restrictions on Mexican sugar imports and Mexican duties on U.S. imports of High Fructose Corn Syrup (HFCS). According to USDA, in conformity with Annex 703.2 of the North American Free Trade Agreement NAFTA, "Mexico is projected to be a net surplus producer of sugar for the next marketing year (FY 2007)."

We detail below the key terms of the agreement:

- The United States will grant duty-free access to 250,000 metric tons of Mexican sugar during the next marketing year (FY 2007). Mexico will provide duty-free access to the Mexican market for an equivalent amount of U.S. HFCS during the same period.
- Effective January 1, 2008, Mexico will not impose duties on U.S. HFCS.
- Mexico will establish a duty-free quota for U.S. sugar imports of not less than 7,258 metric tons (raw value) for each of marketing years 2006, 2007, and 2008. The over-quota tariff on U.S. sugar will be eliminated as of January 1, 2008, as provided for in NAFTA.
- From October 1, 2007 to December 31, 2007, the United States will provide duty-free access for Mexican sugar of a minimum of 175,000 metric tons and, based on market conditions, up to 250,000 metric tons. Mexico will grant duty-free access to an equivalent amount of U.S. HFCS during the same period.

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- On July 3, 2006, Mexico and the United States submitted a joint letter to the WTO Dispute Settlement Body (DSB) concerning the elimination of Mexico's 20 percent tax on soft drinks made with sweeteners other than cane sugar.

In an effort to resolve the bilateral sweetener dispute, the United States in October 2005 granted Mexico additional sugar market access of 250,000 MT due to a shortage of sugar in the southern states resulting from Hurricane Katrina. In exchange, Mexico granted reciprocal market access to U.S. HFCS to a maximum of 250,000 MT of fructose from October 1, 2005 to September 30, 2006. Although welcomed, these concessions did not end the HFCS dispute because: (i) the Mexican Congress refused to revoke the 20 percent tax on HFCS in the 2006 Income Tax Law; and (ii) Mexico decided to appeal the WTO Panel Report on Soft Drinks and Other Beverages.

On December 6, 2005, Mexico notified the WTO DSB of its intention to appeal the October 7, 2005 Panel Report in *Mexico - Tax Measures on Soft Drinks and Other Beverages* (DS308).[16] On March 6, 2006, the WTO's Appellate Body upheld the Panel ruling that Mexico's 20-percent tax on soft drinks not made with cane sugar violated WTO rules, thus rejecting Mexico's appeal. On July 5, 2006, the United States and Mexico agreed to a deadline for Mexico to comply with the WTO ruling. With the possibility of facing U.S. retaliation upon failing to comply with the WTO ruling, Mexico came under strong pressure to seek a negotiated solution and the repeal of the 20 percent tax on HFCS. Nevertheless, the Mexican government indicated that it would continue to impose tariffs on U.S. HFCS imports as long as Mexican sugar is subject to tariffs upon entry into the United States.

II. United States Welcomes Agreement; Mexico's Private Sector Is Ambivalent

U.S. lawmakers and trade associations praised the agreement, in particular the provisions on the elimination of tariffs on NAFTA sugar as of January 1, 2008:

- **Chairman of the Senate Finance Committee Charles Grassley (R-IA)** stated that "under the agreement, Mexico will lift its tariffs on imports of U.S.-produced high fructose corn syrup and will eliminate its discriminatory tax on this product," and that "through new tariff-rate quotas, U.S. high fructose corn syrup exporters will have expanded access to the Mexican market starting in October 2006, and free trade will begin starting on January 1, 2008." He added that he is "glad Mexico is now

[16] On October 7, 2005, a WTO panel found that certain Mexican taxes on soft drinks and sweeteners were inconsistent with Mexico's national treatment obligations under General Agreement on Tariffs and Trade (GATT) Article III. The panel rejected Mexico's argument that its measures were necessary to secure compliance by the United States with U.S. obligations under the NAFTA.

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coming into compliance with its NAFTA and WTO obligations," and that he hopes the agreement will "put disputes between the United States and Mexico over high fructose corn syrup behind us."

- The **U.S. Corn Refiners Association,** the members of which produce HFCS, also welcomed the agreement because it "guarantees access for HFCS to the Mexican market, eliminates the soft drink tax, and removes all tariffs on HFCS exports." The association added that the agreement "sets in motion an irreversible path to free trade in January 2008."
- The **American Sugar Alliance (ASA)** has expressed deep concerns regarding the "unneeded and unjustified" large quantities of Mexican sugar imports that will be gain access to the U.S. market. According to ASA, the agreed import quantities between Mexico and the United States "will lead to disorder, oversupply, and unfairly injure efficient American producers."

Mexico's National Chamber for the Sugar and Alcohol Industries (Cámara Nacional de las Industrias Azucarera y Alcoholera) expressed mixed reviews. The Chamber stated that the Mexican sugar industry was not entirely in favor of the agreement, despite the agreement's allowing Mexican producers to increase their market share in the United States ahead of 2008. According to a Chamber official, "the Mexican sugar industry still would like to be able to send all of its surplus sugar to the U.S. market."

Outlook

Three factors motivated the parties to break a deal on the sweetener dispute: (i) the upcoming elimination of trade barriers to sweetener trade by January 1, 2008 as provided for in the NAFTA; (ii) the possibility of U.S. sanctions against Mexican imports if Mexico failed to repeal the 20 percent tax at the next Congressional session; and (iii) increased pressure on the part of U.S. sugar users and HFCS producers, several of which faced shortages in the aftermath of Hurricane Katrina.

The Mexican government is likely to increase its lobbying efforts with the Mexican Congress to repeal the 20 percent tax on HFCS during the next Congressional session. However, the Mexican Congress will only consider the repeal of the HFCS tax when it debates the 2007 Income Tax Law in late November or early December 2006. At present, it is unclear whether the current Congress or the new Congress, which will take office on December 1, will consider the 2007 Income Tax Law. It is clear, however, that the next Mexican President will face a divided Congress – a factor that could delay Mexico's compliance with the NAFTA sugar agreement.

In the past six months, the United States and Mexico have successfully resolved major trade disputes on sugar, cement, tequila, and pork products. The resolution of these disputes is significant given the two

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countries inability to resolve them over the past several years. The resolution of the sugar dispute is meaningful. The sugar dispute, like the well-known dispute on trucking, arose directly from the terms of the NAFTA, and the alleged failure of the respective Governments to live up to the commitments that they made in the text of the Agreement. In the sugar case, the allegations of non-compliance set off a chain of events that caused its own trail of actions and reactions by the two Governments, some of which also involved litigation in the NAFTA and the WTO. The settlement is an important step to bringing this issue to a close.

According to experts, the prospects for resolution of the trucking dispute are slim in the short term because: (i) U.S. trucking companies are not putting enough pressure on the U.S. government to seek entry into Mexican highways; and (ii) Mexico's transportation sector is seeking special treatment in the U.S. and fears competition if U.S. carriers are granted access to Mexican highways. In contrast to sugar, the trucking dispute is highly sensitive due to U.S. industry groups' concerns regarding the Mexican trucking industry's alleged failure to meet U.S. safety and environmental requirements.

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United States Highlights

Senate Finance Committee Approves Vietnam PNTR Bill

On July 31, 2006, the Senate Finance Committee voted to report favorably S. 3495, which would provide Permanent Normal Trade Relations (PNTR) to Vietnam. The committee approved the legislation by a margin of 18 to 0 with two senators, Sens. Rick Santorum (R-PA) and Jim Bunning (R-KY), voting "present." The committee considered the measure on July 27 but could not vote because of the absence of a quorum. The committee's markup and vote clears the way for the full Senate to vote on the measure, but the timing of this vote is uncertain. The House Ways and Means Committee has yet to hold a hearing or markup on its version of the Vietnam PNTR bill, H.R. 5602; it must complete these tasks before the full House can vote on the measure.

Following the committee's vote, Senator Max Baucus (D-MT), Ranking Member on the committee and co-sponsor of the legislation, stated that Congress "should be leaping at the chance to fully engage the U.S. with Vietnam's emerging economy and its 83 million new customers" and thus "should work hard and work fast to approve Vietnam PNTR as soon as possible." He also stated that the Finance Committee had taken "an important step" in approving PNTR for Vietnam and that "Congress needs to bring this 15-year process of reconciliation with Vietnam to its long-sought conclusion."

With strong support and little dissent over Vietnam's human rights and religious freedom record, the Finance Committee's vote bodes well for full Congressional approval of PNTR for Vietnam. It therefore appears likely that the full Congress will grant Vietnam PNTR status as part of its accession bid to the World Trade Organization (WTO). Despite the Finance Committee's approval, the timing for full Congressional approval of the PNTR measure remains unclear. The House Ways and Means Committee must first review its version of the bill before a finalized version of the legislation is sent to the House floor for a vote. With the House now on Summer recess, the Ways and Means markup and subsequent House floor vote will not occur until after the House reconvenes on September 6. If House and Senate leadership are unable to schedule floor votes shortly thereafter, the PNTR vote might be delayed until mid-November, as both chambers will adjourn again in late September for the Fall mid-term elections. However, President Bush has expressed a strong desire to have PNTR completed before he attends the November Asia-Pacific Economic Cooperation (APEC) summit in Hanoi. It is thus likely that the House and Senate will find the time to complete their votes on Vietnam PNTR in the weeks following the August recess.

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Senate Passes Legislation Extending Sanctions on Burma for Three More Years

On July 26, 2006, the U.S. Senate passed legislation (H.J. Res. 86) by voice vote extending economic sanctions on Burma by up to three years. The legislation will next move to President Bush for his signature, which according to sources is likely. On July 11, the House approved the same measure which includes a ban on all imports from Burma, first imposed in 2003. Although the legislation authorizes the sanctions for three more years, the House and Senate must vote to renew the sanctions each year.

Senator Mitch McConnell (R-KY) sponsored the Senate version of the measure and stated that “passage of this bill will mean continued sanctions against the illegitimate, dictatorial regime that currently holds Burma in its grip--the Orwellian-named State Peace and Development Council, or SPDC." Senator Max Baucus (D-MT) stated that he supported the bill but expressed “reservations about the efficacy of unilateral sanctions,” as “Burma's human rights record has worsened, rather than improved, in the three years since Congress enacted the Burmese Freedom and Democracy Act.” He added, however, that the extension of sanctions “adds our voice to the voice of the Burmese people, muffled by the oppressive regime, in calling out for democracy and human rights."

AFBF President Calls for One-Year Extension of Farm Bill

On July 27, 2006, President of the American Farm Bureau Federation (AFBF) Robert Stallman stated that given the collapse of the World Trade Organization’s (WTO) Doha Round, the United States should extend its current farm support programs for at least one year. Stallman stated that “by extending the current farm program, with minor changes to take into account recent trade rulings, [the United States] will move forward with the kind of policy that helps ensure U.S. farmers have the support they need to survive in today's contentious global trading environment."

Stallman’s remarks followed Secretary of Agriculture Mike Johanns’s July 24th statement that the United States should produce a new Farm Bill in 2007, when the current bill is set to expire. Stallman argued that there was “little point” in eliminating farm subsidies unilaterally while U.S. trading partners continue their own subsidy programs. Stallman added that unilateral elimination of farm subsidies could weaken the United States in future negotiations because countries “don't get credit in negotiations for what you do on your own.”

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Stallman noted EU Trade Commissioner Peter Mandelson's request that President Bush veto any extension of the current farm legislation, but he opined that Bush will likely not take Mandelson's advice because "it would be wrong" if the United States gave EU officials "what they want." In his remarks, Stallman also expressed support for extending Trade Promotion Authority (TPA) which expires July 1, 2007 because "extending TPA will allow U.S. trade negotiators to aggressively pursue regional and bilateral trade opportunities, which will secure market access for our farm goods that the Doha Round has not offered."

With the July collapse of the Doha Round, WTO Members have been left scrambling to re-prioritize their bilateral and unilateral initiatives. In an attempt to influence this process, U.S. agricultural and other groups will voice their opinions on U.S. trade objectives. Chief on the agricultural groups' list is the Farm Bill, which Congress has already begun to consider in anticipation of the legislation's 2007 expiry. The Doha Round's collapse has left U.S. legislators far less constrained when considering U.S. farm subsidies, as the United States must only comply with current WTO subsidy caps, rather than the much lower levels that would have emerged in any final Doha agreement. To take full advantage of this reality, the AFBF and other agricultural groups will aggressively lobby against the reduction of U.S. farm subsidies in a new Farm Bill, and Stallman's comments are indicative of this effort. On the other hand, many observers note that the collapse of the Doha Round will likely lead to increased litigation at the WTO, with several new cases perhaps focusing on U.S. agricultural subsidies for corn, rice, and sorghum. Moreover, Brazil has indicated that it might seek enforcement of a WTO ruling against U.S. cotton subsides which could result in almost $1 billion in retaliatory tariffs against U.S. exports. Such cases will likely cause the Bush Administration and Congressional free traders to advocate a new farm bill which avoids current and new trade disputes. With no Doha Round agreement to provide a concrete framework to constrain U.S. subsidy levels, the likely outcome of the conflict between the AFBF's position and the possible WTO disputes will be a 2007 Farm Bill that provides nearly the same overall level of domestic support but through new and different programs meant to assuage WTO Members' complaints. Although this strategy could create new conflicts at the WTO, it will allow the United States to dodge current disputes, while assuaging U.S. farmers in the short term. Furthermore, if the Doha Round ever does result in a new agreement on agricultural subsidies, the United States might be able to avoid future conflicts altogether, as the agreement's new limits could obviate the basis for disputes against the "new" U.S. subsidy programs before they have a chance to materialize.

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Japan Eases U.S. Beef Ban After Concluding Meatpacking Facility Inspections

On July 27, 2006, Japan re-opened its market to U.S. beef after inspecting U.S. meatpacking facilities. Japanese officials stated that Japan will now accept shipments of boneless beef from cattle under the age of 20 months. U.S. Secretary of Agriculture Mike Johanns stated that “this has been a long process as we've confirmed that our system is in full compliance with Japan's import requirements and provided Japan with clear, scientific data confirming that American beef is extremely safe.” He added that “it is gratifying to know that these efforts paid-off, as did the patience demonstrated by Congress."

Japan began its ban on U.S beef imports after the December 2003 discovery of a Canadian-born cow found in the United States with bovine spongiform encephalopathy (BSE). Following two years of intense debate with the United States over U.S. beef safety, Japan agreed to allow U.S. and Canadian boneless beef imports from cattle aged 20 months or less on December 12, 2005. In turn, the United States lifted its ban on imports of certain cuts of Japanese beef. Japan again closed its borders to U.S. beef on January 20, 2006 after finding backbone, or vertebral column, in a U.S. veal shipment at a Japanese airport - a violation of the beef trade agreement between the two countries.

Pursuant to a June 21, 2006 agreement with the United States, Japan agreed to resume trade after it inspected 35 U.S. meatpacking facilities, approving 34 of the plants. The final plant may receive approval in the coming months. However, there is no formal agreement between the parties that Japan cannot again halt all beef trade if a noncompliant shipment is discovered, although U.S. officials are confident that Japan would not take such action if an error is made.

Senate Agriculture Committee Chairman Saxby Chambliss (R-GA) expressed hope that Japan will work with the United States to increase the amounts of U.S. beef that Japan would accept. He added that he remains “concerned with the restrictions on cattle over 20 months of age but [is] optimistic that internationally-accepted scientific standards will prevail and lead to a full restoration of beef trade between our nations in the near future.” House Agricultural Committee Chairman Bob Goodlatte (R-VA) stated that the United States has “long encouraged our trading partners to take a science-based approach in their trading policies and I hope that, in the future, the Japanese government will follow the science.” He added that “this is a positive step toward normalizing trade and regaining market access for our producers."

Since Japan reinstated its ban on U.S. beef imports, Members of Congress and U.S. agricultural groups have expressed extreme discontent with Japan and have threatened to impose sanctions against Japan if

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it failed to reopen its borders. U.S. trade officials have pressured Japan to eliminate the ban in an effort to assuage U.S. interests and avoid a bilateral trade war. With Japan's completion of the U.S. meatpacking facility inspections and its resumption of beef trade with the United States, Congressional tempers have died down, leaving Congress to focus on other important trade items.

CIT: Byrd Amendment 'Support Provision' Violates First Amendment

On July 13, 2006, the United States Court of International Trade (CIT) ruled that certain provisions of the Continued Dumping and Subsidy Offset Act (CDSOA, or the "Byrd Amendment") violated the First Amendment of the U.S. Constitution. The case, P.S. Chez Sidney L.L.C. v. International Trade Commission, Ct. Int'l Trade, No. 02-00635 July 13, 2006, emerged out of an attempt by Louisiana seafood producer PS Chez Sidney L.L.C. to receive government payments under the Byrd Amendment to U.S. crawfish producers. The United States International Trade Commission (ITC) found that Chez Sidney declined to support the underlying dumping petition against freshwater crawfish tail meat from China and thus was not entitled to receive Byrd monies. Chez Sidney and Amici challenged the ITC's determination at the CIT, arguing that "the support requirement amounts to compelled speech burdened by unconstitutional conditions, that it involves imposition of a viewpoint-based eligibility requirement for a government subsidy, and that it is an over-broad burden on speech in a limited public forum."

The Byrd Amendment mandates the distribution of antidumping (AD) and countervailing duties (CVD) to the U.S. companies that petitioned for trade relief. The law has come under intense scrutiny both in U.S. courts and at the World Trade Organization (WTO). On April 7, 2006, the CIT ruled that the Byrd Amendment cannot apply to AD/CVD orders on imports from Mexico or Canada because NAFTA Section 408 "demands that preferential treatment be given to goods from Canada and Mexico by exempting such goods from the auspices of any qualifying amendment" of U.S. trade law, unless Congress has "explicitly stated an intent to change the statutory remedies as to Canada and Mexico." U.S. law contains no such statement. In March 2005, the World Trade Organization (WTO) allowed seven WTO Members, including Canada and Mexico, to impose retaliatory duties on U.S. imports based on the United States' failure to comply with a 2003 WTO Appellate Body (AB) decision that the law was inconsistent with global trade rules. On February 8, 2006, President Bush signed the Deficit Reduction Act of 2005, which repeals the Byrd Amendment, but only for entries made on or after October 1, 2007.

In Chez Sidney, the CIT (Judge Evan J. Wallach) noted that "[w]hen speech is burdened by government regulation because of its content, including by the denial of a benefit of a constitutionally protected interest, that regulation is subject to strict scrutiny unless it falls within [certain] exemptions…." As none

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of those exceptions apply to the Byrd Amendment, the Courts must examine the Byrd Amendment's "support provisions" under strict scrutiny, which mandates that, for the law to be constitutional, "the government must show that the burden it imposes is 'necessary to serve a compelling state interest,' and that it is 'narrowly drawn to achieve that end.'" Judge Wallach found that the Byrd Amendment's support provisions "simply cannot meet that standard" because "[t]o the extent that the Government seeks, and is required to seek, accurate information about the level of support for an antidumping or subsidy petition it can, and indeed must, make the inquiry at issue. To the extent, however, that it conditions the payment of benefits to those who answer the inquiry upon the content of their opinion, it may no more do so than it may base the condition upon the color of their skin."

The court continued by noting that Congress could have achieved the same ends – assisting members of domestic industry injured by foreign dumping and subsidies – by a "narrower inquiry," namely "was the questionnaire respondent injured by the imports at issue?" Thus, where the law requires a domestic company to support an AD/CVD petition or else be burdened for opposing it, where it requires the Government to seek the company's "honest opinion," and where a "narrower and more accurate alternative exists, the strict scrutiny test is simply not met." Judge Wallach therefore concluded that "[i]mposition by law of a penalty for failure to support a particular governmental policy, must of necessity derogate from that consent and thus affect the very foundation of legitimacy of government. As to Plaintiff's First Amendment claim, therefore, the CDSOA's support requirement, having failed to meet strict scrutiny, is in violation of the Constitution."

Judge Wallach's decision is another blow to the troubled Byrd Amendment, but the immediate practical implications of the CIT's decision in Chez Sidney are limited because the court reserved ruling on the appropriate remedy. Instead, Judge Wallach provided for an immediate appeal to the Court of Appeals for the Federal Circuit on the substance of the decision. Thus, the practical consequences of the decision will remain undecided until all avenues of appeal are exhausted, including the Supreme Court.

The full text of the decision is available on the CIT's website at:

http://www.cit.uscourts.gov/slip_op/Slip_op06/06-103.pdf

COAC Seeks Appointment Nominees, Holds Open Meeting on Customs Issues

On July 17, 2006, the Bureau of Customs and Border Protection (CBP) published in the Federal Register a request that individuals wishing to serve on the Departmental Advisory Committee on Commercial Operations of Customs and Border Protection and Related Homeland Security Functions (COAC) apply

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for appointment. Interested parties can submit by mail their application consisting of a letter describing their interest and qualifications and an enclosed resume to Ms. Wanda J. Tate, Program Management Specialist, Office of Trade Relations, Customs and Border Protection, 1300 Pennsylvania Ave., NW, Room 4.2A, Washington, DC 20229. Parties may also submit applications by email to traderelations@dhs.gov or by fax to (202) 344-1969. Applications must reach CBP on or before September 15, 2006. COAC provides advice and makes recommendations to the CBP commissioner and the secretaries of homeland security and treasury on all matters involving the commercial operations of CBP.

Separately, COAC announced that it will hold an open meeting on August 3, 2006. Agenda items for the meeting include advance data requirements, CBP's strategic plan, trade enforcement initiatives, the World Customs Organization (WCO) Framework, and the Customs-Trade Partnership Against Terrorism (C-TPAT). The meeting will occur from 9 a.m. to 1 p.m. in the Horizon Ballroom of the Ronald Reagan Building, 1300 Pennsylvania Ave. N.W., Washington, D.C.

Sens. Grassley and Baucus Introduce Customs and Trade Facilitation Bill

On July 13, 2006, Senate Finance Committee Chairman Sen. Charles Grassley (R-IA) and Ranking Committee Member Sen. Max Baucus (D-MT) introduced legislation to "empower United States trade agencies to work with federal, state and local officials, U.S. and foreign ports, private sector stakeholders and foreign governments to ensure safe and efficient international trade." According to the Senators, the Customs and Trade Facilitation Reauthorization Act of 2006 (S. 3658) will add personnel at all U.S. ports and will "restore vital resources for trade facilitation and enforcement at the Bureau of Customs and Border Protection (CBP) and the Bureau of Immigration and Customs Enforcement (ICE)." The legislation would also require CBP to formulate a plan for "the swift resumption of trade in the event of a transportation disruption that could harm the U.S. economy." The legislation has been referred to the Senate Finance Committee for consideration.

In introducing the legislation, Sen. Grassley highlighted the balance in customs and trade facilitation between economic growth and national security. He stated that the United States must "find the right balance to ensure that the dual demands of facilitating the efficient flow of international trade and securing our borders is each fully met [and] this bill achieves the right balance." Sen. Baucus added that "it is absolutely possible, and essential, to make trade both secure and efficient," and that "we need the

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smart solutions in this bill to ensure both the safety and the smooth flow of the international trade on which our economy depends."

The Customs and Trade Facilitation Reauthorization Act would require, within one year, an assessment of non-intrusive container scanning in foreign ports and would add personnel for all U.S. ports of entry. It also would require "enhanced cargo targeting and analysis to facilitate trade and restart the movement of cargo following a transportation disruption" and mandate that the Commissioner of Customs "develop a trade resumption plan, which must be routinely exercised with federal, state, local officials and private stakeholders." At an international level, the legislation authorizes the negotiation of bilateral customs partnerships with foreign governments to facilitate safer U.S.-bound trade and authorizes a Customs Industry Partnership Program (including the Customs-Trade Partnership Against Terrorism, or C-TPAT), as well as multilateral negotiations in the World Customs Organization (WCO) and the World Trade Organization (WTO), to facilitate safer trade. The legislation also requires a "one-portal" government-wide system to collect mandatory import and export clearance documentation and would add Treasury Department personnel for "oversight of delegated customs functions carried out by the Bureau of U.S. Customs and Border Protection." In addition, the legislation creates a new CBP Intellectual Property Rights Division.

The timetable for congressional consideration of S. 3658 is unclear. With the support of both Sen. Grassley and Sen. Baucus, the bill should have no problem moving through the Senate Finance Committee. However, given the looming summer and mid-term elections recesses in both the House and Senate, whether the bodies will have enough time to consider and to pass the measure is another story.

The legislation's full text is available from the U.S. Government Printing Office (GPO) at: http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_cong_bills&docid=f:s3658is.txt.pdf

Senate Finance Committee Requests Written Comments on Miscellaneous Tariff Measures

On July 11, 2006, Senate Finance Committee Chairman Sen. Charles Grassley (R-IO) and ranking member Sen. Max Baucus (D-MT) requested that interested parties submit written comments on miscellaneous tariff measures introduced in the Senate during the 109th Congress for possible inclusion in a Senate Miscellaneous Tariff Bill (MTB). A list of the Senate bills under consideration is available on the Committee's website at: http://www.finance.senate.gov/sitepages/2006MTB.htm.

Interested parties wishing to comment on any of these measures can submit single-spaced statements not exceeding 10 pages by e-mail to mtb2006@finance-rep.senate.gov in Microsoft Word format. E-mail

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subject lines should include the Senate bill number and the topic at issue. Interested parties can also send written comments by mail to the Senate Finance Committee, 219 Dirksen Senate Office Building, Washington, D.C., 20510, attention "MTB." Parties should notify Claudia Bridgeford at 202-224-4515 that comments have been mailed. Statements should include the Senate bill number and the topic at issue, as well as the name, company, address, phone number, fax, and e-mail address of the sender. Interested parties should submit their comments no later than August 15, 2006.

OEE Seeks Passage of EAA and Further Compliance of U.S. Export Control Regime

On June 29, 2006, Women in International Trade (WIIT) hosted an event on “Export Controls Enforcement” with Wendy Wysong, Deputy Assistant Secretary of Commerce for Export Enforcement at the U.S. Department of Commerce (DOC) Bureau of Industry and Security (BIS). Wysong offered a brief overview of the U.S. export controls regime and offered her views on three recent DOC enforcement decisions against those violating U.S. export controls:

- Deemed Export Advisory Committee. On May 22, 2006, BIS announced the creation of an Advisory Committee that will review deemed export requirements and provide recommendations to the Department of Commerce (DOC) on them. The Committee’s main goal is to maintain national security while permitting businesses and researchers to employ foreign nationals who play a key role in their operations. Wysong stressed that the Administration “will continue to pay close attention to deemed export controls” in the near future to ensure that deemed export licensing policies protect national security, while preserving the United States’ leading role in technological innovation.
- Revisions and Clarification of Export and Reexport Controls for China. On July 6, 2006, DOC published in the Federal Register (FR) a proposed rule that would loosen controls on certain high-technology exports and tighten restrictions on certain defense-related exports to China. Under the proposed rule, a total of 47 categories of high-technology products will be subject to new export controls. Validated end-users would have to meet several criteria including “a demonstrated record of engaging only in civil end-use activities and not contributing to the proliferation of weapons of mass destruction or otherwise engaged in activity contrary to U.S. national security or foreign policy interests.” DOC and other government agencies such as the State Department would have to approve the list of validated end-users. Under the proposed rule, exporters would also be required to obtain an end-user certificate issued by China's Ministry of Commerce for all items that require an export license to China and exceed a total value of $5000. The rule would also establish an

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"authorization" for validated end-users to facilitate legitimate exports to certain civilian destinations in China, thereby eliminating the need for U.S. companies to obtain individual export licenses. Wysong stated that although China is an important trading partner for the United States, the Administration is concerned about the "strategic intentions" of its defense and military programs. The proposed rule would therefore target certain technologies that could potentially strengthen China's military capabilities.

- Antiboycott Penalty Guidelines. On June 30, 2006, BIS published in the FR a proposed rule that "would set forth BIS policy concerning voluntary self disclosures of violations of part 760 (Restrictive Trade Practices or Boycotts) of the Export Administration Regulations (EAR) and violations of part 762 (Recordkeeping) of the EAR that relate to part 760." The proposed rule would also "set forth the factors that BIS considers when deciding whether to pursue administrative charges or settle allegations of such violations as well as the factors that BIS considers when deciding what level of penalty to seek in administrative cases."

Wysong concluded her remarks by stating BIS' "next steps": (i) enhanced penalties for violators of U.S. export controls laws; (ii) passage of the Export Administration Act (EAA); and (iii) further guidance on effective export compliance programs.

President Bush Nominates New Asst. Secretary for Commerce

On July 13, 2006, President Bush announced that he would nominate Christopher Padilla to be Assistant Secretary of Commerce (Export Administration). Padilla currently serves as Chief of Staff to Deputy Secretary of State Robert Zoellick. Prior to this position, he served as Assistant United States Trade Representative (AUSTR) for Intergovernmental Affairs and Public Liaison. Padilla received his bachelor's and master's degrees from Johns Hopkins University.

As Assistant Secretary of Commerce (Export Administration), Padilla will serve as the Department of Commerce's principal officer for carrying out the policies and programs necessary to administer the Export Administration Act, the Export Administration Regulations and other measures regarding the control of U.S. exports, anti-boycott compliance, fastener quality, foreign technical assistance, industrial base, U.S. and foreign defense conversion activities, and the coordination of interagency activities related to critical infrastructure protection.

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DOC Proposes Rule to Tighten Defense-Related Exports to China, Loosen Controls on High-Technology Exports; Negative Reaction by U.S. Industry

On July 6, 2006, the U.S. Department of Commerce (DOC) published in the Federal Register (FR) a proposed rule that would loosen controls on certain high-technology exports and tighten restrictions on certain defense-related exports to China. David McCormick, Undersecretary of Commerce for Industry and Security stated that the "proposed rule achieves two important and complementary objectives: supporting American companies in competing in the vast Chinese market for civilian technology, while preventing the export of technologies that contribute to China's military modernization." According to the FR notice that DOC's Bureau of Industry and Security (BIS) issued, the proposed rule will be open to public comment for a period of 120 days, or until November 3.

Under the proposed rule, a total of 47 categories of high-technology products, from machine tools and computers to telecommunications test equipment and navigational equipment, will be subject to new export controls. The rule would also establish an "authorization" for validated end-users to facilitate legitimate exports to certain civilian destinations in China that would eliminate the need for U.S. companies to obtain individual export licenses. Validated end-users would have to meet several criteria including "a demonstrated record of engaging only in civil end-use activities and not contributing to the proliferation of weapons of mass destruction or otherwise engaged in activity contrary to U.S. national security or foreign policy interests." DOC and other government agencies such as the State Department will have to approve the list of validated end-users.

Under the proposed rule, exporters will also be required to obtain an end-user certificate issued by China's Ministry of Commerce for all items that require an export license to China and that exceed a total value of $5000. The new end-user certificate will replace the current end-user certificate which applies only to items controlled for national security purposes. The rule would also eliminate the current requirement that exporters submit the end-user certificate to BIS with their license application but would require that exporters retain end-user certificates for five years. An end-user certificate would continue to be required for all computer exports. DOC officials stated that the proposed expansion of the end-user certificate requirement would facilitate BIS' ability to conduct end-use checks on exports and re-exports of controlled goods and technologies to ensure that recipients use them for civilian and not military purposes.

DOC's McCormick asserted that the new rule will not be a "catch-all" regulation "that subjects everything from fountain pens to office furniture to government scrutiny." He added that "these changes carefully

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target certain technologies that, while unrestricted until now, have the potential to materially enhance China's military capabilities," and that "this approach is prudent and fully consistent with America's long-standing embargo of military sales to China . . . by denying only those exports destined for military use, the impact on industry will be lessened."

The proposed rule on high-technology exports to China has received negative responses from U.S. industry representatives who expressed their concerns at a July 17 DOC public hearing on the rule. DOC's Bureau of Industry and Security (BIS) held the hearing "to provide an opportunity for U.S. government officials to answer questions from companies, organizations, and individuals that have an interest in understanding the proposal."

William A. Reinsch, president of the National Foreign Trade Council (NFTC) stated that an industry coalition on export controls, created under the auspices of the NFTC and the Coalition for Employment through Exports (CEE), will formalize its response to the new rule in comments to the DOC over the next few weeks. Reinsch singled out as "unfair" the provision requiring companies to apply for a license to export any of the 47 categories of products to China if they "know" that the product might be used for military purposes. Reinsch added that DOC's definition of "know… is so broad that exporters could find themselves misreading the intent of the importer in China" and face fines and possible imprisonment for misleading the licensing authorities. Reinsch stated that the rule thus frightens many U.S. companies. Reinsch also opined that the proposed rule will likely be ineffective in deterring China's use of the listed technologies because the United States will apply the rule unilaterally, and "we don't see any major exporting nation that's going to do the same thing." He added that DOC likely developed the proposed rule "on autopilot without a lot of intercession by senior government people [or] the regulatory folks at the State, Defense, and Commerce [Departments]."

USTR Susan Schwab's Briefing to ABCDoha on U.S. Trade Agenda

On July 7, 2006, United States Trade Representative (USTR) Susan Schwab provided a briefing to the American Business Coalition for Doha (ABCDoha) on the U.S. trade agenda and discussed the current state of the World Trade Organization's (WTO) Doha Round as well as U.S. Free Trade Agreements (FTAs). Schwab also responded to questions posed by the media. Please find below ABCDoha's summary of Schwab's briefing

Briefing by USTR Susan Schwab to ABCDoha

USTR Schwab: The United States has an ambitious trade agenda on several fronts. Aside from the Doha Round, the US-Peru bilateral free trade agreement (FTA) will be presented before Congress soon,

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as will an agreement with Oman and a vote on granting Vietnam Permanent Normal Trade Relations (PNTR) status. Doha is the most ambitious and important multilateral free trade effort in a decade. Its importance reaches all sectors of the economy, including service providers, manufacturing and farming. For United States businesses, it holds the promise of being able to reach the other 95% of the world population.

Topic: What did the United States learn from the ministerial meeting at Geneva?

ABCDoha writes that the energy that comes with knowing of an imminent breakthrough is lacking. The United States came prepared to negotiate, but it did not appear that all of its trade partners did. Perhaps they thought that the United States would be willing to give up more and get less in return – but this is not possible. Until some terms are defined, especially what “sensitive products” and “special safeguard mechanisms” are, the United States won’t know what actual results will come from the proposed agricultural tariff cuts. Right now, market access is a black box with too many loopholes, and the United States cannot evaluate what is on the table. One example is the latest European Union offer, which it claims improves upon its 2005 offer. However, the new offer is vague and riddled with loopholes. An Australian analysis of the EU offer shows that their 54% average tariff cut will actually only be a 40% average cut because of these loopholes. Some advanced developing countries are now questioning the value of open markets to development. Most developing nations are still very much interested in a robust Doha Round, but a few powerhouses such as China, India and Brazil are hiding behind the poorest nations, while they should be opening their markets to other developing countries. Seventy percent of tariffs paid by developing countries are to other developing countries, and Doha should promote more South-South trade, not just North-South trade.

Topic: United States Goals and Commitments at Geneva

ABCDoha writes that the goal of the United States at Geneva was to boost its allies. The United States cannot be expected to negotiate with itself. It has expressed flexibility in modifying its domestic support for agriculture, but it seemed like the other trading partners did not truly hear this willingness or were unwilling to acknowledge that the United States can only be flexible if its get something in return. At Geneva, the ministers resolved to ask Director General Pascal Lamy to engage in shuttle diplomacy and act as a catalyst for further discussions. The United States will not give up during this process, but it expects its trade partners to step up. It wants to deliver on the Doha promises of 2001 and 2004 to spur growth and development. Hopefully the United States is not being too ambitious. It does not wish to

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define success downward, but rather to raise everyone's gain. Real proposals are needed that will eliminate the black box.

To gain support in a democracy, a trade agreement needs to provide large enough gains for a large enough group so that a coalition can come together in order to offset those groups that will always oppose the agreement. But a comprehensive and ambitious agreement is also a good goal on the merits, as it will bring major improvements in market access. The United States acknowledges that the poorest countries need flexibility to meet goals in any trade agreement. In Hong Kong, the United States made a commitment to help these countries with capacity building and will double aid for trade from $1.3 to 2.7 billion by 2010. Ambassador Schwab is sure that this goal will be met since former USTR Rob Portman is now in charge of the Office of Management and Budget (OMB).

The non-agricultural sector is still important, but the key to these negotiations is agriculture. The United States believes in the Swiss formula that will cut highest tariffs most. It is the best plan for both developed and developing countries, and the United States expects advanced developing countries also to participate in this plan. The United States also wants to see more services market access. This will benefit both developing and developed nations' economies. Unilateral services liberalization can only help developing countries, because these nations will gain by having more advanced finance and infrastructure sectors that can grow their export potential and promote indigenous entrepreneurship. The United States is still committed to see the Doha Round through and see an agreement in 2006. It is also committed to its bilateral agreements. In fact, the United States' best allies at Doha are its FTA partners.

Questions from the Media

Question: Is the near-term fate of Doha in the hands of Director-General Lamy?

ABCDoha writes that Schwab stated the future of Doha is in the hands of all participants. Lamy is serving as a facilitator and a catalyst, testing commitment and trying to encourage discussion. But he will not be making the agreement. Right now, there are no plans for a G6 meeting, nor for a "Green Room" meeting or another meeting of all members of the Doha Round. But Ambassador Schwab would not be surprised if the ministers end up in Geneva again around the end of July. At the G8 meeting in St. Petersburg, the leaders will have a session on trade. Furthermore, there will be an outreach meeting at the G8 with President Lula of Brazil and Prime Minster Singh of India, and this will likely include a discussion on trade.

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Question: What is your assessment of Russia's accession to the WTO? Do you foresee any main sticking points?

Both Presidents Putin and Bush are on record hoping to work out a bilateral WTO accession agreement, hopefully before the G8 meeting or soon thereafter. Accession to the WTO is good for Russia, not a gift it is giving to other countries. Schwab declined to comment on any sticking points.

Question: What should be expected from the G8 leaders? What do you think of Japan's position?

Schwab will not predict what the G8 leaders might do. The Japanese sticking point is in increasing access to their market. For example, they have a 750% tariff on rice. In comparison, the average global tariff is 62%, and even this is enough to block trade. The U.S. average tariff is 12%, and in the EU it is twice that. Japan will greatly benefit from an open system, and they need to make contributions that are commensurate to the benefits they will receive.

Question: If it is so obvious that everyone will benefit from an ambitious Doha agreement, why do some disagree?

Real trade agreements with real results are tough to negotiate. The United States must show leadership and promote ambitious goals. It does not question the motives of its trading partners, but the United States started the Doha Round in 2001 and helped resuscitate it in 2005. It therefore seems strange that it is taking international blame for the impasses of 2006. It is not the United States' ambition to have a small agreement result from Doha. It is committed to the idea that a small package is only acceptable if one does not need to give up anything.

Question: Was the lack of energy at Geneva a sign that others don't want an ambitious deal, especially within the framework of the Trade Promotion Authority, which will expire next summer?

There is a difference between public rhetoric and what is said in small meetings and private conversations. Often more amenable positions are shared in private. There is enough potential there to see a deal. But some countries just want the whole thing to go away – they know who they are. Developing countries have the most to gain from Doha, and the most to lose if it fails. These countries recognize this and are still very interested in reaching a deal. The United States is running out of time on the Trade Promotion Authority. It is possible that there will be an extension of the TPA, but Schwab wouldn't bet the Round on it. Maybe all the ministers needed to get to a precipice to see the possibility that it might fail before they could begin to move forward again.

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Question: What have the discussions been like on the textile industry?

Most of the NAMA conversation at Geneva focused on manufactured goods and did not reach textiles or apparel. Discussions on textiles have been a bit schizophrenic in the past. Some countries want to see the textile market opened up but are also afraid of competition from China. It has been hard to see a consensus form on textiles.

Question: What is the update on Latin America? Peru? Colombia? ATPA?

Schwab is pleased that four of the six Central American countries entered CAFTA on July 1st. The Peru FTA is ready to move in Congress – it is now up to the Congressional leadership to launch the process. There are hearings at the Senate Finance Committee and House Ways and Means Committee coming up for the Peru FTA. Negotiators are still ironing out some technical details with the Colombia FTA, but this process is moving forward. The Vietnam WTO accession agreement will need to have a PNTR vote get through Congress. The Andean Trade Preference Act (ATPA) will expire at the end of this year along with the General System of Preferences. The USTR office will have conversations about these with the Congressional leadership on next steps.

Question: What is the chance of getting a Russia-US WTO agreement before the G8? Considering Russia's activity in the oil sector and jailing businessmen, should they be in the WTO?

A good USTR does not handicap trade agreements, so Schwab will not speculate on the timing of an agreement. Russia's best interest is to become integrated into the world economy, and this cannot happen without joining a system of rules. It is in Russia's best interest to protect intellectual property, especially in the interest of their own entrepreneurs and creative class. There have been real improvements in the protection of intellectual property in Russia, which have been good for Russia's own economy. Agricultural issues still remain to be resolved, but it is normal for any trade agreement to get hung up on agricultural issues.

Question: There is a general feeling that U.S./Brazil relations are blocking international trade agreements. Brazil appears to be a culprit in the failures of Doha and the FTAA. What is the updated message to Brazil from the United States to get them to come into alignment on trade issues?

Schwab disagrees with the premise of the question. There are not serious problems between United States and Brazil. Rather, they have a healthy relationship in Doha. President Lula and Bush have

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spoken about the importance of Doha. The two countries may disagree on how to get to an agreement, as they represent their own business interests, but both countries want to see a successful Doha Round.

Question: Is a powerful signal from the G8 meeting in St. Petersburg necessary for the future of Doha?

It is hard to argue with a powerful signal from G8 leaders. But the negotiators have a lot of work ahead getting details worked out. Once a political convergence takes place, there will still be a daunting task of working through the details of the consensus. So there is a huge task at hand for the leaders and for everyone else. Work from both ends will be needed.

"Patriot Corporations" Act Would Grant Preferential Federal Contracting, Tax Preferences to Certain Firms

On June 28, 2006, Rep. Janice Schakowsky (D-Ill.) introduced a House bill that would provide federal contracting preferences and a five percent income tax reduction to "patriot corporations." Under the "Patriot Corporations of America Act of 2006" (H.R. 5699), the Secretary of the Treasury would certify as a "patriot corporation" any firm that during the taxable year:

- Produces domestically at least 90 percent of goods and services sold;
- Conducts domestically at least 50 percent (on a cost basis) of research and development;
- Pays at least 70 percent of employee standardized health insurance plan costs;
- Pays at least five percent of employee wages to a portable pension fund;
- Limits management compensation to a maximum of 10,000 percent of the corporation's lowest-paid full-time employee;
- Maintains neutrality in employee organizing drives; and
- Complies with Federal environmental, labor relations, workplace safety, consumer protection or other regulations specified by the Treasury Secretary.

The proposed legislation also includes two sections that would amend the U.S. Internal Revenue Code of 1986 to pay for the legislation's cost, which according to Schakowsky could reach $70 billion annually. Section 3 of the bill would revise Internal Revenue Code Section 7701(a) to treat as a domestic corporation "any corporation which would be treated as a foreign corporation… principally for the purpose of avoiding being treated as a domestic corporation." Section 4 of the bill would add to Section 1 of the Code a provision reducing the tax rate reduction benefit for families with incomes over $1,000,000.

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Section 3 would apply to taxable years beginning after December 31, 2007 and Section 4 to taxable years beginning after December 31, 2006.

The bill presently enjoys partisan support: its co-sponsors include Reps. Sherrod Brown (D-Ohio), John Conyers (D-Mich.), Peter DeFazio (D-Ore.), Tom Lantos (D-Calif.), Barbara Lee (D-Calif.), David Obey (D-Wis.), Major Owens (D-N.Y.), Hilda Solis (D-Calif.), and Lynn Woolsey (D-Calif.).

The legislation does not describe how the U.S. government would apply preferential treatment to "patriot corporations" when evaluating government procurement bids or proposals. Nevertheless, the legislation, if passed, would likely be inconsistent with the United States' obligations as a signatory to the World Trade Organization's (WTO) Government Procurement Agreement (GPA), which prohibits signatories from discriminating against other signatories' products or suppliers when making government contracting decisions covered by the agreement. However, because the GPA is a plurilateral agreement, the United States' obligations under the agreement are limited to other GPA signatories. The legislation's tax provisions will likely cause further objection among congressional Members. These reasons, coupled with the already-busy congressional schedule and mid-term elections, make it unlikely that the Congress will pass the legislation.

USTR Announces Results of 2005 Annual GSP Review

On June 30, 2006, the Bush Administration announced that Brazil, Kazakhstan, Pakistan and Swaziland will remain eligible for the United States' Generalized System of Preferences (GSP) program that provides duty-free treatment to 5000 products imported from 136 developing countries. The Office of the United States Trade Representative (USTR) stated that the eligibility determinations were part of the 2005 GSP annual review, under which USTR receives petitions from "interested parties" seeking to remove countries from the GSP program based on "their alleged failure to meet statutory criteria for GSP eligibility." USTR defines an interested party as any "party who has significant economic interest in the subject matter of the request, or any other party representing a significant economic interest that would be materially affected by the action requested, such as a domestic producer of a like or directly competitive article, a commercial importer or retailer of an article which is eligible for the GSP or for which such eligibility is requested, or a foreign government." Statutory criteria include protecting internationally recognized labor rights, protecting intellectual property rights (IPR), and providing preferential tariff treatment to imports from other developed countries which causes or is likely to cause a "significant adverse effect" on U.S. commerce. USTR stated that after examining workers' rights in Swaziland and

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IPR protection in Pakistan, Kazakhstan and Brazil, "the administration determined to continue each country's GSP eligibility" because of the steps each took in addressing U.S. concerns.

USTR also noted that several petitions remain under review including workers' rights in Uganda, IPR protection and enforcement in Lebanon and Uzbekistan, and Bulgaria's and Romania's tariff treatment to developing countries. In the 2005 review, USTR also determined that certain imports from specific developing countries can "compete effectively" with imports from non-GSP eligible countries and therefore are no longer eligible for GSP duty-free treatment. (Under GSP criteria, if a certain product from a developing country exceeds $120 million in imports in 2005 or accounts for more than 50 percent of total imports of that product, then it has reached its "competitive need limits" and thus becomes ineligible for duty-free treatment under the GSP program.) USTR determined that products such as crabmeat from Venezuela, copper wire from Turkey, and aluminum alloy plates from Russia have reached their "competitive needs limit."

A complete list of product determinations under the GSP Review is available at:

http://www.ustr.gov/assets/Trade_Development/Preference_Programs/GSP/asset_upload_file909_9601.pdf

U.S. and Canada Sign Lumber Agreement, Builds on April 27 Version

On July 1, 2006, United States Trade Representative (USTR) Susan Schwab and Canadian International Trade Minister David Emerson initialed the final text of an agreement that would end the U.S.-Canada softwood lumber dispute. The officials signed the agreement during the World Trade Organization's (WTO) trade ministerial negotiations in Geneva. Sources from both sides note that both governments sought to sign the agreement before Canadian Prime Minister Stephen Harper's July 6 meeting with President Bush in Washington, DC – Harper's first Washington visit as Canada's new PM. Upon signing the agreement, USTR Schwab stated that "the resolution of this long standing dispute with our largest trading partner is another achievement for the President's broad trade agenda."

According to USTR officials, the final agreement builds upon the framework deal announced April 27 and includes new details developed during "intense" bilateral negotiations over the past few weeks. On April 27, 2006, U.S. and Canadian officials announced that both sides had negotiated a seven-year, renewable "framework agreement" to end the latest incarnation of the bilateral dispute over trade in softwood lumber. The framework agreement contemplates that the United States would revoke the current countervailing duty (CVD) and antidumping (AD) orders and stop collecting duties. All parties to related litigation must agree to terminate their cases. The framework also proposes that the United States will return

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approximately $4 billion of the nearly $5 billion in duties that have been collected from Canadian exporters since the 2002 imposition of AD/CVDs on Canadian lumber imports. Half of the remaining $1 billion would go to members of the Coalition of Fair Lumber Imports – the domestic industry group which originally petitioned for trade relief – with the remainder to "meritorious initiatives in the North American lumber market and the United States as identified by the U.S. government in consultation with Canada." The proposed agreement would be for a term of seven years and may be renewed for two more years.

The framework agreement proposes an export measure, a third-country trigger and a surge mechanism. Canadian regions (the British Columbia (BC) interior, the BC Coast and each of the provinces east of BC) must decide between one of two options for applying the export measure: (i) a lumber export charge based on a composite lumber price from the trade periodical Random Lengths; or (ii) a lower export charge plus a volume restraint. The following table details the two options:

Price	Option A –Export Charge (%)	Option B – Export Charge plus Volume Restraint*
Over US$355	0	0
US$336-355	5	2.5% + regional share of 34% of U.S. Consumption
US$316-335	10	3% + regional share of 32% of U.S. Consumption
US$315 or under	15	5% + regional share of 30% of U.S. Consumption

Under the third-country trigger, Canada will refund any export charges paid in any two consecutive quarters if three conditions existed during those quarters: (i) the third country share of U.S. lumber consumption increased by 20 percent over the same quarter in the previous year (in two consecutive quarters); (ii) Canadian market share decreased in the same two quarters; and (iii) U.S. domestic producers' market share decreased in the same two quarters. The export measure will not apply to any region that has triggered the surge mechanism, which occurs when a region's exports exceed 110 percent of its allocated share in any one period. If a region's exports are between the trigger volume and the trigger volume plus 1 percent, then the trigger volume is reduced by the average in the next period. If a region exports more than the trigger volume plus 1 percent in any one period, then the region will pay 150 percent of the normal export charge for that period.

Although the signing means that the agreement's text is final, the agreement cannot take effect until the Canadian government ratifies it and Canadian producers accounting for 95 percent of total cash deposit

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refunds agree to drop ongoing litigation. The agreement does not require congressional ratification in the United States. Canadian officials hope that Canada's Parliament will consider the agreement as soon as possible, so it can be implemented by October 1, 2006. Canadian sources indicate that the government immediately will begin drafting legislation and a necessary Ways and Means motion in order to introduce them when Parliament reconvenes in September. Parliamentary passage, however, is not guaranteed, as the agreement faces opposition in Canada from softwood producers, especially in British Columbia and Ontario. Their opposition might cause members of Parliament representing these districts to vote against ratifying the agreement. Moreover, even if Parliament does ratify the agreement, these Canadian producers have warned that the deal contains provisions that would keep them from providing the requisite industry support for the agreement to take effect.

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Free Trade Agreements

House Ways and Means Committee Holds Hearing on U.S.-Peru FTA

Summary

On July 12, 2006, the House Ways and Means Committee held a hearing on the U.S.-Peru Free Trade Agreement (FTA), the "Peru Trade Promotion Agreement" (PTPA). The hearing included **on-the-record** oral testimony from government and business representatives. We review below this testimony and the discussion between the Committee and witnesses.

The full text of the witnesses' statements is available on the Committee website at: http://waysandmeans.house.gov/hearings.asp?formmode=detail&hearing=491

Analysis

On July 12, 2006, the House Ways and Means Committee held a hearing on the PTPA. The hearing included **on-the-record** oral testimony from government and business representatives. We review here the most relevant oral testimonies.

- **Everett Eissenstat, Assistant United States Trade Representative (AUSTR) for the Americas,** stated that the PTPA "sets out fair and reciprocal trade rules, which will promote economic growth and prosperity to both countries." According to Eissenstat, the PTPA will eliminate unfair barriers to U.S. exporters and "opens a market of 28 million consumers to U.S. manufacturers, farmers, ranchers, and service providers." Eissenstat forecasts that Texas, Florida, California, Louisiana, and Illinois will benefit the most from the PTPA. Eissenstat added that the PTPA "makes permanent the trade benefits Congress first authorized for Peru in 1991 under the Andean Trade Preference Act," which in turn helps "create favorable conditions and incentives in creating sustained real growth characterized by more jobs and investment in Peru." He stated that the political and economic benefits of the PTPA for the United States are "significant" and that the agreement "makes trade between us a two-way street."

  Eisenstatt noted that "on day one of the Agreement, 80 percent of U.S. industrial products will be able to enter Peru duty-free, [and] within five years, an additional six percent of [U.S.] industrial products will become duty-free and another four percent within seven while duties on the remaining 10 percent will be phased-out over ten years." On agriculture, he stated that the agreement "lowers tariffs and assures that [U.S.] exporters will not face higher tariffs in the future": almost 90 percent of [U.S.]

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current agricultural trade with Peru will enter the Peruvian market duty-free on day one of the agreement, and Peru will immediately eliminate its price band system on trade with the United States. According to Eissenstat, Peru will gradually eliminate tariffs on other agriculture products, most within five to fifteen years, and all within 17 years. He also stated that the agreement eliminates non-tariff barriers (NTBs) that "currently limit U.S. products and services from competing in Peru's market," and that the PTPA "will also provide important new opportunities for U.S. companies in Peru across a wide range of services sectors, including telecommunications, banking, insurance, audio-visual services, transportation, engineering, computer and related services and express delivery services."

On labor, Eissenstat stressed that Peru has undertaken significant labor reforms in the past several years and is committed to implement additional reforms in an effort to address U.S. concerns. He noted that "Peru has ratified all eight core conventions of the International Labor Organization (ILO) and Peru's Constitution guarantees freedom of association, collective bargaining, and the right to strike." According to Eissenstat. the PTPA "includes a variety of tools that will help ensure that workers in Peru benefit from these reforms," and the agreement will require Peru to effectively enforce its labor laws. Should Peru fail to do so, "the United States can invoke the Agreement's consultation and dispute settlement procedures, which could ultimately lead to the imposition of an annual monetary assessment of up to $15 million." Eissenstat concluded that the PTPA also "calls for Peru to provide fair, equitable and transparent domestic legal procedures through which persons can seek enforcement of Peru's labor laws."

- On behalf of the U.S. Chamber of Commerce and the U.S. Peru Trade Coalition, **Richard Norman, Vice President of Human Resources at Coats North America,** stated that the PTPA "is a critical step in U.S. efforts to promote sustainable economic growth in the Western Hemisphere through trade rather than aid." He noted that the agreement will improve market access for U.S. agricultural and industrial products and services to Peru. He stressed that the PTPA "offers critical support and stronger ties to a close ally in the Andes, a region where political and economic instability poses a threat to the U.S. and regional security." Norman called on the U.S. Congress to support the PTPA to prevent losing access to the Peruvian market, given that extension of the Andean Trade Preference and Drug Eradication Act (ATPDEA) is uncertain.
- On behalf of the Association of American Chambers of Commerce in Latin America and the American Chamber of Commerce of Peru**, Francisco X. Santeiro** endorsed both the Peruvian and Colombian FTAs. He stated that the PTPA and the recently concluded U.S.-Colombia FTA "will foster growth, development, enhance the rule of law, and lend support to a close ally." He praised the PTPA's

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success in fostering U.S.-Peru bilateral trade, which reached US$7.4 billion in 2005 and provided tens of thousands of U.S. jobs. Santeiro said that the PTPA is an "outstanding agreement" for the express delivery services industry because the chapters on customs administration and trade facilitation will allow Peru to move towards "greater automation and efficient use of information technology in its customs procedures."

- **Brett Gibson, Legislative Representative, American Federation of Labor and Congress of Industrial Organizations (AFL-CIO)** opined that the Peru FTA "provides precisely the wrong answers to the challenges faced in Peru and the United States," and that the agreement is "based on a failed model that neither addresses the problems confronted by workers in Peru, nor contributes to the creation of good jobs and decent wages" in the United States. According to Gibson, contentious labor issues remain in Peru, including: (i) workers' rights provisions that are "entirely inadequate to ensure that workers' fundamental human rights are respected"; (ii) a dispute settlement mechanism for workers' rights and environmental protections that is "far weaker than that available for commercial provisions"; (iii) "flawed provisions on services, investment, government procurement, and intellectual property rights will undermine the ability of both governments to protect public health, strong communities, and the environment"; and (iv) labor laws "that still do not comply with ILO core labor standards" and are not respected in practice. Gibson noted that, in addition to these problems, the AFL-CIO is concerned with Peru's labor laws because "they do not comply with core ILO labor standards and existing laws and not respected in practice."

Outlook

With the Peruvian Congress' approval of the PTPA in June 2006, the U.S. Congress has a powerful incentive to consider the Peruvian FTA in a relatively short timeframe because it will be more difficult to do so after the August recess when the focus will be on the November 2006 elections. However, leading House Democrats remain concerned over the FTA's alleged lack of labor protections; their protests, could delay consideration of the Agreement. At the PTPA hearing, Ways and Means Committee Democrats criticized the Agreement labor's provisions. Trade Subcommittee Chairman Clay Shaw (R-FL) noted that the Peruvian agreement "was more than just about trade," arguing that "it would be tragic" for the United States to implement the FTA. Trade Subcommittee ranking member Ben Cardin (D-MD) stated that "the status quo [of the Peruvian FTA was] unacceptable" because the Peruvian laws allegedly fail to comply with ILO standards, allowing employers to subcontract temporary employees and failing to sanction those that interfere with union activities. Representative Sander Levin (D-MI) criticized the Administration because "it [has] failed to create a bipartisan foundation for trade."

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In recent weeks, House Ways and Means Committee Chairman Bill Thomas (R-CA) and Senate Finance Committee Chairman Charles Grassley (R-IA) have given indications that ATPDEA preferences may not be renewed.

On July 11, 2006, Peruvian President Alejandro Toledo met with President George Bush to lobby U.S. lawmakers to ratify the agreement with Peru. President Toledo called on the U.S. Congress to approve the agreement as quickly as possible and asked President Bush that the Agreement "does not suffer from partisan politics." The timing of congressional consideration of the U.S.- Peru FTA remains unclear. USTR officials stated on July 11, that consideration of the Peruvian FTA remains "an open question" but hinted that the House Ways and Means and Senate Finance Committees could act on the Agreement before the August recess. However, House Majority Leader John Boehner (R-OH) has refused to comment on the possible timeframe for the vote of the Peruvian FTA. If the House and Senate votes on the agreement were to be delayed until after the November elections, Peruvian officials are likely to become concerned because Peru will lose the duty-free benefits of the ATPDEA, which expires on December 31, 2006.

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U.S. and Korean Negotiators End Second Round of FTA Talks A Day Early

Summary

On July 14, 2006, U.S. and Korean negotiators ended a day early the second round of five-day talks on the U.S.-Korea (KORUS) Free Trade Agreement (FTA) in Seoul. South Korea ended the final day of negotiations after the U.S. delegation suspended working group meetings on trade remedies and services, two areas that Korea has prioritized. The United States suspended the meetings after Korea informed the U.S. delegation that it intended to implement without further discussion a "positive list" reimbursement system for pharmaceutical products. The United States argues that this system would discriminate against U.S. and other foreign pharmaceutical firms that wish to sell their products in the Korean market. Despite the impasse over pharmaceuticals, negotiators made some progress in agriculture, automobiles, tariff elimination for industrial goods, and services and investments. The parties plan to meet in the United States September 4-8 for a third round of talks but have not yet designated a city.

Analysis

The United States and Korea on July 14 concluded the second round of FTA negotiations in Seoul. The talks, scheduled for five days, ended a day early due to disagreements over Korea's pharmaceutical policies. As with the first round of talks, the parties divided the negotiations into 17 working groups and two "special working groups" on automobiles and pharmaceuticals. The talks yielded mixed results in agriculture and automobiles, with negotiators agreeing on some issues but leaving others for future rounds. Both sides agreed on tariff elimination schedules for industrial goods and plan to exchange initial offers on agriculture and textile tariff elimination schedules before September's third round of talks. The United States walked out of pharmaceutical talks and cancelled meetings of the textile and trade remedy working groups, eliminating any chance of progress in these areas. Below we highlight the second round developments regarding these issues:

- **Agriculture.** Agricultural talks produced mixed results. Negotiators agreed to exchange offers on a timeframe for tariff-elimination by mid-August, thus giving each side time to review the offers before the third round of talks in September. However, Korea has not backed down from its demand to exclude rice from the agreement.

- **Automobiles.** Negotiators also made mixed progress on automobiles. Although both parties agreed to extend U.S. and Korean tariff reductions only to automobiles that contain a certain percentage of

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U.S. or Korean manufactured parts, the two sides failed to resolve a disagreement over Korea's tax and tariff treatment of foreign autos. U.S. negotiators held firm on demands that Korea eliminate an eight percent import tax on foreign automobiles and pushed Korea to replace an automobile tax based on engine displacement with a tax based on a vehicle's value.

- **Industrial Goods.** Negotiators agreed on timetables for the phase out of tariffs on industrial goods. The parties will divide the timetable into five phases: (i) tariffs to be eliminated immediately upon the FTAs' implementation; (ii) tariffs to be eliminated within three years; (iii) tariffs to be eliminated in five years; (iv) tariffs to be eliminated over ten years; and (iv) tariffs that will remain.

- **Pharmaceuticals.** Negotiators failed during the first round of talks to agree on a consolidated draft text for pharmaceuticals. They made no further progress during the second round because the United States' boycotted the Pharmaceutical Working Group meeting on day two of the talks after Korea presented its unconditional "positive list" system for pharmaceutical reimbursement. U.S. negotiators appear to have expected the discussion in the second round to include Korea's proposed "positive list" reimbursement policy, but according to Assistant United States Trade Representative (AUSTR) Wendy Cutler, "[we] were informed that Korea was going to switch to a positive list system… before we had the opportunity to have meaningful negotiations on these issues." Cutler, who headed the 75 member U.S. delegation, stated that Korea's decision "is inconsistent with both the mandate of the Pharmaceutical Working Group and the market-opening spirit of the FTA," adding that it "precluded meaningful negotiations at this time." Cutler also indicated that the United States has not changed its basic position on its opposition to the new system, but "differences in views in the pharmaceutical sector… are not insurmountable."

  In May 2006, the Korean Ministry of Health and Welfare announced a new "positive list" proposal for pharmaceutical reimbursement that would require any new drug to receive explicit government approval to become eligible for reimbursement under Korea's National Health Insurance (NHI). The system would replace the "negative list" mechanism under which NHI reimburses most drugs unless the government explicitly excludes the drug from the eligibility list. Although South Korea has indicated that a drug's reimbursement eligibility under the new system would be based on the drug's price competitiveness and efficacy, the government has not made public the details of how the approval process would operate or the requirements that the government would consider when determining a product's reimbursement eligibility. The United States has expressed concern that the new approach lacks transparency and would discriminate against higher cost, innovative U.S. drugs.

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South Korea's chief negotiator Kim Jong Hoon maintains that the system would "be applied in a fair manner, not discriminating against foreign or innovative drugs."[17]

- **Services and Investment.** Both sides exchanged initial services offers that included reservation lists of services that each side would like excluded from full liberalization as part of the FTA. Korea presented the United States with a reserve list of over 100 services, reportedly including public utilities, broadcasting, law, mandatory education and delivery services. Negotiators agreed to table these issues for discussion in the third round of negotiations when they will exchange request lists based on each other's reserve lists. The parties also exchanged initial offers for investment.
- **Textiles and Trade Remedies.** Negotiators made no progress in textiles and trade remedies due to the United States' cancellation of both working group meetings. During the negotiations' first round, Korea urged the United States to review its antidumping and rules of origin (ROOs) policies, which Korean negotiators claim harm Korea's textile export industry and other key Korean exporters.

Outlook

Having resolved many of the agreement's less sensitive issues during the talks' first round, negotiators made little progress in Seoul when faced with more contentious issues. Even in areas such as automobiles – where the parties had already agreed on a consolidated draft text – difficult problems remain unsolved. The United States and Korea will hold a third round of talks in the United States September 4-8 and hope to complete negotiations by end-2006 to allow Congress sufficient time to pass the agreement's implementing legislation. The agreement's future would become uncertain if Congress has not approved the agreement by the expiry of trade promotion authority (TPA) in July 2007. However, the abrupt ending to the second round of talks suggests that unless negotiators make substantial progress on divisive issues such as agriculture, automobiles, pharmaceuticals, textiles and trade remedies in September, these issues might delay the FTA's completion beyond the TPA-determined deadlines, or they could even derail the agreement altogether. On the other hand, USTR Schwab has recently indicated that the renewal or extension of TPA in 2007 is not, as many have suggested, out of the question. Thus, should contentious issues prolong the KORUS negotiations beyond 2006, it might not cause the agreement to fail.

17 For a complete discussion of the Korean pharmaceutical system, please see the Annex to this Report.

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ANNEX

ANALYSIS OF KOREA'S PHARMACEUTICAL REIMBURSEMENT SYSTEM

The Korean government operates a pharmaceutical reimbursement system under which the government: (i) approves all new pharmaceutical products for sale in the Korean market; (ii) sets the products' prices; and (iii) determines the products' eligibility for reimbursement under Korea's national health care system. The United States claims that this system can harm U.S. producers by underpricing U.S. pharmaceutical products and granting an unfair competitive advantage to Korean generic pharmaceutical manufacturers. Although market access for U.S. pharmaceutical products has improved in recent years, the Korean government is considering a 2006 proposal that would revamp the reimbursement mechanism and might create new market access or investment barriers for U.S. pharmaceutical manufacturers. We discuss below the current and new systems, as well as U.S. concerns therewith.

I. THE CURRENT SYSTEM AND U.S. CONCERNS

Korea's current system mandates that new pharmaceutical products must undergo three phases of government review before producers may sell their pharmaceuticals in the Korean market:

- Government approval for sale in the Korean market
- Korean market price determination
- Reimbursement approval under the Korean National Health Insurance (NHI) system

The Korean government controls each of these steps. Under this system, Korean pharmacists purchase drugs from wholesalers at government-set prices. The government will reimburse the pharmacists for the full amount of any drug (purchased at the government-set price) that the government has determined to be eligible for reimbursement. The government does not reimburse pharmacists' purchases of pharmaceuticals that the government has not approved for sale in the Korean market or has not listed as eligible for reimbursement.

The United States has expressed concern that both the Korean government's **price setting policy** and its **reimbursement eligibility approval process** have the potential to create **market access barriers** for U.S. pharmaceutical products.

Price setting

To determine a pharmaceutical's price, the Korean government categorizes all new products as either "innovative" or not innovative. If the government determines a product to be "innovative," it will base the

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product's Korean market price on its average ex-factory price in seven advanced (A7) economies: the United States, United Kingdom, Germany, France, Italy, Switzerland and Japan. The government bases the Korean market price for all other new pharmaceutical products on a comparison of five "comparable" products the government selects from broad drug categories.

The United States claims that the Korean government's pharmaceutical policies allow it, in certain situations, to underprice foreign pharmaceutical products, thus discouraging U.S. firms from entering the Korean market. U.S. pharmaceutical companies base new product pricing in part on product research and development (R&D) costs. New product R&D requires an enormous initial investment and companies set product prices at levels that allow them to recoup this investment cost and earn a profit. The Korean policy, however, can prevent pharmaceutical companies from freely setting product prices based on market principles and instead often establishes drug prices below an amount that would allow companies to recoup R&D costs and earn a profit.[18]

As noted above, if the Korean government does not grant a product "innovative" status, the government will determine its price based on a comparison with "comparable" products. If the government does deem the drug "innovative," it will set the drug's price at the international market price and not utilize such a comparison. Because the government selects the "comparable" products for its pricing of non-innovative drugs, its choice strongly influences the drug's ultimate price in the Korean market. Deliberate selection of low-cost comparable products can lead to an artificially low set-price for the new drug under review. If such pricing causes the new product's government-set Korean market price to be below the point of profitability (*i.e.*, less than R&D and other costs), it will discourage the drug's producer from introducing the product into the Korean market.

If the Korean government enacted this policy in a uniform and transparent manner, the United States would have a lesser basis for challenge. However, if the Korean government unreasonably declares a Korean drug to be "innovative" (thus set at higher, market-based prices) yet deems a similar foreign-made drug to be "non-innovative" (thus set at a lower price that precludes profitability), the Korean price-setting policy can serve as a discriminatory barrier to foreign firms' access to the Korean pharmaceuticals market. Inadequate transparency can compound such problems for foreign firms.

However, even assuming that the Korean government applies its current price-setting system in a uniform and reasonable manner (*i.e.*, that it does not discriminate against foreign firms when determining whether

[18] According Korean press reports, newly developed drug prices in Korea in 2005 averaged only 66 percent of the advanced country average.

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a drug is “innovative”), the system can favor Korean producers of generic drugs. In the Korean market, foreign pharmaceuticals compete against domestically produced generic alternatives. Because the generic products imitate existing products, their producers are not burdened with expensive up-front R&D costs. Few, if any, U.S. pharmaceutical firms produce these generic drugs, and their products' prices therefore must account for R&D expenses. The Korean generic drug manufacturers, on the other hand, do not face strong price pressure to recoup expenses and can still make a profit from artificially low government-set prices on “non-innovative” drugs.

Consider the following example:

	Market Price	Set Price	Production Cost per Dose	R&D Cost per Dose	Profit
Foreign Brand A (Innovative – A7)	15	15	1	10	4
Foreign Brand B (Non-innovative)	15	11	1	10	0
Korean Generic C	7	6	1	0	5

Company A has invested 10 dollars per dose in R&D and faces a strong incentive to price its product at 15 dollars per dose. Because its drug has been deemed “innovative,” Company A's product will get A7 pricing (reflecting international market prices) and will be sold in the Korean market at $15. This pricing nets Company A a profit of $4.

Company B faces the same R&D cost pressures as Company A but does not receive A7 pricing because it is not deemed “innovative.” Instead, the Korean government sets Company B's product's price at the equivalent of 11 dollars per dose, based on an *ad hoc* comparison to “comparable” products. If Company B sells to a Korean pharmacy at this price, it cannot profit.

Korean Generic Company C faces no R&D cost pressures. Because Company C did not incur any up-front R&D costs, it can charge the lower, government-set price and still net a profit of $5 per dose.

Under this scenario, foreign firms (like all U.S. pharmaceutical companies) that incur R&D costs will not enter the Korean market, unless their products are deemed “innovative” because their non-innovative drugs will not generate a profit at the low government-set prices. Moreover, because the Korean price-

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setting system lacks transparency and predictability, U.S. firms cannot guarantee that their products will be deemed "innovative." The system can thus deter a U.S. company from even trying to enter the Korean market, as its efforts could entail large up-front costs (marketing, etc.) that the firm might be unable to recoup unless its product is declared "innovative." In such instances, the Korean system acts as a barrier to entry into the Korean pharmaceuticals for these firms.

Reimbursement Eligibility

The United States also claims that the Korean government's process for determining a drug's eligibility for full reimbursement under the current Korean pharmaceutical system lacks transparency and predictability and is not based on sound science. Although Korea does allow pharmaceutical companies to appeal reimbursement approval decisions, the Korean government has not codified the process into law and the process lacks independence because the same office that makes the initial eligibility determination also hears and considers appeals.

For obvious reasons, a drug's eligibility for full government reimbursement will greatly affect a Korean pharmacist's decision to purchase that drug: he will always choose a drug that allows for complete reimbursement of his purchase amount over a comparable one that does not unless he can charge his customers a price high enough to make up for the reimbursement amount. Consider the following example of eligible drug A and non-eligible drug B, which have comparable uses:

Drug	Purchase Amount	Reimbursement Amount	Consumer Price	Profit
A	$10	$10	$15	$15
B	$10	$0	$15	$5

Under this scenario, a pharmacist will only buy the equally-priced, but non-eligible, drug B if he can charge his customers $10 more than drug A, such that he will be assured an equivalent profit margin.

Thus, the Korean reimbursement eligibility process can create a perverse incentive for pharmacists to purchase an "eligible" drug, regardless of an alternative, ineligible drug's medical advantages over its eligible counterpart. A drug's ineligibility also discourages Korean doctors from prescribing a drug even if the Korean government has approved it for sale in the Korean market. Patients will discontinue visits to doctors who prescribe ineligible drugs for which patients must bear the full cost.

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II. U.S. CONCERNS ABOUT KOREA'S NEW PHARMACEUTICAL POLICY

The Korean government's 1999 implementation of A7 pricing improved market conditions for foreign drug manufacturers. However, the Ministry of Health and Welfare's (MHW) May 2006 announcement to introduce in September a new NHI reimbursement system has undermined U.S. confidence in Korea's commitment to maintain a fair and open market for U.S. pharmaceutical products. The United States has expressed concern that the new system's "positive list" approval requirement will further **reduce transparency** and **increase unpredictability** and might create **market access or investment barriers** for U.S. firms.

The details of the new system are not public. From what we understand of the system, under the "positive list" approach, NHI will cover reimbursement costs only for drugs that receive Korean government reimbursement approval. This differs from the current "negative list" approach under which NHI covers most drugs unless the government explicitly excludes a drug from the reimbursement list. The government has stated that under the new system it will consider a drug's reimbursement eligibility based on a its price competitiveness and efficacy, but the government has not detailed the approval process or clarified specific eligibility requirements or standards for coverage of new products. It appears that the new system will not affect products already eligible for reimbursement, but uncertainty about new product reimbursement eligibility might deter U.S. and other foreign pharmaceutical manufactures from investing in the Korean market (e.g., marketing). The government has indicated that it will create an appeal mechanism, but it has not provided details about how the mechanism might operate. The United States also worries that the appeals process might lack independence.

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U.S. and Malaysia Complete Second Round of FTA Negotiations

Summary

On July 17, 2006, U.S. and Malaysian officials met in Washington, D.C. for the second round of formal bilateral Free Trade Agreement (FTA) negotiations. Officials from the Office of the United States Trade Representative (USTR) conducted discussions with their Malaysian counterparts in several areas including government procurement and pharmaceuticals. After the Washington talks, there will be three more rounds of negotiations to be tentatively held on September 17, October 30 and December 11, 2006.

Analysis

On July 17, 2006, U.S. and Malaysian officials met in Washington, D.C. for the second round of formal bilateral FTA negotiations. Talks lasted through the week, and the officials divided into 22 negotiating groups to discuss issues including government procurement and pharmaceuticals. They also began to analyze the draft FTA text in detail and to explore market access and tariffs. Assistant United States Trade Representative (AUSTR) for Asia Pacific Barbara Weisel and Malaysian International Trade and Industry Ministry Secretary General Mohamad Sidek Hassan led the respective U.S. and Malaysian delegations.

U.S. Sentiment. U.S. negotiators have stated that they are "pleased" with the forward movement of the negotiations. Building on her comments from the first round of negotiations, Weisel stated that discussions continued to be productive and constructive. According to USTR, the talks "enabled the two sides to get a clear and thorough understanding of each others' priorities and sensitivities in each area," adding that "the two teams also identified areas of agreement as well as areas where further discussion will be needed." USTR also indicated that the "solid" progress negotiators made during the talks will likely allow the parties to conclude negotiations by the end of 2006. Sources have noted that USTR is focusing much of its resources on its FTA negotiations with South Korea and Malaysia.

Malaysian Sentiment. Malaysian International Trade and Industry Minister Datuk Seri Rafidah Aziz stated that Malaysia is not following a set timeframe for concluding the FTA talks, and that Malaysia will not sign any agreement that is to its disadvantage. Malaysia suspended FTA talks with New Zealand recently because it did not agree with New Zealand's requests in government procurement, environment, manpower and competition policy. Rafidah, however, has indicated that the United States and Malaysia both possess the political will to continue with negotiations and indicated that the first round of negotiations held the week of June 12 in Kuala Lumpur, Malaysia proceeded very well. Sources note that

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Malaysian negotiators are also pushing for increased information sharing, technical cooperation and training to build capacity in enforcement of international agreements.

Key Issues. The U.S. and Malaysian delegations discussed several key issues during the negotiations' second round:

- **Government procurement.** According to Malaysian sources, the United States seems to be more concerned about transparency in the awarding of international procurement contracts in Malaysia than about Malaysia's actual procurement policy. Rafidah stated that the United States has not questioned whether the contracts were awarded to ethnic Malays (also known as "bumiputras") or Malaysian companies as long the contracts were transparent through the processes of notice, tender and bidding. Malaysian government regulations mandate that companies bidding for government contracts have at least 30 percent Malay equity, and that 60 percent of government contracts go to Malay companies. The regulations are part of Malaysia's New Economic Policy (NEP) - an affirmative action policy that favors the majority bumiputras who the government believes lag behind the ethnic Chinese minority. U.S. officials have stated that this government policy discriminates against U.S. companies contracting in Malaysia.
- **Pharmaceuticals.** According to sources, the United States is seeking stronger intellectual property (IP) protection on pharmaceuticals – a stance consistent with its positions in other FTAs. U.S. negotiators discussed data exclusivity as part of the agreement's IP provisions and will likely require that patents on pharmaceutical products last for longer than the existing 20 years - a time period that they have included in other FTAs. Malaysian pharmaceutical producers have voiced dissatisfaction with the data exclusivity provisions because "Malaysian pharmaceutical manufacturers all make generic versions of medicines [and] are still decades away from inventing new medicines," according to the Malaysian Organization of Pharmaceutical Industries (MOPI). MOPI also reported that the Malaysian government grants 98 percent of its patents to foreigners and that Malaysian pharmaceutical producers would not be able to compete with foreign pharmaceutical companies if Malaysia signs an FTA that meets U.S. data exclusivity demands.
- **Financial Services.** U.S. officials continued to push for financial services liberalization concessions during the negotiations. Liberalization in banking and financial services is one of USTR's top priorities in its FTA talks with Malaysia (and other countries), and officials from both sides began discussing several components of the financial services text. In particular, they addressed U.S. provisions seeking greater regulatory transparency for banks, securities firms and insurance companies, as well as investment provisions.

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- **Market access.** On market access issues, both sides continued exploring "the possibility of further increasing trade through the elimination of remaining tariffs." Malaysia has submitted its request for early duty elimination for textiles and garments, rubber and wood, ceramics, electrical and electronics, and agricultural products. Malaysia also proposed faster elimination of tariffs on non-sensitive products and flexibility for the elimination of tariffs on sensitive products. Both the United States and Malaysia also proposed adequate safeguard provisions to allow for remedial measures in the event that injury to domestic industries occurs as a result of liberalization.

- **Intellectual Property (IP).** Sources indicate that the Malaysian delegation is working hard to convince U.S. negotiators that Malaysia's commitment to IP protection will protect U.S. investors. At the negotiations, Malaysian officials highlighted to U.S. officials that the World Economic Forum 2005-2006 ranked Malaysia 20th among 117 countries in IP protection, ahead of China, India, Taiwan, Thailand and South Korea. Malaysian officials also pointed out that ample Malaysian legislation exists to protect IP interests, including Malaysia's Intellectual Property Corporation of Malaysia Act 2002, the Trade Marks Act 1976, the Patents Act 1983, the Copyright Act 1987, the Industrial Design Act 1996, the Layout Designs and Integrated Circuit Act 2000, the Geographical Indications Act 2000, and the Optical Disc Act 2000. Rafidah has also stated that Malaysia is committed to its multilateral obligations under the World Trade Organization (WTO), the World Intellectual Property Organization (WIPO) and related IP international conventions where Malaysia is a party to the Paris and Berne Conventions. As a WTO Member, Rafidah also stated that Malaysia is signatory to the Trade-Related Aspects of Intellectual Property Rights Agreement (TRIPS). In response, U.S. officials allege that Malaysia suffers from "rampant software piracy," and USTR included Malaysia on the "watch list" of its 2006 "Special 301" report on the adequacy and effectiveness of U.S. trading partners' IPR protections. U.S. officials have called for greater transparency and intellectual property rights (IPR) monitoring.

Outlook

From all accounts, the second round of U.S.-Malaysia FTA negotiations progressed without major problems or delays. Officials managed to begin discussions on government procurement, IP issues and financial services - all considered contentious agenda items. That said, discussions on government procurement and IP are still in the preliminary stages, and U.S. and Malaysian negotiators have yet to explore in-depth issues surrounding auto trade. Both sides are also still examining the other's draft text, although many of the working groups established in the previous round have had ample discussion on the agreement's different chapters. The third and fourth rounds, to occur in the Fall, will likely see longer and

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more focused discussions, especially on government procurement, financial services, IP, and auto trade. Although negotiators will face a tough time addressing these more contentious issues, both parties have agreed to continue working together between rounds and plan to exchange information such as texts and data by August - one month before the negotiations' third round begins in Malaysia. All in all the political will seems to exist for both sides, and they appear to remain on track to complete the agreement by early 2007 – in time for congressional consideration of the FTA's formal implementing legislation before the mid-2007 expiry of Presidential Trade Promotion Authority (TPA). The recent collapse of the WTO's Doha Round should further assist the countries' efforts to complete the agreement under this timeframe, as USTR and its Malaysian counterpart are free to apply to the U.S.-Malaysia FTA agency resources that were previously committed to Doha.

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Free Trade Agreements Highlights

Senate Finance Approves Peru FTA in "Mock Markup"

On July 31, 2006, the Senate Finance Committee approved by a party line vote of 12 to 7 amended draft legislation to implement the U.S.-Peru Trade Promotion Agreement (PTPA). Last week, the Committee approved an amendment to the draft legislation that would make implementation of the Peruvian agreement contingent upon: (i) Peru's opening of its market to U.S. beef without age restrictions; and (ii) Peru's full compliance regarding sanitary and phytosanitary (SPS) requirements and technical barriers to trade (TBT). The Committee failed, however, to vote on the amended draft bill because it lacked a quorum (*i.e.*, sufficient Committee Members present to vote). The Committee added the amendment because Peru's market remains closed to U.S. beef due to the 2001 discovery of bovine spongiform encephalopathy (BSE) in the United States.

On July 20, 2006, the House Ways and Means Committee approved by a party line vote of 23 to 13 draft legislation to implement the PTPA. On labor, the Committee defeated an amendment offered by Ways and Means Ranking Democrat Rep. Charles Rangel (D-NY) that would have delayed the agreement's effective date until the United States and Peru formally commit to conform their labor codes to the basic International Labor Organization (ILO) labor standards within three years of the FTA's implementation. The committee also rejected an amendment offered by Rep. Ben Cardin (D-MD) that would have withdrawn a U.S. commitment to allow Peruvian companies to operate landside aspects of U.S. port activities.

A "mock markup" allows lawmakers the opportunity to offer technical changes or to make legislative recommendations to the Bush Administration regarding FTA implementation before the Administration submits the formal implementing legislation. After reviewing the draft implementing legislation from both committees, the President will submit the formal bill to Congress in its final form. This process allows Congress to have input into the final FTA text, as Presidential Trade Promotion Authority (TPA) limits House and Senate consideration of the final implementing legislation to a simple "up-or-down" vote without amendment. Under TPA, the House and Senate will have a maximum of 90 legislative days from the date of the final bill's submission to conduct a vote on the agreement.

Senate Finance Committee Chairman Charles Grassley (R-IA) indicated that the PTPA continues to face opposition over concerns regarding Peru's labor laws and enforcement, adding that he believed that passage of the agreement would be "hard but not impossible." Should the Bush Administration refuse to include the Finance Committee's beef/SPS amendment in the final implementing legislation, opposition to

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the agreement could increase, as was the case when the Administration failed to include a Committee amendment to the Oman FTA regarding forced labor. Although any increase in opposition based on the Beef/SPS amendment would likely be small, it might still be important, given that the PTPA vote should be very close. Thus, the Bush Administration might include the amendment in order to prevent even minimal attrition.

Final Congressional consideration of the Peru agreement is expected before the November elections, but the timeframe remains unclear given the FTA’s contentious nature and other items on the Congressional agenda.

U.S. Implements U.S.-Bahrain FTA as of August 1, 2006

On July 27, 2006, President Bush issued a proclamation implementing the U.S.-Bahrain Free Trade Agreement (FTA) on August 1, 2006. United States Trade Representative (USTR) Susan Schwab stated that the agreement "marks a milestone in strengthening ties and promoting freedom in the Middle East and is an important step in advancing President Bush's proposal to establish a Middle East Free Trade Area (MEFTA) by 2013.” The United States and Bahrain signed the FTA on September 14, 2004 and on January 11, 2006, President Bush signed into law the FTA’s implementing legislation (H.R. 4340 and S. 2027). Under the agreement, all trade in consumer and industrial products and 81 percent of U.S. agricultural exports to Bahrain will be duty-free.

The bilateral agreement is another step in furthering the President's goal of creating USMEFTA by 2013. Through USMEFTA, “the United States seeks to expand trade with and investment in Middle East countries to further their domestic reforms and the rule of law, protect intellectual property, and create a foundation for economic growth and prosperity.” President Bush announced USMEFTA in May 2003, and since then the United States has completed free trade agreements with Bahrain, Morocco and Oman and has initiated FTA talks with the United Arab Emirates (UAE). The United States had previously entered into FTAs with Israel and Jordan that are also considered part of the USMEFTA initiative.

Senate Finance Committee Delays Vote on Draft Peru FTA Legislation During “Mock Markup,” Approves Amendment on Beef

On July 27, 2006, the Senate Finance Committee held a “mock markup” of draft legislation to implement the U.S.-Peru Free Trade Promotion Agreement (PTPA) but failed to vote on the draft bill because it lacked a quorum. The Committee, however, did approve an amendment to the draft legislation that would make implementation of the Peruvian FTA contingent upon: (i) Peru’s opening of its market to U.S. beef

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without age restrictions; and (ii) Peru's full compliance regarding sanitary and phytosanitary (SPS) requirements and technical barriers to trade (TBT). Peru's market remains closed to U.S. beef due to the 2001 discovery of bovine spongiform encephalopathy (BSE) in the United States. Several U.S. Senators now appear skeptical of Peru's compliance with its SPS commitments unrelated to the FTA. Sen. Kent Conrad (D-ND) stated that "Peru arbitrarily blocks U.S. beef exports; therefore [it] must abide by its commitments and obligations." Sen. Max Baucus (D-MT) stated that "[i]t is hard to contemplate approving an agreement when our trading partner has already proven itself unwilling to live up to [the] trade commitments it has made." Everett Eissenstat, Assistant United States Trade Representative (AUSTR) for the Americas, however stressed that Peru is in "full compliance" with its SPS commitments under the FTA.

A "mock markup" allows lawmakers the opportunity to offer technical changes or to make legislative recommendations to the Bush Administration regarding FTA implementation before the Administration submits the formal implementing legislation. After reviewing the draft implementing legislation from both committees, the President will submit the formal bill to Congress in its final form. This process allows Congress to have input into the final FTA text, as Presidential Trade Promotion Authority (TPA) limits House and Senate consideration of the final implementing legislation to a simple "up-or-down" vote without amendment. Under TPA, the House and Senate will have a maximum of 90 legislative days from the date of the bill's submission to conduct a vote on the agreement.

The Finance Committee voted against an amendment that would have incorporated International Labor Organization Labor (ILO) standards into the FTA text and would have installed into the labor chapter the same dispute settlement mechanism as other parts of the agreement. Sen. Conrad also offered an amendment that would have prohibited duty-free entry of Peruvian goods produced with forced labor. This amendment was almost identical to that which the Committee approved for the U.S.-Oman FTA's draft implementing legislation, but which the Administration rejected for the final bill submitted to Congress. Before the Committee could vote on the Sen. Conrad's amendment, he withdrew it because he knew that the Administration again would reject the language. Sen. Conrad stated that he preferred instead to "work on broader legislation to clarify existing U.S. labor laws regarding forced labor."

The Finance Committee's deliberations indicate that leading House and Senate Democrats remain concerned over the FTA's alleged lack of labor protections, and that Members from both parties are dismayed over Peru's refusal to admit U.S. beef imports. These protests could erode support for the agreement's final implementing legislation, the approval of which is far from certain. Senate Finance Committee Chairman Charles Grassley (R-IA) indicated that the Peruvian FTA continues to face

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opposition over concerns regarding Peru's labor laws and enforcement, adding that he believed that passage of the agreement would be "hard but not impossible." The Bush Administration's failure to include the Finance Committee's beef/SPS amendment in the final implementing legislation might increase opposition to the agreement, as was the case with the Administration's refusal to include the Committee's forced labor amendment in the Oman FTA. According to Grassley, Congress might consider the final Peru agreement before the November elections, but the timeframe remains unclear given some of the FTA's more contentious issues and other items in the Congressional agenda as well.

The Senate Finance Committee will likely complete the "mock markup" of the PTPA during the week of July 31 before it adjourns for the August recess. On July 20, 2006, the House Ways and Means Committee approved by a party line vote of 23 to 13 draft legislation to implement the PTPA.

House Passes Oman FTA 221-205 Along Partisan Lines; Labor, Port Security Issues Narrow Margin of Victory

On June 20, 2006, the House of Representatives approved legislation (H.R. 5684) implementing the U.S.-Oman Free Trade Agreement (FTA) by a margin of 221 to 205. Votes were mostly along party lines: 22 Democrats and 199 Republicans voted for the bill; 176 Democrats and 28 Republicans voted against. The House's approval of the implementing legislation completes congressional consideration of the Oman FTA. On June 29, 2006, the U.S. Senate voted 60 to 34 to approve an identical version of the implementing legislation (S. 3569). The bill will now move to the President to be signed into law. The Administration has not indicated when the signing will occur, but the timing of recent bilateral FTAs indicates that President Bush could sign the bill into law within the next month.

Chairman of the House Ways and Means Committee Rep. Bill Thomas (R-CA) stated that the agreement "has importance far beyond its economic benefits" and added that "Oman has been a valuable ally of the United States for more than 170 years, leading the way in promoting peace and economic freedom in the Middle East." Thomas was likely referring to President Bush's goal of completing a U.S.- Middle East Free Trade Area (USMEFTA) by 2013. Through USMEFTA, "the United States seeks to expand trade with and investment in Middle East countries to further their domestic reforms and the rule of law, to protect intellectual property, and to create a foundation for economic growth and prosperity." President Bush announced the USMEFTA Initiative in May 2003, and the United States has signed FTAs with Israel, Jordan, Bahrain and Morocco and is in formal FTA negotiations with the United Arab Emirates (UAE). Although the Israel, Jordan and Morocco FTAs were completed before 2003, the Bush Administration has included them in the USMEFTA initiative.

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After the House passed the Oman FTA, several House Democrats continued to express their opposition to the agreement. House Ways and Means Committee Ranking Member Rep. Charles B. Rangel (D-NY) stated that the United States “should negotiate trade agreements that are good for America and will not drive the rights of workers to the lowest possible denominator.” Ranking Member of the House Ways and Means Committee Trade Subcommittee Rep. Ben Cardin (D-MD) stated that Omani labor law does not protect the five basic labor rights set out by the International Labor Organization (ILO), and that Bahrain, another U.S. FTA partner, does protect such rights. Opposition Democrats also voiced concern with an FTA provision that they alleged would hinder U.S. efforts to block the foreign purchase of terminal operating rights at U.S. ports. Democrats argue that if the United States were to block an acquisition, as it did in the recent case of Dubai Ports World, Oman could challenge the decision before a binational dispute settlement panel which would be an "essential security" exception.

Unsurprisingly, congressional Democrats used the Oman vote to voice their concerns with labor issues, aligning their opposition with that of U.S. organized labor – a traditional Democratic supporter – before the Fall midterm elections. With the Congressional docket clear of the Oman agreement, the next trade measures that Congress will likely consider are the Peru Trade Promotion Agreement (PTPA) and granting Vietnam Permanent Normal Trade Relations (PNTR) as part of its accession bid to the World Trade Organization (WTO). Regardless of Democrats’ motives for opposing the Oman FTA, the legislation’s narrow margin of victory indicates that these upcoming votes will also likely be very contentious. The Omani agreement benefited from the geopolitical concerns expressed in the greater USMEFTA initiative. Neither the Peru FTA nor Vietnam’s PNTR can rely on such a boost.

Deputy USTR Discusses U.S.-Asian Trade Agenda Before House International Relations Committee

On June 20, 2006, Deputy United States Trade Representative (USTR) Karan Bhatia testified before the House Committee on International Relations on the Bush Administration’s free trade initiatives in Asia. Bhatia’s remarks focused on free trade agreement (FTA) negotiations with Korea, Malaysia and Thailand. He also addressed U.S. economic relations including trade and investment framework agreements (TIFAs), World Trade Organization (WTO) accession negotiations and other dialogues with regional trading partners such as Japan, China, India, Taiwan and Association of Southeast Asian Nations (ASEAN) members.

Bhatia provided an overview of U.S. trade policy in Asia, outlining its objectives and plotting the Administration’s future course. Bhatia stated that the United States seeks through its trade relations with

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Asia: (i) to create opportunities abroad for U.S. farmers, workers and business through the reduction of trade and investment barriers; (ii) to strengthen and to reinforce bilateral relationships and U.S. foreign policy objectives through enhanced commercial and investment channels; and (iii) to ensure that U.S. trading partners in the region honor and abide by their economic agreements. Bhatia praised the robust trade relationship between the United States and Asia and noted the increased trade and investment with the region. U.S. exports to Pacific Rim nations grew by $50 billion between 1995 and 2005 to $233 billion, and bilateral trade totals nearly $800 billion annually, accounting for one third of all U.S. trade. U.S. foreign direct investment (FDI) to the region grew threefold since 1995. Bhatia stated that the Bush Administration would continue to work hard to "deepen [U.S.] economic engagement in the region, encourage bilateral and regional trade and investment, and bring the countries of the region into the rules-based international trading system."

Bhatia emphasized the U.S.-Asia FTAs' importance to "help seed regional trade, raise standards for multilateral agreements, and promote economic and political reform."

- **Singapore**. He opined that the Singapore FTA, the United States' first in Asia, has benefited U.S. businesses, and that U.S. exports to Singapore had grown by 24 percent since the agreement entered into force in 2004.
- **Thailand**. On Thailand, Bhatia indicated that although negotiations were suspended in February due to Thailand's ongoing political crisis, the USTR would work closely with Thailand to restart negotiations upon the formation of the Thai government. Bhatia stated that during recent meetings with the Thai Deputy Prime Minister, USTR and Thai officials agreed to hold "informal consultations on outstanding issues… to rapidly reengage and conclude this deal… hopefully later this year."
- **Korea**. Regarding the Korea-U.S. (KORUS) FTA, Bhatia stated that although the talks remain "challenging… in a number of areas, the progress to date has generally been encouraging." He suggested that time still remained to conclude the KORUS agreement before the July 2007 expiry of Presidential Trade Promotion Authority (TPA). U.S. and Korean negotiators suspended last week's second round of negotiations a day early after the United States boycotted meetings to protest a new Korean pharmaceutical reimbursement policy.
- **Malaysia**. On Malaysia, Bhatia described robust bilateral economic ties, noting that Malaysia was the United States' tenth largest trading partner, and that the United States was Malaysia's largest foreign investor. He stated that an FTA with Malaysia would "demonstrate U.S. commitment to the region"

and strengthen "support for [U.S.] efforts on key political and security issues." The United States and Malaysia will conclude a second round of FTA negotiations on June 21.

Regarding Vietnam's WTO accession, Bhatia stated that ensuring Vietnam's entry was "one of our top trade priorities" and encouraged Congress to grant Vietnam Permanent Normal Trade Relations (PNTR) that would allow the United States to benefit from Vietnam's WTO commitments. Vietnam has recently attracted the attention of some members of Congress who have expressed concerns about granting Vietnam PNTR before receiving assurances from Vietnam that it would protect its citizens' religious freedom.

House Ways and Means Approves Peru Agreement in "Mock Markup"

On July 20, 2006, the House Ways and Means Committee approved by a party line vote of 23 to 13 draft legislation to implement the U.S.-Peru Trade Promotion Agreement (PTPA). Following the "mock markup" of the PTPA, Ways and Means Committee Chairman Rep. Bill Thomas (R-CA) stated that the House would not be able to consider the PTPA before Congress' August recess but will likely vote on the final agreement before Congress adjourns for the Fall mid-term congressional elections. Meanwhile, the Senate Finance Committee is expected to hold its own mock markup before the Summer recess.

The two most contentious issues during the markup were labor standards and U.S. port management. On labor, the committee defeated by a vote of 14-23 an amendment offered by Ways and Means Ranking Democrat Rep. Charles Rangel (D-NY) that would have delayed the agreement's effective date until the United States and Peru formally commit to conform their labor codes to the basic International Labor Organization (ILO) labor standards within three years of the FTA's implementation. The committee also rejected an amendment offered by Rep. Ben Cardin (D-MD) that would have withdrawn a U.S. commitment to allow Peruvian companies to operate landside aspects of U.S. port activities. Under the current agreement, Peruvian companies can perform landside port functions including operating and maintaining docks, loading and unloading of vessels, and ship cleaning. Committee Democrats argued that such a provision could pressure the United States to allow other foreign governments access to U.S. landside port operations.

A "mock markup" allows lawmakers the opportunity to offer technical changes or to make legislative recommendations to the Bush Administration regarding FTA implementation before the Administration submits the formal implementing legislation. After reviewing the draft implementing legislation, the President will submit the bill to Congress in its finalized form. This process allows Congress to have input into the final FTA text, as Presidential Trade Promotion Authority (TPA) limits House and Senate

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consideration of the final implementing legislation to a simple "up-or-down" vote without amendment. Under TPA, the House and Senate will have a maximum of 90 legislative days from the date of the bill's submission to conduct an vote on the agreement. Due to political considerations related to the Fall midterm elections, the congressional vote on the final PTPA implementing legislation is expected to be quite contentious, with ultimate passage uncertain.

Peruvian and USTR officials have stated that they would like Congress to consider the PTPA before the Congressional summer recess in August. However, the PTPA will have to wait until after the House considers the Oman FTA's implementing legislation, which the Administration has already submitted to Congress (the Senate passed the measure by a 60 to 34 margin). Given this scheduling, the tight congressional schedule and the few remaining legislative days before the August Summer recess, consideration of the Peruvian agreement might not occur until the Fall. Moreover, the agreement is expected to elicit strong opposition from many congressional Democrats (and some Republicans, as well), so the Administration might not have sufficient time to gather the votes necessary for passage before Congress adjourns at the end of July.

USTR Commends Omani Labor Reforms as FTA Vote Looms

On July 13, 2006, United States Trade Representative (USTR) Susan Schwab commended Oman for issuing a Royal Decree to amend its labor laws in response to U.S. congressional concerns with the U.S-Oman Free Trade Agreement (FTA). Schwab stated that "the government of Oman had committed to implement a number of changes by October 31[but] has taken an extraordinary step in addressing many of these commitments almost four months early and clearly demonstrated that it takes labor law reforms seriously." Schwab added that Oman would prepare other regulations to address the United States' remaining labor concerns and would implement those regulations by the October deadline.

Oman issued Royal Decree 74/2006 on July 8. The Decree establishes the legal foundation for changes to Omani labor laws and practices that the government will immediately implement. Omani officials stated that the Decree: (i) explicitly prohibits forced labor; (ii) endorses collective bargaining and acknowledges the use of strikes "as a collective bargaining technique"; (iii) provides enforcement tools for the prohibition against forced or coerced labor by providing for imprisonment and/or fines of up to $1300 per violation; (iv) immediately ends the government's involvement in union activities; (v) prohibits termination of employment or any other form of employer retribution for workers performing union duties; and (vi) increases fines for violating Oman's prohibition against the use of child labor or the improper use of female labor. Oman's ambassador to the United States, Hunaina Al-Mughairy, stated that "Royal Decree

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74/2006 was signed by his majesty [Sultan Qaboos bin Said] as a demonstration of Oman's good faith and continuing efforts to improve working conditions and rights for all workers in the Sultanate."

On June 29, the Senate approved legislation (S. 3569) to implement the U.S.-Oman FTA by a vote of 60 to 34. The House is expected to consider the implementing legislation (H.R. 5684) in late July. During committee mark-up, Senate and House Democrats opposed the FTA because of labor concerns, particularly the Bush Administration's omission of a provision in the implementing legislation to deny trade benefits to any imports made with forced labor. Despite Oman's latest labor reforms, most House Democrats who opposed the FTA for labor reasons will still likely vote against it, as their opposition is less about specific labor issues and more about their election-year alignment with U.S. organized labor, which opposes the agreement and is a traditional Democrat supporter. For example, following the Omani decree's issuance, House Ways and Means Committee Democrats maintained their opposition to the FTA on the grounds that the decree addressed "fully only one of the 10 areas where Oman's labor laws do not comply with basic international standards." Despite Democrats' continued opposition, the House will likely approve the agreement largely along partisan lines, although the Omani Decree might increase the FTA's margin of victory.

U.S. to Sign TIFA with Cambodia; USTR Announces ASEAN TIFA Close to Completion

On July 11, 2006, Deputy United States Trade Representative (USTR) Karan Bhatia announced that the United States and Cambodia will sign a Trade and Investment Framework Agreement (TIFA) to improve trade and investment ties between the two economies on July 12, 2006. Bhatia made the announcement during his remarks during a U.S.- Association of Southeast Asian Nations (ASEAN) Business Council briefing. Bhatia added that Cambodia is "a recent World Trade Organization (WTO) Member with a promising record of reform and strong economic growth," and that "the United States hopes to use that dialogue, its TIFA dialogue, to strengthen U.S. engagement in Cambodia and create new opportunities for businesses in both countries." Bhatia also noted that USTR is "looking to support ASEAN integration and to institutionalize our relationship with ASEAN through a TIFA with ASEAN as an institution and I believe we are very close to concluding that." He stated that "tied to this [potential ASEAN TIFA] will be a work plan with concrete initiatives aimed at promoting trade and investment in specific sectors."

TIFAs are limited trade agreements that establish "joint councils of trade and economic officials to discuss trade issues." Under U.S. trade policy, TIFAs are the first step towards the initiation of formal bilateral or regional Free Trade Agreement (FTA) negotiations. The U.S.- Cambodia TIFA indicates that although

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the United States is not yet ready to begin formal FTA talks, it views Cambodia as a viable FTA partner if the countries can resolve initial outstanding trade issues. The next step in the process would be for the countries to enter into a Bilateral Investment Treaty (BIT) which protects the rights of foreign subsidiaries and investors in the countries' home markets.

A TIFA with ASEAN, however, would prove more complicated than the TIFA with Cambodia. ASEAN (Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar (Burma), the Philippines, Singapore, Thailand, and Vietnam) is a large geographic zone comprised of economies at various stages of development. With a U.S.-Singapore FTA already in effect and USTR negotiating an FTA with Thailand and Malaysia, it is unclear how USTR would formulate a TIFA that would treat all ASEAN Members equally, despite their heterogeneous economic ties with the United States. However, because the United States has signed TIFAs with Brunei Darussalam, Indonesia, Malaysia, the Philippines and Thailand, and will sign a TIFA with Cambodia on July 12, a U.S.-ASEAN TIFA could build upon common elements of these agreements. The United States also would need to complete TIFAs with the remaining three ASEAN countries, including Myanmar, against which the United States still imposes a unilateral import ban due to human rights concerns. Indeed, the U.S. Congress in May 2006 reauthorized annual sanctions against Myanmar under the Burmese Freedom and Democracy Act of 2003 – a clear indication that a U.S.-ASEAN TIFA would be unlikely in the near-term.

U.S. and Colombia Finalize FTA Text; Bush Administration to Announce Intent to Sign Agreement

On July 8, 2006, the United States and Colombia finalized the text of a Free Trade Agreement (FTA), and the Bush Administration stated that it will notify Congress "in the near future" of its intent to sign the bilateral agreement. Under Section 2015(a)(1) of the Trade Act of 2002, the President must notify Congress 90 days in advance of signing any trade agreement. The 90-day period is intended to give Congress an opportunity to review the entire agreement before the president signs it. Following the Administration's announcement that it has signed the agreement, the House Ways and Means Committee and the Senate Finance Committee will hold hearings on the agreement and "mark-up" the proposed implementing legislation before the Administration sends a final version to Congress for its approval.

On June 14, 2006, President Bush and Colombian President Alvaro Uribe met in Washington, D.C. to discuss the FTA's outstanding details, primarily the agreed-upon translations of certain agreement sections. According to the Office of the United States Trade Representative (USTR), the two sides had a good exchange on the sections of concern, including agriculture and sanitary and phytosanitary

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standards (SPS). The resolution of these issues cleared the way for the parties to finalize the FTA text and for the Bush Administration to announce its intent to sign the agreement.

On February 27, 2006, the United States and Colombia completed FTA negotiations with a final draft agreement. The Colombian agreement was part of the U.S.-Andean FTA, which included Peru and Ecuador. The U.S.-Andean talks stalled in late 2005 over intellectual property and agriculture issues, and the parties at that time agreed to divide the regional FTA into three separate bilateral agreements. The United States and Peru subsequently completed a bilateral FTA, and President Bush formally notified Congress of the United States' intent to enter into the agreement. The Ecuador agreement has proven more problematic. A congressional vote on the Colombian FTA will likely have to wait until Congress votes on formal implementing legislation for the previously completed U.S.- Oman and U.S.- Peru FTAs as well as a vote on granting Vietnam Permanent Normal Trade Relations (PNTR). Under such a timeline, Congress will likely consider the Colombia FTA's implementing legislation after the summer and mid-term election recesses but before the end of 2006. USTR, however, continues to advocate congressional consideration of the Peru and Colombia agreements together. Congressional leadership has not indicated that it would consider this alternative.

House Members Demand Proof of Korea's Open Auto Markets Before USTR Cuts Tariffs in FTA Negotiations

In a July 7, 2006 letter to United States Trade Representative (USTR) Susan Schwab, a bipartisan group of 40 members of the U.S. House of Representatives demanded that South Korea be required to demonstrate increased market access for foreign automobiles before the United States lowers tariffs on Korean autos as part of the U.S.-South Korea Free Trade Agreement (KORUS FTA). The letter's release coincides with the second round of negotiations on the KORUS FTA which start on July 10 in Seoul. Michigan Reps. Dale Kildee (D-MI), Fred Upton (R-MI), and Sander Levin (D-MI) organized the letter which also included the signatures of eight other house members from Michigan - home to U.S. auto manufacturing.

The House members stated that Korea should significantly increase the import share of its auto market, from roughly 3 percent to the 40 percent range found in other developed countries. The letter targets non-tariff barriers (NTBs), noting that "Korea employs a wide variety of non-tariff barriers that have been successful at keeping Korea insulated from import competition from around the world," and that "in an effort to bring down these non-tariff barriers, the United States negotiated two bilateral auto agreements (MOUs) with Korea in the 1990s to open Korea's auto market to imports … these agreements looked

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good on paper, but they were unsuccessful in opening the Korean auto market." The letter concludes that the United States must “take a new approach” and seek tangible evidence that Korea's auto market is open by "reaching and sustaining specific and measurable benchmarks” before agreeing to cut U.S. auto tariffs. The letter states that “a key benchmark would be significant improvement in import market share that is in the range of the [Organization for Economic Cooperation and Development, OECD] average,” and that “Korea will need to undertake a comprehensive dismantling of its longstanding auto non-tariff barriers [to achieve this], given Korea's history of one-way automotive trade."

The congressional letter is not the first of its kind on the KORUS FTA and autos trade. Senators George Voinovich (R-OH) and Carl Levin (D-MI), co-chairmen of the Senate Auto Caucus, expressed concern over KORUS FTA auto trade issues, including Korean NTBs and the resultant bilateral trade imbalance, in a February 2, 2006 letter to fellow congressional members and then-USTR Rob Portman. These letters indicate that automobile market access in both nations will be one of the more contentious FTA negotiating areas. Korea’s NTBs in the auto market were included in USTR’s 2006 National Trade Estimate (NTE) report on foreign trade barriers, and U.S. congressional members have demanded that U.S. negotiators refuse to eliminate U.S. auto tariffs in other bilateral FTAs. To address these potential auto-related problems during the KORUS FTA negotiations, the parties have created a working group on auto trade issues, but it is unclear whether it will resolve the issue. Because of the significant influence of the U.S. auto lobby, Congress will certainly pressure USTR on automobile market access at home and in Korea. Korean officials will be similarly reluctant to cease protecting their auto sector without guarantees for increased access to the U.S. market. Should the final FTA not adequately resolve these issues, many in Congress will likely withhold their support for the agreement.

DR-CAFTA Takes Effect in Guatemala

On June 30, 2006, United States Trade Representative (USTR) Susan Schwab announced that the Dominican Republic- Central America Free Trade Agreement (DR-CAFTA) would enter into force with Guatemala on July 1. Guatemala is the fourth country to implement the agreement. DR-CAFTA entered into force for El Salvador on March 1, 2006 and for Honduras and Nicaragua on April 1, 2006. The countries yet to implement the agreement include Costa Rica and the Dominican Republic. USTR Schwab was pleased that “the President has issued a proclamation to implement the CAFTA-DR agreement for Guatemala as of July 1, 2006” and stated that the United States’ “constructive engagement has had positive results and [the United States is] pleased that Guatemala is now ready to join El Salvador, Honduras and Nicaragua in full implementation of this agreement.”

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On December 30, 2005, USTR announced that the United States would not implement DR-CAFTA by its January 1, 2006 target date. The U.S. Government delayed the agreement's implementation for Guatemala pending the Guatemalan government's passage of legislation on intellectual property rights (IPR) and sanitary and phytosanitary (SPS) issues. Once Guatemala passed those laws, the parties could implement the agreement on the first day of the following month.

USTR has not provided a timetable for when the remaining DR-CAFTA countries will be eligible for implementation, but sources indicate that the Dominican Republic will "qualify" for implementation in July 2006. Costa Rica has yet to ratify the agreement and its implementation timeframe remains unclear, but USTR Schwab has stated that USTR "will continue our work with the remaining two CAFTA-DR partners to ensure timely and full implementation of the agreement."

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Multilateral

Doha: What's Next?

Summary

Entrenched positions prevented World Trade Organization (WTO) Members from reaching an agreement on agricultural and non-agricultural market access (NAMA) modalities at the June 27-30, 2006 Doha Round negotiations. Discussions between the Group of Six (G-6) nations – Australia, Brazil, the European Union, India, Japan and the United States – did not result in any substantive agreement that could serve as a basis for discussion with the other Member's trade ministers. The meeting's failure did not surprise observers, and some participants noted that negotiations never really started.

A July 1 formal meeting of the Trade Negotiating Committee (TNC) mandated that WTO Director-General Pascal Lamy hold intensive consultations with the G-6 nations to break the deadlock. There is a sense of urgency among Members to reach a consensus on modalities as soon as possible in order to complete Doha Round negotiations by the end of 2006. However, some Members have begun to express skepticism about the feasibility of this timeframe. If Members fail to meet this deadline, the round's future would grow uncertain, and it is unclear whether Members would be able to muster the political will necessary to revive the stalled negotiations.

Analysis

We review below the Members' failure to agree on agriculture and NAMA modalities and highlight the main obstacles that prevented an agreement.

Negotiating Modalities

The November 2001 Doha Mandate calls for an agreement on "modalities," which are documents that define rules and limits for preparing new schedules of concessions. These concessions include new tariff bindings and cuts on bound tariffs in both agricultural and non-agricultural products, as well as a reduction in agricultural export subsidies and domestic supports. Once Members have prepared, revised and annexed the new schedules to a Protocol, the Protocol becomes the legal source for the Members' obligations.

Members have repeatedly failed to meet established deadlines to complete modalities. In the latest failed attempt, the Chair of the Negotiating Group on Market Access Ambassador Don Stephenson of Norway and the Chair of the Special Session of the Committee on Agriculture Ambassador Crawford

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Falconer of New Zealand on June 22 circulated "on their own responsibilities" their respective draft texts for negotiating full modalities. However, Members and analysts strongly criticized these draft texts because they merely compile existing positions for each issue, resulting in vague and highly bracketed texts. The drafts reflect how far Members are from reaching a consensus in most outstanding issues.

Many negotiators have assumed that end-July 2006 will likely be the decisive moment if Members want to conclude the Round by December 2006. Anything later would leave too little time for the technical work of translating the agreed agricultural and NAMA formulas into national schedules of commitments. The same limitations apply to an agreement on services, but finalizing services commitments is even more time-consuming because they lack formulas for liberalization, and they usually involve negotiations with domestic service regulators that can be as contentious as those with foreign trading partners' service regulators.

The Hong Kong Ministerial Declaration calls on Members "to conclude the negotiations launched at Doha successfully in 2006." WTO Members are under pressure to stick to this deadline because the Bush Administration needs to submit a final Doha Round package to Congress prior to the expiry of trade promotion authority (TPA) on July 1, 2007. Because it is unclear whether Congress will renew TPA, a post-2006 Doha agreement might not be able to gain Congressional approval "as a package."

Obstacles to An Agreement

Broad Agenda Prevented Members Focus On Core Issues

On June 28, 2006, WTO Director-General Pascal Lamy circulated an agenda for the informal ministerial meetings, suggesting a sequential treatment of outstanding issues in the agriculture and NAMA modalities texts. The proposed sequence prioritized certain critical issues such as market access, sensitive products and domestic supports for agriculture, and formula and coefficients for tariff reductions, the treatment of unbound tariff lines and the flexibilities for developing countries for NAMA. However, Members differed on the agenda, given the issues inter-relation and Members' respective negotiating interests and concerns.

The "Triangular Obstacle"

Director-General Lamy has repeatedly stated that any solution to break the deadlock must be "triangular": the EU must offer more on agricultural market access; the United States must offer bigger reductions in agricultural domestic supports; and Brazil and India must improve market access for industrial goods. Members must also agree on the treatment of sensitive agricultural products for developed countries and

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sensitive and special products for developing countries. These products would be shielded from the full force of tariff reduction. Japan and the EU are among the major demandeurs of protection for “sensitive” products, while India and the Group of 33 seek important flexibilities for their “special products.” The United States, on the other hand, has sought very narrow exceptions for sensitive and/or special products.

Members Reject Lamy’s “Magic Number 20”

On June 28, 2006, Director-General Lamy expressed his “own intuition” about how far each camp would likely have to go to strike an agreement in the wake of the informal ministerial gathering. Lamy indicated that a middle-ground agreement might center around a “20-20-20” formula that would involve three elements:

- **The parameters of the G-20’s proposed farm tariff cuts.** The G-20 has proposed an average farm tariff reduction of 54 percent for developed countries, assuming that developing countries would cut tariffs by two-thirds of this amount. Both the EU and the G-10 find this formula unacceptably high, and the EU has instead proposed a 39 percent average tariff reduction. On the other hand, the U.S. proposal seeks to slash tariff barriers by an average of 66 percent, and the United States has expressed an unwillingness to lower its market access demands to the G-20 level. It is uncertain how EU and U.S. negotiators will overcome domestic resistance and agree to a more or less ambitious (respectively) figure than each side has already proposed. France and Finland, for example, have demanded that EU Trade Commissioner Peter Mandelson not offer any further concessions. Separately, 57 of 100 U.S. Senators signed a June 23 letter to President George W. Bush stating that it would be unacceptable to ask US farmers “to give more [on domestic support] while getting less in market access.” These proposals are also weakened by the numerous sensitive and special products exceptions for both developed and developing countries. China, India, Indonesia and other G-33 countries want the right to define 20 percent of agricultural products as “special” to protect the livelihood of subsistence farmers and demand that tariffs on these products not be cut at all. Such exceptions would exempt over 90 percent of imported farm products from any tariff reductions.
- **A Swiss formula with a coefficient of 20 for reducing developing country industrial tariffs.** This formula would require India to cap its industrial bound tariffs at 20 percent, and force reductions to its applied tariffs on 57.2 – 84.4 percent of products. The formula would also require Brazil to reduce applied rates on roughly half of all products as a result of the proposed coefficient. Developing countries, including Argentina, Brazil and India have rejected such a formula.

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- **A $20 billion ceiling for U.S. overall trade-distorting domestic support.** Although capping U.S. overall trade-distorting support at $20 billion would not reduce the supports from current levels (estimated at $19.67 billion in 2005), Lamy's suggestion improves upon the U.S. proposal which seeks to reduce the ceiling level to $23 billion. However, other WTO Members have rejected both of these proposals, and EU Trade Commissioner Peter Mandelson has stated that the US should reduce its allowable ceiling to a "starting point" of $15 billion.

The Blame Game

Analysts have noted that criticism in Geneva focused heavily on India and the United States and was less focused on the EU than it has been in recent months. Several important parties including the EU and Brazil appear to be pressing for a compromise that would likely take the direction of Lamy's proposal. However, India and the United States appear less committed to compromise. India maintained an intransigent stance in NAMA negotiations at the June 27-30 meeting in Geneva. Indian Commerce Minister Kamal Nath indicated to reporters on June 30 that he would not agree to a Doha Round deal that would lower India's near 10 percent gross domestic product growth. Indian concerns about upsetting subsistence farmers outweigh excitement over the benefits that the Round could bring for the country's services sector. This concern may explain India's hard stance regarding "special product" exemptions in the agriculture negotiations. Critics say that the United States is preventing a deal because it demands too much liberalization from others while offering too little on domestic support. Furthermore, many U.S. Congressmen argue that no deal is better than a bad deal and they appear more keen on bilateral trade agreements in which the United States can dictate terms more easily than at the multilateral level. The United States, however, has countered that it is willing to give more on domestic support but only if the EU and other WTO Members commit to "real tariff cuts" with few "loopholes" like the special and sensitive products exemptions.

Outlook

On July 1, 2006, WTO Members requested that Director-General Lamy "conduct intensive and wide-ranging consultations with the aim of facilitating the urgent establishment of modalities in agriculture and NAMA" and report to the TNC "as soon as possible." As part of this consultation process, Mr. Lamy has begun a world tour to visit the G-6 members, starting with a two-day visit to Japan where he met with Japanese Prime Minister Junichiro Koizumi, Minister of Economy, Trade and Industry Toshihiro Nikai, Minister of Agriculture, Forestry and Fisheries, Shoichi Nakagawa and Foreign Minister Taro Aso. Lamy has also spoken with officials from Australia, Brazil, India, the EU and the United States.

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It is unlikely, however, that Lamy's efforts will produce another ministerial-level meeting at the end of July. Several ministers have reportedly stated that they would not come back to Geneva for nothing, which is exactly what Lamy's efforts have thus far produced. Sources in Geneva also predict that the next TNC meeting, scheduled for July 29, will be cancelled. Some observers, including World Bank President Paul Wolfowitz and United Nations Secretary General Kofi Annan, have expressed hope that key WTO Members might achieve a breakthrough during the July 15-17 Group of Eight (G-8) industrialized nations meeting in St. Petersburg, Russia. G-8 leaders have invited leaders from five developing countries – Brazil, China, India, Mexico and South Africa – to join a special G-8 + 5 "outreach session" that will follow the formal G-8 meeting and focus on stalled Doha round talks. In a July 7 letter to G-8 + 5 leaders, Wolfowitz encouraged leaders to adopt at the meeting WTO Director-General Lamy's 20-20-20 Plan. However, given key Members prior lack of support for Lamy's plan and the G-8 meeting's already full agenda it is unlikely that the G-8 + 5 will arrive at any agreement regarding Doha, particularly in light of the fact that Lamy has still not secured an invite to the summit.

If Lamy's efforts fail to produce a compromise among WTO Members, sources predict that he would by the end of the summer 2006 prepare a report to Members on the Doha Round's next possible steps. Members' failure to compromise would leave the round's future uncertain and open to influence from factors such as U.S. Congressional willingness to renew TPA, which is set to expire on June 30, 2007. Congressional opponents of TPA renewal might use further delays in concluding the round as evidence of TPA's ineffectiveness as a trade policy tool. The lack of an agreement might also undermine traditional support for TPA extension, as business leaders and congressional members might be unable to point to the Doha agreement's tangible benefits for U.S. manufacturing, agriculture and services sectors. On the other hand, members of Congress who favor TPA renewal might cite such delays as justification for the need to renew TPA, without which the United States could not likely conclude any future multilateral or bilateral trade deals.

Initial predictions regarding TPA renewal have been bleak because of waning congressional support for trade agreements due to partisan politics. This support might decline even further if Democrats gain seats in the House or Senate in the Fall mid-term elections, which many congressional observers consider likely. On the other hand, United States Trade Representative (USTR) Susan Schwab recently expressed limited optimism regarding TPA renewal, stating her belief that the Bush Administration can achieve a TPA extension, but that she "wouldn't bet the round on it." Her words are the first indication from the Administration that it may be willing to expend the necessary political capital to get TPA passed.

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If the Administration decides to expend this capital, TPA renewal is possible, despite the aforementioned obstacles.

Failure to conclude the Doha Agreement in 2006 will place the fate of the round in the hands of the U.S. Congress – a fickle and uncertain entity. Better to finish the agreement in 2006 and thus secure its future – and overwhelming economic potential – before external factors and American politics can alter its course. Unfortunately, the path of least resistance appears unlikely, and the fate of the Doha round may ultimately become intertwined with the fate of TPA in Congress. Of course, the other alternative is the complete collapse of the round, thereby scrapping five years of negotiations and the tremendous benefits that an ambitious Doha Round agreement could bring to the world's poor.

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U.S. Services Coalition Releases Summary of Revised U.S. Services Offer

Summary

On July 11, 2006, the Coalition of Services Industries (CSI) released a summary of the United States' revised World Trade Organization (WTO) services offer. The summary outlines the U.S. offer including new commitments in research and development (R&D) and technical testing and analysis services, online games services, physical well-being services, and a number of small service activities categorized as "other business services." The new U.S. offer also includes revisions to legal services and computer and related services (CRS) commitments. Under the timeframe established at the December 2005 WTO Ministerial Conference in Hong Kong, all WTO Members must submit their revised services offers by July 31, 2006. We will send a detailed report of the new U.S. services offer once its full text is available. We include here the CSI summary's full text.

Analysis

- The U.S. proposes to offer new commitments in privately-funded **Research and Development** services and non-government-mandated **Technical Testing and Analysis services**. The U.S. enjoys a wide trade balance in private R&D and tech testing: for the combined sectors, 2004 exports were $9.8 billion and imports were $4.7 billion. More than 85% of our exports were through affiliates of U.S. companies abroad (Mode 3). Offering new commitments will strengthen the U.S. negotiating position in asking other countries to open up to U.S. suppliers of these important services. These commitments also respond to requests from Australia, Canada, Chile, the European Communities, India, Hong Kong China, Japan, Mexico, New Zealand, Norway, Pakistan, Saudi Arabia, Singapore, Switzerland, and others.

- The U.S. proposes to improve upon its already extensive list of business services commitments by offering new commitments in a catch-all category "**Other business services**," which covers small but increasingly important activities such as credit reporting services, collection agency services, telephone answering services, duplicating services, mailing list compilation and mailing services, specialty design services, business brokerage services, appraisal services other than for real estate, and secretarial services. This responds to the plurilateral request from India, Chile, Hong Kong China, Mexico, New Zealand, Pakistan, Switzerland, Singapore and others for further cross-border commitments.

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- The U.S. proposes to include **online game services** (interactive computer games played online over remote servers), a rapidly growing market of major export interest to the United States. The submission makes clear that online game services do not include games or activities that involve gambling, betting, or wagering. Offering new commitments for online game services will help the United States raise awareness of these new services and strengthen the U.S. position in asking others to guarantee market access and national treatment to U.S. suppliers.
- The U.S. proposes to offer new commitments for **physical well-being services**, which include services such as fitness centers, spas, non-therapeutic massage, and ayurvedics. This category specifically excludes regulated medical services and does not affect the ability of state or Federal authorities to regulate substances that may be affiliated with these services. This responds to requests from India, Korea, and Thailand.

Other Changes

- The U.S. is reformatting its legal services commitments without changing their substance. The reformat reduces the number of pages in the legal services sector from 28 to 8.
- The U.S. will remove an unnecessary exception for computer reservation services from our Computer and Related Services offer and indicate that they are classified under Air Transport Services.
- The U.S. submission proposes to update road transport services commitments to reflect the expiration of certain provisions and to improve clarity.

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Multilateral Highlights

Lamy Suspends Doha Round After Last-Minute Talks Collapse

On July 24, 2006, World Trade Organization (WTO) Director General Pascal Lamy announced that he was suspending the WTO's Doha Development Round after fourteen-hour negotiations between six of the WTO's major players collapsed without an agreement on modalities for agricultural and non-agricultural market access (NAMA). Officials quickly pointed fingers for the talks' failure, blaming each other's lack of flexibility in key areas such as domestic supports and market access. Although a suspension of several months at minimum is likely, Members have not abandoned Doha entirely and have indicated a willingness to resume negotiations "in the future." Lamy has not announced when the round might resume, however, talks scheduled for July 28 and 29 were cancelled, and some Members have indicated that resumption could take "months to years."

Trade negotiators from the Group of Six (G6) – Australia, Brazil, the European Union, India, Japan, and the United States – met in Geneva on July 23 in an attempt to reach a last-minute breakthrough in the deadlocked Doha Round negotiations. However, the talks collapsed after United States Trade Representative (USTR) Susan Schwab refused to offer further cuts to the U.S. offer of a $22 billion ceiling on domestic supports for agriculture. Schwab had indicated that the United States would consider reducing its October 2005 offer in return for more ambitious market access offers from other WTO Members. During the July 23 negotiations, the EU reportedly offered to increase its market access offer to a 51 percent average tariff cut up from an earlier proposal of 41 percent. However, because the United States demanded a figure higher than the 54 percent offer by the Group of 20 (G20), Schwab rejected the EU proposal and refused to alter the U.S. position on domestic supports.

Officials were quick to assign blame for the talk's collapse. EU Trade Commissioner Peter Mandelson blamed the failure on the United States' inflexible negotiating position. According to Mandelson, the United States was "unable to show any flexibility on the issue of farm subsidies," and "was unwilling to accept… or acknowledge, the flexibility being shown" by other G6 members. EU Agricultural Commissioner Mariann Fischer Boel labeled the talks "a big failure" and cited the United States' preference "to stand still" rather than budge on its offer to make deeper domestic support cuts. The United States rejected EU accusations and opined that other Members' unwillingness to embrace more ambitious market access offers for agriculture and NAMA had caused the round's collapse. Schwab stated that "the United States came to Geneva with the flexibility to offer more on domestic support and market access" but that "unfortunately the promises of flexibility and market access coming from [other

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Members] did not materialize in Geneva." Schwab also criticized U.S. trading partners as being "more interested in loopholes than they were in market access," referring to EU and developing countries' demands that significant percentages of "sensitive" and "special" products be exempted from their tariff reduction commitments.

Despite the negotiations' failure, parties indicated that they had not yet given up on concluding the Round. Boel described the collapse as "a time out in the talks," adding that the day's failure "does not mean they cannot pick back up again in the future." USTR Schwab reaffirmed the United States' commitment to a successful and ambitious Doha Development agreement that "creates real market openings, that brings new economic opportunities, [and] opens markets for all WTO member countries." It remains to be seen, however, whether the parties can muster the political will to risk one more attempt at resolving the impasse after repeated failure. Moreover, the failures of the WTO Members to reach a final Doha Round Agreement by the end of 2006 means that the United States must extend or renew Presidential Trade Promotion Authority (TPA) in 2007 – a task that most observers believe is far from certain, given current congressional skepticism towards trade liberalizing agreements. (The relatively benign U.S.-Oman Free Trade Agreement passed the House by a margin of only 16 votes) Under TPA, Congress has a strict timeframe to approve or deny an international trade agreement, without amendment. Without TPA, the United States will be unable to enter into meaningful negotiations at the bilateral or multilateral level because its trading partners will be hesitant to agree to provisions that might be altered during the process of congressional consideration. Thus, WTO Members' failures in 2006 mean that any future agreement will depend on not only Members' as-yet-unseen ability to agree on the agreement's terms but also the U.S. Congress' willingness to reauthorize TPA. Neither outcome appears certain.

Mexico, Argentina Initiate WTO Compliance Proceedings in US OCTG Case

On July 14, 2006, Mexico and the United States informed WTO Members that they reached a procedural agreement for carrying out a compliance panel proceeding in the dispute involving U.S. antidumping duties on imports of Mexican oil country tubular goods (OCTG). The latest stage of this dispute arises from the claim by the United States that it has complied with an adverse WTO ruling that found that the U.S. Department of Commerce (DOC) sunset review of the antidumping order on OCTG from Mexico was inconsistent with U.S. obligations under the WTO Antidumping Agreement (ADA).

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Mexico disagrees with U.S. claims that the DOC's new "Section 129" sunset review determination regarding the OCTG antidumping duty order has brought the United States into compliance with the earlier WTO ruling. Section 129(b) of Uruguay Round Agreements Act is the U.S. law that governs U.S. implementation of adverse rulings that affect DOC determinations. Under the procedural agreement reached with the United States, Mexico can initiate the compliance proceeding by requesting consultations with the United States on the issue. If the parties fail to resolve the dispute within 15 days of the request for consultations, Mexico can thereafter request the establishment of a WTO compliance panel to rule on the dispute.

The underlying WTO Panel decision in the case upheld Mexico's claim that the U.S. sunset review that led to the continuation of antidumping duties against Mexican OCTG imports was inconsistent with the WTO Antidumping Agreement. The Panel found that DOC's determination that revocation of the antidumping order on OCTG from Mexico would be likely to lead to continuation or recurrence of dumping was inconsistent with Article 11.3 of the ADA. The United States was given until May 28, 2006 to bring itself into compliance with its WTO obligations.

Separately, Argentina is also contesting U.S. compliance in a WTO compliance proceeding against the United States. That case also arises out of a claim that the United States failed to implement a previous WTO ruling that found that DOC's sunset review of the antidumping duty order on Argentine OCTG was inconsistent with U.S. obligations under the ADA. The WTO compliance panel is set to rule on U.S. compliance in that case in November.

In another development, Argentina has also recently requested WTO dispute settlement consultations with the United States regarding a DOC administrative review of OCTG imports from Argentine producer Acindar.

U.S. Becomes Focus of Two New WTO Panels: Gambling and Shrimp

On July 19, 2006, the World Trade Organization (WTO) established two new dispute settlement panels in which the United States is the respondent. The WTO first established a panel to determine whether the United States has complied with a previous WTO ruling regarding U.S. restrictions on cross-border Internet gambling (DS285). The Caribbean nation of Antigua and Barbuda made the panel request, charging that the United States has done nothing to bring its laws and measures in line with a WTO Appellate Body (AB) ruling which backed Antigua's assertion that the United States included specific commitments on market access for cross-border gambling and betting services in its WTO services schedule. Based on a previous understanding between the two countries, the United States agreed not

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to block Antigua's request for the compliance panel. The panel will have 90 days to issue its findings. Both the United States and Antigua have the right to appeal the panel's ruling, with the appeals process taking an additional 90 days.

The WTO also established a dispute settlement panel to rule on whether the United States violated multilateral trade rules in imposing anti-dumping duties on imports of shrimp from Ecuador (DS335). The WTO Dispute Settlement Body (DSB) formed the panel after Ecuador made a second request for it to do so; the United States blocked Ecuador's first request at the June 19 DSB meeting. Ecuador challenges the U.S. Department of Commerce's (USDOC) February 2005 decision to impose definitive anti-dumping duties of 2.35 percent-4.48 percent on shrimp imports from Ecuador. Ecuador's challenge focuses on DOC's use of "zeroing" to calculate the weighted average dumping margins for its Shrimp imports, arguing that if DOC had not relied upon zeroing, the investigation would have resulted in a finding of no dumping. The panel is due to issue its ruling on Ecuador's claims sometime toward the middle of 2007.

Ecuador's complaint is one of many active and completed WTO cases against the United States' zeroing methodology. On April 18, 2006, the AB issued its report regarding "United States — Laws, Regulations and Methodology for Calculating Dumping Margins ('Zeroing')" (DS294) brought by the European Communities. In its report, the AB reversed the Panel's finding that the "zeroing" methodology applied by Commerce in the administrative reviews at issue was consistent with Article 9.3 of the WTO Anti-Dumping Agreement and Article VI:2 of the GATT 1994. The AB's justification for its ruling was that "the methodology applied by the Commerce in the administrative reviews at issue results in amounts of assessed anti-dumping duties that exceed the foreign producers' or exporters' margins of dumping." Japan also requested the creation of a panel in February 2005 as part of its complaint (WT/DS322) against several U.S. laws and regulations related to "zeroing" and sunset reviews, as well as the specific application of those measures in 16 antidumping cases against Japanese imports; that panel decision has been delayed until late August or early September 2006. On April 24, 2006, Thailand requested consultations with the United States concerning the U.S. zeroing methodology in the AD investigation of Thai shrimp imports – part of the same investigation underlying Ecuador's complaint. Those consultations are still ongoing, with India, China, and Brazil as third parties.

Religious Freedom Clouds Vietnam PNTR Consideration; WTO Pushes for October Accession

On July 19, 2006, Chairman of the Senate Finance Committee Sen. Charles Grassley (R-IA) indicated that congressional concerns over religious freedom could delay consideration of legislation (S. 3495)

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providing Permanent Normal Trade Relations (PNTR) to Vietnam. Grassley stated that he is “running into some members who are raising questions about religious freedom and Vietnam and not wanting to vote on [PNTR] too soon until we get some certification from Vietnam what exactly the situation's going to be in the future.” He added, however, that he will advocate committee consideration of the Vietnam PNTR bill at the same time as the implementing legislation for the U.S.-Peru Trade Promotion Agreement (PTPA). Grassley opined that the Finance Committee could hold the informal markup of the PTPA and a formal markup of the Vietnam bill prior to Congress’ scheduled summer adjournment on August 3 but added that the committee might be unable to address the PTPA’s formal implementing legislation before the summer recess.

In response to congressional concerns over Vietnam’s religious freedom record, Grassley has asked the Vietnamese embassy in Washington for feedback on such issues. Sen. Gordon Smith (R-OR), cosponsor of S. 3495, will also hold a briefing for all senators on religious freedoms in Vietnam, with John Hanford, the State Department's ambassador at large for international religious freedom.

Separately, chairman of the World Trade Organization's (WTO) working group on Vietnam’s accession Eirik Glenne stated that he plans to conclude multilateral negotiations soon so that WTO Members could approve Vietnam's final accession terms in October. Speaking at a July 19 meeting of the working party for Vietnam’s accession, Glenne stated that he “would push Members” to complete the final working party report over the next few months. That report will outline Vietnam's commitments to bring its trade practices in line with multilateral rules. Glenne added that the goal is to finalize all outstanding accession issues so that the WTO's ruling General Council can approve Vietnam's membership terms at its October 10-11 meeting, thus allowing allow Vietnam to accede to the WTO before it hosts the annual Asia-Pacific Economic Cooperation (APEC) leader's summit in Hanoi in November.

As Grassley noted, Congressional concerns on Vietnam’s religious rights record could dampen what was a fast-moving PNTR vote. Vietnam, however, does have solid Congressional support, especially from influential congressmen such as Grassley and Sen. Max Baucus (D-MT), Ranking Member of the Senate Finance Committee. These supporters will likely lobby to ensure that the House and Senate consider Vietnam’s PNTR before the congressional summer recess. However, given the busy congressional schedule and the few remaining days before the August recess, a PNTR vote might not occur until the Fall. If this should occur, the mid-term election recess might further delay the vote until mid-November. On the other hand, President Bush has indicated that he would like to have PNTR approved before he arrives in Vietnam for the APEC summit. Thus, one can expect Grassley and other Republican leaders to do all they can to ensure that Congress votes before President Bush departs for Hanoi.

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U.S. Requests Panel Selection in Airbus-Boeing Dispute

On July 7, 2006, the United States filed a request with the World Trade Organization (WTO) to intervene in the selection of members to a second dispute panel in the Boeing-Airbus dispute (DS316). On May 9, the WTO Dispute Settlement Body (DSB) accepted the United States' request to establish an additional panel to rule on EU subsidies to the European aircraft consortium Airbus. The United States requested the second panel to challenge new Airbus subsidies since the original July 2005 U.S. panel request, as well as other subsidies that the EU claims fell outside the first request's mandate.

In its request, the United States asked the WTO to select the three panelists following the failure of U.S. and EU officials to agree upon a list of candidates. The task of selecting the panelists typically falls under the jurisdiction of WTO Director-General Pascal Lamy, but Lamy rescued himself citing his "previous direct and active involvement" in the Airbus-Boeing dispute as EU trade commissioner. Deputy Director-General Alejandro Jara likely will be tasked with the panel selection. The EU has not yet requested that the WTO select the members of the second panel related to its counter-complaint (DS317) against alleged illegal U.S. subsidies to Boeing.

Sources note that there initially appeared to be no real desire by either party to move the panel process forward, but recent financial troubles at Airbus' parent company, the European Aeronautic Defense and Space Company (EADS), have led U.S. officials to worry that European governments might provide new aid to Airbus. Sources stated that EADS is considering developing new mid-size aircraft to challenge Boeing and could ask European governments to back the initiative with new "launch aid."

The U.S. WTO complaints focus on the EU's "launch aid" program, under which European governments cover startup costs for Airbus' new aircraft. Airbus does not repay these "loans" unless the plane is a success. The EU's complaint contends that Boeing receives preferential tax breaks and similar "launch aid" from the U.S. military and Japan, especially for the Boeing 787 Dreamliner which competes against the Airbus A-350. Given U.S. fears that EADS could restart the "launch aid" program, the U.S. request on panel selection is the first sign of movement in the case since the May 2006 establishment of the second panel. It is likely that the EU will counter the U.S. request with its own request for panel selection. Experts predict that should the U.S. and EU cases result in panel (and ultimately Appellate Body) decisions, the complainants in each case will likely win, resulting in combined retaliatory tariffs of nearly $40 billion – by far the largest dispute settlement amount in the WTO's history.

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WTO Members Continue to Point Fingers While WTO Services Chair Calls for "Major Improvements" to Revised Offers

Two weeks after World Trade Organization (WTO) Members failed to agree on agriculture and non-agricultural market access (NAMA) modalities in Geneva, key Members continue to pass blame for the talks' failure and to maintain their inflexible negotiating positions on agriculture and NAMA. On July 12, Deputy Assistant U.S. Trade Representative (USTR) for Agricultural Affairs Jason Hafemeister stated that any Doha Round deal must hinge on market access and blamed the United States' World Trade Organization (WTO) negotiating partners for the round's stagnation. Hafemeister stated that countries' refusal to negotiate market access is "what's endangering the round right now," adding that "the discussion is going to start with market access." He maintained the United States' position that U.S. negotiators would be willing to "improve" or "adjust" the October 2005 U.S. offer to cut domestic agricultural support if the EU, India, and other WTO Members would first agree to more ambitious agricultural and industrial market access offers. Hafemeister criticized the EU's unwillingness to provide details of its offer to come close to a Group of 20 (G-20) proposal for an average 54 percent cut in agricultural tariff cuts for developed countries. The EU has argued publicly that these cuts should be kept between 39-46 percent. Hafemeister also censured Japan and members of the Group of 10 (G-10) developed countries for their support of a tariff reduction offer "that's even weaker than the EU's."

Separately, India's Commerce Minister Kamal Nath on July 12 signaled India's unwillingness to compromise on its demand for flexibilities for developing countries on agricultural and non-agricultural market access. India has demanded the right to grant "special product" status to 20 percent of its agricultural products to protect Indian subsistence farmers. The United States argues that such a demand would exempt over 90 percent of India's agricultural tariffs from any reduction, thereby eviscerating developing country market access gains that U.S. agricultural exporters could reap from a Doha agreement. Linking the special and sensitive product exemptions with India's "subsistence and livelihood," Nath stated that these are "not negotiable for any country." India has also rejected offers to bind its industrial tariff lines at 20 percent. The Indian government has emphasized manufacturing growth as a driver of improved living conditions for its large but poor population and fears that greater market access will jeopardize this mechanism. Nath had stated earlier that India would reject any offer that would lower India's economic growth.

On July 14, 2006, chairman of the World Trade Organization's (WTO) Doha Round services negotiating group, Fernando de Mateo, stated that WTO Members' revised market access services offers would require "major improvements" by the end of July if the Members wished to complete negotiations. De

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Mateo made his remarks while delivering a report on the negotiating group's progress. Despite his pessimistic tone, de Mateo opined that the negotiations have progressed "as well as might be expected" in the face of stalled talks in agriculture and non-agricultural market access (NAMA). De Mateo stated that the "real test of substance" will be the submission of revised offers due July 31.

He also stated that the initial services offers fell short of expectations, and that "revised offers that offer little cannot provide a solid basis for the successful conclusion of the services negotiations." In discussing the services negotiations' links to the agriculture and NAMA talks, de Mateo asserted that "while the situation in those other areas is surrounded with uncertainties, members must address the services negotiations with the positive assumption that the situation [in agriculture and NAMA] will be unblocked in the near future." Many WTO Members have indicated that the ambition of their services offers hinged on the outcome of the agriculture and NAMA negotiations, despite the fact that both sectors have remained deadlocked for several months. On the July 31 deadline for revised offers that Members established at the December 2005 Hong Kong Ministerial Conference, de Mateo stated that the deadline is less important than the substance of the offers and added that "the first and most important priority is to ensure that the quality of the revised offers is satisfactory."

The head of the WTO's services division, Abdel-Hamid Mamdouh, stated that the "overwhelming majority" of WTO Members present at the July 14 negotiating group meeting said they were working hard on preparing revised offers. According to Mamdouh, the "majority" includes the United States, the EU, Brazil, China and India.

WTO Director-General Pascal Lamy Welcomes WTO Agreement on Regional Trade Agreements

On July 10, 2006, World Trade Organization (WTO) Director General Pascal Lamy praised the formal approval by the Negotiating Group on Rules of a new WTO transparency mechanism for regional trade agreements (RTAs). RTAs include bilateral free trade agreements (FTAs) between countries that are not in the same region. Under the new transparency mechanism, the Committee on Regional Trade Agreements (CRTA) will review any RTAs that fall under Article XXIV of the General Agreement on Tariffs and Trade (GATT) and Article V of the General Agreement on Trade in Services (GATS). The new transparency mechanism mandates that parties to an RTA immediately notify the WTO upon ratifying the agreement. The mechanism will only be implemented on a temporary basis. WTO members will review, and if necessary modify, the mechanism, potentially replacing it with a permanent system adopted as a result of the WTO's Doha Round negotiations.

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Observers note that the measure will contribute to the multilateral trading system because more than half of global trade is conducted under RTAs, and most WTO members are a party to at least one RTA. At present, 197 RTAs are in force and have been notified to the GATT/WTO, while an additional 70 are estimated to be operational but not yet notified. However, according to the WTO, differences between WTO members on "how to interpret the criteria for assessing the consistency of RTAs with WTO rules" have created a backlog of uncompleted reports at this Committee. Many trade experts also note that the proliferation of RTAs could undermine the completion of multilateral trade negotiations as part of the Doha Round by confusing the terms of the debate and by undermining the benefits and incentives of a multilateral agreement. The Rules Committee's transparency mechanism might help bring RTAs into conformity with WTO disciplines, thereby eliminating some of the tension between RTAs and the multilateral trading system.

Japanese Prime Minister, Cabinet Ministers Promise Cooperation to Conclude Doha by End-2006; Lamy Holds "Confessionals" In Effort to Determine Members' "Bottom-Line" Positions on Doha

On July 6, 2006, Japanese Prime Minister Junichiro Koizumi assured World Trade Organization (WTO) Director General Pascal Lamy that he had directed Japanese Minister of Agriculture, Forestry and Fisheries Shoichi Nakagawa and Minister of Economy, Trade and Industry Toshihiro Nikai to cooperate with WTO Members to complete the WTO's Doha Round of multilateral trade negotiations by the end of 2006. During a two-day visit to Japan, Lamy met with Koizumi, Nakagawa, Nikai and Japanese Foreign Minister Aso Taro to discuss the stalled global trade talks. Lamy encouraged Japan to agree to lower tariffs on farm products and to consider maximum tariffs on agricultural goods. Although none of the Japanese ministers indicated that Japan was willing or able to offer further concessions in the negotiations, Lamy stated that he "[came] out of these discussions with the distinct impression that Japan has flexibilities that it can employ." Japan, along with the European Union, has demanded special treatment of "sensitive" agricultural products such as rice.

Following the July 6 visit to Japan, Lamy spoke with top trade officials from the other Group of Six (G-6) members including the United States, the EU, Brazil, India and Australia. Lamy also met with India's Commerce Minister Kamal Nath in Geneva on July 12. After the latest ministerial talks collapsed in early July, WTO Members requested that Lamy hold intensive consultations to break the Doha deadlock over "modalities" on agriculture and non-agricultural market access (NAMA).

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Sources noted that unless Lamy convinced one of the “key WTO players” – the United States, the EU, or Brazil and India – to change its positions on agriculture and NAMA, the WTO’s Doha Round could fail. After the collapse of the Geneva ministerial meeting, Lamy’s confessionals are a last-ditch effort to bridge the gaps between the Members’ rigid negotiating positions. Those gaps, however, might prove too large to fix without further face-to-face meetings between the key players.

U.S. and Mexico Agree to WTO Ruling Compliance Date on Soft Drink Tax

On July 5, 2006, the United States and Mexico agreed to a deadline for Mexico to comply with a World Trade Organization (WTO) ruling (DS308, *Mexico–Tax Measures on Soft Drinks and Other Beverages*) that a Mexican tax on soft drinks and other beverages with non-sugar sweeteners was inconsistent with WTO rules. According to a joint communication circulated to WTO Members, Mexico will have until January 1, 2007 to comply with the WTO Appellate Body’s (AB) findings. Should the Mexican Congress enact legislation in December repealing the tax, the deadline will be extended to January 31, 2007. The United States also announced that, in light of the agreement, it will withdraw its request for WTO arbitration on the deadline.

On March 16, 2004, the United States requested consultations with Mexico concerning Mexican tax measures on soft drinks and other beverages that use any sweetener other than cane sugar. The measures included (i) a 20 percent tax on soft drinks and other beverages that use any sweetener other than cane sugar (the “beverage tax”) and (ii) a 20 percent tax on the commissioning, mediation, agency, representation, brokerage, consignment and distribution of soft drinks and other beverages that use any sweetener other than cane sugar (the “distribution tax”). The United States contends that these taxes are inconsistent with General Agreement on Tariffs and Trade (GATT) Articles III, III:2 and III:4. On June 10, 2004, the United Stated requested the establishment of a Panel, and the dispute settlement body (DSB) composed the Panel on August 18, 2004. On October 7, 2005 the Panel found that certain Mexican taxes on soft drinks and sweeteners were inconsistent with Mexico’s National Treatment obligations under GATT Article III. Mexico appealed the decision, and on March 6, 2006, the AB upheld the Panel’s key findings. In late June, the United States asked the WTO to determine the compliance deadline for Mexico after the two countries were unable to reach an agreement on the date.

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Tension Grows Between U.S. and Russia On WTO Accession; Lead to Failure in Reaching Agreement, Negotiations to Continue Through Fall

On July 4, 2006, Russian President Vladimir Putin stated that Russia will not continue to abide by World Trade Organization (WTO) rules it has voluntarily adopted unless it reaches a bilateral agreement with the United States as part of Russia's accession to the WTO. Putin stated that "if for some reason we fail to reach agreement, [Russia] will reject all the obligations on agreements that we have taken on ourselves and are fulfilling before joining the [WTO]." Putin's statements indicate Russia's growing impatience with its drawn-out WTO accession and have increased tensions between the United States, the EU, and Russia. Russian and U.S. trade officials have stated that they would like to complete a U.S.-Russia bilateral accession agreement by the July 15-17 annual G-8 economic summit in St. Petersburg, Russia; Russian officials have stated, however, that if an agreement "does not happen, it will be no tragedy [and Russia] will continue working."

Sources note that bank and insurance branching rights remain a key reason for the deadlocked U.S.-Russia agreement. The EU failed to secure a commitment on branching in its May 2004 bilateral, and Russian officials have used this omission as a reason to deny U.S. demands that Russia further liberalize its banking sector. Without branching rights, foreign banks and insurance firms must establish independent companies in Russia subject to local laws and supervisory requirements. Russia has agreed to offer limited branching rights that would allow insurance firms to open branches but only nine years after Russia becomes a WTO member. Russia, however, still refuses to provide branching rights for foreign banks or to allow foreign majority ownership. In place of foreign majority ownership, Russia seeks a permanent 50 percent cap on foreign ownership of banks and insurance firms. U.S. financial service companies have stated that the proposed cap is unacceptable and argue that it would set a terrible precedent for other accession negotiations.

Russia's weak intellectual property rights (IPR) protection regime also concerns U.S. businesses and Members of Congress. The Office of the United States Trade Representative (USTR) in its "2006 Special 301 Report" on U.S. trade partner's IPR protection maintained Russia's status as a Priority Watch List country, citing Russia's "rampant counterfeiting and piracy problems." Russia has remained on the list since 1997. The report stated that in the context of WTO accessions, the United States "expects Russia to commit to provide protection against unfair commercial use of undisclosed test and other data submitted by pharmaceutical and agricultural chemical companies seeking marketing approval for their

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products." The United States remains unsatisfied with Russia's IPR commitments in its bilateral accession agreement.

The EU has also expressed growing displeasure with Russia's implementation of its commitments under the EU-Russia bilateral accession agreement. Despite concluding the agreement in May 2004, EU officials allege that Russia has not begun to phase out charges levied on European carriers for flying over Russian airspace. EU officials also charge that Russia maintains export duties on products such as paper, steel, iron and other metals, despite its commitment to remove them.

Russia's WTO accession has also raised the ire of several leading U.S. Congressmen: Senate Finance Committee Chairman Sen. Charles Grassley (R-IA) and the committee's ranking minority member Sen. Max Baucus (D-MT), as well as Chairman of the House Ways and Means Committee Rep. Bill Thomas (R-CA) and the committee's ranking minority leader Rep. Charles Rangel (D-NY), released a May 11 letter to President Bush opposing Russia's WTO accession. The four lawmakers stated that they will continue to oppose the agreement until Russia takes a series of steps demonstrating its willingness to abide by WTO rules, particularly on IPR and agricultural market access. Grassley has also opined that completing the WTO accession negotiations with Russia by the G-8 summit is unlikely, despite the Administration's desire to do so.

WTO accession procedures mandate that acceding countries conclude bilateral market access deals with any WTO Member that requests negotiations. The United States is the only remaining country with which Russia has yet to conclude a bilateral deal. Russian officials set year-end 2006 as the revised target for Russia's accession, and Russia must complete its remaining bilateral negotiations by fall 2006 to meet this deadline. Sources note, however, that an early-2007 accession is more likely. Given the state of Russia's bilateral talks with the United States, this timeframe seems more likely, although increasing tensions could delay the agreement even further.

On July 11th, United States Trade Representative (USTR) Susan Schwab departed for Moscow for two days of meetings aimed at completing a bilateral agreement with Russia. However, U.S. and Russian officials stated July 15 that despite progress in bilateral negotiations, the parties have not reached an agreement. Aides for Presidents Bush and Putin stated that both sides moved forward on contentious issues such as financial services and IPR, but they could not close the gaps on these and other contentious issues before the G-8 summit in St. Petersburg. The officials opined that the countries could complete the agreement by the fall.

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After attending the negotiations, USTR Susan Schwab stated that a remaining dispute on meat and poultry safety was the primary reason that the two sides did not achieve a bilateral agreement. She also stated that both sides "have virtually closed the industrial tariff side; virtually closed the services side; made excellent progress on intellectual property rights; and are very close on agricultural issues, with the exception of some agricultural market access issues, including what is known as sanitary and phytosanitary-- SPS--issues, just having to do with regulatory processes." President Bush, also present at the meeting, stated that "the reason [we failed to reach an agreement] is because we want the agreement that we reach to [be] accepted by our U.S. Congress" and added that "there's more work to be done [and] we'll continue to negotiate in good faith to try to reach an agreement that has been difficult to achieve." President Putin reiterated that he is optimistic that negotiations will be successful but added that "Russia will continue to work further, pursuing our interest, the interest of our developing economy."

On SPS issues, sources stated that the issue of Russian barriers to U.S. meat exports has proved most contentious. Russia is insisting on auditing the U.S. system for certification of livestock at pork and beef producers. To date, Russia has not re-opened its borders to U.S. beef exports following a December 2003 discovery of a cow in the United States with bovine spongiform encephalopathy (BSE). Sources also stated that issues related to poultry also remain unsettled.

On financial issues, U.S. and Russian negotiators have made progress toward an agreement that would liberalize the Russian financial sector. According to sources, Russia is prepared to ease investment restrictions in the insurance sector. Russia has also indicated that it might agree to phase out the existing 49 percent limit on foreign investment in any given insurance company, eventually permitting 100 percent foreign ownership. It has also indicated a willingness to raise the existing 25 percent cap on total foreign investment in the financial sector, including both banks and insurers, to 50 percent. The United States, however, was unable to win any concessions that would allow banks to establish foreign branches in Russia – a primary demand of the U.S. banking sector.

President Bush's comments related to congressional "passage" of the bilateral agreement itself are somewhat misleading, as Congress does not "pass" a bilateral WTO accession agreement. Congress can, however, affect a country's WTO accession in two ways. First, Section 1106 of the Omnibus Trade and Competitiveness Act of 1988 (see attached chart) requires the President, when considering the WTO accession of countries like Russia, to negotiate an agreement addressing the operations of the country's state trading enterprises (STEs) when such companies might adversely affect U.S. economic interests. In this agreement, the acceding country commits that its STEs will act according to "commercial considerations" and will not discriminate against U.S. firms. However, if the President fails to complete

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the agreement, the United States will withhold the application of the WTO Agreement to the acceding country until Congress passes a law granting such treatment. Second, the United States must grant Permanent Normal Trade Relations (PNTR) to a country acceding to the WTO before the United States can receive the increased access to the country's market that WTO accession facilitates. (Under WTO rules, a WTO Member must give an acceding country unconditional, non-discriminatory access to its market in order to receive the same treatment from the acceding country. U.S. refusal to grant PNTR would deny Russia such access.) Although the congressional PNTR vote cannot hinder a country's accession to the WTO, it is a rhetorical symbol of an acceding country's "admission" into the global trading community, and countries do not like to accede to the WTO without PNTR.

President Bush's comments have not addressed Section 1106 or PNTR, but they perhaps indicate that USTR has not negotiated an agreement with Russia related to its STEs. USTR has also provided no indication of whether the parties have reached an agreement. If no Section 1106 agreement exists, then the prospects of congressional "passage" can directly influence the terms of the bilateral accession agreement. Congress has made strict IPR, financial services and agricultural market access demands which, if unmet, could lead it to oppose extension of the WTO Agreement to Russia. On the other hand, if the United States has negotiated a Section 1106 Agreement with Russia, then President Bush's statements relate to PNTR alone and are more of an excuse for the United States' refusal to give up on its bilateral demands than a real reason for its recalcitrance, which many observers attribute to geopolitical, rather than economic, concerns over Iran and North Korea. Bush's comments under this scenario would also fail to provide Russia with a real reason to make further commitments, as Russia can, at least in theory, still accede to the WTO without PNTR. Perhaps this explains why Russia continues to rebuff U.S. demands.

U.S. Banks Worried About U.S. Concessions in Potential Russia WTO Accession Deal

On July 13, 2006, the Bankers' Association for Finance and Trade (BAFT) stated it had not "given up hope" that the United States will not "give ground" to Russia on banking issues in U.S.-Russia bilateral negotiations as part of Russia's World Trade Organization (WTO) accession bid. BAFT representatives also stated that they will continue to pressure U.S. negotiators to demand that Russia allow foreign banks to establish branches and liberalize investment in its banking sector. Cory Strupp, BAFT general counsel, stated that "if Russia wants to be a member of the WTO, they ought to agree to certain fundamental principles to reduce trade barriers and open their markets," and that "if Russia can't work this out, it sets precedent not only in the context of the WTO negotiations but in the context of bilateral agreements."

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Under current Russian banking rules, a U.S. financial company wishing to establish operations in Russia must secure a host country charter and establish a separately incorporated Russian entity with a separate board of directors. U.S. companies are also unable to operate on the basis of their global capital and instead may use only the capital that they possess in Russia. Russia also limits the amount of foreign capital in the Russian banking system to 25 percent. Russia has offered to raise the cap on a discretionary basis to 50 percent as part of the bilateral accession negotiations, but U.S. financial services providers view that offer as too weak and seek instead the complete elimination of foreign investment caps.

Despite continued disagreement between the United States and Russia over issues such as bank branching, intellectual property rights (IPR) and agricultural market access, reports have emerged that U.S. negotiators are eager to complete Russia's bilateral accession agreement before the July 17 Group of Eight (G-8) summit in St. Petersburg. The Bush Administration therefore may be willing to concede the banking issue to finalize an agreement under this timeframe. WTO accession procedures mandate that acceding countries conclude bilateral market access deals with any WTO Member that requests negotiations. The United States is the only remaining country with which Russia has yet to conclude a bilateral deal but appears eager to conclude a deal in the near term, thus clearing the way for Russia to join the WTO. However, should U.S. negotiators conclude a bilateral agreement that fails to address U.S. banking and IPR concerns, the agreement will likely face harsh criticism from U.S. businesses and Congress. This criticism will likely translate into a contentious congressional battle over granting Russia Permanent Normal Trade Relations (PNTR) – a step that the United States must take before it can benefit from the increased access to the Russian market that Russia's WTO accession will provide. WTO "most favored nation" (MFN) rules require than all Members provide each other with unconditional, non-discriminatory access to their markets. PNTR would provide Russia with such access to the U.S. market.

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