ACKNOWLEDGEMENTS

The Office of the United States Trade Representative (USTR) is responsible for the preparation of this report, which was written by USTR staff. Acting U.S. Trade Representative Peter F. Allgeier gratefully acknowledges the contributions of the Departments of Agriculture, Commerce, Labor, Justice, State, Transportation and the U.S. International Trade Commission.

In preparing the report, substantial information was solicited from our Embassies abroad. Drafts of the report were circulated through the interagency Trade Policy Staff Committee. USTR is especially appreciative of the consistent support provided by the Commerce Department's International Trade Administration throughout the process of preparing the report.

Assistant U.S. Trade Representative for Policy Coordination:
Carmen Suro-Bredie

Project Director:
Donald W. Eiss

Project Advisors:
Laura S. Newport
Matthew Ekberg

Production Assistant:
Gloria D. Blue
Nicholas Miede
Matthew Toxey Vitart
Matthew Hornung

TABLE OF CONTENTS

LIST OF FREQUENTLY USED ACRONYMS

AD	Antidumping
AGOA	African Growth and Opportunity Act
APEC	Asia Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
ATC	Agreement on Textiles and Clothing
ATPA	Andean Trade Preferences Act
ATPDEA	Andean Trade Promotion & Drug Eradication Act
BIA	Built-In Agenda
BIT	Bilateral Investment Treaty
BOP	Balance of Payments
CACM	Central American Common Market
CAFTA	Central American Free Trade Area
CARICOM	Caribbean Common Market
CBERA	Caribbean Basin Economic Recovery Act
CBI	Caribbean Basin Initiative
CFTA	Canada Free Trade Agreement
CITEL	Telecommunications division of the OAS
COMESA	Common Market for Eastern & Southern Africa
CTE	Committee on Trade and the Environment
CTG	Council for Trade in Goods
CVD	Countervailing Duty
DDA	Doha Development Agenda
DSB	Dispute Settlement Body
EAI	Enterprise for ASEAN Initiative
DSU	Dispute Settlement Understanding
EU	European Union
EFTA	European Free Trade Association
FTAA	Free Trade Area of the Americas
FOIA	Freedom of Information Act
GATT	General Agreement on Tariffs and Trade
GATS	General Agreements on Trade in Services
GDP	Gross Domestic Product
GEC	Global Electronic Commerce
GSP	Generalized System of Preferences
GPA	Government Procurement Agreement
IFI	International Financial Institution
IPR	Intellectual Property Rights
ITA	Information Technology Agreement
LDBDC	Least Developed Beneficiary Developing Country
MAI	Multilateral Agreement on Investment
MEFTA	Middle East Free Trade Area

MERCOSUL/MERCOSUR	Southern Common Market
MFA	Multifiber Arrangement
MFN	Most Favored Nation
MOSS	Market-Oriented, Sector-Selective
MOU	Memorandum of Understanding
MRA	Mutual Recognition Agreement
NAFTA	North American Free Trade Agreement
NEC	National Economic Council
NIS	Newly Independent States
NSC	National Security Council
NTR	Normal Trade Relations
OAS	Organization of American States
OECD	Organization for Economic Cooperation and Development
OPIC	Overseas Private Investment Corporation
PNTR	Permanent Normal Trade Relations
ROU	Record of Understanding
SACU	Southern African Customs Union
SADC	Southern African Development Community
SPS	Sanitary and Phytosanitary Measures
SRM	Specified Risk Material
TAA	Trade Adjustment Assistance
TABD	Trans-Atlantic Business Dialogue
TACD	Trans-Atlantic Consumer Dialogue
TAEVD	Trans-Atlantic Environment Dialogue
TALD	Trans-Atlantic Labor Dialogue
TBT	Technical Barriers to Trade
TEP	Transatlantic Economic Partnership
TIFA	Trade & Investment Framework Agreement
TPRG	Trade Policy Review Group
TPSC	Trade Policy Staff Committee
TRIMS	Trade Related Investment Measures
TRIPS	Trade Related Intellectual Property Rights
UAE	United Arab Emirates
UNCTAD	United Nations Conference on Trade & Development
URAA	Uruguay Round Agreements Act
USDA	U.S. Department of Agriculture
USITC	U.S. International Trade Commission
USTR	United States Trade Representative
VRA	Voluntary Restraint Agreement
WAEMU	West African Economic & Monetary Union
WTO	World Trade Organization

FOREWORD

The 2005 National Trade Estimate Report on Foreign Trade Barriers (NTE) is the twentieth in an annual series that surveys significant foreign barriers to U.S. exports.

In accordance with section 181 of the Trade Act of 1974 (the 1974 Trade Act), as amended by section 303 of the Trade and Tariff Act of 1984 (the 1984 Trade Act), section 1304 of the Omnibus Trade and Competitiveness Act of 1988 (the 1988 Trade Act), section 311 of the Uruguay Round Trade Agreements Act (1994 Trade Act), and section 1202 of the Internet Tax Freedom Act, the Office of the U.S. Trade Representative is required to submit to the President, the Senate Finance Committee, and appropriate committees in the House of Representatives, an annual report on significant foreign trade barriers.

The statute requires an inventory of the most important foreign barriers affecting U.S. exports of goods and services, foreign direct investment by U.S. persons, and protection of intellectual property rights. Such an inventory facilitates negotiations aimed at reducing or eliminating these barriers. The report also provides a valuable tool in enforcing U.S. trade laws, with the goal of expanding global trade, which benefits all nations, and U.S. producers and consumers in particular.

The report provides, where feasible, quantitative estimates of the impact of these foreign practices on the value of U.S. exports. Information is also included on some of the actions taken to eliminate foreign trade barriers. Opening markets for American goods and services either through negotiating trade agreements or through results-oriented enforcement actions is this Administration's top trade priority. This report is an important tool for identifying such trade barriers.

SCOPE AND COVERAGE

This report is based upon information compiled within USTR, the U.S. Departments of Commerce and Agriculture, and other U.S. Government agencies, and supplemented with information provided in response to a notice in the *Federal Register,* and by members of the private sector trade advisory committees and U.S. Embassies abroad.

Trade barriers elude fixed definitions, but may be broadly defined as government laws, regulations, policies, or practices that either protect domestic products from foreign competition or artificially stimulate exports of particular domestic products. This report classifies foreign trade barriers into ten different categories. These categories cover government-imposed measures and policies that restrict, prevent, or impede the international exchange of goods and services. They include:

- Import policies (e.g., tariffs and other import charges, quantitative restrictions, import licensing, customs barriers);

- Standards, testing, labeling and certification (including unnecessarily restrictive application of sanitary and phytosanitary standards and environmental measures, and refusal to accept U.S. manufacturers' self-certification of conformance to foreign product standards);

- Government procurement (e.g., buy national policies and closed bidding);

- Export subsidies (e.g., export financing on preferential terms and agricultural export subsidies that displace U.S. exports in third country markets);

- Lack of intellectual property protection (e.g., inadequate patent, copyright, and trademark regimes);

- Services barriers (e.g., limits on the range of financial services offered by foreign financial institutions,[1] regulation of international data flows, and restrictions on the use of foreign data processing);

- Investment barriers (e.g., limitations on foreign equity participation and on access to foreign government-funded research and development (R&D) programs, local content and export performance requirements, and restrictions on transferring earnings and capital);

- Anticompetitive practices with trade effects tolerated by foreign governments (including anticompetitive activities of both state-owned and private firms that apply to services or to goods and that restrict the sale of U.S. products to any firm, not just to foreign firms that perpetuate the practices);

- Trade restrictions affecting electronic commerce (e.g., tariff and nontariff measures, burdensome and discriminatory regulations and standards, and discriminatory taxation); and

- Other barriers (barriers that encompass more than one category, e.g., bribery and corruption,[2] or that affect a single sector).

The NTE covers significant barriers, whether they are consistent or inconsistent with international trading rules. Many barriers to U.S. exports are consistent with existing international trade agreements. Tariffs, for example, are an accepted method of protection under the General Agreement on Tariffs and Trade (GATT). Even a very high tariff does not violate international rules unless a country has made a bound commitment not to exceed a specified rate. On the other hand, where measures are not consistent with international rules, they are actionable under U.S. trade law and through the World Trade Organization (WTO).

This report discusses the largest export markets for the United States, including: 56 nations, the European Union, Taiwan, Hong Kong, the Southern African Customs Union and one regional body. Some countries were excluded from this report due primarily to the relatively small size of their markets or the absence of major trade complaints from representatives of U.S. goods and services sectors. However, the omission of particular countries and barriers does not imply that they are not of concern to the United States.

In prior reports, most non-market economies also were excluded, since the trade barriers in those countries were qualitatively different from those found in other economies. However, as the economies of the republics of the former Soviet Union and most economies of the countries of Central Europe evolve away from central planning toward a market orientation, most of them have changed sufficiently to warrant an examination of their trade regimes. Where such examination has revealed trade barriers, those barriers have been included in this report. Based on an assessment of the evolving nature of U.S. trade and investment relationships in the various regions of the world, the following additional modifications were made to the report: (1) in recognition of their accession to the European Union, individual sections for Poland and Hungary have been dropped and these countries are treated as part of the European Union section; (2) the entry for the Gulf Cooperation Council has been replaced by the individual sectors for each of the Gulf Cooperation Council members; and (3) South Africa, along with Botswana, Lesotho, Namibia, and Swaziland, is treated as part of one NTE section for the Southern African Custom Union.

The merchandise trade data contained in the NTE report are based on total U.S. exports, free alongside (f.a.s.)[3] value, and general U.S. imports, customs value, as reported by the Bureau of the Census, Department of Commerce. (NOTE: These data are ranked according to size of export market in the Appendix). The services data are from the October 2004 issue of the Survey of Current Business (collected from the Bureau of Economic Analysis, Department of Commerce). The direct investment data are from the September 2004 issue of the Survey of Current Business (collected from the Bureau of Economic Analysis, Department of Commerce).

TRADE IMPACT ESTIMATES AND FOREIGN BARRIERS

Wherever possible, this report presents estimates of the impact on U.S. exports of specific foreign trade barriers or other trade distorting practices. However, it must be understood that these estimates are only approximations. Also, where consultations related to specific foreign practices were proceeding at the time this report was published, estimates were excluded, in order to avoid prejudice to those consultations.

The estimates included in this report constitute an attempt to assess quantitatively the potential effect of removing certain foreign trade barriers on particular U.S. exports. However, the estimates cannot be used to determine the total effect upon U.S. exports to either the country in which a barrier has been identified or to the world in general. In other words, the estimates contained in this report cannot be aggregated in order to derive a total estimate of gain in U.S. exports to a given country or the world.

Trade barriers or other trade distorting practices affect U.S. exports to another country because these measures effectively impose costs on such exports that are not imposed on goods produced domestically in the importing country. In theory, estimating the impact of a foreign trade measure upon U.S. exports of goods requires knowledge of the (extra) cost the measure imposes upon them, as well as knowledge of market conditions in the United States, in the country imposing the measure, and in third countries. In practice, such information often is not available.

Where sufficient data exist, an approximate impact of tariffs upon U.S. exports can be derived by obtaining estimates of supply and demand price elasticities in the importing country and in the United States. Typically, the U.S. share of imports is assumed to be constant. When no calculated price elasticities are available, reasonable postulated values are used. The resulting estimate of lost U.S. exports is approximate, depends upon the assumed elasticities, and does not necessarily reflect changes in trade patterns with third countries. Similar procedures are followed to estimate the impact upon our exports of subsidies that displace U.S. exports in third country markets.

The task of estimating the impact of nontariff measures on U.S. exports is far more difficult, since there is no readily available estimate of the additional cost these restrictions impose upon imports. Quantitative restrictions or import licenses limit (or discourage) imports and thus raise domestic prices, much as a tariff does. However, without detailed information on price differences between countries and on relevant supply and demand conditions, it is difficult to derive the estimated effects of these measures upon U.S. exports. Similarly, it is difficult to quantify the impact upon U.S. exports (or commerce) of other foreign practices such as government procurement policies, nontransparent standards, or inadequate intellectual property rights protection.

In some cases, particular U.S. exports are restricted by both foreign tariff and nontariff barriers. For the reasons stated above, it may be difficult to estimate the impact of such nontariff barriers on U.S. exports. When the value of actual U.S. exports is reduced to an unknown extent by one or more than one nontariff measure, it then becomes derivatively difficult to estimate the effect of even the overlapping tariff barriers on U.S. exports.

The same limitations that affect the ability to estimate the impact of foreign barriers upon U.S. goods exports apply to U.S. services exports. Furthermore, the trade data on services exports are extremely limited and of questionable reliability. For these reasons, estimates of the impact of foreign barriers on trade in services also are difficult to compute.

With respect to investment barriers, there are no accepted techniques for estimating the impact of such barriers on U.S. investment flows. For this reason, no such estimates are given in this report. The NTE includes generic government regulations and practices which are not product-specific. These are among the most difficult types of foreign practices for which to estimate trade effects.

In the context of trade actions brought under U.S. law, estimations of the impact of foreign practices on U.S. commerce are substantially more feasible. Trade actions under U.S. law are generally product-specific and therefore more tractable for estimating trade effects. In addition, the process used when a specific trade action is brought will frequently make available non-U.S. Government data (U.S. company or foreign sources) otherwise not available in the preparation of a broad survey such as this report.

In some cases, industry valuations estimating the financial effects of barriers are contained in the report. The methods computing these valuations are sometimes uncertain. Hence, their inclusion in the NTE report should not be construed as a U.S. Government endorsement of the estimates they reflect.

March 2005

Endnotes

1. The current NTE report covers only those financial services-related market access issues brought to the attention of USTR by outside sources. For the reader interested in a more comprehensive discussion of financial services barriers, the Treasury Department publishes quadrennially the National Treatment Study. Prepared in collaboration with the Secretary of State, the Office of the Comptroller of the Currency, the Federal Reserve Board, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission, and the Department of Commerce, the Study analyzes in detail treatment of U.S. commercial banks and securities firms in foreign markets. It is intended as an authoritative reference for assessing financial services regimes abroad.

2. Corruption is an impediment to trade, a serious barrier to development, and a direct threat to our collective security. Corruption takes many forms and affects trade and development in different ways. In many countries, it affects customs practices, licensing decisions, and the awarding of government procurement contracts. If left unchecked, bribery and corruption can negate market access gained through trade negotiations, undermine the foundations of the international trading system, and frustrate broader reforms and economic stabilization programs. Corruption also hinders development and contributes to the cycle of poverty.

Information on specific problems associated with bribery and corruption is difficult to obtain, particularly since perpetrators go to great lengths to conceal their activities. Nevertheless, a consistent complaint from U.S. firms is that they have experienced situations that suggest corruption has played a role in the award of billions of dollars of foreign contracts and delayed or prevented the efficient movement of goods. Since the United States enacted the Foreign Corrupt Practices Act (FCPA) in 1977, U.S. companies have been prohibited from bribing foreign public officials, and numerous other domestic laws discipline corruption of public officials at the state and federal levels. The United States is committed to the active enforcement of the FCPA.

The United States Government has taken a leading role in addressing bribery and corruption in international business transactions and has made real progress over the past quarter century building international coalitions to fight bribery and corruption. Bribery and corruption are now being addressed in a number of fora. Some of these initiatives are now yielding positive results.

The United States Government led efforts to launch the Organization for Economic Cooperation and Develpoment (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (Antibribery Convention). In November 1997, the United States and 33 other nations adopted the Antibribery Convention, which currently is in force for 36 countries, including the United States. The Antibribery Convention obligates its parties to criminalize the bribery of foreign public officials in the conduct of international business. It is aimed at proscribing the activities of those who offer, promise, or pay a bribe. (For additional information, see www.export.gov/tcc and www.oecd.org).

The United States played a critical role in the successful conclusion of negotiations that produced the United Nations Convention Against Corruption, the first global anti-corruption instrument. The Convention was opened for signature in December 2003, and is pending entry into force. The Convention requires countries to adopt such measures as may be necessary to criminalize fundamental anticorruption offenses, including bribery of domestic as well as foreign public officials. As of early March 2005, one hundred eighteen countries, including the United States, have signed the Convention and nineteen have ratified it.

In March 1996, countries in the Western Hemisphere concluded negotiation of the Inter-American Convention Against Corruption (Inter-American Convention). The Inter-American Convention, a direct result of the Summit of the Americas Plan of Action, requires that parties criminalize bribery throughout the region. The Inter-American Convention entered into force in March 1997. The United States signed the Inter-American Convention on June 2, 1996 and deposited its instrument of ratification with the Organization of American States (OAS) on September 29, 2000. Twenty-eight of the thirty-three parties to the Inter-American Convention, including the United States, participate in a Follow-up Mechanism conducted under the auspices of the OAS to monitor implementation of the Convention. The Inter-American Convention addresses a broad range of corrupt acts including domestic corruption and transnational bribery. Signatories agree to enact legislation making it a crime for individuals to offer bribes to public officials and for public officials to solicit and accept bribes, and to implement various preventive measures.

The United States Government continues to push its anti-corruption agenda forward. Consistent with the Bipartisan Trade Promotion Authority Act of 2002 (TPA), the United States Government is seeking and obtaining binding commitments in free trade agreements (FTAs) that promote transparency and that specifically address corruption of public officials. Also consistent with TPA, the United States Government is seeking to secure a meaningful agreement on trade facilitation int eh World Trade Organization and has been pressing for concrete commitments on customs operations and transparency of government procurement ergimes of our FTA partners. The United States Government is also playing a leadership role on these issues in the G-8 Forum, the Asia Pacific Economic Cooperation (APEC) Forum, the Southeastern Europe Stability Pact and other fora.

3. Free alongside (f.a.s.): Under this term, the seller quotes a price, including delivery of the goods alongside and within the reach of the loading tackle (hoist) of the vessel bound overseas.

ANGOLA

TRADE SUMMARY

The U.S. trade deficit with Angola was $3.9 billion in 2004, an increase of $151 million from $3.8 billion in 2003. U.S. goods exports in 2004 were $594 million, up 21.1 percent from the previous year. Corresponding U.S. imports from Angola were $4.5 billion, up 6.0 percent. Angola is currently the 68th largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Angola in 2003 was $1.5 billion, the same as in 2002. U.S. FDI in Angola is primarily concentrated in the petroleum sector.

IMPORT BARRIERS

Tariffs and Non-Tariff Barriers

Angola is a member of the WTO, the Common Market for Eastern and Southern Africa (COMESA), and the Southern African Development Community (SADC). In March 2003, Angola agreed to adhere to the SADC Free Trade protocol that seeks to facilitate trade by harmonizing and reducing tariffs and by establishing regional policies on trade, customs, and methodology. The protocol has not yet been implemented.

The government recently announced a new customs law outlining revised duty rates that came into effect in January 2005. The new program reduces tariff barriers by eliminating duties on basic products like rice, wheat flour and beans, and reduces other duties from 5 percent to 10 percent. Customs duties fall into one of six categories ranging from as low as 2 percent, which applies to raw materials necessary for the nation’s development, up to 30 percent. Additional fees include clearing costs (2 percent), VAT (2 percent to 30 percent depending on the good), revenue stamp (0.5 percent), port charges ($500/20 foot container or $850/40 foot container), and port storage fees (free for the first 15 days). In December 2004, the government announced a new special customs regime for the port of Cabinda, which eliminates import and export duties for Cabinda province. The new regime does not apply to the petroleum industry, or to passenger vehicles, alcoholic beverages, tobacco and jewelry.

Customs Barriers

Administration of Angola’s customs department has improved in the last few years. In 2002, the Angolan government hired the British company Crown Agents to improve its customs clearance practices and, as a result, the average port clearance time has fallen from several months to less than two weeks. Required customs paperwork includes the “Documento Unico” (single document), proof of ownership of the good, bill of lading, commercial invoice, packaging list, and specific shipment documents verifying the right to import or export the product.

Pre-shipment inspection (PSI) by BIVAC International is required for imports of goods valued at more than $5,000. Imports without proper PSI documentation may be charged duties of up to 100 percent *ad valorem*. However, art, antiques, precious metals and stones, cinematographic films, newspapers and periodic publications, and other items defined by law are generally exempted from PSI review. U.S. exporters have complained of over-valuation of goods. Despite a September 2003 announcement that it would be abandoning its PSI system, Angola later reversed its position in favor of keeping PSI for the foreseeable future.

The importation into Angola of certain goods requires an import license issued by the Ministry of Trade. The import license is renewable annually and covers any good imported by the licensed importer. The importation of certain goods also requires specific authorization from various government ministries, which can delay the customs clearance process. Goods that require ministerial authorization include: pharmaceutical substances and saccharine and derived products (Ministry of Health); radios, transmitters, receivers, and other devices (Ministry of Post and Telecommunications); weapons, ammunitions, fireworks, and explosives (Ministry of Interior); plants, roots, bulbs, germs, buds, fruits, seeds, and crates and other packages containing these products (Ministry of Agriculture); fiscal or postal stamps (Ministry of Post and Telecommunications); poisonous and toxic substances and drugs (Ministries of Agriculture, Industry, and Health); and samples or other goods imported to be given away (Customs).

If they present a letter from the Minister of Petroleum or Mines, companies operating in the oil and mining industries may import, without duty, equipment to be used exclusively for oil and mine exploration.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

Angola has adopted SADC guidelines on biotechnology, which effectively prohibit imports of biotechnology grain or seed until regulatory systems governing biotechnology have been developed. Angola requires milling or sterilization (i.e. a process that renders the grain incapable of germinating) of whole grain food aid shipments that may contain biotechnology products.

Angola does not currently enforce any labeling law. In early 2003, the Ministry of Industry issued a decree that requires labeling in Portuguese, but the rule has not been implemented. In practice, imports are admitted into the country with little reference to health, testing, or weight standards.

GOVERNMENT PROCUREMENT

Angola is not a signatory to the WTO Agreement on Government Procurement. The Government of Angola solicits bids for supplies and services in local and international publications 15 days to 90 days before the bids are due. Bid documents are normally obtained from a specific government ministry, department, or agency for a non-refundable fee. Completed bids, accompanied by a specified security deposit, are usually submitted directly to the ministry in question. The bidding process often does not meet international standards of objectivity and transparency. In addition, information about government projects and tenders is not often readily available from the appropriate authorities, and the interested parties must spend considerable time on research. Under the Promotion of Angolan Private Entrepreneurs Law, the government gives Angolan companies preferential treatment in tendering for goods, services and public works contracts.

Some U.S. firms that have won bids to sell goods or services to the government or parastatal companies have experienced delays ranging from months to years in receiving payment or have received reduced payments.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Although Angola has basic intellectual property rights protection and is working to strengthen existing legislation and enforcement, current protection is weak due to a lack of capacity. Intellectual property rights are regulated by the Ministry of Industry (trademarks, patents, and designs), and by the Ministry of Culture (authorship, literary, and artistic rights). Intellectual property is protected by Law 3/92, for industrial property and Law 4/90 for the attribution and protection of copyrights.

Angola is a member of the World Intellectual Property Organization and uses its international classification system to identify and codify requests for patents and for the registration of trademarks. Each petition for a patent that is accepted is subject to a fee that varies by type of patent requested. Angola’s legislature approved the Paris Convention for the Protection of Industrial Property in June 2003. No suits involving U.S. intellectual property are known to have been filed in Angola.

SERVICES BARRIERS

Foreign participation in the services sector is generally not restricted. The banking sector comprises the bulk of the services sector and has grown substantially over the past two years, with Portuguese banks leading the expansion and South African banks not far behind. The underdeveloped banking sector collects most of its profits from service fees, largely in foreign exchange transactions. Years of non-transparent lending, a lack of qualified human resources, and unclear regulations have led to a high rate of non-performing loans. Deposits fluctuate in monthly cycles because many companies keep only enough money in Angolan banks to meet cash needs, thereby inhibiting banks from making long-term loans. As a result of increasing competition and experience, banking services are improving. In addition to banks, Angola's financial sector is expected to have three insurance companies by the beginning of 2005, partly in response to new laws requiring automotive, aviation, and worker safety insurance.

INVESTMENT BARRIERS

Angola is officially open to foreign investment, but its regulatory and legal infrastructure is inadequate to facilitate direct investment and provide sufficient protection. Angola created a National Private Investment Agency (ANIP) in July 2003 to assist investors and facilitate new investment. In 2003, the Angolan government replaced the 1994 Foreign Investment Law with the Law on Private Investment (Law 11/03). Law 11/03 lays out the general parameters, benefits, and obligations for foreign investment in Angola, and recognizes that investment plays a vital role in the country's economic development. It seeks to encourage foreign investment by providing equal treatment for domestic and foreign investors, offering fiscal and customs incentives, simplifying the investment application process, and lowering the required investment capital. Nevertheless, the new investment law is vague on profit repatriation and includes weak legal safeguards to protect foreign investors. The law also does not allow for international arbitration and requires that any investment dispute be handled in Angolan courts. A Voluntary Arbitration Law that provides the legal framework for non-judicial resolution of disputes has not yet been approved.

The old Foreign Investment Law expressly prohibited foreign investment in the areas of defense, internal public order, and state security; banking activities relating to the operations of the Central Bank and the Mint; the administration of ports and airports; and other areas considered by law to be the State's exclusive responsibility. Although Law 11/03 does not explicitly restate these prohibitions, these areas are assumed to be off-limits to investors. Investments benefit from a more standardized set of incentives under the Law on Tax and Customs Incentives for Private Investment, approved by the National Assembly in July 2003. Companies should apply for these incentive benefits when negotiating with ANIP.

Although the new investment law is part of an overall effort by the Angolan government to create a more investor-friendly environment, the process by which this and similar laws are developed is often shrouded in secrecy and generally not open to public review prior to enactment. Many laws governing the economy have vague provisions that permit wide interpretation and application by the government across sectors. Investments in the petroleum, diamond, and financial sectors continue to be governed by specific legislation. Foreign investors can set up fully-owned subsidiaries in many sectors, but frequently are strongly encouraged, though not formally required, to take on local partners.

Obtaining the proper permits and business license to operate in Angola is time-consuming and adds to the cost of investing. In 2004 the World Economic Forum ranked Angola 103 out of 104 countries in terms of global business competitiveness, and a World Bank study identified Angola as one of the most time-consuming countries in the world to establish a business, requiring 146 days compared to a regional average of 63 days. According to the new investment law, ANIP and the Council of Ministers should take no more than two months to approve a contract with an investor, but in practice this process normally takes two to three months. After contract approval, the company must register and file paperwork with the relevant government ministries. In August 2003, the government established a one-stop shop, or "Guiche Unico," to simplify the process and reduce the time required to register a company. Despite a rocky start, the "Guiche Unico" is working better and faster and has reduced the time it takes to register a company.

Plans for future oil investment have been chilled by a proposed foreign exchange law governing the petroleum sector that would direct all oil revenue into the Angolan banking system, thereby negating the right to repatriate profits. Following protests by the major oil companies, the central bank is negotiating a moderated version of the legislation to be presented to the oil companies in early 2005.

ELECTRONIC COMMERCE

Due to the 27-year civil war, Angola has been late to join the computer and Internet development process, leaving access to computers and the Internet very low. Access to computers and the Internet in workplaces is increasing but remains a rarity. A small number of Internet cafes exist in Luanda and a few major provincial cities; high-speed Internet is now available, albeit at extraordinarily high prices. Thirteen Angolan companies currently provide Internet service, up from five the previous year, and several Angolan companies are licensed to sell computers. The country's basic telecommunications law governs information technology but includes no specific regulations regarding electronic commerce.

OTHER BARRIERS

Corruption

Petty corruption is prevalent due to extremely low civil service salaries, dependence on a centralized bureaucracy and antiquated regulations dating back to the Portuguese colonial era. Procedures to register a company are complicated and may involve 14 steps with many different government ministries, thus giving rise to rent-seeking opportunities. Investors are often tempted to seek quicker service and approval by paying gratuities and other facilitation fees. Bribery has become less of a problem in the customs department under Crown Agent's management.

Angola's public and private companies have not traditionally used transparent accounting systems consistent with international norms, and few companies in Angola employ international audit standards. The government approved an audit law in 2002 that sought to require audits for all "large" companies, but it has not yet been possible to enforce this rule due to the lack of a professional accounting institute.

Investors have at times experienced harassment, political interference in their business dealings, and pressure to sell their investments. In some cases, these practices have involved individuals with powerful positions within the government who exert pressure directly or through the established bureaucracy, which is often a passive conduit. As a result, some investors have experienced significant delays in payments from government contracts and delays in obtaining the proper permits or approval of projects.

Recovering from War

Angola's destroyed or badly damaged infrastructure from its 27-year civil war substantially increases the cost of doing business. The country is in the process of rebuilding its communications, energy, transportation, and road infrastructure. The government is placing particular emphasis on electricity sector development. Domestic and international communications, while improving, are difficult and costly. The cell phone network is oversubscribed and unreliable, having grown by 400 percent over the past two years, but coverage is improving and reached all provincial capitals by the end of 2004. There are frequent interruptions in the power and water supplies. As a result, investors face additional costs to support their businesses, such as paying for security, back-up electricity generators, and water tanks.

ARAB LEAGUE

The Arab League boycott of Israel is a significant barrier to U.S. trade and investment in some countries in the Middle East and North Africa. Arab League members include the Palestinian Authority and the following states: Algeria, Comoros, Djibouti, Egypt, Iraq, Jordan, Lebanon, Libya, Mauritania, Morocco, Somalia, Sudan, Syria, Tunisia, Yemen, and the Gulf Cooperation Council (GCC) countries (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates). The United States continues to oppose the boycott, and U.S. government officials have urged Arab League members to end its enforcement. Toward that goal, U.S. embassies and government officials raise the boycott with host country officials, noting the persistence of illegal boycott requests and the impact on both U.S. firms and on the countries' ability to expand trade and investment. Under U.S. antiboycott legislation enacted in 1978, U.S. firms are prohibited from responding to any request for information that is designed to determine compliance with the boycott, and are required to report receipt of any such request to the U.S. Department of Commerce's Office of Antiboycott Compliance (OAC).

The primary aspect of the boycott prohibits the importation of Israeli-origin goods and services into boycotting countries. This conflicts with the obligation of Arab League member states that are also members of the World Trade Organization to treat Israeli imports on a Most Favored Nation (MFN) basis. The secondary and tertiary aspects of the boycott discriminate against U.S. and other foreign firms that wish to do business with both Israel and boycotting countries. These constrain U.S. exports to the region. The secondary aspect of the boycott prohibits individuals – and private and public sector firms and organizations – in Arab League countries from engaging in business with U.S. and other foreign firms that contribute to Israel's military or economic development. Such firms are placed on a blacklist maintained by the Damascus-based Central Boycott Office (CBO), a specialized bureau of the Arab League. The tertiary aspect of the boycott prohibits business dealings with U.S. and other firms that do business with blacklisted companies.

While the legal structure of the boycott in the Arab League remains unchanged, its enforcement varies widely from country to country. Some member governments of the Arab League have consistently maintained that only the Arab League as a whole can revoke the boycott. Other member governments support the view that adherence to the boycott is a matter of national discretion, and a number of states have taken steps to dismantle some aspects of it.

Enforcement of the boycott remains the responsibility of individual member states and enforcement efforts vary widely from country to country. Egypt has not enforced any aspect of the boycott since 1980, pursuant to its peace treaty with Israel, although U.S. firms occasionally find some government agencies using outdated forms containing boycott language. Jordan ended its enforcement of the boycott with the signing of its peace treaty with Israel in 1994. Algeria, Morocco, Tunisia, and the Palestinian Authority do not enforce the boycott.

In September 1994, the GCC countries announced an end to the secondary and tertiary aspects of the Arab League boycott of Israel, eliminating a significant trade barrier to U.S. firms. In December 1996, the GCC countries recognized the total dismantling of the boycott as a necessary step to advance peace and promote regional cooperation in the Middle East and North Africa. Although all GCC states are complying with these stated plans, some commercial documentation continues to contain boycott language. U.S. companies are required to notify the U.S. Department of Commerce's Office of Antiboycott Compliance when they receive such documentation.

Bahrain does not have any restrictions on trade with U.S. companies that have relations with Israeli companies. Outdated tender documents in Bahrain occasionally refer to the secondary and tertiary aspects of the boycott, but such instances are usually quickly remedied. Israeli products are reported to occasionally be found in the Bahraini market. Kuwait no longer applies a secondary boycott of firms doing business with Israel, and has taken steps to eliminate all direct references to the boycott of Israel in its commercial documents. Kuwait still applies a primary boycott of goods and services produced in Israel.

In January 1996, Oman and Israel signed an agreement to open trade missions in each country. However, in October 2000, following the outbreak of the second Intifada, Oman and Israel suspended these missions. Omani customs formerly processed Israeli-origin shipments entering with Israeli customs documentation. However, Omani firms have recently reportedly avoided marketing any identifiably Israeli consumer products. Israeli immigration stamps in third country passports are not an issue. Telecommunications links and mail flow normally between the two countries. In April 1996, Qatar and Israel agreed to exchange trade representation offices. The Israeli trade office opened in May 1996 and remains open. Qatar does not practice the Arab Boycott, but some government tender documents and laws still include outdated boycott language.

Saudi Arabia enforces only the primary level of the Arab League boycott on Israeli products. If a foreign company is found to have imported an Israeli-made product, or a product with some Israeli content, the Saudis will ban that company from exporting to the Kingdom. Usual practice has been that the Saudi government will remove its ban after the company agrees to stop shipping Israeli products. In 2003, according to press reports, Saudi Arabia banned three American companies for violating the primary boycott.

U.S. firms have faced boycott requests in the United Arab Emirates as a result of bureaucratic and administrative inefficiencies, rather than efforts to circumvent UAE government policy not to enforce the secondary and tertiary aspects of the boycott. The UAE is taking steps to eliminate these prohibited boycott requests.

ARGENTINA

TRADE SUMMARY

The U.S. goods trade deficit with Argentina was $359 million in 2004, a decrease of $473 million from $732 million in 2003. U.S. goods exports in 2004 were $3.4 billion, up 39 percent from the previous year. Corresponding U.S. imports from Argentina were $3.7 billion, up 18.2 percent. Argentina is currently the 31st largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Argentina were $68 million in 2003, and U.S. imports were $751 million.

The stock of U.S. foreign direct investment (FDI) in Argentina in 2003 was $11.0 billion, down from $11.2 billion in 2002. U.S. FDI in Argentina is concentrated largely in the manufacturing, finance, and mining sectors.

IMPORT POLICIES

Argentina made significant progress in reducing tariffs and non-tariff barriers during the 1990's, including in the areas of investment and government procurement. Starting in late 2000, however, the government implemented new trade policies and overturned old trade policies frequently enough to foster uncertainty and confusion in the exporting and importing community.

During 2003, most of the exchange controls for imports imposed during the 2002 crisis were relaxed or abolished. Imports can now be paid for in advance, regardless of the type of good involved. However, importers must show that imported products entered Argentina within 360 days of payment. There are no restrictions on payments for services imports (such as freight, insurance, technical assessment, and professional fees). Foreign currency earned through exports may be used for foreign debt payments if the debt was accrued prior to December 2001. Purchases of foreign currency to settle debts owed to foreign creditors are permitted within 15 days of each scheduled payment. Purchases of foreign currency to pay dividends are permitted once the balance sheets are finished and audited.

There are special rules for establishing the clearance of foreign currency in the local exchange markets for new private debt in foreign currency, and for the private issuance of bonds denominated in foreign currency.

Hard currency export earnings, both from goods and services, must be cleared in the local foreign exchange market with exceptions, and there are time limits to fulfill this obligation (from approximately 130 to 350 working days for goods, depending on the goods involved, and 105 working days for services). There are more liberal time limits for certain capital goods and situations where exports receive long-term financing. The foreign exchange clearance requirement does not apply to exports of certain minerals or for exports to Argentine foreign trade zones, and is limited to 30 percent of total revenues for hydrocarbons exports.

Imports of used clothing are prohibited except for donations to government or religious organizations. Argentina also prohibits the importation and sale of used tires, re-manufactured automotive parts, and used or refurbished medical equipment, such as imaging equipment. Imports of television sets from the Manaus Industrial Zone were restricted by safeguards.

Tariffs

Argentina's average applied tariff was 13 percent in 2004. Argentina is a member of MERCOSUR, a customs union comprising Argentina, Brazil, Paraguay, and Uruguay. Full CET product coverage is scheduled for implementation in 2006. CET tariffs range from zero percent to 35 percent *ad valorem*, with a limited number of country-specific exceptions. A temporary CET surcharge applied to most imports since 1997 was abolished by Argentina on September 6, 2004.

A statistical fee of 0.5 percent is added to most imports (90 percent of all harmonized system tariff lines). Export taxes average 5.3 percent, and exporters may claim reimbursement for some domestically paid taxes. The average reimbursement for exporters is 4.2 percent. Toys, footwear, and textiles are subject to both *ad valorem* and specific tariffs. High specific duties on Chinese toys, non-sport footwear, and textiles were imposed in October 2001, which affects U.S. firms established in Argentina that use inputs from China. In December 2001, Ministry of Economy Resolution 825/2001 established a phase-out program, according to which these duties should be equivalent to a maximum 35 percent *ad valorem* tariff by January 2007.

Import Licensing

Argentina implemented a non-automatic import license requirement during 2004, which affects imports of textiles, refrigerators, and washing machines. However, import licenses are not required for textiles produced by companies in Brazil and Argentina when the Argentine and Brazilian companies have reached private agreements that restrain the two-way trade in textiles. There is also an automatic license requirement for most footwear imports. The Argentine government says this requirement is needed for informational purposes, but the private sector claims that it is an obstacle to trade. Ministry of Economy Resolution 495/2004 modified a 2003 resolution and established minimum specific import duties on shoe imports on July 22, 2004, to be in force for 180 days. These import duties do not apply to imports from MERCOSUR countries and cannot exceed the equivalent of a 35 percent *ad valorem* tariff.

Customs Procedures

Argentina abides by the WTO Agreement on Customs Valuation. In October 2001, Argentina eliminated a pre-shipment inspection (PSI) regime that U.S. exporters considered an obstacle to legitimate trade. Argentina has import monitoring mechanisms, similar to an import licensing regime, that affect roughly one-fifth of its imports, principally textiles, toys and footwear. U.S. firms complain of cumbersome certificate of origin requirements, particularly in the electronics and textile sectors.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Agricultural Products

Since 2002, Argentina has prohibited the import of beef and beef products from the United States due to concerns about bovine spongiform encephalopathy (BSE). These unjustified prohibitions continue in place without a science-based risk assessment. In addition, Argentina's prohibitions are inconsistent with the relevant international standard. These restrictions effectively eliminate U.S. exports of beef and products containing beef including pet food.

Also in 2002, Argentina banned the import of chicken products from the United States. Argentina's decision was based on an outbreak of Newcastle's Disease in California, Nevada, and Arizona, which has been controlled. In August 2004, the United States requested that Argentina restore market access for poultry and poultry products from those regions of the United States that are disease-free. This ban has affected an estimated $5 million annually in potential U.S. exports of poultry products. Argentina has not responded to this request.

Argentina maintains unjustified restrictions on U.S. exports of swine genetics. In addition, Argentina has continued to delay issuing the final approval for expanding the areas in the United States authorized to export citrus fruit.

Non-agricultural Products

Argentina began mandating compliance with new safety certifications on a wide range of products in early 1998, affecting U.S. exports of low voltage electrical products (household appliances, electronics products and electrical materials), toys, covers for dangerous products, gas products, construction steel, personal protective equipment and elevators. The procedures for compliance often appear to many business people to be inconsistent, redundant and non-transparent. Regulations that require product testing can be cumbersome and costly and are especially problematic for US small and medium-sized companies. The most restrictive requirements were supposed to have been in effect by the end of 2002, but this was postponed until December 31, 2003, and again until December 31, 2004 (this time by Technical Coordination Secretariat Resolution 33/2004). Argentina's certificate of origin regulations require separate certificates for each of the countries involved in manufacturing the various components of a final product. Originally, Argentina failed to fulfill the notification and comment requirements of the WTO Agreement on Technical Barriers to Trade (TBT) in its development of these measures.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Argentina was placed on the 2004 Special 301 Priority Watch List because of serious concerns over the lack of adequate protection for copyright and patents. In addition, unauthorized use of protected seed varieties remains a problem.

Patents

In May 1999, the United States initiated a WTO case against Argentina because of, *inter alia*, its failure to protect patents and test data. The United States added additional claims in May 2000, when further TRIPS obligations came into force. In April 2002, the United States and Argentina reached a partial settlement, in which Argentina clarified certain aspects of its IP system and undertook to pass certain legislative amendments to, *inter alia*, provide for process patent protection and to ensure that preliminary injunctions are available in IP court proceedings. However, Argentina still does not provide adequate protection for undisclosed test data submitted by research-based pharmaceutical companies for marketing approval. Consultations continue with respect to the remaining unresolved issues, and the United States retains its right to seek resolution under the WTO dispute settlement mechanism, if necessary.

The National Intellectual Property Institute (INPI) started to approve pharmaceutical patents in October 2000. INPI has been extremely slow since that time in issuing pharmaceutical patents to products with commercial value. INPI implemented fast-track procedures to reduce the large patent application backlog in early 2004.

Copyrights

Argentina's copyright laws generally provide good protection. Argentina adopted legislation in 1999 to ratify the World Intellectual Property Organization (WIPO) Copyright Treaty and the WIPO Performances and Phonograms Treaty, though some implementation issues exist. The Argentine government has also yet to fully comply with an agreement with the private sector to prevent the use of unlicensed software in government offices.

Enforcement of copyrights on recorded music, videos, books, and computer software remains inconsistent. Argentine Customs and other government authorities generally cooperate with industry efforts to stop shipments of pirated merchandise, but inadequate resources and multiple and slow court procedures have hampered the effectiveness of enforcement efforts. The legal framework regarding Internet piracy provides few incentives to investigate and punish those who post infringing materials. Inadequate border controls, particularly at the Paraguayan/Brazilian border, further contribute to the regional circulation of pirated goods.

SERVICES BARRIERS

Argentina enacted broad liberalization in the services sector as part of its economic reform program in the 1990s, but some barriers continue to exist. For example, the Argentine Government obliges cable/pay television operators to register their programming with a government body. This government body imposed restrictions on the frequency of advertisements on cable-TV providers. In addition, restrictions regarding the showing, printing and dubbing of films have burdened U.S. exports, as has the practice of charging *ad valorem* customs duties based on the previously estimated value of the content, rather than solely on the value of the physical materials being imported.

In the WTO, Argentina has committed to allow foreign suppliers of non-insurance financial services to establish all forms of commercial presence and has committed to provide substantially full market access and national treatment to foreign suppliers of non-insurance financial services. The only significant remaining issue involves lending limits for foreign bank branches that are based on local paid-in capital, not parent bank capital. This effectively removes the rationale for establishing in branch form. This issue has become largely moot due to the ongoing banking crisis that began in December 2001 with the freezing of bank accounts and the subsequent devaluation and asymmetric pesification of deposits, loans and other assets.

There are nationality restrictions for some internal shipping, private security, and education providers. Provinces can impose their own barriers on the provision of services.

INVESTMENT BARRIERS

Upon becoming a Member of the WTO, Argentina notified the WTO of measures inconsistent with its obligations under the WTO Agreement on Trade-Related Investment Measures (TRIMS). These measures deal with local content and trade balancing in the automotive industry. Proper notification allowed developing country WTO Members, including Argentina, to maintain such measures for a five-year transitional period, ending January 1, 2000. In November 2001, the WTO granted an extension to the TRIMS transitional period that allowed Argentina and several other countries to maintain measures inconsistent with TRIMS until December 31, 2003. Argentina apparently maintained some measures that may be inconsistent with the TRIMS Agreement past the 2003 deadline. The United States is consulting on next steps with U.S. industry and with the Argentine government.

In mid-2003, the Argentine Congress passed the Cultural Assets Preservation Law, which established an ownership cap of 30 percent for investment in media enterprises by foreign nationals. Excluded from the ownership limitation were existing investors and investors from countries in which Argentine nationals may own more than 30 percent of media firms. The 2003 legislation provides that prior law, under which there was no ownership cap, will continue to apply to foreign investments made before the passage of the new legislation. The new ownership limitations, however, will apply to any future foreign investments (including changes in ownership) in the media sector.

Under the United States-Argentina Bilateral Investment Treaty (BIT), which entered into force in 1994, investors of either country may seek binding international arbitration of claims that a host government violated certain obligations of the treaty. Several U.S. investors have initiated dispute settlement under the BIT in response to measures imposed by Argentina during the financial crisis that began in 2001. Most of the disputes relate to Argentine measures affecting investors in the utilities and energy sectors. Among other things, the Argentine government set utility tariff rates to be denominated in pesos in early 2002, and has kept many rates frozen since then, despite the fact that many utilities owe dollar-denominated debt to offshore creditors. The Argentine government has also pressured power companies to invest amounts alleged to be owed to them by the government into power plants that the government wants to construct.

ELECTRONIC COMMERCE

Argentina has taken steps to lower the cost of Internet usage and has shown interest in U.S. electronic commerce initiatives in the FTAA and the WTO. The United States and Argentina signed a bilateral initiative in 2000 to promote the growth of electronic commerce. Despite supporting electronic commerce, Argentina does not participate in the WTO Information Technology Agreement (ITA). In addition, Argentina does not allow the use of electronically produced airway bills, limiting their ability to speed up customs processing and the growth of electronic commerce transactions.

AUSTRALIA

TRADE SUMMARY

The U.S. trade surplus with Australia was $6.7 billion in 2004, an increase of $53 million from 2003. U.S. goods exports to Australia in 2004 were $14.3 billion, up 9.0 percent from the previous year. Corresponding U.S. imports from Australia were $7.5 billion, up 17.6 percent. Australia is currently the 14th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Australia were $5.8 billion in 2003, and U.S. imports were $3.2 billion. Sales of services in Australia by majority U.S.-owned affiliates were $14.6 billion in 2002 (latest data available), while sales of services in the United States by majority Australia-owned firms were $10.2 billion.

The stock of U.S. foreign direct investment (FDI) in Australia in 2003 was $41.0 billion, up from $34.4 billion in 2002. U.S. FDI in Australia is concentrated largely in the manufacturing, mining, and finance sectors.

FREE TRADE AGREEMENT (FTA)

The governments of the United States and Australia concluded an FTA on February 8, 2004, that entered into force on January 1, 2005. The FTA addressed many of the issues raised in the 2004 National Trade Estimate report. Under the FTA, more than 99 percent of U.S. exports of manufactured goods to Australia are now duty free and all U.S. agricultural exports to Australia, totaling nearly $700 million, receive duty-free access as of January 1, 2005.

IMPORT POLICIES

Tariffs

Australia has been reducing its tariffs gradually since the 1970s, which has brought 86 percent of tariffs to between zero percent and five percent, with more than 99 percent of tariff rates applied on an *ad valorem* basis. More than 96 percent of Australia's tariff lines are bound in the World Trade Organization (WTO). Australia's simple average bound tariff rate is 10.5 percent and its average applied normal trade relations (NTR), also known as most favored nation (MFN), tariff is 4.3 percent. The average applied NTR/MFN rate for industrial products is 4.7 percent, with most bound rates ranging from zero percent to 55 percent. The average applied NTR/MFN tariff for agricultural products is less than one percent, with bound rates generally ranging from zero percent to 29 percent. Tariff-rate quotas are in place for five cheese items and non-manufactured tobacco. Australia retains two tariff peaks on textiles, clothing, and footwear (TCF) (maximum 25 percent) and passenger motor vehicle (maximum 15 percent).

Under the FTA, 99 percent of U.S. manufactured goods and 100 percent of U.S. food and agricultural goods exports to Australia are now subject to zero duties. The FTA will also eliminate tariffs within four years in the automotive sector and within 10 years in the textiles sector. U.S. industry estimates the removal of tariffs affecting trade in textiles, autos, and auto components will lead to increases in U.S. exports to Australia of $100 million to $500 million in textiles and increases of $100 million to $500 million in exports of autos and components.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Sanitary and Phytosanitary Measures

The Australian government maintains an extremely stringent regime for the application of sanitary and phytosanitary (SPS) measures, resulting in restrictions and prohibitions on imports of many agricultural products. Key U.S. products currently prohibited under Australia's SPS regime include Florida citrus, stone fruit, poultry (fresh, cooked, and frozen), and apples. In 2004, Australia issued new import rules for pork. Under these new rules, the United States gained access to the Australian market and is now shipping processed pork to Australia. The U.S. government continues to underscore the need for Australia to comply with its obligations under the WTO SPS Agreement by conducting science-based import risk assessments and applying measures that are no more trade restrictive than necessary. The U.S. and Australian governments have held extensive and detailed consultations on these issues over the past three years, and these discussions have generated progress on specific issues. The FTA created a new mechanism for scientific cooperation between U.S. and Australian SPS authorities to resolve specific bilateral, animal, and plant health matters. This new mechanism is intended to facilitate engagement at the earliest appropriate point in each country's regulatory process to cooperate in the development of science-based measures that affect trade between the two countries.

Biotechnology

Commercial Release

The Gene Technology Act 2000 is the Commonwealth government component of a national regulatory scheme for gene technology and products produced through modern agricultural biotechnology. The Act regulates the use of all agricultural biotechnology products in Australia and requires that the Office of the Gene Technology Regulator license all biotechnology activities involving the intentional release of biotechnology products into the environment. Issues related to the marketability and trade implications of the commercialization of biotechnology crops do not fall within the scope of the evaluations provided in the Act. The Commonwealth, State, and Territory governments consider these matters both individually and through joint forums. Most of Australia’s States and Territories restrict biotechnology products through planting moratoria or bans on plantings of food-related biotechnology products licensed by the Commonwealth Office of the Gene Technology Regulator. The United States has objected to these actions as they appear to be based on marketing and trade concerns rather than science. Such actions have held up the commercialization of biotechnology canola. It should be noted that biotechnology cotton, a non-food-related biotechnology product, has been successfully introduced and planting of this product now dominates the cotton industry in Australia.

Biotechnology Food Approvals

Imported foods using biotechnology can be offered for sale and consumption in Australia only after being assessed and approved by Food Standards Australia New Zealand (FSANZ) and being listed in the Food Standards Code. As of November 2004, there were 23 products on the FSANZ-approved list of "food produced using gene technology."

Biotechnology Food Labeling

The joint Australia-New Zealand regulatory regime for food, which includes mandatory labeling requirements for certain foods produced using biotechnology, became effective in December 2001. Biotechnology labeling is required if a food in its final form contains detectable DNA or protein resulting from the application of biotechnology, with a few exceptions. Meeting these biotechnology food labeling regulations may be burdensome for manufacturers, packers, importers, and retailers, particularly involving U.S. agricultural exports, a large share of which are processed food.

GOVERNMENT PROCUREMENT

Australia is the only major industrialized country that is not a signatory to the plurilateral WTO Agreement on Government Procurement (GPA). As such, Australia is not bound by the GPA's rules on open and non-discriminatory policies in government procurement. Under the FTA, Australia will open its government procurement market to U.S. suppliers and eliminate discriminatory preferences for most domestic suppliers.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Australia is a member of the World Intellectual Property Organization (WIPO) and is a party to most multilateral IPR agreements, including: the Paris Convention for the Protection of Industrial Property; the Berne Convention for the Protection of Literary and Artistic Works; the Universal Copyright Convention; the Geneva Phonogram Convention; the Rome Convention for the Protection of Performers, Producers of Phonograms, and Broadcasting Organizations; and the Patent Cooperation Treaty. Under the FTA, Australia is obligated to accede and become a party to the 1996 WIPO Copyright Treaty and Performances and Phonograms Treaty.

Australia permits the parallel importation of computer software, electronic versions of books, periodicals, sheet music, sound recordings, branded goods (clothing, footwear, toys, and packaged food), and some electronic games. The Australian government continues to prohibit the parallel importation of films. An estimated 20 percent of the DVDs in Australia are illegal parallel imports. Locally replicated DVD-Rs, videocassettes copied from VCDs and DVDs, illegally parallel-imported DVDs, and pirated VCDs continue to be the major threat to Australia's otherwise low rate of piracy of audio-visual materials. Counterfeit DVDs imported from Asia also are an emerging problem. U.S. copyright holders remain concerned over past decisions by the Australian Competition and Consumer Commission (ACC) that equate the holding of a copyright with "market power."

Due to the FTA, Australia now provides copyright protection for the life of the author plus 70 years (for works measured by a person's life), or 70 years (for corporate works). The FTA also clarifies that the right to reproduce literary and artistic works, recordings, and performances encompasses temporary copies, an important principle in the digital realm. In addition, the FTA obligates Australia to criminalize by 2007 the sale, distribution, and use of devices to defeat technological protection measures. Australia also agreed to obligations with respect to the liability of Internet service providers in connection with copyright infringements that take place over their networks.

Under the patent provisions of the FTA, Australia confirms that its law makes patents available for any invention, subject to limited exclusions, and confirms the availability of patents for new uses or methods of using a known product. To guard against arbitrary revocation, Australia will limit the grounds for revoking a patent to the grounds that would have justified a refusal to grant the patent; fraud is also grounds for revocation. Under the FTA, Australia also will make patent term adjustments to compensate if there are unreasonable delays that occur while granting the patent, or if there is unreasonable curtailment of the effective patent term as a result of the marketing approval process for pharmaceutical products. The FTA protects test data that a company submits in seeking marketing approval for pharmaceutical and agricultural chemical products by precluding other firms from relying on the data. It also requires measures to prevent the marketing of pharmaceutical products that infringe patents.

The trademark and geographical indication provisions of the FTA establish that trademarks must include marks in respect of goods and services, collective marks, and certification marks, and that geographical indications are eligible for protection as marks. Australia also will provide protection for marks and geographical indications, as well as efficient and transparent procedures governing the application for protection of marks and geographical indications. The FTA also provides for rules on domain name management that require a dispute resolution procedure to prevent trademark cyber-piracy.

The FTA establishes strong penalties for piracy and counterfeiting. The Agreement criminalizes end-user piracy and requires Australia to authorize the seizure, forfeiture, and destruction of counterfeit and pirated goods and the equipment used to produce them. Australia also must empower its law enforcement agencies to take enforcement action at the border against pirated or counterfeit goods without waiting for a formal complaint.

The United States government raised concerns that Australia’s FTA implementing legislation, which Australia’s parliament approved in August 2004, did not fully implement a number of the FTA commitments on intellectual property. The United States and Australia subsequently addressed those concerns in an exchange of letters in November 2004, through which Australia agreed to take steps, including making legislative and regulatory changes, to implement several IP commitments. Australia’s parliament approved related legislation in December 2004. Concerns remain, however, about the Australian government’s implementation of its FTA commitments with respect to pharmaceutical patent protection and satellite piracy.

SERVICES BARRIERS

Telecommunications

U.S. industry remains concerned about the ability of the majority government-owned telecommunications firm, Telstra, to abuse its monopoly power. This has included delays in making an acceptable public offer for access to its network, and the inflated pricing of its wholesale services such as leased lines and interconnection with its mobile network. Australia’s government has made significant progress in addressing some of these issues by approving a reference interconnection offer and proposing a schedule of mobile termination rates that would introduce significant price reductions (termination rates in Australia are among the highest in Asia). Telstra has provided evidence that its leased line rates are now comparable with other competitive markets, and companies seeking to challenge these rates have the opportunity to do so under Australia's rules. The Australian government has submitted legislation to permit it to sell off all of its 51-percent share of Telstra; the legislation was rejected once, but is expected to be re-submitted. The Australian government has not, however, addressed the issue of foreign equity limits in Telstra, now limited to 35 percent. The FTA includes several important new obligations for major suppliers, including resale, provisioning of leased circuits and co-location, ensuring access for U.S. firms.

Audiovisual Trade Barriers

The Australian Broadcasting Authority's (ABA) Content Standards require that 55 percent of all free-to-air television programming broadcast between 6:00 a.m. and midnight be of Australian origin (with subquotas and point systems applying to various content genres). In addition, the television advertising quota stipulates that at least 80 percent of total commercial television advertising during that same period must be Australian produced. Australia's Broadcasting Services Amendment Act requires pay television channels with significant drama programming to spend 10 percent of their programming budget on new Australian drama programs. Australian radio industry quotas require that up to 25 percent of all music broadcast between 6:00 a.m. and midnight be "predominantly" Australian in origin/performance. The FTA allows existing restrictions to remain, but limits or prohibits their extension to other media or means of transmission.

INVESTMENT BARRIERS

Pursuant to Australia's foreign investment law, the government's Foreign Investment Review Board (FIRB) screens in advance potential foreign investments in Australia above a threshold value of A$50 million. The FIRB may deny approval of particular investments above that threshold on "national interest" grounds. The FTA, however, exempts all new "greenfield" U.S. investments from FIRB screening entirely. The FTA also raises the threshold for screening of most U.S. acquisitions of existing investments in Australia from A$50 million to A$800 million (indexed annually).

OTHER BARRIERS

Commodity Boards and Agricultural Support

The export of almost all wheat, barley, rice, and sugar remains under the monopoly control of commodity boards. The privatization of the Australian Wheat Board, Ltd., (AWB) in July 1999 saw its export controls transferred to the Wheat Export Authority (WEA), and the AWB retained veto rights over containerized export requests. After a review during 2000, the Australian government extended the WEA's export monopoly until 2004. In 2000, the Australian government launched an eight-year adjustment assistance package for the dairy industry. In 2002, it initiated a four-year, A$150 million sugar industry package; this package was increased by A$440 million in 2004. Both programs support regional adjustment, diversification and industry restructuring. Depending on the program, assistance includes sustainability grants, income support, crisis counseling, interest rate subsidies, and short-term income support.

Automotive and Textile, Clothing, and Footwear (TCF) Sector Support Programs

Automotive producers benefit from import duty credits designed to promote production, investment, and research and development. In 2002, the program was extended to 2015 with declining benefits to compensate for planned additional tariff reductions. The TCF industry receives grants under the Australian government's Strategic Investment Program for research and development, restructuring, and investment to assist firms to restructure prior to legislated tariff cuts in 2005. In November 2003, the Australian government announced a tariff reduction schedule and a reduced and final assistance scheme for the period 2005 through 2015.

Pharmaceuticals

The U.S. pharmaceutical industry has raised concerns that the Australian government's policies regarding the pharmaceutical sector do not appropriately value innovation and diminish the contribution of Australia to research and development of innovative pharmaceutical products.

The lack of transparency of the Australian government's pharmaceutical listing and reimbursement decision-making process, including the absence of an appeals process, also is problematic. The FTA partially addresses these transparency concerns and requires establishment of an independent review process. The two governments also established a Medicines Working Group that will provide for continued dialogue between the two governments on emerging health care policy issues.

The industry also has raised concerns about a proposal of Australia’s government to require a 12.5 percent cut in the reimbursement price of pharmaceuticals in a therapeutic drug class when a generic drug in that class comes onto the market. Some consultation on this proposal between industry representatives and Australian health officials has occurred, but the U.S. government remains concerned about the lack of transparency of the process to implement this proposal and the potential impact of the proposal on the innovative and generic pharmaceutical sectors.

Blood Plasma Products

Foreign companies face substantial barriers to the provision of blood plasma products in the Australian market. Hospitals are reimbursed only for blood plasma products produced by an Australian company under a monopoly contract granted by the government. While foreign blood products may be approved for sale in Australia, the exclusive contract makes it virtually impossible for foreign firms to sell their products in Australia except to fill shortages or provide products not otherwise available in Australia. The FTA commits Australia to review its arrangements for the supply of blood fractionation services by no later than January 1, 2007. The Commonwealth government will recommend to Australia's States and Territories that future arrangements for the supply of blood plasma products be conducted through an open tender process.

BAHRAIN

TRADE SUMMARY

The U.S. trade balance with Bahrain went from a trade surplus in 2003 of $130 million to a trade deficit of $105 million in 2004. U.S. exports in 2004 were $301 million, down 40.9 percent from the previous year. Corresponding U.S. imports from Bahrain were $405 million, up 7.1 percent. Bahrain is currently the 88th largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Bahrain in 2003 was $196 million, up from $70 million in 2002.

IMPORT POLICIES

As a member of the GCC, Bahrain applies the GCC common external tariff of five percent for most products, with a limited number of GCC-approved country-specific exceptions. Bahrain's exceptions to the common external tariff include alcohol (125 percent) and tobacco (100 percent). Four hundred seventeen food and medical items are exempted from customs duties entirely.

Upon entry into force of the U.S.-Bahrain FTA, 100 percent of bilateral trade in consumer and industrial products will become duty-free immediately. In addition, Bahrain will provide immediate duty-free access to virtually all products in its tariff schedule and will phase out tariffs on the remaining handful of products within ten years. On agricultural products, Bahrain will provide immediate duty-free access for U.S. agricultural exports in 98 percent of agricultural tariff lines. Bahrain will phase out tariffs on the remaining products within ten years.

Bahrain requires that pharmaceutical products be imported directly from a manufacturer with a research department and that the products be licensed in at least two other GCC countries, one of which must be Saudi Arabia. Drugs and medicines may be imported only by a drug store or pharmacy licensed by the Ministry of Commerce after approval by the Ministry of Health. Bahrain prohibits the importation of weapons (except under special license), wild animals, radio-controlled model airplanes, pornography, foodstuffs containing cyclamates, and children's toys containing methyl chloride (and other articles declared harmful by the Ministry of Health). Bahrain is also taking steps to ban the import of 127 chemicals.

STANDARDS, TESTING, LABELING AND CERTIFICATION

As part of the GCC Customs Union, member countries are working toward unifying their standards and conformity assessment systems, and have progressed considerably toward the goal of a unified food standard – originally targeted for adoption by 2006. However, each country currently applies either its own standard or a GCC standard, which can cause confusion for U.S. exporters.

Bahrain usually incorporates international or GCC standards, and the development of standards in Bahrain is based on the following principles: (a) no unique Bahraini standard is to be developed if there is an identical draft GCC standard in existence; and (b) developing new Bahraini standards must not create trade barriers. The total number of GCC standards adopted as Bahraini standards currently stands at 1020, out of which 320 are mandatory and 700 are voluntary. There are also approximately 434 draft GCC standards under development.

Bahrain has replaced its product shelf-life requirements, a major impediment to U.S. processed food exports to the Gulf region, with international (Codex) standards.

GOVERNMENT PROCUREMENT

In October 2002, Bahrain implemented a new government procurement law that establishes the basic framework for a transparent, rules-based government procurement system. It provides that certain procurements may be conducted as international public tenders open to foreign suppliers. To implement this law, a tender board, chaired by a Minister of State, was established in January 2003 to oversee all government tenders and purchases.

In the past, government tendering procedures for large projects were not highly transparent. U.S. companies sometimes reported operating at a disadvantage compared with other international firms. Contracts were not always decided solely based on price and technical merit, and selected, pre-qualified firms were occasionally invited to bid on major government tenders. However, as of January 2003, the Tenders Board processes all tender decisions valued at BD 10,000 ($26,525) or higher. Individual ministries and departments may still process projects valued at less than $26,525. U.S. firms report that the process is greatly improved over the previous system, though some challenges remain. A local representative with strong connections may still be important in the bidding process. When the U.S.-Bahrain FTA enters into effect, Bahrain will be required to conduct procurement covered by the FTA in a fair, transparent, and non-discriminatory manner.

EXPORT SUBSIDIES

Bahrain has phased out most subsidies for export industries, but permits duty-free importation of raw materials for export products and of equipment and machinery for newly established export industries. All industries in Bahrain, including foreign-owned firms, benefit from government-subsidized utilities.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The U.S.-Bahrain FTA commits Bahrain to enforce world-class IPR protection. Bahrain is also in the process of joining the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty. The government has made significant progress in reducing copyright piracy, and there are no reports of significant violations of U.S. patents and trademarks in Bahrain. The government's copyright enforcement campaign began in late 1997 and was based on inspections, closures, and improved public awareness. The campaign targeted the video, audio and software industries with encouraging results. However, software piracy, which has shifted from retail to end-user violations, remains problematic.

SERVICES BARRIERS

Financial Sector

In March 2004, as part of an effort to stimulate the insurance industry and reinforce Bahrain's position as a major insurance center in the Middle East, the Bahrain Monetary Authority (BMA) lifted the requirement that foreign insurance brokers and loss adjusters have a local partner to operate. These firms, which were previously required to have at least 51 percent Bahraini-ownership, are now permitted to operate with 100 percent foreign-ownership. The BMA is holding consultations on further reform in areas such as captive insurance, solvency, business conduct, risk management and financial crime, enforcement, BMA reporting and public disclosure, intermediaries, and Islamic insurance. As a result of the FTA, Bahrain will lift the moratorium on the issuance of new insurance licenses for life and medical insurance upon entry into force of the agreement and will lift the moratorium for non-life insurance licenses 6 months afterward.

In 2004, Bahrain's Central Bank issued seventeen new licenses – one investment bank, four offshore banking units, one full commercial bank, two investment advisory brokers, two financial services ancillary service providers, three representative offices, one money exchange unit, and three Islamic banking and financial institutions.

Telecommunications

The telecommunications sector was the first key sector to be liberalized in Bahrain following the governments announced interest in opening traditionally government-controlled industries. The Telecommunications Regulatory Authority (TRA), established in late 2002, awarded a mobile telecommunications services license to MTC Vodafone, thus ending the monopoly of Bahrain's telecommunications services provider, BATELCO. The license was awarded under the Telecommunications Law, which took effect January 2003. The TRA Chair announced in April 2003 that all licenses, including those currently held by BATELCO, would be issued for fifteen years. A total of nine different licenses will be issued.

On July 1, 2004, the telecommunications sector was fully liberalized, including paging services, very small aperture terminals (VSAT), public access mobile radio services, international telecommunications facilities, international telecommunications services, national fixed services, internet service providers (ISP), and value-added services licenses. As of December 2004, the TRA announced the provision of three International Telecommunications Facility Licenses (IFLs), five International Telecommunications Services Licenses (ISLs), five VSAT licenses, fifteen value-added Services (VAS) "Class" licenses and eight Internet Service Provider (ISP) licenses.

Agent and Distributor Rules

U.S. firms interested in selling products exclusively in Bahrain are no longer required to appoint a commercial agent, though they may opt to do so anyway. Certain exceptions to this rule are provided under existing Bahraini commercial registration laws.

INVESTMENT BARRIERS

The U.S.-Bahrain BIT provides benefits and protection to U.S. investors in Bahrain, such as most-favored-nation treatment and national treatment, the right to make financial transfers freely and without delay, international law standards for expropriation and compensation cases, and access to international arbitration. The BIT provides national and most-favored-nation treatment for U.S. investments across all sectors, with exceptions for ownership or control of television, radio or other forms of media, fisheries, initial privatization, air transportation, the purchase or ownership of land, and, until January 1, 2005, the purchase or ownership of shares traded on the Bahrain Stock Exchange (BSE).

Bahrain permits 100 percent foreign-ownership of new industrial entities and the establishment of representative offices or branches of foreign companies without local sponsors. Wholly foreign-owned companies may be set up for regional distribution services and may operate within the domestic market as long as they do not exclusively pursue domestic commercial sales. However, local businesses licensed for retail and companies listed on the BSE are still required to have 51 percent Bahraini or GCC-ownership. Foreign companies established before 1975 may be exempt from this rule under special circumstances.

Since January 2001, foreign firms and GCC nationals may own land in Bahrain. Non-GCC nationals may now own high-rise commercial and residential properties, as well as property in tourism, banking, financial and health projects, and training centers, in specific geographic areas.

In an attempt to streamline licensing and approval procedures, the Ministry of Commerce opened the Bahrain Investors Center (BIC) in October 2004 for both local and foreign companies seeking to register in Bahrain. According to Ministry of Commerce officials, 80 percent of all licenses can be processed and verified within approximately twenty-four hours, an additional 10 percent within five working days and the remaining 10 percent, involved in environmental, power, health and other important utilities and services, are processed separately and licenses are issued on a case-by-case basis.

ELECTRONIC COMMERCE

In September 2002, Bahrain implemented an Electronic Transactions law, recognizing the validity of electronic transactions. In order to encourage use of this technological advancement, the Ministry of Commerce has implemented electronic government. Banks offer electronic banking and the parastatal telecommunications company now accepts electronic transactions for bill payments.

BOLIVIA

TRADE SUMMARY

The U.S. trade deficit with Bolivia was $67 million in 2004, an increase of $65 million from $2 million in 2003. U.S. goods exports in 2004 were $194 million, up 6.2 percent from the previous year. Corresponding U.S. imports from Bolivia were $261 million, up 41.3 percent. Bolivia is currently the 100th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Bolivia in 2003 was $375 million, down from $408 million in 2002.

FREE TRADE NEGOTIATIONS

In May 2004, the United States initiated free trade agreement (FTA) negotiations with three Andean nations – Colombia, Ecuador and Peru. Bolivia is participating as an observer in the negotiating sessions and as a full participant in the trade capacity building (TCB) talks. The United States intends to include Bolivia in the agreement at a later stage. The four Andean countries collectively represented a market of about $8.5 billion for U.S. exports in 2004, and were home to about $7.2 billion in U.S. foreign direct investment.

IMPORT POLICIES

Tariffs

Bolivia has a three-tier tariff structure. Capital goods designated for industrial development are not subject to any duty; non-essential capital goods are subject to a five percent tariff; and most other goods are subject to a ten percent tariff.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Labeling

Labeling requirements for food products were established in 2003 (Supreme Decree 26510). Although products normally retain their original labels, complementary labeling showing the importer or distributor's taxpayer identification number (RUC), sanitary registration number and translation of ingredients into the Spanish language are required.

Standards

The Government of Bolivia sets no specific standards for imports. The National Certification and Standardization Organization (IBNORCA) is in charge of developing Bolivian product standards. In the near future, products for use in the oil and gas industry will have to comply with certain standard requirements.

GOVERNMENT PROCUREMENT

Since 1999, the control of the most significant entities once owned by the Bolivian Government has been in private (mostly foreign) hands. Government expenditures, however, still account for a significant portion of Bolivia's GDP. The central government, regional governments (at the state and municipal levels) and other government agencies remain important buyers of machinery, equipment and materials, as well as of other products and services.

In an effort to provide incentives for local production, the government changed its purchasing rules in March 2004 (Supreme Decree 27328, dated 31 January 2004). Government purchases (except insurance contracts) under $20,000 (U.S.) may be done through direct invitation and price comparison (minimum three quotes). The Government of Bolivia is legally required to call for tenders when purchases are above $20,000 and under $1,000,000. Importers of foreign products can only participate in these procurements if locally manufactured products and service providers are not available or a contract is not awarded. For proposed purchases of $1,000,000 to $1,875,000, local bids must be sought. Importers of foreign products face restrictions similar to those for procurements under $1,000,000. The government can call for international bids only for purchases over $1,875,000 and under $5,000,000. Suppliers submitting bids for purchases over $5,000,000 must comply with specified prerequisites, which are established in the bidding documents for each purchase.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Bolivia belongs to the World Trade Organization (WTO), the World Intellectual Property Organization (WIPO) and is a signatory of the Paris Convention for the Protection of Industrial Property, the Berne Convention for the Protection of Literary and Artistic Works, and the Geneva Phonograms Convention. Bolivia is on the U.S. Trade Representative's Special 301 Watch List. In 1999, the Bolivian government established the National Intellectual Property Rights Service (SENAPI) to administer IPR issues. In 2003, USAID began supporting the institutional development of SENAPI as a regulatory agency. As of December 2004, that process was not yet complete.

Bolivia's existing legislation governing protection of IPR is insufficient, and enforcement efforts have been sporadic and largely ineffective. Piracy rates of videos, sound recordings and software remain among the highest in Latin America. The International Intellectual Property Alliance (IIPA) estimates that piracy levels in Bolivia have reached 100 percent for motion pictures and 90 percent for recorded music. The 1992 Copyright Law recognizes copyright infringement as a public offense, and in May 2001 the new Bolivian Criminal Procedures Code began to provide for the criminal prosecution of IPR violations. In 2003, Bolivia had its first criminal IPR prosecution. However, laws are largely not enforced, and U.S. firms have had little success in getting justice in this area from Bolivian courts.

INVESTMENT BARRIERS

The 1990 Investment Law, together with other legislation, opened Bolivia's economy to foreign investment. The law established guarantees such as equal treatment of foreign companies, the unimpeded repatriation of profits, convertibility of currency and the right to international arbitration in all sectors. In kind transfers are not allowed. Companies must follow the Bolivian commercial code to close down operations and then repatriate their capital. Bolivia is still discussing a bankruptcy law. Arbitration is limited to contractual rights. In the mid-1990s, the Government of Bolivia implemented its "capitalization" (privatization) program. This program differs from traditional privatizations in that the funds invested by foreign investors: (a) could only be used to acquire a 50 percent maximum share of business equity of the former state-owned company; and (b) were directed into investment funds to support the pension system, rather than to the Bolivian Treasury.

Bolivia has signed bilateral investment treaties with several countries, including the United States. The U.S.–Bolivia Bilateral Investment Treaty (BIT) entered into force in June 2001. The BIT's guarantee of recourse to international arbitration is important because U.S. companies are reluctant to pursue commercial disputes in the Bolivian legal system, fearing a prolonged, non-transparent and occasionally corrupt process.

The Bolivian hydrocarbons law, following Article 139 of the Constitution, stipulates that all hydrocarbons deposits, whatever their state or form, belong to the Bolivian government. No concessions or contracts may transfer ownership of hydrocarbon deposits to private or other interests. The government exercises its right to explore and exploit hydrocarbon reserves and trade hydrocarbon products through the state-owned firm, Yacimientos Petroliferos Fiscales Bolivianos (YPFB). The law allows YPFB to enter into joint venture contracts for limited periods of time with national or foreign individuals or companies wishing to exploit and trade hydrocarbons.

In 1996, the Government of Bolivia reduced royalties paid to the Bolivian Treasury and local governments under these joint venture contracts and eventually attracted $3 billion in new investment to Bolivia. In 2003, the Bolivian government announced that it would review those contracts, as well as the entire capitalization process, to see if the needs of the Bolivian people were being served. As of December 2004, the Bolivian Congress was considering a draft hydrocarbons law that, if approved, could breach existing government contracts with investors by *inter alia* removing the companies' right to freely commercialize natural gas.

BRAZIL

TRADE SUMMARY

The U.S. trade deficit with Brazil was $7.3 billion in 2004, an increase of $595 million from $6.7 billion in 2003. U.S. goods exports in 2004 were $13.9 billion, up 23.7 percent from the previous year. Corresponding U.S. imports from Brazil were $21.2 billion, up 18.1 percent. Brazil is currently the 15th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Brazil were $4.8 billion in 2003, and U.S. imports were $1.9 billion. Sales of services in Brazil by majority U.S.-owned affiliates were $12.8 billion in 2002 (latest data available), while sales of services in the United States by majority Brazil-owned firms were $366 million.

The stock of U.S. foreign direct investment (FDI) in Brazil in 2003 was $29.9 billion, up from $27.6 billion in 2002. U.S. FDI in Brazil is concentrated largely in the manufacturing, finance, and utilities sectors.

IMPORT POLICIES

Brazil's average applied tariff rate was 10.8 percent in 2004. Brazil is a member of MERCOSUL, a customs union comprising Argentina, Brazil, Paraguay, and Uruguay. Full Common External Tariff (CET) product coverage is scheduled for implementation in 2006. CETs range from zero percent to 35 percent *ad valorem*, with a limited number of country-specific exceptions. Currently, Brazil maintains 100 exceptions to the CET, with tariffs reaching as high as 55 percent on peaches. A temporary CET surcharge applied to most imports since 1997 was abolished by Brazil on January 1, 2004.

High CETs significantly impede increased U.S. imports of agricultural products, distilled spirits, and computer and telecommunications equipment. Brazil applies additional import taxes and charges that can effectively double the actual cost of importing textile products into Brazil. High tariffs on information technology products and components as well as high taxes have led to a large gray market in personal computers. One safeguard measure is in place against toy imports. A number of imports are prohibited, including all used consumer goods such as machinery, foreign blood products, refurbished medical equipment, automobiles, clothing, and other consumer goods. A 25 percent merchant marine tax on freight at certain ports puts U.S. agricultural products at a competitive disadvantage to MERCOSUL products. Brazil applies a 60 percent flat import tax on most manufactured retail goods imported by individuals that go through a simplified customs clearance procedure called RTS (simplified tax regime).

Import Licensing/Customs Valuation

All importers must register with the Secretariat of Foreign Trade (SECEX) to access the SISCOMEX computerized trade documentation system. SISCOMEX registration requirements are onerous, including a minimum capital requirement. In addition, fees are assessed for each import statement submitted through SISCOMEX. Most imports into Brazil are covered by an "automatic import license" regime. Brazil's non-automatic import licensing system includes imports of products that require authorization from specific ministries or agencies such as beverages (Ministry of Agriculture), pharmaceuticals (Ministry of Health), and arms and munitions (National Defense Ministry). Although a list of products subject to non-automatic import licensing procedures is published on the Brazilian Ministry of Development, Industry and Trade website, specific information related to non-automatic import license requirements and explanations for rejections of non-automatic import license applications are lacking. These measures have made importing into Brazil less transparent and more cumbersome for U.S. exporters.

U.S. companies continue to complain that Brazil employs a variety of customs-related non-tariff barriers. For example, product registrations from the Ministry of Health are required for imported processed food products and food supplement products. On March 1, 2000, the term of validity for such a registration was shortened. Registration fees for these imports, as well as for medical and pharmaceutical products, have increased significantly. Implementation of such import measures continues to have a negative impact on U.S. exports, especially given the high tariffs on medical equipment.

The United States has raised a concern with Brazil that the state of Rio de Janeiro administers the ICMS tax (a value-added tax collected by individual states) in a way that provides a preferential tax advantage to a Brazilian soda ash supplier located within the state. Similarly, some U.S. companies have raised concerns about the arbitrary application of various quotas and non-automatic import licensing procedures, such as authorizations from the Federal Police and the Nuclear Regulatory Agency. For example, Brazil maintains extremely restrictive import quotas and requires non-automatic import license approval for imports of lithium compounds, including lithium carbonate and lithium hydroxide, citing the potential nuclear applications of these products. However, these products are widely available without restriction in global markets. The United States has raised this issue with Brazil on several occasions, both bilaterally and in the WTO. In addition, some U.S. companies have claimed that the manner in which the PIS/COFINS tax (a value-added tax collected by the federal government) has been applied to imports under the 2004 tax reform has disadvantaged imported goods vis-à-vis domestic manufactured goods.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Sanitary and Phytosanitary Measures

While some progress has been made in the area of sanitary and phytosanitary measures, significant issues remain that restrict U.S. agricultural and food exports. For example, due to concerns about bovine spongiform encephalopathy (BSE), Brazil restricts U.S. exports of low-risk beef and beef products without scientific justification and contrary to international standards. Brazil continues to prohibit the import of poultry and poultry products from the entire United States. Brazil has indicated that these restrictions are based, in part, on an alleged lack of reciprocity. Brazil's ban on durum and white wheat from the states of Washington, Oregon, Idaho, California, Nevada, and Arizona due to phytosanitary concerns remains in place. While the United States understands that some of these SPS measures are being rewritten, the ban continues to adversely affect U.S. agricultural exports.

Biotechnology

Brazil has not been able to put into place a long-term regulatory framework for biotechnology. Congress did not pass the proposed Biosafety Bill in time for the 2004/2005 planting season, prompting the federal government to issue Provisional Measure 223 (MP223) on October 18, 2004 to allow the planting and commercialization of the 2004/05 soybean crop. On December 21, 2004, the Congress passed Law 11.092/05, which transformed an amended MP223 into a full-fledged law, and sent the measure on to President Lula for his signature. Many of the MP223's original provisions remain intact under Law 11.092/05. For instance, under the law, marketing of the biotechnology soybean crop is possible until January 31, 2006, with a possible 60-day extension. The law also continues to prohibit the sale of biotechnology soybean from the 2004/05 harvest for use as seed. Some farm organizations had sought an elimination of this restriction, which the Governor of Parana state has used to prohibit sales of biotechnology seeds in his state and to place restrictions on exports of biotechnology soybeans through the Port of Paranagua. Article 7 of Law 11.092/05 introduced a problematic requirement (not present in MP 223 as originally proposed by the Lula Administration) that manufacturers of biotechnology seeds show receipts prior to collecting payments for their product. As Law 11.092/05 also prohibits the sale of biotechnology seeds, it may prove difficult for seed manufacturers to obtain the necessary receipts. President Lula signed Law 11.092/05 in early January 2005. A Biosafety Bill, the current version of which would allow for seed sales to be legalized, remains before Congress.

GOVERNMENT PROCUREMENT

Brazil is not a signatory to the WTO Agreement on Government Procurement, and transparency in its procurement processes could be improved. The U.S. Government has received complaints relating to practices that lead to non-transparent preferences for Brazilian products in procurement bids for government and non-profit hospitals, including favoring domestically produced “similars” over imported refurbished medical equipment. Limitations on foreign capital participation in procurement bids reportedly impair access for potential service providers in the energy and construction sectors. Brazilian federal, state and municipal governments, as well as related agencies and companies, in general follow a "buy national" policy. Law 8,666 (1993), which covers most government procurement other than informatics and telecommunications, requires non-discriminatory treatment for all bidders regardless of the nationality or origin of the product or service. However, the law's implementing regulations allow consideration of non-price factors giving preferences to certain goods produced in Brazil and stipulating local content requirements for eligibility for fiscal benefits. Decree 1,070 (1994), which regulates the procurement of information technology goods and services, requires federal agencies and parastatal entities to give preferences to locally produced computer products based on a complicated and nontransparent price/technology matrix. However, Brazil permits foreign companies to compete in any procurement-related multilateral development bank loans and opens selected procurements to international tenders.

EXPORT SUBSIDIES

The Government of Brazil offers a variety of tax, tariff, and financing incentives to encourage production for export and the use of Brazilian-made inputs in domestic production. For example, Brazil’s National Bank for Economic and Social Development (BNDES) provides long-term financing to Brazilian industries through several different programs. The interest rates charged on this financing are linked to international rates and are generally lower than the interest rates on alternative domestic financing. One BNDES program, FINAME, provides capital financing to Brazilian companies for, among other things, expansion and modernization projects as well as acquisition or leasing of new machinery and equipment. One goal of this program is to support the purchase of domestic over imported equipment and machinery. These programs can be used for financing capacity expansions and equipment purchases in industries such as steel.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Patents and Trademarks

Brazil's industrial property law (Law 9,279/1996) became effective in May 1997. Concerns continue about a provision in Brazil’s industrial property law that prohibits importation as a means of satisfying the requirement that a patent be “worked” in Brazil. This issue was the subject of a U.S. dispute settlement proceeding at the WTO, which was terminated without prejudice in June 2001. The dispute was terminated based on Brazil's commitment to provide advance notice to, and hold consultations with, the United States should it deem it necessary in the future to grant a compulsory license for failure to work a patent.

Law 10,196 (2001) includes some problematic provisions, including a requirement that Health Ministry approval be obtained prior to the issuance of a pharmaceutical patent. This raises concerns with respect to Article 27 of the TRIPS Agreement, and U.S. officials have raised this concern with their Brazilian counterparts.

The U.S. Government has also received complaints that unauthorized copies of pharmaceutical products have received sanitary registrations that rely on undisclosed tests and other confidential data, raising concerns of consistency with TRIPS Article 39.3.

Due to a lack of government focus and resources, Brazil's patent office, the National Institute for Industrial Property (INPI), has amassed a backlog of more than 60,000 patent applications -- an estimated 18,000 for pharmaceuticals -- and 500,000 trademark applications. In 2004, INPI received a $10 million increase in its budget and authorization to hire an additional 500 employees over the next several years, 300 as patent examiners. Nonetheless, the Brazilian government projects it will take five to six years to work through the patent and trademark application backlogs.

Law 10,603 (2002) on data confidentiality covers pharmaceuticals for veterinary use, fertilizers, agrotoxins, and their components and related products; the law does not cover pharmaceuticals for human use. If the product is not commercialized within two years of the date of sanitary registration, third parties may request use of the data for registration purposes.

Copyrights

Brazil’s Law 9,610 (1998) on copyrights included changes intended to bring Brazil into compliance with the Berne Convention and TRIPS. A software law (1998) protects computer programs for 50 years as "literary works", and makes software infringement a fiscal and an intellectual property crime. Brazil is not a party to the WIPO Treaties on Copyright, and Performances and Phonograms.

Copyright enforcement remains weak. Despite Brazil’s copyright law, losses from copyright infringement in Brazil have risen in recent years. According to the International Intellectual Property Alliance (IIPA), estimated losses due to piracy of copyrighted materials totaled $931.9 million in 2004. Piracy problems have been particularly acute with respect to sound recordings and videocassettes, and an estimated 75 percent of audiocassettes sold are pirated copies. Piracy is a serious problem in other industries as well, including digital media and disc-based entertainment and business software. Despite inspections at border crossings, a substantial amount of pirated material continues to enter Brazil from Paraguay. Brazil has launched a MERCOSUL initiative to share intelligence and coordinate actions to combat piracy and smuggling in the Brazil-Paraguay-Argentine border area. Although a significant number of raids and seizures on the border and in the interior were carried out in 2004, the conviction rate remains low. Furthermore, the judicial process is often slow, and prison sentences are routinely commuted to fines, undermining efforts to create deterrence.

On June 30, 2004, the Administration announced that it would continue to review Brazil's eligibility for GSP for a ninety-day period, which concluded on September 30, in response to a petition filed by the International Intellectual Property Alliance (IIPA) to remove Brazil's GSP benefits due to its failure to offer adequate protection to copyrighted materials. In a series of meetings during that period, the U.S. Government and the Brazilian government examined both steps taken and future plans to strengthen and improve copyright enforcement. As a result of these discussions, a number of key priorities and actions to combat copyright piracy through enforcement of existing laws have been identified. Accordingly, the United States and Brazil expect to maintain a dialogue on developments in this critical area. In the meantime, the review of the petition has been formally extended through March 31, 2005 in order to assess Brazil's progress.

SERVICES BARRIERS

Telecommunications

Privatization within the telecommunications sector, which is based on the General Telecommunications Law of 1997, has presented regulatory challenges. In the fixed-line sector, interconnection charges and other incumbency advantages have provided strong barriers for entry, and the companies created during a transitional duopoly stage have not fared well.

Brazil has not yet ratified its original WTO basic telecommunications commitments. In 2001, Brazil withdrew its schedule of commitments because of concerns raised by certain WTO Members that it maintained the legal prerogative of the Executive Branch to limit foreign participation in this sector, thereby creating significant uncertainty for investors. This legal prerogative is contained in Brazil's 1997 General Law on Telecommunications and is inscribed in Brazil's constitution. While Brazil has not sought the constitutional change required to allow a revision of its offer to open up this sector, the current regulatory environment generally reflects the obligations contained in the WTO Basic Telecommunications Reference Paper.

Audio Visual Services

Foreign ownership of cable companies is limited to 49 percent, and the foreign owner must have a headquarters in Brazil and have had a presence in the country for the prior 10 years. Foreign cable and satellite television programmers are subject to an 11 percent remittance tax; however, the tax can be avoided if the programmer invests 3 percent of its remittances in co-production of Brazilian audio-visual services. National cable and satellite operators are subject to a fixed title levy on foreign content and foreign advertising released on their channels.

Law 10,610 (2002) limits foreign ownership in Brazilian media to 30 percent, including the print and "open broadcast" (non-cable) television sectors. Open television companies also have a regulation requiring that 80 percent of their programming content be domestic in origin.

Law 10,454 (2002) aims to promote the national film industry through creation of the National Film Agency (ANCINE) and through various regulatory measures. The law imposes a fixed title levy on the release of foreign films in theaters, foreign home entertainment products, and foreign programming for broadcast television. Remittances to foreign producers of audiovisual works are subject to a 25 percent income withholding tax. Brazilian distributors of foreign films are subject to a levy equal to 11 percent of their withholding taxes. This tax, called the CONDECINE (Contribution to the Development of a National Film Industry), is waived for the Brazilian distributor if the producer of the foreign audiovisual work agrees to invest an amount equal to 70 percent of the income withholding tax on their remittances in co-productions with Brazilian film companies. The CONDECINE tax is also levied on any foreign cinematographic or videophonographic advertisement. The fee may vary according to the advertising content and the transmission segment.

Brazil also requires that 100 percent of all films and television shows be printed locally. Importation of color prints for the theatrical and television markets is prohibited. A theatrical screen quota for local films is maintained at 63 days per calendar year. Quotas on domestic titles for home video distributors, while not currently enforced, present another potential hindrance to commerce.

Express Delivery Services

A bill (PL 1491/99) that would reorganize the National Postal System remains under discussion in the Brazilian Congress. The current proposal would create a regulatory agency for postal services as well as a new Postal Company of Brazil, owned and operated by the federal government. Although the bill would end the government monopoly over postal services after a ten-year period, it would also create a monopoly on the delivery of certain types of correspondence and parcels that are not now subject to regulation, such as express delivery packages, thereby significantly inhibiting market access by U.S. firms. Brazil also applies a 60 percent flat import tax on most manufactured retail goods imported by individuals that go through a simplified customs clearance procedure called RTS (simplified tax regime) that is used by express delivery services.

Financial services

Brazil has not yet ratified its commitments from the 1997 Financial Services negotiations or taken the necessary steps to make them binding under the GATS (accept the Fifth Protocol). Brazil is potentially South America's largest insurance market, and earnings from premiums have grown rapidly in recent years. In 1996, Brazil eliminated the distinction between foreign and domestic capital, and many major U.S. firms have since entered the market, mainly via joint ventures with established companies. However, foreign participation is limited to 50 percent of the capital of a company and to one third of its voting stock. Brazil maintains a government-owned reinsurance monopoly, however, through the Brazil Reinsurance Institute (IRB). While a 1996 constitutional reform allowed the abolishment of the monopoly, private reinsurance companies have been precluded from operating in Brazil pending passage of legislation to privatize the IRB, the constitutionality of which was challenged in the Supreme Court. While the Supreme Court decided in September 2004 that the bill was constitutional, the Lula administration has not decided to resubmit to Congress a bill privatizing IRB. A 2003 constitutional amendment allows for the regulation of the reinsurance sector, including market entry. Implementing these provisions would require passage of a complementary law. If Brazilian shipping companies wish to obtain foreign hull insurance, they must submit information to IRB demonstrating that the foreign insurance policy is less expensive than that offered by Brazilian insurers. Brazilian importers must obtain cargo insurance from insurance firms resident in Brazil, although the firms may be foreign-owned. Brazil has not ratified its 1998 WTO commitments on insurance.

Service trade opportunities in some sectors have been affected by limitations on foreign capital participation. Brazil's constitution precludes the expansion of foreign-owned banks until new financial sector legislation is issued. For practical reasons, the required legislation has not been issued, but the President of Brazil has the authority to authorize new foreign participants on a case-by-case basis. In practice, Brazil has approved most plans by foreign service suppliers to enter the market or expand existing operations. U.S. financial service suppliers have established significant operations in Brazil. As of December 2003, foreign-owned or controlled assets accounted for 24 percent of Brazil’s total financial sector equity.

INVESTMENT BARRIERS

In addition to restrictions discussed above, various prohibitions limit foreign investment in internal transportation, public utilities, media and other "strategic industries." Foreign ownership of land adjacent to national borders remains prohibited under Brazilian law, unless approved by the National Security Council. Despite investment restrictions, U.S. and other foreign firms have major investments in Brazil, with the U.S. accounting for more than one-third of total foreign investment. There is neither a bilateral investment treaty nor a treaty on the avoidance of double taxation between the United States and Brazil.

Energy

In 2004, Brazil implemented new energy legislation to restructure the power generation and distribution sector. The new model gives the state a leading role in determining, for example, how much new power capacity is needed, based on forecasts by a newly created independent Energy Research Institute (IPE). The new model separates into two different competition groups power generators that have not yet amortized their investments (new energy) and those that have (old energy), based on whether the generators' investment had been built by a certain cutoff date. This dual-pool structure has disadvantaged some U.S. companies that invested in the sector during privatization in the late nineties and whose investments have not been amortized, but were nevertheless included in the old energy pool. The Brazilian government is still in the midst of implementing the new model.

BULGARIA

TRADE SUMMARY

The U.S. trade deficit with Bulgaria was $355 million in 2004, an increase of $49 million from $286 million in 2003. U.S. goods exports in 2004 were $172 million, up 11 percent from the previous year. Corresponding U.S. imports from Bulgaria were $507 million, up 14.9 percent. Bulgaria is currently the 104th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Bulgaria in 2003 was $186 million, up from $142 million in 2002.

IMPORT POLICIES

Tariffs

Bulgaria's trade policies are shaped primarily by its World Trade Organization (WTO) membership and by its status as a candidate for EU membership. Bulgaria has a preferential trade agreement with the European Union (EU) under its Europe Agreement, and free trade agreements with the European Free Trade Area (EFTA) countries. It also has free trade agreements with its Central European neighbors (CEFTA), Turkey, Macedonia, Estonia, Israel, Lithuania and Latvia, as well as with Albania, Serbia and Montenegro, Bosnia and Herzegovina and Moldova. Upon accession to the EU, Bulgaria will be required to align its tariffs with those of the EU.

For 2005, Bulgaria's average import tariff is 11 percent; the average level for industrial goods is 8 percent and the average level for agricultural goods is 22 percent. The maximum *ad valorem* level for agricultural goods, which is applied on 0.38 percent of tariff positions, is 75 percent. Bulgaria has eliminated all tariffs on industrial imports from the EU under its association agreement with the European Union. Industrial exports to Bulgaria from the rest of the world face tariffs ranging from zero percent to 26.8 percent.

Bulgaria's agricultural trade regime is characterized by high MFN tariffs, particularly for red meat and poultry, and by preferential agreements with the EU and CEFTA. *Ad valorem* duties and minimum customs charges of more than 100 percent serve as incentives to importers for smuggling and fraud. Cargoes are often improperly identified, and falsely labeled and declared in an effort to avoid customs charges. The Bulgarian customs service also uses minimum import prices, which appear to be applied arbitrarily, to calculate customs duties, particularly on poultry shipments.

Bulgaria provides the EU with preferential tariff rates and reciprocal duty elimination on numerous agricultural products, as well as on wine. These preferences are hurting U.S. agricultural exporters who face higher MFN rates. In particular, the high import tariffs favor Bulgaria's inefficient domestic chicken and pig meat industries. Import tariffs on U.S. chicken are 68 percent, with frozen cut parts subject to a 74 percent tariff.

The U.S. Government is currently reviewing Bulgaria's continued eligibility for the U.S. Generalized System of Preferences (GSP) program in view of the preferential treatment it affords to the EU. The U.S. has urged the Bulgarian government to lower MFN tariffs on a range of items to reduce the tariff differential and its negative effect on U.S. commerce.

Non-tariff Barriers

In general, customs regulations and policies are reported to be cumbersome, arbitrary and inconsistent. Problems cited by U.S. companies include excessive documentation requirements, slow processing of shipments, and corruption. The Customs Agency requires invoices even for equipment transfers from offices of the same company located in other countries to Bulgaria. Bulgaria uses the single customs administrative document used by EU members.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The registration processes for pharmaceutical products and for drug pricing and reimbursement, including the process by which the National Health Insurance Fund classifies drugs, are cumbersome and non-transparent. Newer drugs are often arbitrarily classified with their older, generic versions for pricing purposes, thereby limiting companies' ability to recover their research and development costs.

GOVERNMENT PROCUREMENT

Bulgaria is an observer but not a signatory to the WTO Agreement on Government Procurement (GPA). In its accession to the WTO, Bulgaria committed to accede to the GPA and to submit an offer by June 1997 and complete negotiations by December 1997. However, the Bulgarian government did not initiate the process for GPA accession until 2000, and has not yet submitted an offer. Upon its accession to the European Union, Bulgaria will be required to comply with the GPA. Although Bulgaria's government procurement legislation underwent a substantial reform in 2004 to align the system with WTO and EU rules, bidders still complain that tendering processes are unclear - and subject to irregularities and corrupt practices. Even though the goal of the 2004 Public Procurement Law was to introduce a more efficient, transparent and accountable system for public procurement, the business community considers it deficient.

The Bulgarian government's lack of institutional support for the Public Procurement Agency inhibits that Agency's ability to perform its monitoring functions. Bulgaria's purchasing process would benefit from improved communications between the Bulgarian government, including bodies such as the National Audit Office and the judiciary, businesses, and from training in public procurement for officials from non-central government entities such as hospitals, universities, and municipalities.

Defense procurement activities are subject to a lack of transparency and corrupt influences, and fail to comply with international standards.

The purchasing, pricing, and reimbursement processes for drugs under Bulgaria's national health system are not transparent. The government can use the price-approval mechanism to regulate the market for any product, and bureaucratic barriers can limit patients' access to new products. Bulgaria's bureaucratic reimbursement process requires multiple approvals, lacks objective criteria, and does not provide for an appeals process. Some members of parliament have publicly advocated a policy of protectionism for Bulgarian-manufactured pharmaceuticals.

Government procurement practices in the energy sector appear to disadvantage foreign insurance companies. All Bulgarian energy entities are now insured by Energiya - a joint venture between the state-owned National Electricity Transmission Company (50 percent), Allainz Bulgaria (25 percent) and other private shareholders (25 percent) established in 1992-1993. According to U.S. industry, procedures for awarding insurance contracts for companies within the energy sector are not transparent.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

In May 2004, Bulgaria was placed on the Special 301 Watch List for the first time in five years. Over the past few years, there has been a steady resurgence of piracy, mainly in the sale of pirated optical disc media (ODM). Recording industry associations estimate that 80 percent of all musical compact discs (CDs) sold in Bulgaria today are pirated. Furthermore, Bulgaria is still widely used for transshipment of pirate CDs from Ukraine and Russia to the Balkans, Greece, and Turkey.

CD-R piracy has been increasing significantly, and the local music business in particular is feeling the brunt of this phenomenon. The possibility that Bulgarian blank CD-R (and inevitably blank DVD-R) production plants are contributing to, or generating, piracy has not been adequately recognized or addressed by Bulgarian authorities.

Although Bulgarian IPR legislation is generally adequate—it includes modern patent and copyright laws and criminal penalties for copyright infringement—industry representatives believe effective IPR protection requires improvements in certain pieces of legislation, including the Penal Code, Penal Procedure Code, and the governmental Decree on the Border Measures for Protection of IPR.

The Council of Ministers has presented a new Draft Law on Administrative Control over the Manufacture and Distribution of ODM, which includes suggestions by IFPI/BAMP. The long-delayed adoption of this optical disc control legislation is currently stalled at the parliamentary level by the ruling coalition. The proposed law is opposed by MPs citing "the independence of Bulgarian producers." Domestic producers have complained about the requirement in the proposed legislation to put a Secure Identification (SID) code on blank discs (in order to track origin), claiming this will put Bulgaria at a disadvantage against Taiwan and other producers.

The government lacks sufficient institutional capacity and will to effectively address major enforcement problems, especially in combating and prosecuting organized crime groups. Many industrial groups currently have intellectual property disputes before the government.

Software piracy continues to be a serious problem, although an industry legalization campaign has made noticeable gains against unauthorized software. Local software industry representatives report that, along with good cooperation from Bulgarian law enforcement authorities, the campaign has brought down the piracy rate to approximately 71 percent of the products in the market. The lack of actual prosecutions and court decisions has kept the piracy rate at a high level. Only five percent of all criminal cases that have been initiated over the last five years have reached a court verdict. Distribution of unlicensed software on computers continues and it is becoming increasingly difficult to effectively address this problem as computer resellers install unlicensed software at the customers' premises. Also, the domestic market offers enormous amounts of illegal CD-ROMs containing a full range of different pirated software. Internet distribution of illegal software is also a growing problem.

The Bulgarian government included in its 2003 drug law a provision to provide protection for confidential test data submitted for marketing approval by pharmaceutical products companies. The law, however, links data protection to a valid patent. Bulgaria joined the European Patent Convention on July 1, 2002 and has obtained observer status in the Administrative Council of the European Patent Organization.

Industry has told us that the Bulgarian government's inability to protect trademarks is a significant barrier to investment and legitimate domestic economic development. U.S. businesses have noted significant difficulties in obtaining relief against trademark infringement. Even if courts understand the law and issue orders, the entities charged with enforcement often cannot be relied upon to carry out the court judgment. Under Bulgarian law, legal entities cannot be held criminally liable. Therefore, the criminal penalties for copyright infringement and willful trademark infringement are limited.

Implementation of "special border measures" for copyright enforcement has created problems for legitimate exporters and importers and further changes are necessary to clarify the law and to better train customs officials. There is no provision for the use of bonds from a complainant to protect the legitimate importer or exporter of goods that are stopped in transit under "special border measures."

There is evidence of significant counterfeit production in Bulgaria and illegal import of counterfeited U.S. brand distilled alcoholic spirits. Some spirits companies have estimated that almost 10 percent of the products sold in the Bulgarian market may be counterfeit.

SERVICES BARRIERS

As in other EU candidate countries, Bulgaria's 1998 Radio and Television Law requires a "predominant portion" of certain programming to be drawn from European-produced works and sets quotas for Bulgarian works within that portion. This requirement, however, is only to be applied to the extent "practicable." Foreign broadcasters transmitting into Bulgaria must have a local representative, and broadcasters are prohibited from entering into barter agreements with television program suppliers.

INVESTMENT BARRIERS

The U.S.-Bulgaria Bilateral Investment Treaty (BIT) took effect in 1994 and provides guarantees for U.S. investors of both national and MFN treatment, the right to make financial transfers freely and without delay, international law standards for expropriation and compensation, and access to binding international arbitration. In 2003, to address several actual and potential incompatibilities between BIT obligations and EU law, the United States exchanged interpretive notes with the governments of Bulgaria and seven other European countries expected to join the EU over the next few years. The United States and the prospective EU Member States also agreed to make several narrow amendments to the texts of the relevant BITs. Both the United States and Bulgaria have ratified the BIT amendments, but the amendments will not enter into force until Bulgaria joins the EU.

The proposed constitutional amendment to lift the existing ban prohibiting foreigners to buy land in Bulgaria favors EU over U.S. investors. While EU citizens and entities will be allowed to acquire property directly by virtue of Bulgaria's accession treaty, all other foreigners will be able to do so only on the basis of an international agreement ratified by the Bulgarian Parliament. In the meantime, the constitutional prohibition against ownership of land by foreign individuals remains in force. However, foreign-owned companies registered in Bulgaria are considered to be Bulgarian persons. U.S. owned companies that register in Bulgaria therefore may acquire land in Bulgaria. Local companies in which foreign partners have controlling interests must obtain prior approval (licenses) to engage in certain activities: production and export of arms/ammunition; banking and insurance; exploration, development, and exploitation of natural resources; and acquisition of property in certain geographic areas. There are neither specific export-performance requirements nor specific restrictions on hiring expatriate personnel, although residence permits are often difficult to obtain.

A recent Bulgarian law eliminated the withholding tax on dividends for European investors, but U.S. investors face a withholding tax of 15 percent.

New insolvency rules in Bulgaria’s Commercial Code and its Law on Public Offering of Securities have greatly improved the legislative protection for minority shareholders. However, enforcement of the law's provisions is inadequate and corporate governance remains weak.

In 2003, Parliament approved a new Telecommunications Law which increases institutional and regulatory liberalization of the Bulgarian telecommunications sector but focuses more on institutional issues and the protection of state interests than on greater market liberalization. The new Telecommunication Act extended until December 2005 the Bulgarian Telecommunications Company’s (BTC) control over the sole telecommunication network.

A June 1999 law regulating gambling imposes additional requirements on foreigners organizing games of chance. Foreigners can receive a license to establish a casino in a hotel only if they satisfy one of the following conditions: (1) purchase or construction of a hotel rated four-star or higher; or (2) investment of at least $10 million and employment of at least 500 workers in economic activities unrelated to gambling.

According to U.S. businesses, other steps needed to improve the environment for foreign investment include improved creditor rights through improvements to bankruptcy law and procedures; reform of the judicial system; improved accounting standards and risk assessment; reform of the energy sector; and transparency and accountability in public policy to reduce the perception of corruption.

ELECTRONIC COMMERCE

Bulgaria’s Law on the Electronic Document and Electronic Signature went into effect in 2001. Three implementation ordinances for this law aimed at improved access to information services and promotion of electronic commerce were approved in 2002: Ordinance on Requirements for Algorithms for Advanced Electronic Signature; Ordinance for Activity of Certification-Service-Providers, Termination Procedure, and Requirements for Provision of Certification Services; and Ordinance for the Order of Registration of Certification-Service-Providers.

OTHER BARRIERS

Selective enforcement

Foreign investors complain that tax evasion by private domestic firms combined with the failure of the authorities to enforce collection from large, often financially-precarious, state-owned enterprises places the foreign investor at a disadvantage.

The multiplicity of Bulgarian licensing and regulatory regimes, their arbitrary interpretation and enforcement by the bureaucracy, and the incentives this creates for corruption, have long been seen as an impediment to investment, private business development and market entry. The 2003 Restriction of Administrative Regulation and Control of Economic Activity Act is expected to considerably lighten the potential of regulatory abuse at all levels of government, and when implemented, should improve the overall business environment.

Execution of judgment

Bulgarian and foreign observers caution that the proceedings for the execution of judgments under the Code of Civil Procedure remain slow and unpredictable. Further reform of the legal framework and its implementation will be needed. The U.S. does not currently have reciprocity with Bulgaria, so Bulgarian courts are not obliged to honor decisions of U.S. courts. In practice, execution of judgments is subject to delays, sometimes resulting from corruption and inefficiency in the judicial system.

Access to international arbitration

Companies that are not registered in Bulgaria, but that are involved in a business transaction in Bulgaria, can conduct arbitration in another country. However, a 2001 law that allows for an international arbiter when a foreign-owned, Bulgarian-registered company is involved requires the arbitration to take place in Bulgaria. The official language of the arbitration will be Bulgarian.

Textiles and apparel

As of January 1, 2002, Bulgaria eliminated all tariffs for industrial imports from the EU under its association agreement with the European Union, including textiles and apparel. Under Protocol One on Textile and Clothing Products of the European Agreement, the EU eliminated quotas on textile and clothing products originating in Bulgaria on January 1, 1998, and eliminated tariffs on textile and clothing products on January 1, 1997. Bulgaria levies tariffs on textile and apparel from the United States, but does not impose any quantitative restrictions (quotas) on imports from the United States.

CAMEROON

TRADE SUMMARY

The U.S. trade deficit with Cameroon was $208 million in 2004, an increase of $85 million from $123 million in 2003. U.S. goods exports in 2004 were $100 million, up 10.2 percent from the previous year. Corresponding U.S. imports from Cameroon were $308 million, up 43.9 percent. Cameroon is currently the 121st largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Cameroon in 2003 was $3.7 billion, up from $2.8 billion in 2002. U.S. FDI in Cameroon is concentrated largely in the manufacturing, utilities, and banking sectors.

IMPORT POLICIES

Cameroon is a member of the Central African Economic and Monetary Community (in French, CEMAC), which also includes Gabon, the Central African Republic, the Republic of Congo, Chad, and Equatorial Guinea. CEMAC countries have a common currency managed by a common central bank, share a common financial regulatory and legal structure, and maintain a common external tariff on imports from non-CEMAC countries. In theory, tariffs have been eliminated within CEMAC, and only a value-added tax should be applied to goods traded among CEMAC members. However, there has been some delay in fully achieving this goal, and currently both customs duties and the value-added tax are being assessed on imports within CEMAC. Trade levels between Cameroon and its neighbors are small compared to the trade flows between Cameroon and its principal trading partners in Europe.

To improve customs revenue collection, the Cameroon government contracted with the Swiss company SGS to assess and collect customs duties. The simple average of CEMAC's common external tariff (CET) is 18.4 percent. The CET is assessed through four tariff rates: 5 percent for essential goods, 10 percent for raw materials and capital goods, 20 percent for intermediate goods, and 30 percent for consumer goods. In addition, there are other taxes assessed on imports, which can vary according to the nature of the item, the quantity of the particular item in the shipment, and even the mode of transport. As a result, average customs charges are in reality much higher.

Import Licensing

Cameroon has simplified its import licensing procedures. A prospective importer is now only required to register with the local Ministry of Commerce and notify SGS of all imports above CFA2,000,000. Special import permits are granted to individuals who import items for personal use. However, export-import companies must secure a commerce register and a taxpayer's card from the Ministry of Economy and Finance prior to registering with the Ministry of Commerce. Contractors importing equipment and supplies related to public contracts may obtain a duty exemption from the Ministry of Economy and Finance only when the duties would count as part of the government investment in the project. CEMAC has no regional licensing system.

Documentation Requirements

Cameroon requires a commercial invoice and a bill of lading for all imported goods. Shipping marks and numbers must match exactly those on the invoices and the goods. Three copies of the invoice are necessary for surface shipments, while four copies are necessary for air shipments. The importer must also present an "agreement" (a written approval certificate acknowledging that the business operator is an exporter or an importer) and/or an exemption, if appropriate. Documentation of bank transactions is required only if the value of the imported goods exceeds CFA francs 2,000,000 (approximately $4,000). This is also true for pre-shipment inspection certificates, which require a "clean report of findings" from SGS. For certain imports, such as second-hand clothing, certificates of non-infestation are also required. SGS officials have also introduced a new service fee for importing second-hand automobiles.

There is a one-stop-shop for customs procedures. All documents must be submitted within 48 hours of a shipment's arrival. While at first this innovation reduced the time needed for processing of paperwork, delays attributed to corruption continue to hamper the process. The International Maritime Traffic Facilitation Committee is studying how to reduce customs-related delays.

Customs Valuation

Cameroon began implementing the WTO Agreement on Customs Valuation in July 2001. Cameroon assesses duties on its own estimated cost of production, rather than the actual purchase price, for three commonly subsidized goods -- beet sugar, flour, and metal rebar. Although the Cameroon government has tried to speed customs clearance, customs fraud is still a major problem and protracted negotiations with customs officers over the value of imported goods are common.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The Department of Price Control, Weights and Measures is officially responsible for standards administration. Labels must be written in both French and English, and must include the country of origin as well as the name and address of the manufacturer. The pre-shipment inspection contractor may inspect the quality of any goods shipped into the country. In the absence of any specified domestic norm or standard, international norms and standards apply. In practice, most imports are admitted into the country without the need to meet specific standards.

GOVERNMENT PROCUREMENT

Cameroon is an observer but not yet a member of the WTO Agreement on Government Procurement. The Government Procurement Regulatory Board (in French, Agence de Regulation des Marches Publics, or ARMP) administers public sector procurement. Although fewer than in previous years, local companies still receive some preferential price margins and other preferences on government procurement and development projects. As part of its economic reform program, the government has established more open tender announcements, established independent monitors for large government contract awards, and instituted more regular audits of tender awards. Cameroon's tight budgetary constraints require that most direct purchases by the Cameroon government have pre-identified sources of financing.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Cameroon is a party to the Paris Convention for the Protection of Industrial Property and the Universal Copyright Convention. IPR enforcement is problematic due to the small size of the market, the cost of enforcement, and the rudimentary understanding of IPR among government officials. U.S. industry complains that piracy is widespread. In November 2001, a law drafted with the assistance of WIPO and passed by the National Assembly sought to bring older Cameroonian laws into accord with the Bangui Agreement and TRIPS. Cameroon is the headquarters for the fourteen-nation West Africa Intellectual Property Organization (OAPI in French) which offers patents and trademarks registration.

SERVICES BARRIERS

Telecommunications

Cameroon has eliminated many restrictions on foreign trade in services and is gradually privatizing its telecommunications sector. In 1999, the government sold the state-owned mobile telephone company to a South African firm and gave a second mobile phone license to Orange, a French company. Negotiations to privatize the main state-owned telephone utility, CAMTEL, collapsed when the two best bidders withdrew their offers. In 2004, the government – with the consent of the World Bank, which is monitoring the government's privatization program – authorized CAMTEL to resume investments in the sector, which had previously been frozen for more than seven years. Through 2006, CAMTEL is to operate as if it were a private company, with no government support, while the government and the World Bank determine how to proceed with further privatization. Some companies are now moving into local VSAT systems for data transmission, international telephone service and Internet access. The Telecommunication Regulatory Board (in French ART) regulates the sector and would have to license new companies.

Banking

The Cameroonian government sold its last state-owned bank in January 2000, the last step in a major banking system restructuring. Four new private banks have begun operations since 2000, and there are now 10 banks in the sector. The Bank of Central African States (in French, BEAC) regulates the sector through the Regional Banking Commission, COBAC. COBAC has the authority to take disciplinary action. Both COBAC and the Cameroon Ministry of Economy and Finance must license banks, and there are special regulations for small-scale credit cooperatives. A national stock exchange in Douala was inaugurated in the second quarter of 2003 but has not yet begun trading operations.

Insurance

Cameroon is one of the fourteen French-speaking African nations that ratified the Inter-African Conference on Insurance Markets Treaty (CIMA) and adopted a common code with respect to the insurance sector. This supra-national code is designed to regulate the insurance sector in all signatory states. Enforcement of the CIMA code of regulations led to the closure of some weak insurance companies and the restructuring of the sector, which is almost completed. Foreign firms can operate in Cameroon, but they must have local partners. There are several foreign insurance companies (including one U.S. firm) working in Cameroon with Cameroonian partners.

INVESTMENT BARRIERS

Capital movements within CEMAC are completely free. Capital movements between CEMAC and third countries are permitted, provided that proper supporting documentation is available and prior notification is given to the exchange control authority. Regarding inward or outward foreign direct investment, investors are required to declare to the Ministry of Economy and Finance only those transactions above a prescribed threshold of CFA 100 million ($200,000), and they must provide such notification within 30 days of the realization of the investment. BEAC's decision to continue to monitor outward transfers, combined with its cumbersome payment system, have led many to conclude that controls on transfers remain in force.

The Cameroon government welcomes foreign investment, although the process of obtaining approvals for investment projects can be tedious. In March 2002, the parliament approved an investment charter that establishes a new framework for investments in Cameroon and that integrates recent laws relating to the forestry, mining and petroleum codes. Implementation of the new charter has been delayed; it may not take effect until 2007. In general, Cameroon's legal system is characterized by favoritism and corruption.

Cameroon has a Bilateral Investment Treaty with the United States that provides for, *inter alia*, non-discriminatory treatment, access by investors to international arbitration, the right to make transfers freely and without delay, and the right of establishment. Cameroon is a member of the

Organization for the Harmonization of Business Laws (in French, OHADA). OHADA codes are applicable throughout French-speaking West and Central Africa.

ELECTRONIC COMMERCE

Investments in the Internet sector are ongoing but it is still challenging to secure Internet access when out of the main cities, Yaoundé and Douala. Demand is growing rapidly, but Internet access, where available, is expensive and very slow during business hours. Cameroonian legislation governing Internet services has not been devised. Currently, no special restrictions on these services have been imposed.

OTHER BARRIERS

Agent and Distributor Rules

Agents and distributors must register with the Cameroon government, and their contracts with suppliers must be notarized and published in the local press.

Procedural and Financial Irregularities

Corruption is pervasive throughout the public and business sectors. The judicial system, characterized by long delays and poorly paid staff, has imposed major expenses on some American companies operating in Cameroon. Court decisions are often arbitrary and subject to corruption. Many accused individuals find it easier and cheaper to bribe a judge than to hire a lawyer to win a case. Local and foreign investors, including some U.S. firms, have found Cameroon courts too complicated and costly to resolve their contract or property rights disputes.

CANADA

TRADE SUMMARY

The U.S. trade deficit with Canada was $65.8 billion in 2004, an increase of $14.1 billion from $51.7 billion in 2003. U.S. goods exports in 2004 were $190.2 billion, up 11.9 percent from the previous year. Corresponding U.S. imports from Canada were $255.9 billion, up 15.5 percent. Canada is currently the largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Canada were $26.7 billion in 2003 (latest data available), and U.S. imports were $19.1 billion. Sales of services in Canada by majority U.S.-owned affiliates were $40.3 billion in 2002 (latest data available), while sales of services in the United States by majority Canada-owned firms were $44.7 million.

The stock of U.S. foreign direct investment (FDI) in Canada in 2003 was $192.4 billion, up from $170.2 billion in 2002. U.S. FDI in Canada is concentrated largely in the manufacturing, finance, and mining sectors.

A Trading Relationship Based on Free Trade

The North American Free Trade Agreement (NAFTA) came into force on January 1, 1994 and replaced a bilateral free trade agreement implemented in 1989. The bilateral phase-out of tariffs between Canada and the United States was completed on January 1, 1998, except for tariff rate quotas (TRQ) that Canada has not eliminated on certain supply-managed agricultural products. However, Canada still maintains some non-tariff barriers of concern at both the federal and provincial levels, impeding access to the Canadian market for U.S. goods and services.

IMPORT POLICIES

Supply-Managed Products

Canada closely restricts imports of certain domestic "supply-managed" agricultural products such as dairy products, eggs and poultry through the use of TRQs. This practice severely limits the ability of U.S. producers to increase exports to Canada above the TRQ volume.

Dairy: Over a number of years, the United States has argued before the WTO that Canada's dairy programs provided export subsidies to its dairy processors and farmers above the level that Canada committed to in the WTO. In its latest ruling in December 2002, a WTO Appellate Body found that Canada's system of subsidizing exports of dairy products continue to violate its WTO commitments. The United States and Canada reached agreement in May 2003 to comply with that report. Canada agreed to end all exports to the United States of subsidized dairy products and to bring all dairy exports to third countries within WTO export subsidy limits, both by August 1, 2003. To accomplish this, by the end of April 2003 all Canadian provinces had imposed regulations on all dairy production, including production by producers who do not hold domestic marketing quotas. The United States is monitoring Canada's compliance with the WTO ruling.

Margarine: The Province of Quebec continues to apply coloring restrictions on margarine. In addition, provincial restrictions on the marketing of butter/margarine blends and imitation dairy products have served to limit and, in certain cases, prohibit the sales of these products in many provinces. The provinces of Ontario, Manitoba and Saskatchewan are challenging Quebec's provincial coloring regulations.

Cheese snack foods: Canada remains unwilling to resume duty-free trade in cheese snack foods between the United States and Canada. Prior to 1999, cheese snack foods were traded duty-free between the U.S. and Canada. Canada ceased issuing duty-free import permits, effective September 1, 2001, and resumed applying a tariff of 245 percent on U.S. exports of breaded cheese sticks to Canada. Canada was responding to a 1999 U.S. Customs Service reclassification of cheese sticks, which subjected U.S. imports of Canadian cheese sticks to a U.S. TRQ and over-quota tariff. After USTR completed consultations with Congress on November 7, 2001, USTR stated that it was prepared to request that the President issue a Proclamation to return duty- and quota-free treatment to Canadian cheese sticks, provided Canada commits to providing the same tariff treatment for imports of similar U.S. cheese snack foods. In early January 2002, the Department of Foreign Affairs and International Trade informed USTR that Canada had no intention of reducing its duties or entering into negotiations with the United States.

Processed egg products: The Canadian Egg Marketing Agency maintains a dual pricing scheme for processed egg products. Under the regime, the domestic Canadian price for shell eggs is maintained at a level substantially above the world price. Producers are also assessed a levy on all eggs sold and a portion of the levy is used to subsidize exports of eggs. This practice artificially increases Canadian exports of egg products at the expense of U.S. exporters.

Fresh Fruits and Vegetables: Canada prohibits imports of fresh or processed fruits and vegetables in packages exceeding certain standard package sizes unless the Government of Canada grants a ministerial easement or exemption. To obtain an easement, Canadian importers must demonstrate that there is an insufficient supply of product in the Canadian domestic market. The bulk restrictions do not apply to intra-provincial shipments. These restrictions apply to all fresh and processed produce in bulk containers and have a particularly negative impact on U.S. potatoes, apples and blueberries. The United States entered into negotiations with Canada in 2004 in an attempt to remove this trade restriction. In addition, Canadian regulations on fresh fruit and vegetable imports prohibit consignment sales of fresh fruit and vegetables in the absence of a pre-arranged buyer.

Restrictions on U.S. Grain Exports

U.S. access to the Canadian grain market has been limited due in part to Canadian varietal controls. Canada requires that each variety of grain be registered and be visually distinguishable. Because U.S. varieties may not be visually distinct, they are not registered in Canada. As a result, U.S. wheat is being sold in Canada as "feed" wheat at sharp price discounts compared to the Canadian varieties. The Canadian Grain Commission (CGC) is currently in the process of introducing a new system called Variety Eligibility Declaration, or VED, which is designed to monitor and control the type of grain that enters the grain handling and transportation system. After extensive consultations on the operational details of the VED system, the CGC is close to making its proposals public.

Personal Duty Exemption

The United States has urged Canada to take steps to facilitate cross border trade for border residents by relaxing its taxation of goods purchased in the United States by Canadian tourists. Canada allows its residents a much smaller amount in non-dutiable purchases when they visit the United States than vice versa, and U.S. border states have repeatedly protested this inequity. While U.S. and Canadian personal exemption regimes are not directly comparable, the United States allows an $800 per person exemption every 30 days, while Canada has an allowance linked to the length of the tourist's absence and allows only C$50 for tourists absent for at least 24 hours and C$200 for visits exceeding 48 hours. This practice is designed to discourage shopping visits to the United States by border residents.

Wine and Spirits

Market access barriers in several provinces continue to hamper exports of U.S. wine and spirits to Canada. These market access barriers include "cost of service" mark-ups, listings, reference prices and discounting, distribution and warehousing policies.

The Canadian Wheat Board and State Trading Enterprises

The U.S. Government continues to have concerns about the monopolistic marketing practices of the Canadian Wheat Board. USTR's four prong approach announced in 2002 to level the playing field for American farmers is producing important results. Most notably, in WTO dispute settlement proceedings against the Canadian Wheat Board and the Government of Canada, a WTO panel found in favor of the United States on claims related to Canada's grain handling and transportation systems. Canada now must comply with those findings. Canada and the United States have agreed on a reasonable time period for compliance, giving Canada until August 1, 2005, to make all necessary legislative and regulatory changes to its grain handling and rail transportation regimes. This time frame is consistent with the period of time for compliance in comparable disputes.

In addition, the United States is seeking reforms to state trading enterprises (STEs) as part of the WTO agricultural negotiations. The U.S. proposal calls for the end of exclusive STE export rights to ensure private sector competition in markets currently controlled by single desk exporters; the establishment of WTO requirements to notify acquisition costs, export pricing, and other sales information for single desk exporters; and the elimination of the use of government funds or guarantees to support or ensure the financial viability of single desk exporters. The United States has succeeded in gaining in the WTO support for the elimination of trade-distorting practices of agricultural state trading enterprises. In October 2003 the Commerce Department imposed 8.87% antidumping and 5.29% countervailing duties on Canadian hard red spring wheat.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Restrictions on Fortification of Foods

Canadian requirements for foods fortified with vitamins and minerals have created a costly burden for some American food manufacturers who export to Canada. Health Canada restricts marketing of breakfast cereals and other products, such as orange juice, that are fortified with vitamins and/or minerals at certain levels. The current regulatory regime requires that products such as calcium-enhanced orange juice be treated as a drug, and forces manufacturers to label vitamin and mineral fortified breakfast cereals as "meal replacements." These standards impose costs on manufacturers who are forced to make separate production runs for the U.S. and Canadian markets.

The Government of Canada is expected to soon release for public consideration a draft policy on supplemental fortification of food and beverages that will reflect the study on Dietary Reference Intakes (DRIs) undertaken by the U.S. Institute of Medicine (IOM) and may offer more latitude to manufacturers for discretionary fortification of foods and beverages than the current regulatory regime. The new policy may reduce the cross-border discrepancy in fortification rules, however, the final regulations are not expected to come into force until late 2005 and may still present barriers to efficient cross-border trade.

Restrictions on Container Sizes

The Processed Products Regulations (Canada Agricultural Products Act) prescribe standard container sizes for a wide range of processed fruit and vegetable products. No other NAFTA country imposes similar mandatory container size restrictions. Currently Canada's "Processed Products Regulations" impose a requirement on manufacturers of baby food to sell in only two standardized container sizes: 4.5 ounces (128 ml) and 7.5 ounces (213 ml). This requirement to sell in container sizes that exist only in Canada creates an unnecessary obstacle to trade in baby food between Canada and the United States.

EXPORT AND DOMESTIC SUBSIDIES

Softwood Lumber

The 1996 U.S.-Canada Softwood Lumber Agreement expired on March 31, 2001. The bilateral agreement was put in place to mitigate the harmful effects of subsidies provided by the Canadian federal and provincial governments to Canadian lumber producers on the U.S. lumber industry. Upon expiration of the 1996 Agreement, U.S. industry filed antidumping and countervailing duty petitions regarding imports of Canadian softwood lumber. The U.S. International Trade Commission ("ITC") subsequently found that the U.S. industry was threatened with material injury by reason of dumped and subsidized imports of Canadian lumber, and the U.S. Department of Commerce ("Commerce") found company-specific antidumping rates ranging from 2.18 percent to 12.44 percent and a countrywide (except for the Maritime provinces) countervailing duty rate of 18.79 percent. On December 14, 2004, Commerce announced the results of the first administrative review of the AD/CVD orders, in which it assessed antidumping rates ranging from 0.92 to 10.59 percent, and a countervailing duty rate of 17.18 percent.

To date, Canada has challenged, or has announced its intent to challenge, the underlying Commerce and ITC findings in the original investigation in ten separate proceedings under the WTO and NAFTA, and litigation is ongoing. The WTO and NAFTA dispute settlement processes have only served to confirm the existence of Canada's subsidization of its softwood lumber industry and the dumping of lumber products into the U.S. market. On November 24, 2004, USTR requested the formation of an Extraordinary Challenge Committee ("ECC") to address deficiencies in the decisions of the NAFTA panel regarding the ITC's threat determination.

The United States continues to believe that it is in the interest of both the United States and Canada to reach a negotiated solution to their longstanding differences over softwood lumber, a view shared by many stakeholders on both sides of the border.

The United States is committed to seeking such a resolution and remains hopeful that we will be able to resume negotiations with Canada in the near future. In the meantime, the litigation will continue, and the United States will vigorously enforce its trade remedy laws.

Technology Partnerships Canada

Technology Partnerships Canada (TPC) is a Canadian Government program that supports the research and development activities of selected industries. Established in 1996, TPC provides loan funding for pre-competitive research and development activities for companies incorporated in Canada that operate in three strategic areas, including aerospace and defense. Funding covers approximately 25 percent to 30 percent of a project’s total costs, but may be significantly higher. Applicants must demonstrate that they have the capabilities to perform the R&D and that the project proposal has economic and commercial merit. To date, the program has made well over

CN$2.7 billion in funding commitments for over 600 projects, of which about 70 percent has been disbursed. Publicly available information indicates that the aerospace and defense industry receives the largest amount of funds under the TPC. Recent Canadian press coverage suggests that repayment rates are very low. The Canadian government restructured the TPC program in 1999 after a WTO Dispute Panel requested by Brazil determined that it was providing an illegal subsidy. The U.S. government will continue to monitor this program and its consistency with WTO provisions.

Pharmaceuticals

The U.S. pharmaceutical industry has raised concerns about aspects of pricing of patented medicines in Canada and encourages Canada and the Patented Medicine Prices Review Board (PMPRB) to move towards a more market-based review system.

The United States is monitoring Canadian policies with respect to patent and data protections. Canadian patent protection has improved following two WTO cases in which Canada agreed to, among other things, amend its patent law to provide 20-year patent protection to all patents filed before October 1989. Canada also has eliminated its regulations which previously allowed generic manufacturers to stockpile pharmaceuticals before a patent expired. However, Canada's compliance with its TRIPS and NAFTA obligations continues to be a source of concern. Although Canada has statutory data protection, several judicial rulings have cast doubt on how well these protections are being enforced as required by TRIPS Article 39.3 and NAFTA Article 1711. Canadian authorities allow parties other than the right-holder effectively to gain marketing approval in direct reliance on protected confidential data and it appears Canada may be in violation of TRIPS Article 39.3. In addition to this perceived discrepancy between the standard applied by Canadian courts and that provided under the TRIPS and the NAFTA, Canada apparently is failing to apply its "linkage regulations" effectively. Such regulations require that Health Canada determine if the marketing of generic pharmaceuticals infringes on existing name-brand patents.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Canada is a member of the World Intellectual Property Organization (WIPO), and adheres to a number of international agreements, including the Paris Convention for the Protection of Industrial Property (1971), the Berne Convention for the Protection of Literary and Artistic Works (1971), and the 1952 Universal Copyright Convention (UCC). Canada is also a signatory of the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty (together the WIPO Treaties), which set the standards for intellectual property protection in the digital environment, but has not yet ratified either treaty. Legislation to ratify both is expected to be introduced to Parliament in 2005.

Canada's Copyright Act contains two provisions under which Canada applies reciprocal rather than national treatment. The first provision is for the payment of a neighboring rights royalty to be made by broadcasters to artists. Under Canadian law, those payments are only guaranteed to artists from countries that are signatories of the 1961 Rome Convention. The United States is not a signatory of the Convention, and Canadian authorities have still not granted U.S. artists national treatment in the distribution of these royalties. The second provision is for the payment of a levy, dubbed the private copy levy, by manufacturers and importers of blank recording media to artists from countries that provide an equivalent payment to Canadian artists. The levy covers analog and digital tapes and diskettes, and was expanded in December 2003 to include MP3 players (though this coverage of MP3 players appears to have been struck down by a court decision in December 2004). Canada's copyright law stipulates this reciprocity criterion in the distribution of the private copy levy to foreign artists. The United States does not impose a levy on analog tape, only on digital audio recording media, with proceeds distributed to applicable artists, including Canadians.

The United States regards Canada's reciprocity requirement for both the neighboring rights royalty and the blank tape levy as denying national treatment to U.S. copyright holders. Consequently, USTR has placed Canada on its Special 301 "Watch List" for the past four years. While Canada may grant some or all of the benefits of the regime to other countries, if it considers that such countries grant or have undertaken to grant equivalent rights to Canadians, Canada has yet to grant these benefits with regard to the United States. A growing coalition of technology and retail companies advocating for the elimination of the private copy levy have successfully added the levy to the list of copyright issues that will be examined as a part of the ongoing Parliamentary review of the Copyright Act.

U.S. intellectual property owners are increasingly concerned about Canada's lax and deteriorating border measures and general enforcement that appear to be non-compliant with TRIPS requirements. The lack of *ex officio* authority for Customs officers makes the importation of pirated product into the Canadian market, from Asia and elsewhere, very easy. For Customs to perform a civil seizure of a shipment under the Customs Act, the right holder must obtain a court order, which requires detailed information on the shipment. However, the Criminal Code allows for a public officer in the course of duty to seize any item discovered to be in violation of the law: Customs can detain suspected counterfeit shipments and contact the RCMP, which can then proceed with investigation under criminal law.

Pirated and counterfeit goods include everything from software and CDs to shampoo and toys, all of which are openly displayed in malls, department stores and chain stores. Of particular concern is the growing number of counterfeit electrical products that pose a significant health and safety risk, potentially compromising the reputation of the right holder. Large amounts of pirate product are openly displayed alongside legitimate product in small retail establishments. The price differential between the pirated and legitimate software is significant and the majority of the pirated products are high quality, factory produced products from Asia. In addition to the sale of pirated software, these same retail establishments sell and install the circumvention devices, also made in Asia, that allow pirated product to be played in a legitimate console. Some retail establishments also sell cable circumvention devices.

Once pirated and counterfeit products clear Canadian Customs, any enforcement efforts are the responsibility of the Royal Canadian Mounted Police (RCMP) and the local police. The RCMP lacks adequate resources, training, and staff. Because there are not adequate laws in place to address these issues, few prosecutors are willing or trained to take on the few cases that come up. Those that are willing to take on an intellectual property case must devise very creative legal plans in order to prosecute. Where an infringement case has actually gone to trial, penalties imposed can be far from deterrent and jail time is rarely imposed. Border enforcement concerns were a major factor in the maintenance of Canada on the Special 301 "Watch List" in 2004.

Music File-Sharing

In March 2004 Canada's Federal Court of Appeal ruled that downloading music from the Internet using peer-to-peer (P2P) software does not constitute copyright infringement. The court denied a motion to compel internet service providers (ISP's) to disclose the identities of clients who were alleged to be sharing copyrighted music files. The recording industry is appealing this decision. Canadian ratification of the WIPO Copyright Treaty would remedy this problem. Another recent legal decision has highlighted Canada's lack of regulations regarding Internet Service Provider (ISP) Liability, specifically a mechanism for "notice and takedown." ISP Liability is not covered by the WIPO Treaties, so Canada will need to develop its own laws to address this issue. The Canadians have indicated that ISP Liability will be covered in the copyright legislation for the WIPO Treaties that they will submit to Parliament.

SERVICES BARRIERS

Audiovisual and Communications Services

In 2003, the Government of Canada amended the *Copyright Act* to ensure that Internet retransmitters are ineligible for the compulsory retransmission license until the Canadian Radio-television and Telecommunications Commission (CRTC) licenses them as distribution undertakings. Internet "broadcasters" are currently exempt from licensing. In 2003 the CRTC confirmed its intention to leave this exemption unchanged.

The Broadcasting Act lists among its objectives, "to safeguard, enrich and strengthen the cultural, political, social and economic fabric of Canada." The federal broadcasting regulator, the Canadian Radio Television and Telecommunications Commission (CRTC), is charged with implementing this policy. The CRTC requires that for Canadian conventional, over-the-air broadcasters, Canadian programs make up 60 percent of television broadcast time overall and 50 percent during evening hours (6 p.m. to midnight). It also requires that 35 percent of popular musical selections broadcast on radio should qualify as Canadian under a Canadian government-determined point system. For cable TV and direct to home (DTH) broadcast services, a preponderance (more than 50 percent) of the channels received by subscribers must be Canadian programming services. For other services, such as specialty television and pay audio services, the required percentage of Canadian content varies according to the nature of the service.

The CRTC also requires that the English and French television networks operated by the Canadian Broadcasting Corporation (CBC) not show popular foreign feature movies between 7 pm and 11pm. The only non-Canadian films that may be broadcast during that time must have been released in theaters at least two years previously, and not be listed in the top 100 of Variety Magazine's top grossing films for at least the previous ten years.

Under previous CRTC policy, in cases where a Canadian service was licensed in a format competitive with that of an authorized non-Canadian service, the CRTC could revoke the license of the non-Canadian service, if the new Canadian applicant so requested. This policy led to one de-listing in 1995, and has deterred potential new entrants from attempting to enter the Canadian market. In July 1997, the CRTC announced that it would no longer be disposed to take such action. Nonetheless, Canadian licensees may still appeal the listing of a non-Canadian service which is thought to compete with a Canadian pay or specialty service, and the CRTC will consider removing existing non-Canadian services from the list, or shifting them into a less competitive location on the channel dial, if they change format to compete with a Canadian pay or specialty service.

Radiocommunication Act

One of the foremost concerns of the Canadian Cable Telecommunications Association (CCTA) is the spread of unauthorized use of satellite television services. Industry findings, extrapolated on a national basis, established that 520,000 to 700,000 households within cabled areas use unauthorized satellite services. Any survey of the incidence of satellite theft outside cabled areas would add to these numbers.

This survey, combined with information obtained through Canadian film producers' investigations and related Internet newsgroups, supports the conclusion that there are approximately 1,000,000 illegal users of U.S. satellite systems in Canada, resulting in a significant annual loss to the legitimate satellite industry. Of this number of illegal users, it is estimated that over 90 percent are involved in the "black market" (i.e., signal theft without any payment to U.S. satellite companies), with the remaining 10 percent subscribing via "gray market." "Gray market" signal theft may be less attractive because of the unfavorable currency conversion in U.S. dollars. These survey results have led the Motion Picture Association to recalculate total losses to the U.S. motion picture industry due to signal theft in Canada. Annual losses to the U.S. motion picture industry due to audiovisual piracy in Canada were estimated to have been $122 million in 2002.

Late in 2003, the GOC introduced amendments to the Radiocommunication Act which would significantly increase penalties for signal theft and for the sale of unauthorized hardware. This draft legislation expired at the end of the Parliamentary session in November 2003 but has been reintroduced in substantially the same form in the current session.

A Quebec court ruled in October 2004 that the Canadian government's measures to prevent Canadians from subscribing directly to U.S.-origin satellite television services are unconstitutional. This ruling, which comes into general effect in October 2005 and which the government has appealed, could be read as striking down any measure to prevent Canadians from viewing foreign-origin television broadcasts. It is not yet clear whether the ruling "decriminalizes" only "gray market" signal theft, or "black market" theft as well.

Basic Telecommunications Services

Under the terms of the WTO Agreement on Basic Telecommunications Services, Canada's commitments permit foreign firms to provide local, long distance, and international services through any means of technology, on a facilities or resale basis. However, Canada retained a 46.7 percent limit on foreign ownership for all services except fixed satellite services and submarine cables. In addition to the equity limitations, Canada also retained a requirement for "Canadian control" of basic telecommunications facilities which stipulates that at least 80 percent of the members of a board of directors must be Canadian citizens. These restrictions prevent global telecommunications service providers from managing and operating much of their own telecommunications facilities in Canada. In addition, these restrictions deny foreign providers certain regulatory advantages only available to facilities-based carriers (e.g., access to unbundled network elements and certain bottleneck facilities). In April 2003 the House of Commons Committee on Industry recommended the complete removal of these restrictions.

Canada has revised its universal service system. Previously, contributions to universal service funds were based upon on a per-minute assessment. This system potentially overcompensated incumbent local suppliers, who also competed in the long distance sector. The Canadian regulator, CRTC, established rules for a more competition-neutral collection system as of January 1, 2001. On May 30, 2002, the CRTC released its price caps decision, which cut contribution rates by 10 percent to 20 percent. This new regime extends through 2006.

As a consequence of foreign ownership restrictions, U.S. firms' presence in the Canadian market as wholly U.S.-owned operators is limited to that of a reseller, dependent on Canadian facilities-based operators for critical services and component parts. This limits those U.S. companies' options for providing high quality end-to-end telecommunications services as they cannot own or operate their own telecommunications transmission facilities.

Barriers to Film Exports

The classification of theatrical and home video product distributed in Canada is within the exclusive jurisdiction of the provinces. There are six different provincial or regional classification boards to which MPA members must submit product destined for theatrical release. Most of these boards also classify product intended for home video distribution.

As a control device, and to display a video's Québec classification, the Québec Cinema Act requires that a sticker be acquired from the Régie du Cinéma and attached to each pre-recorded video cassette and DVD at a cost of C$0.40 per unit. The Québec government proposes to reduce the sticker cost to C$0.30 for English and French versions of films dubbed into French in Québec. In addition to the direct cost of acquiring the stickers, there are the administrative costs of attaching stickers to each unit and removing them from all returns, plus the per-title, per-distributor administrative fee of C$55.00 charged by the Régie.

In an effort to create a uniform, consumer-friendly classification system that more readily comports with national advertising campaigns and other practical concerns of the industry, the Canadian video distribution industry has initiated a voluntary national classification system for works distributed on videocassette and DVD. Under this system, a film's national rating is determined by averaging its provincial ratings and is displayed on the packaging. While some provinces accept the average national classification for the purpose of providing consumer information on pre-recorded video material, three of the provincial/regional boards - Manitoba, Québec, and the Maritime Provinces (New Brunswick, Nova Scotia and Prince Edward Island) - also require that their own classification be displayed.

The lack of unanimous acceptance of the voluntary national classification, and the negative precedent established by the Québec stickering regime continue to create significant consumer confusion and expense.

INVESTMENT BARRIERS

General Establishment Restrictions

Under the Investment Canada Act, the Broadcasting Act, the Telecommunications Act and standing Canadian regulatory policy, Canada maintains restrictions that inhibit new or expanded foreign investment in the energy, publishing, telecommunications, transportation, film, music, broadcasting, and cable television sectors.

Investment Canada Act

The Investment Canada Act (ICA) is intended to regulate foreign investment in Canada. The Government of Canada reviews the direct or indirect acquisition by a non-Canadian of an existing Canadian business of substantial size (as defined below). It also reviews the specific acquisition of an existing Canadian business or establishment of a new Canadian business by a non-Canadian in designated types of business activity relating to Canada's culture, heritage or national identity (as described below) where the federal government has authorized such review as being in the public interest. The Government of Canada must be notified of any investment by a non-Canadian to:

- establish a new Canadian business (regardless of size); or
- acquire direct control of any existing Canadian business which either has assets of C$5 million or more, or is in a business that is identified by regulation to be culturally sensitive, or in uranium production, financial services or transportation services; or
- acquire the indirect control of any existing Canadian business, the assets of which exceed C$50 million in value in a non-cultural business, or between C$5 million and C$50 million in a cultural business.

In January 2005, the C$5 million threshold was increased to C$250 million in cases where the country of the acquiring non-Canadian investor is a member of the World Trade Organization (WTO). The WTO exemption for amounts over $5 million does not include investments in production of uranium; financial services; transportation services or a cultural business. The dollar threshold varies year-to-year and is a function of GDP growth.

In addition, there is no review process applicable to an indirect acquisition of a Canadian business by a non-Canadian whose country is a member of the WTO. The reviewing authority is the Department of Canadian Heritage in the case of investments related to cultural industries, and the Department of Industry in other instances. The ICA sets strict time limits within which the reviewing authority must respond, in an effort to ensure that the legislation does not unduly delay any investment in Canada. In practice, Canada has allowed most transactions to proceed, though in some instances only after compliance by the applicant with certain undertakings.

Publishing Policy

Since January 1992, Canadian book publishing and distribution firms that would transfer to foreign ownership as a result of an indirect acquisition need not be divested to Canadians, but the foreign investor must negotiate specific commitments to promote Canadian publishing. Foreign investors may directly acquire Canadian book firms under limited circumstances. Under an agreement on periodicals reached with the United States in May 1999, Canada permits 100 percent foreign ownership of businesses to publish, distribute and sell periodicals. However, direct acquisition by foreign investors of existing Canadian-owned businesses continues to be prohibited.

Film Industry Investment

Canadian policies prohibit foreign acquisitions of Canadian-owned film distribution firms. A new distribution firm established with foreign investment may only market its own proprietary products. Indirect or direct acquisition of a foreign distribution firm operating in Canada is only allowed if the investor undertakes to reinvest a portion of its Canadian earnings in a manner specified by the Canadian Government.

GOVERNMENT PROCUREMENT

As a party to the WTO Government Procurement Agreement (GPA), Canada allows U.S. suppliers to compete on a non-discriminatory basis for its federal government contracts covered by the GPA. However, Canada has not yet opened "sub-central" government procurement markets (i.e., procurement by provincial governments), despite commitments in the GPA to do so no later than July 1997. Some Canadian provinces maintain "Buy Canada" price preferences and other discriminatory procurement policies that favor Canadian suppliers over U.S. and other foreign suppliers. Because Canada does not cover its provinces, Canadian suppliers do not benefit from the United States' GPA commitments with respect to 37 state governments' procurement markets. In recent years, several U.S. states and Canadian provinces have cooperated to make reciprocal changes in their government procurement systems that may enhance U.S. business access to the Canadian sub-federal government procurement market. However, the Administration and a number of U.S. states have expressed concern that Canadian provincial restrictions continue to result in an imbalance of commercial opportunities in bilateral government procurement markets.

ELECTRONIC COMMERCE

There are currently few barriers to U.S.-based electronic commerce in Canada. In the WTO context, Canada has consistently supported the U.S. initiative for duty-free cyberspace. The CRTC announced in 1999 that it would not attempt to regulate the Internet, but this decision is subject to review after five years (expected in 2004).

Canada’s Personal Information Protection and Electronic Documents Act, which took effect on January 1, 2001, requires persons or firms which collect personal information in the course of commercial activities to inform the subject of all purposes to which the data may be put, and to obtain informed consent for its use.

CHILE

TRADE SUMMARY

The U.S. trade deficit with Chile was $1.1 billion in 2004, an increase of $119 million from $990 million in 2003. U.S. goods exports in 2004 were $3.6 billion, up 33.5 percent from the previous year. Corresponding U.S. imports from Chile were $4.7 billion, up 27.8 percent. Chile is currently the 30th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Chile were $1.0 billion in 2003 (latest data available), and U.S. imports were $650 million. Sales of services in Chile by majority U.S.-owned affiliates were $2.3 billion in 2002 (latest data available).

The stock of U.S. foreign direct investment (FDI) in Chile in 2003 was $10.0 billion, the same as in 2002. U.S. FDI in Chile is concentrated largely in the finance, manufacturing, and mining sectors.

IMPORT POLICIES

Tariffs

Chile has actively pursued free trade agreements with its leading commercial partners for over a decade and has concluded several major pacts in the last several years. The U.S.-Chile Free Trade Agreement (FTA) entered into force on January 1, 2004. The FTA eliminates tariffs on 87 percent of bilateral trade immediately, and will establish duty-free trade in all products within a maximum of twelve years. Approximately 75 percent of U.S. farm exports will enter Chile duty-free within four years.

Chile has a relatively open trade regime. The uniform applied rate for virtually all goods is 6 percent. Importers also must pay a 19 percent Value Added Tax (VAT) calculated on the customs value plus the import tariff. (In the case of duty-free imports, the VAT is calculated on the customs value alone.)

There are several exceptions to the uniform tariff. Higher effective tariffs will remain throughout the U.S.-Chile FTA's 12-year transition period for wheat, wheat flour, and sugar, which are still subject to an import price band system. In August 2001, Chile formally registered its new consolidated sugar import tariff with the World Trade Organization (WTO), which increased the tariff from 31.5 percent to 98 percent. In order to increase the import tariff, Chile was obligated to offer quotas as compensation to its three principal suppliers, Argentina, Guatemala and Brazil.

Under the U.S.-Chile FTA, the 50 percent surcharge on used goods has been eliminated for U.S. originating goods. The importation of used passenger and cargo transport vehicles is prohibited, with a few exceptions. Many computer products and books enter Chile duty-free. Used clothing and other used textile articles classified under HS 63.09 became duty-free upon entry into force of the Agreement.

Import Controls

Customs authorities must approve and issue a report for all imports valued at more than $3,000. Imported goods must generally be shipped within 30 days from the day of the report, but longer periods may be authorized. Commercial banks may authorize imports of less than $3,000. Larger firms must report their import and export transactions to the Central Bank. Commercial banks may sell foreign currency to any importer to cover the price of the imported goods and related expenses, as well as to pay interest and other financing expenses that are authorized in the import reports. There are virtually no restrictions on the types or amounts of goods that can be imported into Chile, nor any requirements to use the official foreign exchange market.

Non-Tariff Barriers

Chile maintains a complex price band system for wheat, wheat flour, and sugar, which will be phased out under the U.S.-Chile FTA for imports from the United States by 2016. The price band system was created in 1985 and is intended to guarantee a minimum and maximum price for the covered commodities. When certain CIF prices (as calculated by Chilean authorities) fall below the floor, a special tax is added to the uniform tariff rate to raise the price to the floor. Price bands effectively set a minimum import price that is normally higher than both international and Chilean domestic prices.

The WTO ruled on October 23, 2002 that Chile's price band system was inconsistent with Article 4.2 of the Agreement on Agriculture. Following arbitration, Chile was given until December 23, 2003, to implement the rulings and recommendations of the WTO to bring the price band system into compliance with its WTO obligations. The Lagos Government and the Chilean Parliament agreed on a compromise proposal on August 7, 2003, eliminating the price band system on vegetable oils and introducing a number of modifications for wheat, wheat flour, and sugar. In the case of sugar, wheat, and wheat flour, the new values for the floor and ceiling prices began in November 2003 and will remain fixed until 2007. Beginning in 2008, the floor will be adjusted downward by 2 percent a year, until 2014, when Chile's President will evaluate whether to continue the price band system or eliminate it. Mixtures (e.g. high fructose corn syrup) containing more than 65 percent sugar content are now subject to the sugar price band system.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Prior to the FTA, many of Chile's trade-restrictive sanitary and phytosanitary (SPS) requirements prevented the entry of a number of U.S. agricultural and food exports. The FTA established a committee to follow up on the implementation of the WTO Agreement on the Application of Sanitary and Phytosanitary Measures and address any trade-restrictive SPS measures. During the negotiations, a bilateral committee was established to address a limited number of issues of concern to both the United States and Chile and important progress was made. However, in 2004 the United States continued to experience difficulties with Chile's unjustified and/or non-science-based restrictions.

Chile maintains restrictions on U.S. beef exports due to concerns about bovine spongiform encephalopathy (BSE) that are not supported by science and are not in conformance with international standards. As a result, the anticipated market access for U.S. beef to Chile envisioned under the FTA has not been realized.

Chile permits the planting of agricultural biotechnology products for export seed propagation only. Biotechnology crops may not be marketed domestically in Chile. A Presidential Commission in Chile was created to review all aspects of agricultural biotechnology and issued its report in June 2003. While the Commission's report supported the increased use of biotechnology crops in Chile for both export and domestic consumption, the old laws and regulations remain in place and restrictions on biotechnology crops continue.

GOVERNMENT PROCUREMENT

Individual government entities in Chile usually conduct their own procurement. In general, Chilean law calls for public bids for large purchases, although procurement by negotiation is permitted in certain cases. Foreign and local bidders on government tenders must register with the Chilean Bureau of Government Procurement. They must also post a bank and/or guarantee bond, usually equivalent to 10 percent of the total bid, to assure compliance with specifications and delivery dates. Chile is not a member of the WTO Agreement on Government Procurement.

The Government of Chile created the Information System for Procurements and Public Contracts for the Public Sector (www.chilecompras.cl) in March 2000. Through this site, anyone can offer products or services and register in the system as a potential supplier for government procurement in their area of interest, free of charge. The system also allows all public agencies with needs for goods and services to publish information concerning their public bidding processes and requirements on the Internet. Public agencies also publish detailed reports on the results of procurement processes.

The U.S.-Chile FTA covers the procurement of most Chilean central government agencies, 13 regional governments, 11 ports and airports, and more than 340 municipalities in Chile. The FTA establishes strong disciplines aimed at preventing discrimination against U.S. firms when bidding on government procurement opportunities that are covered by the FTA.

EXPORT SUBSIDIES

Chile's Ministry of Foreign Affairs promotes the country's exports, including through grants to private companies or industries for some export promotional activities. ProChile, the Export Promotion Bureau of Chile, promotes specific products to targeted exports markets. It provides matching funds of up to 50 percent to participating firms on approved market promotion activities.

Chile provides a simplified duty drawback program for nontraditional exports that reimburses firms a percentage of the value of the export. Companies purchasing capital equipment domestically can borrow up to seventy-three percent of the amount of customs duties that would have been paid on the capital goods if they had been imported. If the capital goods are ultimately used in the production of exports, the loan balances and any unpaid interest are waived and the producer is not required to repay the loan. Another export-promotion measure lets all exporters defer import duties for up to seven years on imported capital equipment or receive an equivalent subsidy for domestically produced capital goods. Chile has announced that it will phase out the simplified drawback program, in accordance with its WTO commitments.

Under Chile's separate Value Added Tax (VAT) reimbursement policy, exporters have the right to recoup the VAT that they have paid when purchasing goods and using services intended for export activities. Chile's export credit guarantee program guarantees 80 percent of exporter credits up to a limit of $132,000**.** Eligible exporters must have annual sales of less than $16.7 million.

The "Country Image" Program is an advertising campaign intended to enhance Chile's image in target export markets. The program is a joint venture between the Chilean public and private sector.

The FTA's Chapter on Market Access eliminates over a transition period the use of duty drawback and duty deferral for imports that are incorporated into any good exported to the U.S. or Chile. Full drawback rights are allowed for the first eight years from entry into force. Beginning on year nine, the amount of drawback allowed is reduced until reaching zero by year 12.

Export Controls

Chilean Customs authorities must approve and issue export reports. Exported goods must generally be shipped within 90 days from the date of the export report, but this period may be extended under certain conditions. Exporters may freely dispose of hard currency derived from exports. As with imports, exporters may use the formal or informal exchange market. Large firms must report all exports to the Central Bank, except for copper exports, which are authorized by the Chilean Copper Commission. Duty-free import of materials used in products for export within 180 days is permitted with prior authorization. Free-zone imports are exempt from duties and value-added tax if re-exported.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Chile was placed on the 2004 Special 301 Watch List because of substantive deficiencies in Chile's IPR laws and the lack of adequate IPR enforcement.

Patents and Trademarks

During 2004, the United States and Chile held a series of meetings on implementation of Chile's FTA obligations to protect intellectual property for pharmaceutical products.

The Institute of Public Health (ISP in Spanish), Chile's version of the U.S. Food and Drug Administration, has issued marketing approvals for unauthorized copies of patented products. Chilean authorities have not established effective coordination between the actions of the ISP and the Industrial Property Department, Chile's patent and trademark office, to prevent this undermining of effective patent protection. To try to prevent the issuance of such marketing approvals, U.S. firms have been obliged to engage in expensive and time-consuming court proceedings.

After a five-year delay, Chile's Congress approved in December 2004 legislation intended to bring the country into compliance with a number of its TRIPS commitments. The new law provides for, among other things, expedited court proceedings and authority to seize illegal copies of patented products. It also is intended to implement certain FTA obligations, such as the extension of the term of protection for patents when there are unreasonable delays in the patent application process, as well as stronger protection for confidential test data submitted to obtain marketing approval for pharmaceutical products and agricultural chemical products. Implementing regulations are expected in mid-2005. The Chilean Government maintains that the new law will address key weaknesses in Chile's patent and data protection. The United States will continue to work with the Chilean government to ensure full implementation of its FTA obligations.

Chile's Trademark Law is generally in line with international standards. Some U.S. trademark holders have complained of inadequate enforcement of trademark rights in Chile. In relation to

Internet domain names, the United States and Chile committed to make a system available for the resolution of disputes, following international standards, to address problems of cyber-infringement of trademarks. The FTA also requires Chile to respect the principle of "first-in-time, first-in-right" to trademarks and geographical indications (geographical names that have a particular association with a product).

Copyrights

Despite active enforcement efforts by the police, piracy of computer software and video recordings in Chile remains significant. Attempts to enforce copyrights in Chile have met with considerable delays in the courts and weak sentences. According to the International Intellectual Property Alliance (IIPA), estimated losses due to piracy of copyrighted materials totaled $106.7 million in 2004. Chile made two sets of amendments to its copyright law in 2003—one to implement TRIPS and one to implement immediate FTA obligations. The FTA's provisions increase the period of protection for copyrights and related rights to "life of the author plus 70 years", establishes strong prohibitions against circumvention of encryption technology attached to digital works, performances and phonograms, protects temporary copies, and establishes a legal framework to combat online piracy. The FTA also criminalizes end-user piracy and mandates both statutory and actual damages for IPR violations and penalizes tampering with anti-piracy technology. The United States will continue to work with the Chilean government to improve enforcement and ensure full implementation of the FTA's enforcement obligations, which enter into force in 2008.

Chile joined both the World Intellectual Property Organization (WIPO) Copyright Treaty and the WIPO Performances and Phonograms Treaty in April 2001.

SERVICES BARRIERS

Chile's relatively open services trade and investment regime stands in contrast to its relatively limited commitments under the General Agreement on Trade in Services (GATS). In particular, Chile maintains a "horizontal" limitation, applying to all sectors in Chile's GATS schedule, under which authorization for foreign investment in service industries may be contingent on a number of factors, including employment generation, use of local inputs and compensation. This restriction undermines the commercial value and predictability of Chile's GATS commitments.

Commitments in services under the U.S.-Chile FTA cover both cross-border supply of services and the right to invest**.** Market access commitments apply across a wide range of sectors, including computer and related services, telecommunications, audiovisual services, construction and engineering, tourism, advertising, express delivery, professional services, distribution services, adult education and training services and environmental services, among others.

Chile has made WTO commitments on most basic telecommunications services, adopting the WTO Reference Paper on Regulatory Commitments and ratifying the GATS Fourth Protocol. Nonetheless, U.S. companies occasionally complain of regulatory delays and a lack of transparency in regulatory decisions. Chile's WTO schedule of commitments excludes local basic telecommunications services, one-way satellite transmissions of Direct-to-Home and Direct Broadcast Satellite television services and digital audio services. It also excludes free reception broadcasting services. The U.S.-Chile FTA establishes requirements for greater levels of transparency in regulatory processes.

Financial Services

During the 1997 WTO financial services negotiations, Chile made commitments in banking services and most securities and other financial services. However, the Chilean WTO Commitment Schedule in the securities sector does not include asset fund management (mutual funds, investment funds, foreign capital investment funds, and pension funds). Chile also reserved the right to apply economic needs and national interest tests when licensing foreign financial service suppliers. In practice, Chile has allowed foreign banks to establish branches or subsidiaries and to provide the same range of services as domestic banks. Foreign insurance companies established in Chile face operate with unlimited access to the Chilean market as long as their legal incorporation meets requirements established in the Chilean Corporate Law Code. Foreign-based insurance companies cannot offer or contract insurance policies in Chile directly or through intermediaries.

Under the U.S.-Chile FTA, U.S. banks, insurance, securities and related services will operate in a more open, competitive and transparent market. The financial services chapter of the FTA includes core obligations concerning non-discrimination and most-favored nation treatment as well as additional market access obligations. U.S. insurance firms now have full rights to establish subsidiaries or joint ventures for all insurance sectors with limited exceptions. Chile also committed to phase in insurance branching rights and to modify its legislation to open cross-border supply of key insurance sectors such as marine, aviation and transport (MAT) insurance, insurance brokerage of reinsurance and MAT insurance. U.S. banks and securities firms are now allowed to establish branches and subsidiaries and may invest in local firms without restriction, except under very limited circumstances. U.S. financial institutions are also able to offer financial services to citizens participating in Chile's privatized voluntary saving plans and they have gained increased market access through Chile's mandatory social security system. Chile now allows U.S.-based firms to offer services cross-border to Chileans in areas such as financial information, data processing and financial advisory services, with limited exceptions. Chilean mutual funds are permitted to use foreign-based portfolio managers.

INVESTMENT BARRIERS

While Chile welcomes foreign investment, some controls and restrictions exist. Foreign direct investment is subject to *pro forma* screening by the Government of Chile. The Foreign

Investment Committee (FIC) of the Ministry of Economy is the institution responsible for approving foreign investment as well as setting terms and conditions for related contracts. FIC approval is required for the following categories of investment projects: those whose total value exceeds $5 million; those related to sectors or activities that are normally developed by the government or carried out by public services; those involving the mass media; and those made by foreign governments or by foreign public entities. Foreign investment projects worth more than $5 million are entitled to the benefits and guarantees of Decree Law (DL) 600. Under this law, the FIC signs a separate contract with each investor that stipulates the time period within which the investment will be implemented, which varies according to the type of investment. Under D.L. 600, profits from an investment may be repatriated immediately, but none of the original capital may be repatriated for one year.

Foreign investors in Chile may own up to 100 percent of an enterprise established under Chilean law, and there is no limit on the period during which they may own property in Chile. Foreign investors have access to all sectors of the economy with some limited exceptions in coastal trade, air transportation and the mass media. Chile permits investment in the fishing sector to the extent that an investor's home country permits Chilean nationals to invest in that sector. Most investment projects require additional permits and/or must fulfill other requirements aside from those set forth in D.L. 600 (e.g., pertaining to environmental protection). All investors, both local and foreign, must comply with sector-specific legislation at the national, regional and municipal levels.

Investors domiciled abroad may bring foreign currency into Chile under Chapter 14 of the Foreign Exchange Regulations of the Central Bank. Chapter 14 allows the investor to freely sell its foreign currency through the formal or informal exchange market. The Central Bank suspended in 2001 its prior controls on capital flows, including the "encaje", a deposit requirement that applied to short-term flows. The Central Bank also eliminated an earlier one-year holding period for indirect investment. Outflows associated with capital returns, dividends, and other investments no longer need government approval. Restrictions on the issuance of American Depositary Receipts (ADRs) have also been lifted. Chilean companies are free to take out loans or issue bonds in a wide range of currencies.

The U.S.-Chile FTA further strengthened the legal framework for U.S. investors operating in Chile. All forms of investment are protected under the FTA, including enterprises, debt, concessions, contracts and intellectual property. The FTA prohibits certain restrictions on investors, such as requirements to buy domestic rather than imported inputs.

The U.S. and Chilean Governments have been discussing a bilateral tax treaty. Until such a treaty takes effect, profits of U.S. companies will continue to be subject to taxation by both governments.

ELECTRONIC COMMERCE

In February 2000, Chile became the first country in Latin America to sign a Joint Statement on Electronic Commerce with the United States, highlighting the countries' agreement that the private sector should take the lead on the establishment of business practices related to electronic commerce. Under the U.S.-Chile FTA, each country committed to non-discriminatory treatment of digital products and to refrain from imposing customs duties on such products.

Chile's 2002 Digital Signature Act establishes the legal framework to regulate commercial operations completed in Chile over the Internet, essentially according electronic contracts the same legal recognition and protections that are given to traditional contracts. In 2003, the government began implementing the electronic invoice, which is intended to promote e-commerce, facilitate tax compliance by firms and strengthen the State's regulatory control. The Chilean Internal Revenue Service (SII) is currently conducting a trial run of the system with eight companies.

OTHER BARRIERS

Luxury Tax

A luxury tax of 42.5 percent is applied to automobiles whose CIF value exceeds $22,788.49. Under the terms of the FTA, the luxury tax on automobiles is being phased out over 4 years by raising the threshold value and lowering the rate each year. The luxury tax is charged on the amount exceeding the threshold value.

Distilled Spirit Tax and Other Taxes

Chile collects an *ad valorem* tax rate of 27 percent for all liquor. Beers and wine are also subject to a 15 *ad valorem* percent tax rate. Other merchandise subject to additional taxes are: articles of gold, platinum, ivory, jewelry, natural or synthetic precious stones (15 percent), compressed air arms, their accessories and bullets (15 percent), fine carpets and upholstery (15 percent), motor homes and caviar (15 percent), caviar preserves and its substitutes (15 percent), natural or artificial nonalcoholic beverages (13 percent).

CHINA

TRADE SUMMARY

The U.S. trade deficit with China was $162.0 billion in 2004, an increase of $38.0 billion from $124.1 billion in 2003. U.S. goods exports in 2004 were $34.7 billion, up 22.4 percent from the previous year. Corresponding U.S. imports from China were $196.7 billion, up 29.0 percent. China is currently the 5th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to China were $5.9 billion in 2003 (latest data available), and U.S. imports were $3.9 billion. Sales of services in China by majority U.S.-owned affiliates were $3.4 billion in 2002 (latest data available), while sales of services in the United States by majority China-owned firms were $125 million.

The stock of U.S. foreign direct investment (FDI) in China in 2003 was $11.9 billion, up from $10.5 billion in 2002. U.S. FDI in China is concentrated largely in the manufacturing, wholesale, and mining sectors.

In 2003, the United States Government observed a significant increase in bilateral trade friction, borne in part by a loss of momentum in China's WTO implementation. U.S. efforts in 2003 to reverse this trend culminated in a December meeting between President Bush and China's Premier, Wen Jiabao, at which the two leaders committed to upgrade the level of economic interaction and to undertake an intensive program of bilateral interaction with a view to resolving problems in the U.S.-China trade relationship. This new approach was exemplified by the highly constructive Joint Commission on Commerce and Trade (JCCT) meeting in April 2004, with Vice Premier Wu Yi chairing the Chinese side and Secretary of Commerce Evans and United States Trade Representative Zoellick chairing the U.S. side, and with leadership from Secretary of Agriculture Veneman on agricultural issues. At that meeting, which followed a series of frank exchanges covering a wide range of issues in late 2003 and early 2004, the two sides achieved the resolution of no fewer than seven potential disputes over China's WTO compliance.

Although U.S. stakeholders were significantly more satisfied with China's WTO performance in 2004 than in the previous two years, serious challenges remain and many U.S. businesses are still not able to maximize their opportunities in the Chinese market. Four areas continue to generate significant problems – intellectual property rights (IPR), services, agriculture and industrial policies.

In the IPR area, while China has made noticeable improvements to its framework of laws and regulations, the lack of effective IPR enforcement remains a major challenge. At the April 2004 JCCT, Vice Premier Wu Yi presented an "action plan" to address the IPR problem in China. Intended to "substantially reduce IPR infringement," this action plan calls for improved legal measures to facilitate increased criminal prosecution of IPR violations, increased enforcement activities and a national education campaign. The United States is monitoring implementation of this action plan closely and is scheduled to conduct an out-of-cycle review in early 2005 under the Special 301 provisions of U.S. trade law to assess China's implementation of its IPR commitments.

In the area of services, concerns in many sectors remain, largely due to transparency problems, delays in the issuance of legislative measures, and China's use of entry threshold requirements that exceed international norms. Indeed, Chinese regulatory authorities continued to frustrate efforts of U.S. providers of insurance, distribution, telecommunications and other services to achieve their full market potential in China.

In the area of agriculture, while the United States was able to make headway on some market issues, in particular biotechnology approvals and the removal of some problematic sanitary and phytosanitary barriers, a number of major concerns remain. Agricultural trade with China remains among the least transparent and predictable of the world's major markets. Capricious practices by Chinese customs and quarantine officials can delay or halt shipments of agricultural products into China, while sanitary and phytosanitary standards with questionable scientific bases and a generally opaque regulatory regime frequently bedevil traders in agricultural commodities.

China has also increasingly resorted to industrial policies that limit market access by non-Chinese origin goods and that aim to extract technology and intellectual property from foreign rights-holders. The objective of these policies seems to be to support the development of Chinese industries that are higher up the economic value chain than the industries that make up China's current labor-intensive base, or simply to protect less-competitive domestic industries.

Meanwhile, transparency concerns cut across sectors, as China's various regulatory regimes continue to suffer from systemic opacity, frustrating efforts of foreign – and domestic – businesses to achieve the potential benefits of China's WTO accession. Although China has made important strides in improving transparency across a wide range of national and provincial regulatory authorities, particularly at the Ministry of Commerce (MOFCOM), many other ministries and agencies have made less than impressive efforts to improve their transparency.

Overall, while China has a more open and competitive economy than 25 years ago, and China's WTO accession has led to the removal of many trade barriers, there are still substantial barriers to trade that have yet to be dismantled. In addition, some agencies and trade associations have renewed efforts to erect new technical barriers to trade. In many sectors, import barriers, opaque and inconsistently applied legal provisions, and limitations on foreign direct investment often combine to make it difficult for foreign firms to operate in China. The central government continues to implement industrial policies and protect noncompetitive or emerging sectors of the economy from foreign competition. Many provincial and lower-level governments have strongly resisted certain reforms that would eliminate sheltered markets for local enterprises or reduce jobs and revenues in their jurisdictions, although they have also supported market access for other foreign investors that do not pose a threat to local vested interests.

If China is to complete the implementation of its WTO commitments and institutionalize market-oriented reforms, it will need to eliminate mechanisms that allow government officials to intervene in the Chinese economy in a manner that is inconsistent with market principles. Despite its remarkable transformation over the past quarter century, China continues to suffer from its command economy legacy. As a result, Chinese economic policy-making often operates in a way that prevents U.S. businesses from achieving their full potential in the China market. China also needs to permit greater market access, especially in the services sector, in the ongoing Doha Development Agenda trade negotiations at the WTO.

IMPORT REGULATION

China has traditionally restricted imports through high tariffs and taxes, quotas and other non-tariff measures, and restrictions on trading rights. In 2002, as part of its first year in the WTO, China significantly reduced tariff rates on many products and the number of goods subject to import quotas, expanded trading rights for Chinese enterprises, and increased the transparency of its licensing procedures. However, during 2003, China's second year of WTO membership, while China continued to reduce tariff rates on schedule and made other implementation progress, bureaucratic inertia and a desire to protect sensitive industries contributed to a significant loss of the momentum created in the first year of China's WTO membership. In 2004, China made progress by implementing required tariff reductions on schedule, including those related to China's continued participation in the Information Technology Agreement, and by fully implementing its trading rights commitments in July, nearly six months ahead of schedule.

Trading Rights

Prior to its WTO accession, China restricted the types and numbers of entities with the right to trade. Only those domestic and foreign firms with trading rights could import goods into, or export goods out of, China. Restrictions on the type and number of firms with trading rights contribute to systemic inefficiencies in China's trading rights system and create substantial incentives to engage in smuggling and other corrupt practices.

Liberalization of China's trading rights system had been proceeding gradually since 1995. The pace accelerated in 1999 when MOFCOM's predecessor, the Ministry of Foreign Trade and Economic Cooperation (MOFTEC), announced new guidelines allowing a wide variety of Chinese firms with annual export volumes valued in excess of $10 million to register for trading rights. In August 2001, China extended this regulation to allow foreign-invested firms to export their finished products. Import rights of foreign-invested firms were still restricted to the importation of inputs, equipment and other materials directly related to their manufacturing or processing operations. Firms and individuals without trading rights, including foreign-invested firms with a manufacturing presence in China seeking to import products made outside of China, were required to use a local agent.

In its WTO accession agreement, China committed to substantial liberalization in the area of trading rights. Specifically, China committed to eliminate its system of examination and approval of trading rights and to make full trading rights automatically available to all Chinese enterprises, Chinese-foreign joint ventures, wholly foreign-owned enterprises and foreign individuals, including sole proprietorships, within three years of its accession, or by December 11, 2004, which was the same deadline for China to eliminate most restrictions in the area of distribution services. China further committed to expand the availability of trading rights pursuant to an agreed schedule during the first three years of its WTO membership.

Through the first two years of its WTO membership, China fully implemented the required liberalization of trading rights for Chinese enterprises. However, China did not meet the December 11, 2003 deadline to grant full trading rights to all joint ventures with foreign ownership. Instead, China continued to limit the availability of trading rights for these enterprises by imposing eligibility conditions, including requirements related to minimum registered capital, import levels, export levels and prior experience.

In January 2004, China circulated a draft of a new Foreign Trade Law for comment. This draft included provisions intended to institute an automatic trading rights system and bring China into full compliance with its WTO commitments on trading rights for all Chinese-foreign joint ventures, wholly foreign-owned enterprises and foreign individuals. With certain modifications requested by the United States, the new Foreign Trade Law took effect on July 1, 2004. It allows all individuals and organizations with business licenses, following registration, to import and export goods and technologies, except for those forbidden by the government or reserved for state trading.

In December 2004, in accordance with the schedule set forth in its WTO accession agreement, China also ended its practice of granting import rights or export rights for certain products – steel, natural rubber, wools, acrylic and plywood – only to designated enterprises. These products can now be traded by any domestic or foreign enterprise or individual.

Under the terms of China’s WTO accession, the importation of some goods, such as grains, cotton, vegetable oils, petroleum, sugar, fertilizers, news publications and related products, can still be reserved primarily for state trading enterprises. However, for grains, cotton, vegetable oils and fertilizers, China committed to make a portion of the tariff-rate quotas (ranging from 10 percent to 90 percent) available for importation through non-state traders. In some cases, the percentage available to non-state traders increases annually for a set number of years.

Import Substitution Policies

Throughout the 1990s, China gradually reduced formal import substitution policies. In its WTO accession agreement, China committed that it would not condition import or investment approvals on whether there are competing domestic suppliers or impose other performance requirements. In anticipation of this commitment, China enacted legal changes in 2000 and 2001 to eliminate local content requirements for foreign investments. Under the prevailing rules, however, investors are still "encouraged" to follow some of the formerly mandated practices. Instances in which the Chinese Government has reportedly pursued import substitution or similar policies include:

Semiconductors

China's 10th Five-Year Plan calls for an increase in Chinese semiconductor output from $2 billion in 2000 to $24 billion in 2010. In pursuit of this policy, China has attempted to encourage the development of China's domestic integrated circuit (IC) industry through, among other things, discriminatory VAT policies. In particular, through a series of measures, China has provided for the rebate of a substantial portion of the 17 percent VAT paid by domestic manufacturers on their locally produced ICs. China, meanwhile, charged the full 17 percent VAT on imported ICs, unless they were designed in China. After bilateral meetings on this issue failed to yield a change in China's policy, in March 2004, the United States filed the first and to date only WTO case against China. In the ensuing consultations, China signaled its willingness to discuss a possible resolution. In July 2004, the United States and China reached a settlement in which China agreed to immediately cease certifying new Chinese IC manufacturers or products as eligible for the VAT rebate and to issue the necessary regulations to eliminate the VAT rebate entirely by November 1, 2004, with an effective date no later than April 1, 2005. China also agreed to repeal the relevant implementing rules that had made VAT rebates available for ICs designed in China but manufactured abroad by September 1, 2004, with an effective date no later than October 1, 2004. China issued the promised measures in September and October 2004.

Fertilizer

In 2001, China began exempting all phosphate fertilizers except diammonium phosphate (DAP) from the VAT. DAP, a product that the United States exports to China, competes with other phosphate fertilizers produced in China, particularly monoammonium phosphate. U.S. producers have complained that China has employed its VAT policies to benefit domestic fertilizer production.

Automobile Investment Guidelines

China's automobile industrial policy offered significant advantages for foreign-invested factories using high-levels of local content. In 2001, in anticipation of China's new obligations as a WTO

Member, the State Economic and Trade Commission (SETC) issued Bulletin No.13, which provided that the preferential policy for automobile localization rates would be cancelled upon China's WTO accession. However, U.S. auto manufacturers reported that some local government officials continued to require local content and cited the old automobile industrial policy's standards. China also committed to issue a revised automotive industrial policy within two years of its WTO accession, or by December 11, 2003, but missed this deadline. In mid-2003, China began circulating a draft of a new automobile industrial policy for review by select domestic enterprises. Foreign automakers later obtained copies from their joint venture partners, but the U.S. Government's request for a copy was refused. In May 2004, China issued the final version of its new automobile industrial policy. This version had been revised to eliminate an earlier controversial requirement that separate distribution channels be used for domestic and imported autos, although it continued to include provisions discouraging the importation of auto parts and encouraging the use of domestic technology. It also included a number of vague provisions, such as in the area of complete knocked-down auto kits, whose implementation will warrant close scrutiny.

Telecommunications Equipment

There have been continuing reports of Ministry of Information Industry (MII) and China Telecom adopting policies to discourage the use of imported components or equipment. For example, MII has reportedly still not rescinded an internal circular issued in 1998 instructing telecommunications companies to buy components and equipment from domestic sources.

Tariffs and Other Import Charges

Under the terms of its WTO accession, China committed to substantial annual reductions in its tariff rates, with most of them taking place within five years of China's WTO accession. The largest reductions took place in 2002, immediately after China acceded to the WTO, when the overall average tariff rate fell from over 15 percent to 12 percent.

China's post-WTO accession tariff rates are "bound," meaning that China cannot raise them above the bound rates without "compensating" WTO trading partners, i.e., re-balancing tariff concessions or, in accordance with WTO rules, being subject to withdrawal of substantially equivalent concessions by other WTO members. "Bound" rates give importers a more predictable environment. China may also apply tariff rates significantly lower than the WTO-required rate, as in the case of goods that the government has identified as necessary to the development of a key industry. For example, China's Customs Administration has occasionally announced preferential tariff rates for items that benefit key economic sectors, in particular for the automotive, steel and chemical industries.

China's WTO accession commitments are having a dramatic effect on tariffs for many products of interest to the United States. Tariffs for some passenger cars were over 100 percent prior to accession, and will be reduced to 25 percent by July 1, 2006. China will also reduce its tariffs on auto parts from about 17 percent to 9.5 percent by July 1, 2006. China's elimination of tariffs on the products covered by the Information Technology Agreement (ITA) – semiconductors and semiconductor manufacturing equipment, computers and computer parts, software, telecommunications equipment and computer-based analytical instruments – began upon accession and is scheduled to be completed by January 1, 2005. U.S. exports of ITA goods to China continued to expand in 2004, increasing by 45 percent from January through September 2004, compared to the same period in 2003, and were projected to exceed $6 billion by the end of 2004.

China also continued its timely implementation of another significant tariff initiative, which involves chemicals. China continued to make the required tariff reductions on more than two-thirds of the 1,100-plus products covered by the WTO's Chemical Tariff Harmonization Agreement in 2004, with continuing significant results. U.S. chemical exports covered by this agreement increased by 36 percent from January through September 2004, and were projected to exceed $5.3 billion by the end of the year, well above 2003's healthy total of $3.9 billion.

A number of other industrial products benefiting from reduced tariffs showed strong growth in 2004. For example, U.S. machinery exports, including products such as machine tools, gas turbines and compressors for refrigeration machines, increased by 42 percent from January through September 2004, with a projected year-end total of $6.5 billion. U.S. medical and optical equipment exports increased by 34 percent from January through September 2004, with a projected year-end total of $2.1 billion.

Meanwhile, by January 1, 2004, tariffs for U.S. priority agricultural products had fallen from an average of 31 percent to 14 percent. The tariff reductions made by China contributed to a marked increase in certain U.S. exports to China in 2004, some of which were also aided by increased demand. Exports of some bulk agricultural commodities increased dramatically, particularly cotton exports (which totaled $1.3 billion during the period from January through September 2004, representing a 270 percent increase over the record level for the same period in 2003) and wheat exports (which totaled $414 million during the period from January through September 2004, representing an increase of nearly 1,600 percent over the same period in 2003). U.S. soybean exports continued to perform strongly, having more than doubled since China's WTO accession (despite declining from $1.2 billion for the period from January through September of 2003 to $929 million for the same period in 2004). Exports of consumer-oriented agricultural products increased by 20 percent from January through September 2004, when compared to the same period in 2003, and were projected to reach $526 million by the end of the year. Exports of forest products such as lumber also performed strongly, increasing by nearly 60 percent for the first nine months of 2004, with a projected year-end total exceeding $400 million. Meanwhile, fish and seafood exports, after having increased from $119 million in 2001 to $135 million in 2002, and then to $176 million in 2003, rose by another 55 percent in the first nine months of 2004 and were projected to reach $274 million by the end of the year.

However, China plans to maintain high duties on some products that compete with sensitive domestic industries. For example, the tariff on large motorcycles will only fall from 60 percent to 45 percent. Likewise, most video, digital video and audio recorders and players still face duties of around 30 percent. Raisins face duties of 35 percent.

Tariff Classification

Chinese customs officers have wide discretion in classifying a particular import. While foreign businesses might at times have benefited from their ability to negotiate tariff classification into tariff categories with lower import duty rates, lack of uniformity makes it difficult to anticipate border charges.

At the end of 2004, the National Development and Reform Commission (NDRC) was in the process of drafting the Administrative Measures for the Import of Automobile Components Fulfilling the Characteristics of a Whole Vehicle. The United States is closely monitoring the drafting process to determine whether any changes in tariff classifications for key automobile components are being contemplated.

Customs Valuation

Importers have often reported inappropriate valuation methods by customs officials, resulting in higher-than-necessary customs charges. In early 2002, China released new valuation regulations in order to bring its valuation practices into conformity with the WTO Customs Valuation Agreement.

Despite the issuance of the new valuation regulations, importers report that many Customs officials continue to use "reference price" lists rather than the actual transaction price for valuation purposes. While at times this can result in lower import charges, it often results in a higher dutiable value. China did make efforts to eliminate the practice of using reference pricing in 2004. Nevertheless, this practice continues to be found at many ports.

In addition, many Customs officials still automatically apply royalty and software fees to the dutiable value, even though China's new regulations correctly direct them to add those fees only if they are import-related and a condition of sale of the goods being valued. By the end of the year, although some improvement appears to have taken place, the new regulations have not led to uniform, WTO-consistent implementation by China's customs officials in this area.

Pursuant of the terms of its WTO accession, China committed to begin applying the WTO Decision on Valuation of Carrier Media Bearing Software for Data Processing Equipment by December 11, 2003. That decision makes clear that duties are to be assessed on the basis of the value of the underlying carrier medium, meaning, for example, the floppy disk or CD-ROM itself, rather than on the imputed value of the content, which includes the data recorded on a floppy disk or CD-ROM. In December 2003, following high-level bilateral engagement, China issued final regulations implementing the WTO decision and began charging duties based on the value of the underlying carrier medium. In 2004, some U.S. exporters reported that China's implementation of these regulations has been uneven and that the treatment of particular products varies from one Customs Administration office to another.

U.S. exporters also complained in 2004 about the Customs Administration's handling of a similar issue. With regard to imports of digital media that contain instructions for the subsequent production of multiple copies of products such as DVDs, the Customs Administration has been inappropriately assessing duties on the imports based on the estimated value of the yet-to-be-produced copies. The United States has urged China to follow the same principle that applies to carrier media bearing software and assess duties based on the value of the underlying carrier medium.

Rules of Origin

In 2004, China was still operating under regulations issued in the 1980s for the purpose of determining origin for import and export purposes. Nevertheless, even though China's Customs Administration was slow in drafting new regulations, importers did not report problems stemming from inappropriate application of rules of origin. With the issuance of the Regulations on the Origin of Imported and Exported Goods in August 2004 and the Rules on the Substantial Transformation Criteria under the Non-Preferential Rules of Origin in December 2004, China finally issued the measures intended to ensure that China's rules of origin for import and export purposes conform with WTO rules. These measures, which were not circulated in advance for public comment, were scheduled to take effect on January 1, 2005.

Border Trade

China's border trade policy continues to generate MFN and other concerns. China provides preferential import duty and VAT treatment to certain products, often from Russia, apparently even when those products are not confined to frontier traffic as envisioned by Article XXIV of GATT 1994. In June 2003, China began to address these concerns when it eliminated preferential treatment for boric acid and 19 other products. Nonetheless, it appears large operators are still able to take advantage of border trade policies to import bulk shipments across China's land borders into its interior at preferential rates. In addition, China continues to use border trade policies to provide preferential treatment for Russian timber imports, to the detriment of U.S. timber exporters.

Antidumping, Countervailing Duty and Safeguard Measures

Since acceding to the WTO, China has emerged as a significant user of antidumping (AD) measures, with a total of 59 antidumping measures covering 18 countries currently in place and 35 ongoing AD investigations in progress. China continued to actively apply its antidumping law in 2004, initiating several new investigations, five of which involved U.S. exports.

Chemical products remain the most frequent target of Chinese antidumping actions.

Most of the rules and regulations used by MOFCOM to conduct its AD investigations were issued as provisional measures by MOFCOM's predecessor agencies − MOFTEC and the State Economic and Trade Commission − shortly after China acceded to the WTO. While these measures generally represent good-faith efforts to implement the relevant WTO commitments and to improve China's pre-WTO accession measures, they also contain vague language, have gaps in areas of practice and allow inordinate discretion. Meanwhile, China's handling of AD investigations and reviews continues to raise concerns in key areas such as transparency and due process. Concerns with transparency, including access to information, are especially acute with regard to the injury portion of investigations. The United States is seeking to clarify and address these concerns both bilaterally and multilaterally.

To date, China has not initiated a countervailing duty investigation. China's only safeguard measure was removed at the end of 2003 after being in place for less than two years.

The Supreme People's Court has issued a judicial interpretation covering the review of AD and other trade remedy decisions. To date, however, judicial review of these types of decisions remains untested.

Non-Tariff Barriers

China's WTO accession agreement obligated China to address many of the non-tariff barriers it had historically used to restrict trade. For example, China is obligated to phase out its import quota system, apply international norms to its testing and standards administration, remove local content requirements, and make its licensing and registration regimes transparent. At the national level, China made progress following its WTO accession in reforming its testing system, revising regulations requiring local content, and improving overall regulatory transparency, including in the licensing area. Despite this progress, however, as China's trade liberalization efforts moved forward, some non-tariff barriers remained in place and even increased in 2004.

Three years after China's WTO accession, many U.S. industries complain that they face significant non-tariff barriers to trade, which are discussed in more detail in various sections below. These barriers include, for example, regulations that set high thresholds for entry into service sectors such as banking and insurance, selective and unwarranted inspection requirements for agricultural imports and the use of questionable sanitary and phytosanitary measures to control import volumes. Many U.S. industries have also complained about China's manipulation of technical regulations and standards to favor domestic industries.

Import Quotas

In the past, China often did not announce quota amounts or the process for allocating quotas. The government set quotas through negotiations between central and local government officials at the end of each year. Quotas on most products were eliminated or scheduled to be phased out under the terms of China's WTO accession. China's accession agreement required China to eliminate existing quotas for the top U.S. priority products upon accession and phase out remaining quotas, generally by two years but no later than five years after accession. On January 1, 2004, China eliminated import quotas on crude oil, refined oil, natural rubber and tires, in accordance with the schedule set forth in its WTO accession agreement. In prior years, China had eliminated import quotas on other products on schedule (such as air conditioners, sound and video recording apparatus, color TVs, cameras and watches) or ahead of schedule (crane lorries and chassis and motorcycles). When the auto quotas officially end on January 1, 2005, China will no longer have any import quotas in place.

Tariff-Rate Quotas

In 1996, China claimed to have introduced a tariff-rate quota (TRQ) system for imports of wheat, corn, rice, soy oil, cotton, barley, and vegetable oils. The quota amounts were not publicly announced, application and allocation procedures were not transparent, and importation occurred through state trading enterprises. China later introduced a TRQ system for fertilizer imports. Under these TRQ systems, China places quantitative restrictions on the amount of these commodities that can enter at a low "in-quota" tariff rate; any imports over that quantity are charged a prohibitively high duty.

As part of its WTO accession commitments, China was to establish large and increasing TRQs for imports of wheat, corn, rice, cotton, wool, sugar, vegetable oils, and fertilizer, with most in-quota duties ranging from 1 percent to 9 percent. Each year, a portion of each TRQ is to be reserved for importation through non-state trading entities. China's accession agreement sets forth specific rules for administration of the TRQs, including increased transparency and reallocation of unused quota to end-users that have an interest in importing.

However, China's implementation of its TRQ systems has been problematic since it joined the WTO. Regulations for the administration of the TRQ systems were issued late, did not provide the required transparency and imposed burdensome licensing procedures. TRQ allocations in 2002 were also plagued by delays. Chinese officials repeatedly argued that the agencies responsible for TRQ administration were unprepared for such a difficult task, resulting in one-time delays in allocations. China's performance improved in certain respects during 2002, and 2003 TRQs were issued close to the prescribed times. However, the most serious problems – lack of transparency, sub-divisions of the TRQ, small allocation sizes and burdensome licensing procedures – persisted in 2003.

In June 2003, following high-level meetings between the United States and China, China agreed to take steps to address most of these concerns as they related to agricultural commodities. China followed through in part in October 2003, when NDRC issued new regulations for shipments beginning January 1, 2004. Key changes made by these regulations included the elimination of separate allocations for general trade and processing trade, the elimination of certain unnecessary licensing requirements, and the creation of a new mechanism for identifying allocation recipients. In 2004, improvements in NDRC's TRQ administration became evident. NDRC implemented the regulatory provision calling for the elimination of separate allocations for general trade and processing trade, increased the size of quota allocations, and improved its handling of reallocations. At the same time, transparency continued to be problematic, although some improvement did take place for some of the commodities subject to TRQs. In addition, while these systemic changes were taking place, exports of some bulk agricultural commodities from the United States continued to show substantial increases, largely due to market conditions. In particular, despite some lingering concerns with NDRC's handling of the cotton TRQs, U.S. cotton exports totaled $1.3 billion during the period from January through September 2004, representing a 270 percent increase over the record level for the same period in 2003. In addition, U.S. wheat exports totaled $414 million during the period from January through September 2004, representing an increase of nearly 1,600 percent over the same period in 2003.

Meanwhile, the administration of China's TRQ system for fertilizer, handled by SETC and subsequently MOFCOM, has begun to improve, and U.S. exporters have made inroads into China's market. However, U.S. exporters continue to complain about a lack of transparency and the inconsistent interpretation of the relevant regulations by provincial government authorities.

Import Licenses

In the early 1990s, China began to reduce substantially the number of products subject to import licensing requirements. With its WTO accession in December 2001, China committed to the fair and non-discriminatory application of licensing procedures. Among other things, China also committed upon its WTO accession to limit the information that a trader must provide in order to receive a license, to ensure that licenses are not unnecessarily burdensome, and to increase transparency and predictability in the licensing process.

MOFTEC issued new regulations and implementing rules to facilitate licensing procedures shortly after China's accession to the WTO. However, license applicants initially reported that they have had to provide sensitive business details unnecessary for simple import monitoring. In some sectors, importers also reported that MOFTEC was using a "one-license-per-shipment" system rather than providing licenses to firms for multiple shipments. This system acted as an impediment to trade. MOFTEC began to allow more than one shipment per license in late 2002 following U.S. interventions, although the measure authorizing the "one-license-per-shipment" system apparently remains in place.

China's inspection and quarantine agency, the State Administration of Quality Supervision and Inspection and Quarantine (AQSIQ), has also imposed inspection-related requirements that have led to restrictions on imports of some U.S. agricultural goods. In particular, two AQSIQ measures issued in 2002 require importers to obtain an import inspection permit or a quarantine permit for many agricultural goods, such as livestock, poultry, grains, oilseeds, planting seeds, horticultural products, and hides and skins, before they can enter China. U.S. exporters have expressed concern that AQSIQ is using the procedures provided for by these measures to control the pace and quantity of some imports, which would be contrary to China's market access and import licensing commitments. They have also been concerned about the burdensome nature of these procedures and reported selective enforcement by AQSIQ.

Following multiple U.S. interventions, some progress appeared to have been achieved in early 2003, as China discontinued arbitrary limits on imported poultry and pork shipments. However, many U.S. concerns have not yet been addressed. In 2004, China made more progress. AQSIQ issued a new decree in June 2004, known as Decree 73, which made quarantine inspection permits for animal and plant products more workable by extending their validity period from three to six months and thereby providing importers with a longer window of opportunity to purchase, transport and discharge their cargoes before their permits expire. In August 2004, China also issued an announcement that appears to exempt 15 categories of animal and plant products from the requirement to obtain quarantine inspection permits in advance of entry and prior to signing an import contract.

While both of the developments in 2004 were positive, Decree 73 raised some new concerns with regard to required contract terms and commercial risk. In an environment where AQSIQ has changed regulations with little or no warning, many U.S. shippers complained that Decree 73 increased the financial risk for exporters shipping commodities to China. China repeatedly assured the United States that Decree 73 was not intended to introduce any new requirements and that U.S. soybean exports, in particular, would not be affected by it. As 2004 was drawing to an end, it appeared that Decree 73 may have created uncertainty about China's presence as a purchaser in the soybean market and contributed to general downward pressure on world soybean prices. Nevertheless, U.S. soybean exports to China continued to go forward, and trade in the other grains and feeds affected by Decree 73 did not appear to have been negatively impacted.

INTERNAL POLICIES

Taxation

In April 2001, the National People's Congress Standing Committee passed long-awaited changes to the tax collection law, designed to standardize and increase the transparency of China's tax procedures. The State Council issued detailed regulations for the implementation of this law in September 2002. As part of a broader campaign to "rectify market order" and eliminate inter-provincial barriers to domestic commerce, the Chinese central government also implemented measures to prevent local governments from applying tax treatment that discriminated in favor of locally owned firms.

In order to narrow the widening urban-rural income gap, the Central Committee of the Communist Party of China and the State Council issued Document No. 1 of 2004, which instructed the governments at all levels to reduce the agricultural tax rate of 8.4 percent by 1 percent in 2004, along with the removal of all taxes on special farm produce except for tobacco. Document No. 1 also calls for further reductions in the agricultural tax rate until it is totally eliminated within five years. Where fiscally feasible, governments were also called upon to reduce or eliminate agricultural taxes more quickly. By the end of 2004, 22 of China's 31 provincial-level governments had eliminated agricultural taxes.

Foreign investors, including those who have used investment as an entry point to the Chinese domestic market, have benefited from investment incentives, such as tax holidays and grace periods, which allow them to reduce substantially their tax burden. Domestic enterprises have long resented rebates and other tax benefits enjoyed by foreign-invested firms, and these benefits may be gradually phased out.

Application of China's single most important revenue source – the VAT, which ranges between 13 percent and 17 percent, depending on the product – is uneven. Importers from a wide range of sectors report that, because taxes on imported goods are reliably collected at the border, they are sometimes subject to application of a VAT that their domestic competitors often fail to pay. As discussed above (in the section on Import Substitution Policies), the United States was successful in obtaining China's agreement to remove discriminatory VAT policies favoring domestically produced semiconductors. China's selective exemption of certain fertilizer products from the VAT has also operated to the disadvantage of imports from the United States. In addition, China retains an active VAT rebate program for exports, although rebate payments are often delayed. In 2003, China announced the reduction of VAT rebates for exports by three percentage points partly in response to foreign complaints about an under-valued RMB. Although State Administration of Taxation officials plan eventually to eliminate rebates in order to increase tax revenues, China has continued this practice in order to spur domestic economic growth. In December 2004, for example, the Ministry of Finance (MOF) and the State Administration of Taxation issued a circular announcing an increase in the VAT rebate rate from 13 percent to 17 percent for the export of certain IT products, including integrated circuits, independent components, mobile telecommunication equipment and terminals, computers and periphery equipment, and numerical-controlled machine tools.

China's 1993 consumption tax system continues to raise concerns among U.S. exporters. Because China uses a substantially different tax base to compute consumption taxes for domestic and imported products, the tax burden imposed on imported consumer goods ranging from alcoholic beverages to cosmetics to automobiles is higher than for competing domestic products.

Standards, Technical Regulations and Conformity Assessment Procedures

In its WTO accession agreement, China committed that it would ensure that its regulatory authorities apply the same standards, technical regulations and conformity assessment procedures to both imported and domestic goods and use the same fees, processing periods and complaint procedures for both imported and domestic goods. China also committed that, in order to eliminate unnecessary barriers to trade, it would not maintain multiple or duplicative conformity assessment procedures and would not impose requirements exclusively on imported products. China further committed to ensure that its standards developers, regulatory authorities and conformity assessment bodies operated with transparency and allowed reasonable opportunities for public comment on proposed standards, technical regulations and conformity assessment procedures.

In anticipation of these commitments, China devoted significant energy to reforming its standards and testing and certification regimes prior to its WTO entry. In April 2001, China merged its domestic standards and conformity assessment agency and entry-exit inspection and quarantine agency into one new organization, AQSIQ. Chinese officials explained that this merger was designed to eliminate discriminatory treatment of imports, including requirements for multiple testing simply because a product was imported rather than domestically produced. China also formed two quasi-independent agencies administratively under AQSIQ: the Certification and Accreditation Administration of China (CNCA), charged with the task of unifying the country's conformity assessment regime, and Standardization Administration of China (SAC), responsible for setting mandatory national standards and unifying China's administration of product standards and aligning its standards and technical regulations with international practices and China's commitments under the WTO Agreement on Technical Barriers to Trade.

Since AQSIQ's issuance of rules in January 2002 to facilitate its adoption of international standards, China has made significant progress toward its goal of having 70 percent of its nearly 20,000 technical regulations based on international standards within 5 years of its accession to the WTO. Nevertheless, in a number of sectors, including autos, auto parts, telecommunications equipment, wireless local area networks (see the "WAPI" section below), radio frequency identification tag technology, audio-video coding, whiskey and other distilled spirits, concern has grown as China has pursued the development of unique technical requirements, despite the existence of well-established international standards. These China-specific standards, which sometimes appear to lack a sound basis, could create significant barriers to entry into China's markets because of the high cost of compliance for foreign companies.

The lack of transparency in China's standards development process also troubles many foreign companies. The vast majority of standards-setting bodies are not fully open to foreign participation, in some cases refusing membership to foreign firms and in other cases refusing to allow companies with majority foreign ownership to vote. In some cases, foreign firms are allowed non-voting observer status, but are required to pay membership fees far in excess of those paid by the voting members.

Despite China's commitment to apply the same standards and fees to domestic and imported products upon its accession to the WTO, many U.S. industries have complained about China's manipulation of technical regulations and standards to favor domestic industries. In fact, SAC issued a strategy report in September 2004 promoting China's development of standards and technical regulations as a means of protecting domestic industry as tariff rates fall. At the sub-national level, importers have expressed concern that local officials do not understand China's WTO commitments and apply arbitrary technical regulations and standards to protect local industries. These problems are compounded by the fact that coordination between AQSIQ and its new affiliated bodies, CNCA and SAC, is lacking, as is coordination between these bodies and China Customs and other ministries and agencies, at both the central and local government levels, with responsibilities relating to technical regulations and standards.

Meanwhile, some importers report discriminatory treatment and uneven enforcement of technical regulations and standards. For example, foreign companies' products can only be tested at certain laboratories. Limited testing and certification capacity means that evaluations sometimes take much longer than international best practice would suggest appropriate. As testing and certification capacity expands to meet this demand, U.S. companies with multi-country operations worry that inexperienced laboratories might make negative determinations that would have global consequences for the company. Meanwhile, redundant testing requirements continue to trouble U.S. companies, particularly in cosmetics, new chemicals, pharmaceuticals, medical equipment, cellular telephones and other telecommunications products and consumer electronic products. In December 2004, SAC created technical committees to develop standards for testing environmental equipment, genetically modified organisms, and new plant and animal varieties, suggesting that foreign companies may soon see additional requirements in these industries as well.

U.S. companies also cite problems with a lack of transparency in the certification process, lack of coordination among standards bodies, burdensome requirements and long processing times for licenses. Some companies have also expressed concern that their intellectual property will be released to competitors when they submit samples of high-technology products for mandatory quality testing. Technical committees that evaluate products for licensing and certification are generally drawn from a pool of government, academic and industrial experts that companies fear may be too closely associated with their competitors. In some cases, laboratories responsible for testing imported products are affiliated with domestic competitors, making the possibility of intellectual property being released more likely.

China's designated standards notification authority, MOFCOM, has been notifying proposed technical regulations and conformity assessment procedures to WTO members, as required by the WTO Agreement on Technical Barriers to Trade (TBT Agreement). Almost all of these notified measures have emanated from AQSIQ or SAC, however, and generally have not included measures drafted by other agencies. Lack of meaningful comment periods is also an issue. In many other cases, Chinese regulatory authorities provided insufficient time to consider interested parties' comments before a regulation was adopted.

In 2004, SAC sought to achieve tighter interagency coordination for a wide-ranging review of existing standards, and increased China's participation in international standards development organizations. SAC also issued two strategy reports discussing the importance of transparency and interagency coordination in the development of technical regulations and standards. These reports also allude to the use of technical regulations and standards in order to minimize royalty payments to foreign intellectual property holders, encourage technology transfer on terms favorable to Chinese companies, and enhance national prestige.

WAPI

A particularly significant example of China's development of unique technical requirements, despite the existence of well-established international standards, arose in May 2003, when China issued two mandatory standards for encryption over Wireless Local Area Networks (WLANs), applicable to domestic and imported equipment containing WLAN (also known as Wi-Fi) technologies. These standards, which were scheduled to become fully effective in June 2004, incorporated the WLAN Authentication and Privacy Infrastructure (WAPI) encryption technique for secure communications. This component of the standards differed significantly from internationally recognized standards. China sought to enforce the use of WAPI by providing the necessary algorithms only to a limited number of Chinese companies. U.S. and other foreign manufacturers would be compelled to work with and through these companies, some of which were competitors, and provide them with technical product specifications. Following high-level bilateral engagement, AQSIQ, SAC and CNCA jointly announced that China would suspend indefinitely its proposed implementation of WAPI as a mandatory wireless encryption standard, that it would work to revise its WAPI standard, taking into account comments received from Chinese and foreign enterprises, and that it would participate in international standards bodies addressing WAPI and wireless encryption for computer networks generally.

New Chemical Regulation

In September 2003, China's State Environmental Protection Administration (SEPA) issued a regulation requiring manufacturers and importers of new chemicals to apply to SEPA's Chemical Registration Center (CRC) for approval and to provide extensive test data to substantiate the physical properties, consumer safety and environmental impact of the new chemical. U.S. industry is primarily concerned that CRC has not been able to make decisions on the approval of new chemicals in a timely manner. U.S. industry estimates that U.S. companies have submitted 35-40 completed applications for new chemicals since October 15, 2003. According to the most recent information available from CRC, approximately 10 of these applications have been approved. U.S. industry notes that several applications have been pending well beyond the 120-day timeline set forth in the regulation. U.S. industry also complains of shifting requirements and implementation changes, such as recently expanded eco-toxicity testing requirements, which mandate that certain eco-toxicity testing (fish eco-toxicity and bio-degradation studies) be carried out in one of six SEPA-accredited laboratories in China. These accredited laboratories have all been established since summer 2004 (in response to the regulation) and industry fears that if inexperience leads one of these new labs to declare a product unsafe, it could affect sales globally. China's lack of a low-volume exemption (exemption where trade in a given chemical falls below an annual volume threshold) also appears to hinder the importation of U.S. chemicals, particularly for high value specialty chemicals sold in small quantities.

Scrap Recycling

In late 2003, China's AQSIQ issued a notice requiring overseas scrap material exporters to register with AQSIQ. The stated purpose of the new requirement was to better monitor the entry of scrap shipments into China reportedly due to high occurrences of receiving dangerous waste and illegal material in past shipments from overseas. It was not until May 2004 that AQSIQ issued the implementing rules. These rules established registration procedures, including an application deadline of July 1, 2004, and set substantive requirements. In response to U.S. and other WTO members' concerns that the application period was too short, AQSIQ extended the application deadline to August 1, 2004, allowed companies who submitted incomplete applications to supplement required documents and extended the new requirement's effective date from November 1, 2004 to January 1, 2005.

AQSIQ made public on its website the names of overseas exporters approved to ship scrap to China in two postings, the first in mid-October and the second at the end of December, only days before the new registration would take effect. In total, about 85 percent of worldwide applicants were granted approval, including hundreds of U.S. exporters. AQSIQ indicated that it would notify applicants that were not approved and that these exporters would be able to apply again six months after receiving notice of their rejection. However, AQSIQ has not given any formal notice about when it will re-open the application process to exporters or new shippers that missed the original deadline.

Quality and Safety Certification

China's "China Compulsory Certification" (CCC) mark system took full effect on August 1, 2003, following a transition period that lasted for fifteen months. The new CCC mark replaces the old "Great Wall" and "CCIB" marks and is now required for more than 130 product categories, such as electrical machinery, information technology equipment, household appliances and their components. Despite this positive change, U.S. companies in some sectors complain that certification remains a difficult, time-consuming and costly process. The process involves on-site inspection of manufacturing facilities outside of China, the cost of which is borne by producers. Some U.S. companies also report that China is applying the CCC mark requirements inconsistently, with Chinese customs officials blocking shipments that should not require a mark. In addition, small and medium-sized U.S. companies without a presence in China find it particularly burdensome to apply for CCC mark exemptions (including for replacement and re-export) because China requires the applications to be done in person in the Beijing offices of CNCA. U.S. companies have also asked China not to require the CCC mark for products that no longer warrant mandatory certification, such as low-risk products and components.

In February 2004, AQSIQ issued a measure requiring that owners of overseas certification markers file with state certification authorities. AQSIQ also issued a measure in June 2004 requiring that testing and certification institutions be officially designated by CNCA before conducting business related to products subject to compulsory certification. China has accredited 66 Chinese enterprises to test products for the CCC mark and 5 Chinese enterprises to certify them. Despite China's WTO commitment that qualifying foreign-owned conformity assessment bodies would be eligible for accreditation, China has yet to grant accreditation to any foreign-invested enterprises.

Redundant Testing

U.S. companies have expressed concern about continued requirements for redundant testing, particularly for cosmetics, pharmaceuticals, medical equipment, cellular telephones and other telecommunications products and consumer electronic products. For example, telecommunications equipment faces CNCA quality and safety tests, but then MII conducts functionality tests that overlap the CNCA tests.

Sanitary and Phytosanitary Measures

Prior to China's accession to the WTO, the United States and other WTO members were concerned about a variety of China's phytosanitary and veterinary import standards that appeared to be based on dubious scientific principles and had not always been consistently applied. To advance its bid to join the WTO, China addressed certain longstanding sanitary and phytosanitary (SPS) barriers to U.S. agricultural imports when it agreed to lift bans on imports of U.S. grain, citrus, meat and poultry with the signing of the U.S.-China Agricultural Cooperation Agreement (ACA) in April 1999. In particular, China agreed to recognize the U.S. certification system for meat and to accept U.S. beef, pork, and poultry meat from all USDA-certified plants. China also lifted its ban on imports of citrus from the United States, allowing imports of citrus from most counties in Arizona, California, Florida, and Texas. In addition, China lifted its ban on imports of wheat and other grains from the U.S. Pacific Northwest and promised to allow the import of U.S. wheat meeting specified tolerances for TCK fungus. China's implementation of the ACA has produced mixed results, however.

With regard to raw poultry and meat, China continues to apply certain standards that do not appear to be based on scientific evidence and that have the effect of slowing imports from the United States. In particular, in 2002, China declared zero tolerance for pathogens in imported raw poultry and meat. While it is possible to reduce contamination through cooking, the complete elimination of pathogens in raw poultry and meat is not reasonably achievable, nor scientifically justifiable. Moreover, China apparently does not apply this same standard to domestic raw poultry and meat, which would appear contrary to WTO national treatment principles.

China issued a new phytosanitary measure in 2004 blocking imports of cherries from the United States.

China also continued to delay the approval of citrus imports from four counties in Florida and to use a variety of phytosanitary measures to block imports of several other U.S. products, including stone fruit, several varieties of apples, pears, fresh potatoes and processed food products containing certain food additives. By the end of 2004, China had agreed to lift the ban on the Florida citrus imports. China had also lifted the ban on cherries, except for those originating in California.

While the 1999 ACA established an agreed level of TCK fungus tolerance in U.S. wheat, and China no longer routinely blocks U.S. wheat exports from the Pacific Northwest on the basis of the TCK fungus, China has imposed a maximum residue level (MRL) for selenium that is below the international standard and threatens all U.S. wheat exports to China. In addition, China has imposed an MRL for vomitoxin in wheat in the absence of any international standard. Although these measures are problematic, U.S. exports of wheat to China increased dramatically in 2004, as China does not appear to be enforcing them.

Meanwhile, in December 2003, China and other countries imposed bans on U.S. bovine products in response to the detection of bovine spongiform encephalopathy (BSE) in a cow imported into the United States from Canada. China's ban included not only beef, but low-risk bovine products, i.e., bovine semen and embryos, protein-free tallow and non-ruminant origin feeds and fats, which pose no risk of BSE and should not be banned under existing international standards. After numerous bilateral meetings and technical discussions, including a visit to U.S. bovine facilities by Chinese food safety officials, China announced a lifting of its BSE ban for low-risk ruminant bovine products in late September 2004. However, China conditioned the lifting of the ban on the negotiation of protocol agreements setting technical and certification parameters for incoming low-risk bovine products. In November 2004, U.S. and Chinese officials finalized and signed protocols that would enable a resumption in exports of U.S.-origin bovine semen and embryos, along with non-ruminant origin feeds and fats. Exports of bovine semen and embryos are contingent on facility certification by Chinese regulatory authorities. U.S. and Chinese officials were unable to reach agreement on provisions that would enable a resumption in exports of U.S.-origin protein-free tallow to China, and by the end of 2004 trade in low-risk bovine products had not yet resumed.

In February 2004, China imposed a nationwide ban on U.S. poultry in response to cases of low-pathogenic Avian Influenza (AI) found in Delaware and did not modify this nationwide ban when a case of highly pathogenic AI was subsequently discovered in Texas. Throughout 2004, the U.S. provided technical information to China on the U.S. AI situation, and in August a high-level Chinese delegation conducted a review of the status of AI eradication efforts in the United States. The United States emphasized it had been recognized as free of high pathogenic AI under international standards. In November 2004, China lifted its nationwide ban on U.S. poultry, leaving in place a ban only for the states of Connecticut and Rhode Island. The United States will soon be providing China with requested information regarding the status of AI in those two states.

Throughout 2004, China's general lack of transparency remained a problem. China either failed to notify or belatedly notified to the WTO numerous food safety measures, resulting in measures that were adopted without the benefit of comments from other interested WTO members. In some cases, the adopted measures were overly burdensome, appeared to lack a scientific foundation, or raised significant national treatment concerns. U.S. engagement with China at the WTO and bilaterally, including through the provision of technical assistance, generated some improvements in China's compliance with its WTO transparency obligations in 2004. At the same time, however, U.S. exports of soybeans, biotechnologically related products, fruit and other products repeatedly fell subject to unnotified entry, inspection and labeling requirements.

China's Biotechnology Regulations

In January 2002, the Ministry of Agriculture (MOA) issued new rules implementing June 2001 regulations on agricultural biotechnology safety, testing and labeling. The product most affected was soybeans, while corn and other commodities also remained at risk. However, the implementing rules did not provide adequate time for completion of required safety assessments before their effective date of March 20, 2002. In response to U.S. interventions, China issued interim rules, which allowed trade to continue while authorities carried out safety assessments of transgenic products. These interim rules were extended twice and were set to expire in April 2004. In December 2003 talks, MOA officials promised that permanent approval of Round-up Ready soybeans would be completed at least 60 days before expiration of the interim rules, which should prevent any trade disruption. China followed through on this promise and approved Round-up Ready soybeans, along with two cotton events and two corn events, in February 2004. Two months later, China issued final safety certificates for five additional corn events and seven canola events, leaving only one corn event still awaiting final approval. MOA has indicated that action on the remaining corn event can be expected by early 2005.

Substantial U.S. concerns with China's biotechnology regulations and implementing rules remain, particularly with regard to risk assessment (including the administration of field trials), labeling and inter-ministerial coordination of biotechnology policy. China is a signatory to the Convention on Biodiversity, but has yet to ratify the Biosafety Protocol.

Labeling

The U.S. processed food industry has registered its concerns with a number of standards and labeling requirements on its exports to China. The meat industry in particular is concerned that meat labeling regulations issued in late 2002 have several requirements that go beyond those of any other country. They assert that these requirements are unnecessary and costly.

Agricultural importers and importers of processed foods are also concerned about measures requiring labels for products containing transgenic material, such as soybeans and corn. The June 2001 biotechnology regulations issued by MOA require labeling of bulk commodities, but implementation has been limited and sporadic. Future implementation of these measures remains uncertain.

The distilled spirits industry is concerned that China will require its products to comply with all existing food labeling requirements. The industry believes that some of these requirements are inappropriate since the industry does not consider distilled spirits to be a food.

EXPORT REGULATION

Export Licenses and Quotas

Over the last several years, China has progressively reduced the number of products requiring some type of export license. In 2004, China continued this trend, as it freed up two more categories of products from this requirement (garlic and carbon steel plate). However, 50 categories of products (totaling 319 items at the 8-digit tariff level) are still subject to various types of export licenses. Products requiring export licenses include some grains, cotton, livestock, raw materials and metals, lethal chemicals and food products. In addition, China occasionally imposes new export licensing requirements on strategically sensitive commodities.

For some products, such as blast furnace coke and fluorspar, the export licensing system raised strong concerns under WTO rules that generally prohibit export restrictions. Export licenses for these two products are accompanied by export quotas and at times have required the payment of high export license fees beyond the administrative costs of administering an export license system.

In 2004, China's export restrictions on blast furnace coke, a key steel input, began to have a significant, adverse effect on U.S. integrated steel producers and their customers. The United States began to raise its concerns with China's coke export restrictions during high-level meetings in Washington in April 2004. The United States urged China to put the practice of using export restrictions behind it, not just for coke but also for other products. In late July 2004, China raised the 2004 quota allotment for coke to 12.3 million MT, and it indicated that it would eventually raise the quota to the 2003 level of 14.3 million MT. Shortly thereafter, MOFCOM also issued an urgent notice reiterating that the sale of export licenses was illegal. In the ensuing months, with the increased supply of Chinese coke and the crackdown on the sale of export licenses, the export prices for Chinese coke declined significantly. U.S. industry was also able to obtain a substantially larger quantity of Chinese coke in 2004 than it had in 2003.

China has imposed quotas and high license fees on exports of fluorspar since before it acceded to the WTO, apparently with the objective of supporting China's domestic users of fluorspar, which face no comparable restrictions. China has refused to modify its practices in this area, despite repeated U.S. requests.

China also requires export licenses on products that are the subject of antidumping duties in a foreign market. The central government has delegated responsibility for issuing these licenses to quasi-governmental industry associations formed to take the place of the ministries that governed production during the earlier central planning era. Foreign investors report that the industry associations are using the power to issue export licenses to force companies to participate in association-supported activities. For example, the steel producers' industry association will not issue an export license to any company that does not contribute to its antidumping defense funds.

December 2004, as the January 1, 2005 deadline for removal of global textile quotas drew near, China announced plans to impose export duties on certain In categories of textile and apparel products. Details of this plan are still unclear but appear to represent an effort by China to manage the export growth of these products in response to concerns from China's trading partners.

Export Subsidies

China officially abolished subsidies in the form of direct budgetary outlays for exports of industrial goods on January 1, 1991. China agreed to eliminate all subsidies prohibited under Article 3 of the WTO Agreement on Subsidies and Countervailing Measures, including all forms of export subsidies on industrial and agricultural goods, upon its accession to the WTO in December 2001.

A general lack of transparency makes it difficult to identify and quantify possible export subsidies provided by the Chinese government. China's subsidy programs are often the result of internal administrative measures and are not publicized. Many of the subsidies take the form of income tax reductions or exemptions that are de jure or de facto contingent on export performance. They can also take a variety of other forms, including mechanisms such as credit allocations, low-interest loans, debt forgiveness and reduction of freight charges. U.S. industry has alleged that subsidization is a key reason that Chinese exports are undercutting prices in the United States and gaining market share. Of particular concern are China's practices in the textiles industry as well as in the steel, petrochemical, high technology, forestry and paper products, machinery and copper and other non-ferrous metals industries.

U.S. subsidy experts are currently seeking more information about several Chinese programs and policies that may confer export subsidies. Their efforts have been frustrated in part because China has failed to make any of its required subsidy notifications since becoming a member of the WTO three years ago. At a meeting of the WTO's Council for Trade in Goods in November 2004, China committed to submit its long-overdue subsidies notification in 2005.

Since shortly after China acceded to the WTO, U.S. corn exporters have been concerned that China provides export subsidies on corn. In 2002 and 2003, it appeared that significant quantities of corn had been exported from China, including corn from Chinese government stocks, at prices that may have been 15 to 20 percent below domestic prices in China. As a result, U.S. corn exporters were losing market share for corn in their traditional Asian markets, such as South Korea and Malaysia, while China was exporting record amounts of corn. In 2004, however, trade analysts began to conclude that, because of several economic factors, including changes in the relationship between domestic prices and world prices, China is now trending toward becoming a net importer of corn.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

While China has made significant progress in its efforts to make its framework of laws, regulations and implementing rules WTO-consistent, serious problems remain, particularly with China's enforcement of intellectual property rights. Throughout 2004, the United States placed the highest priority on the need for improvements in China's enforcement efforts, as counterfeiting and piracy in China are at epidemic levels and cause serious economic harm to U.S. businesses in virtually every sector of the economy. In April 2004, in response to concerns raised by the United States, China's Vice Premier Wu Yi presented an "action plan" to address the IPR problem in China. Intended to "substantially reduce IPR infringement," this action plan calls for improved legal measures to facilitate increased criminal prosecution of IPR violations, increased enforcement activities and a national education campaign. The United States is monitoring implementation of this action plan closely and will conduct an out-of-cycle review in early 2005 under the Special 301 provisions of U.S. trade law to assess China's implementation of its IPR commitments. The United States will take whatever action is necessary at the conclusion of the out-of-cycle review to ensure that China develops and implements an effective system for IPR enforcement, as required by the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement). Supplementing these efforts is the Strategy Targeting Organized Piracy (STOP!), a U.S. government-wide initiative begun in October 2004 to empower U.S. businesses to secure and enforce their intellectual property rights in overseas markets, to stop fakes at the U.S. borders, to expose international counterfeiters and pirates, to keep global supply chains free of infringing goods, to dismantle criminal enterprises that steal U.S. intellectual property and to reach out to like-minded U.S. trading partners in order to build an international coalition to stop counterfeiting and piracy worldwide.

Legal Framework

In anticipation of its accession to the WTO, China began modifying the full range of IPR laws, regulations and implementing rules, including those relating to patents, trademarks and copyrights, in an effort to comply with the TRIPS Agreement. By the end of 2001, China had completed amendments to its patent law, trademark law and copyright law, along with regulations for the patent law and regulations addressing computer software protection and the protection of layout designs of integrated circuits. After it acceded to the WTO, China issued regulations for the trademark law and the copyright law. China also issued various sets of implementing rules and judicial interpretations in the patent, trademark and copyright areas. Overall, the legal changes made by China represent major improvements that have moved China generally in line with international norms in most key areas, although more work needs to be done, particularly with regard to administrative and criminal enforcement. In addition, new legislation may be required in certain "cutting edge" areas.

In the trademark area, some progress was made in 2004 on the recognition of foreign well-known marks, more than a year after the issuance of implementing rules in June 2003 on well-known marks. A handful of foreign marks have been recognized as well-known by the China Trademark Office, all in the last year. The State Administration for Industry and Commerce also announced plans to amend its Regulations on Trademark Administrative Enforcement in order to guide regional industrial and commercial administrations in facilitating effective trademark enforcement and protection. Nevertheless, the administrative enforcement system for trademarks is generally regarded by U.S. industry as non-deterrent. The fines remain very low, and new measures are needed to clarify the conditions for imposing administrative penalties, including the calculation of fines and the destruction of counterfeit and pirated products and the equipment used to make them.

By the end of 2004, with copyright infringement on the Internet becoming a growing phenomenon in China because of loopholes in existing regulations and implementing rules, China still had not acceded to two World Intellectual Property Organization (WIPO) treaties, the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty. These treaties, commonly known as the "WIPO Internet treaties," entered into force in 2002 and have been ratified by many developed and developing countries. The United States considers the WIPO treaties to reflect many key international norms for providing copyright protection over the Internet. While China's existing regulations, implementing rules and judicial interpretations do increasingly address certain copyright issues related to the Internet, and China is currently drafting further Internet-related regulations to provide better IPR protection on the Internet, China needs to accede to the WIPO treaties and harmonize its regulations and implementing rules with them to meet international norms. China's accession to the WIPO treaties is an increasingly important priority for the United States and many other countries because China has the second largest number of Internet users of any country in the world, and rapid growth in broadband penetration in China not only increasingly affects China's market but also foreign markets due to the borderless nature of the Internet.

China also took steps in 2004 to improve border measures meant to protect against the import and export of infringing products and to make it easier for rights-holders to secure effective enforcement at the border when the Customs Administration issued new regulations and implementing rules. These measures address the duties of the Customs Administration and improve guidance on the implementation of the customs IPR recordal mechanism. However, in other areas, such as the storage and disposition of infringing goods and the transferral of cases for possible criminal prosecution, these measures lack clarity or could benefit from further changes.

Enforcement

Although the central government has worked effectively to modify a range of China's IPR laws and regulations in an effort to bring them into line with China's WTO commitments, IPR enforcement continues to be inadequate. In 2004, IPR infringement in China continued to affect products, brands and technologies from a wide range of industries, including films, music, publishing, software, pharmaceuticals, chemicals, information technology, textile fabrics and floor coverings, consumer goods, electrical equipment, automotive parts and industrial products, among many others. According to figures released by the State Council's Development Research Center in July 2003, the market value of counterfeit goods in China was between $19 billion and $24 billion in 2001, which translates into enormous losses for intellectual property rights-holders. According to some reports, inadequate enforcement has resulted in infringement levels in China that have remained at 90 percent or above in 2004 for virtually every form of intellectual property, while estimated U.S. losses due to the piracy of copyrighted materials alone range between $2.5 billion and $3.8 billion annually. This situation not only has had an enormous economic impact, but also presents a direct challenge to China's ability to regulate many products that have health and safety implications for China's population and, as an increasing amount of counterfeit and pirated products are being exported from China, for others around the world.

China's IPR laws and regulations provide for three different mechanisms for IPR enforcement – enforcement by administrative authorities, criminal prosecutions and civil actions for monetary damages or injunctive relief. However, China's IPR enforcement efforts are hampered by the challenges of coordination among Chinese government ministries and agencies, local protectionism and corruption, high thresholds for initiating investigations and prosecuting cases, and inadequate and non-transparent administrative penalties.

The United States has repeatedly urged China to take immediate and substantial steps to put it on the path toward effective enforcement mechanisms, and it has also sought to foster improvements through a variety of technical assistance programs. Following a series of high-level meetings, China announced a comprehensive action plan on IPR enforcement in April 2004, with the stated goal of significantly reducing infringement across the country. China specifically committed that it would: (1) significantly reduce IPR infringement levels; (2) take steps by the end of 2004 to increase penalties for IPR violations by subjecting a greater range of violations to criminal investigation, applying criminal sanctions to the import, export, storage and distribution of pirated and counterfeit products and applying criminal sanctions to on-line piracy; (3) crack down on IPR violators by conducting nation-wide enforcement actions and increasing customs enforcement actions; (4) improve protection of electronic works by ratifying and implementing the WIPO Internet treaties as soon as possible, and by extending an existing ban on the use of pirated software in government offices; and (5) launch a national IPR education campaign. China also agreed to establish an IPR working group that would function under the auspices of the JCCT to consult and cooperate with the United States on the full range of issues described in China's IPR action plan.

In the months following these commitments, Vice Premier Wu Yi pledged that China would move forward with the legislative and judicial measures needed to improve China's IPR protection regime. Vice Premier Wu Yi also made clear that China would turn its attention to educating consumers and enforcing laws already in place. In August 2004, Vice Premier Wu Yi proclaimed that China would soon launch a year-long campaign targeting IPR infringement that would focus on "key stages," including import/export activities, trade fairs and exhibitions, wholesale markets, processing of brand name goods, printing and replication. This campaign seeks to integrate the work of multiple government agencies in order to combat IPR abuses in fifteen provinces and cities designated for priority action, both for enforcement and education purposes, and is scheduled to proceed in three phases: (1) planning and mobilization (September 2004); (2) implementation (October 2004 to June 2005); and (3) summary (July to August 2005). Meanwhile, in late December 2004, the Supreme People's Court and Supreme People's Procuratorate issued a judicial interpretation intended to address a variety of problems with criminal enforcement in China.

Administrative Enforcement

China continues to take a large number of administrative enforcement actions against IPR violators. However, these actions do not appear to deter further IPR infringement.

In 2004, under the leadership of Vice Premier Wu Yi, the central government initiated anti-counterfeiting and anti-piracy campaigns. These campaigns resulted in high numbers of seizures of infringing materials. Nevertheless, the cases subsequently brought by the administrative authorities in connection with these types of campaigns usually result in extremely low fines. When the administrative authorities decide on fines, the amounts can be artificially low because the administrative authorities often establish value based on the price charged for the counterfeit or pirated goods rather than treat the infringing goods as having the value of the genuine articles. In addition, evidence showing that a person was caught warehousing infringing goods is not sufficient to prove an intent to sell them, and as a result the administrative authorities will not even include those goods in the value of the infringing goods when determining the fine amounts. The lack of deterrence from the fines is compounded by the fact that the administrative authorities rarely forward an administrative case on to the Ministry of Public Security for criminal investigation, even for commercial-scale counterfeiting or piracy. As a result, the infringers consider the seizures and fines simply to be a cost of doing business, and they are usually able to resume their operations without much difficulty.

In bilateral meetings with China in 2004, the United States continued to emphasize that China needs to revise its IPR legal framework to provide for substantially higher administrative fines and that, for these fines to have a deterrent effect, the administrative authorities need to provide greater transparency throughout the enforcement process, issue written decisions and publicize the results. The United States has also emphasized that it is crucial for the administrative authorities to establish clear standards for the transfer of cases to the Public Security Bureau and the Supreme People's Procuratorate for criminal prosecution.

Criminal Enforcement

Effective criminal enforcement could offer the deterrence needed for China to begin to handle the rampant IPR infringement hurting both foreign and domestic enterprises. At present, however, criminal enforcement has virtually no deterrent effect on infringers. China's authorities have pursued criminal prosecutions in a relatively small number of cases. While the number of criminal trademark prosecutions is increasing, very few criminal copyright prosecutions have been initiated. When criminal prosecutions are pursued, moreover, a lack of transparency makes it sometimes difficult to find out if they resulted in convictions and, if so, what penalties were imposed and whether the penalties were suspended.

Prior to the issuance of the December 2004 judicial interpretation on criminal enforcement, the United States had called for several critical legal changes. A key concern for the United States involved criminal liability thresholds, which were very high and seldom met. In order to bring a criminal action against an alleged infringer, evidentiary proof of sales totaling RMB 200,000 ($24,100) for enterprises and RMB 50,000 ($6,030) for individuals was required. This proof-of-sale requirement was unworkable, as it did not apply to counterfeit or pirated goods discovered in a warehouse but not yet sold, and infringers generally do not issue receipts or keep detailed records of the sales that they have made. In addition, the United States was concerned about the scope of China's laws and regulations. For example, it was clear that China's laws and regulations would be much more effective if they applied to the willful manufacture, storage, distribution and use of counterfeit and pirated goods, rather than only when a sale could be proved. Similarly, China's failure to treat the export of counterfeit or pirated goods on a commercial scale as a criminal act was problematic.

An initial review of the judicial interpretation issued by the Supreme People's Court and the Supreme People's Procuratorate in late December 2004 shows that it reduces the monetary thresholds for criminal prosecutions of trademark and patent counterfeiting and copyright piracy and contains new provisions addressing online copyright piracy and accomplice liability, including the import/export of counterfeit goods. It is too early to tell how effective this judicial interpretation will be in improving China's criminal enforcement record. As drafted, the judicial interpretation is only an initial step in rectifying China's deficient criminal enforcement system. The changes set forth in the judicial interpretation will not, by themselves, result in significantly decreased infringement levels. Rather, the central government must also issue clear mandates to the Public Security Bureau, the Supreme People's Procuratorate, the Customs Administration and other IPR enforcement agencies as well as the courts requiring them to undertake corresponding institutional reforms of their investigatory and prosecutorial guidelines and practices. Standards for referrals from the administrative system to the criminal system must also be clarified and brought in line with the judicial interpretation. In addition, the central government must ensure appropriate allocation of resources and expertise to the IPR enforcement agencies, while also providing rigorous oversight, in order to ensure that these agencies coordinate their enforcement activities and improve their ability to effectively investigate, prosecute and ultimately convict IPR criminals.

Civil Enforcement

In part because of the ineffectiveness of the administrative and criminal enforcement mechanisms in China, there has been an increase in the number of civil actions being brought for monetary damages or injunctive relief. Most of these actions have been brought by Chinese rights-holders. This increased use of civil actions has coincided with an increasing sophistication on behalf of China's IPR courts, as China continues to make efforts to upgrade its judicial system. These efforts are still in progress, however. U.S. companies continued to complain in 2004 that there is still a lack of consistent and fair enforcement of China's IPR laws and regulations in the courts. They have found that most judges lack necessary technical training and that court rules regarding evidence, expert witnesses, and protection of confidential information are vague or ineffective. In addition, in the patent area, where enforcement through civil litigation is of particular importance, a single case still takes four to seven years to complete, rendering the new damages provisions adopted to comply with China's TRIPS Agreement obligations less meaningful.

SERVICES BARRIERS

Until China's entry into the WTO, China's services sectors were among the most heavily regulated and protected sectors of the national economy. Foreign service providers were largely restricted to operations under the terms of selective "experimental" licenses. However, both as a matter of policy and as a result of its WTO commitments, China decided to significantly liberalize foreign investment in its service sectors. At present, the market for services, underdeveloped due to historical attitudes and policies, has significant growth potential in both the short and long term.

China's WTO commitments are designed to provide meaningful access for U.S. service providers. In its accession agreement, China committed to the substantial opening of a broad range of services sectors through the elimination of many existing limitations on market access, at all levels of government, particularly in sectors of importance to the United States, such as banking, insurance, telecommunications and professional services. These commitments are far-reaching, particularly when compared to the services commitments of many other WTO members.

China also made certain "horizontal" commitments, which apply to all sectors listed in its services schedule. The two most important of these cross-cutting commitments involve acquired rights and the licensing process. Under the acquired rights commitment, China agreed that the conditions of ownership, operation and scope of activities for a foreign company, as set out in the respective contractual or shareholder agreement or in a license establishing or authorizing the operation or supply of services by an existing foreign service supplier, will not be made more restrictive than they were on the date of China's accession to the WTO. In other words, if a foreign company had pre-WTO accession rights that went beyond the commitments made by China in its services schedule that company could continue to operate with those rights. In the licensing area, prior to China's WTO accession, foreign companies in many sectors did not have an unqualified right to apply for a license to operate in China. They could only apply for a license if they first received an invitation from the relevant Chinese regulatory authorities, and even then the decision-making process lacked transparency and was subject to inordinate delay and discretion. In its accession agreement, China committed to licensing procedures that were streamlined, transparent and more predictable.

In 2004, China made progress on some fronts. For example, China lifted geographic restrictions in the banking and insurance sectors on or ahead of schedule. In addition, the licensing process in many sectors proceeded in a workman-like fashion. Indeed, every U.S. insurer that has applied to enter the China market has received a license, while some licenses have been granted to U.S. and other foreign institutions in the non-bank motor vehicle financing sector. China also went beyond its WTO commitments when it entered into bilateral aviation and maritime agreements with the United States.

However, many challenges remain in securing the benefits of China's services commitments. While China continued to keep pace nominally with the openings required by its WTO accession agreement, it frequently maintained or erected terms of entry that were so high or cumbersome as to prevent or discourage many foreign suppliers from gaining market access. For example, despite some progress, excessive capital requirements continue to restrict market entry for foreign suppliers in many sectors, such as insurance, banking, telecommunications and non-bank motor vehicle financing, among several others. In addition, in sectors such as insurance and legal services, branching restrictions have been put into effect that call into question commitments made by China in its Services Schedule. In other sectors, particularly express delivery and construction services, problematic measures continue to threaten to take away previously acquired market access rights.

Insurance Services

China's insurance market is growing steadily, but not as quickly as it could. According to the China Insurance Regulatory Commission (CIRC), 2004 premium income totaled $52 billion, an increase of 11.3 percent from 2003. Total insurance company assets reached $142 billion, an increase of nearly 30 percent from the previous year. In 2004, the operations of foreign insurers in China had continued to expand. Foreign insurer premium income grew by over 45 percent to $1.2 billion, or 2.3 percent of total premiums. While foreign insurers still have a relatively low share of the national market, in some areas market share is increasing. According to CIRC, in 2004, the 37 foreign insurers present in China held a 15.3 percent market share in Shanghai and an 8.2 percent market share in Guangzhou.

In its WTO accession agreement, China agreed to phase-in expanded ownership rights for foreign companies, for the most part during the first three years of China's WTO membership. Upon China's accession to the WTO, foreign life insurers were to be permitted to hold 50 percent equity share in a joint venture; within two years of accession, foreign property, casualty and other non-life insurers were to be permitted to establish as a branch, joint venture or a wholly foreign-owned subsidiary; and, within three years of accession, or by December 11, 2004, foreign insurers handling large scale commercial risks, marine, aviation and transport insurance, and reinsurance were to be permitted 51 percent foreign equity share in a joint venture (with the right to establish as a wholly foreign-owned subsidiary within two more years). China further agreed that all foreign insurers would be permitted to expand the scope of their activities to include group, health and pension lines of insurance within by December 11, 2004. In addition, China agreed to eliminate geographic restrictions on all types of insurance operations by December 11, 2004.

Shortly after China acceded to the WTO, CIRC issued several new insurance regulations, including ones directed at the regulation of foreign insurance companies. These regulations implemented many of China's commitments, but they also created problems in three critical areas – capitalization requirements, transparency and branching. In particular, China's capitalization requirements were significantly more exacting than those of other populous countries, and they limited the ability of foreign insurers to make necessary joint venture arrangements. The regulations also continued to permit considerable bureaucratic discretion and to offer limited predictability to foreign insurers seeking to operate in China's market. With regard to branching, China scheduled a commitment to allow non-life firms to establish as a branch in China upon accession and to permit internal branching in accordance with the lifting of China's geographic restrictions. China further agreed that foreign insurers already established in China that were seeking authorization to establish branches or sub-branches would not have to satisfy the requirements applicable to foreign insurers seeking a license to enter China's market. China's regulations regarding foreign insurers' branching rights, however, remain vague, and CIRC has so far insisted that non-life insurers that are already in the market as a branch and that wish to branch or sub-branch cannot do so unless they first establish as a subsidiary, a costly condition. Further complicating this issue, CIRC has apparently waived this requirement for at least one foreign non-life insurer, but has not explained how or whether other foreign insurers could apply for this waiver.

In May 2004, CIRC took steps to address concerns related to China's high capitalization requirements by issuing the Detailed Rules on the Regulations for the Administration of Foreign-Invested Insurance Companies. These new rules lower capital requirements for national licenses from RMB 500 million ($60.3 million) to RMB 200 million ($24.1 million) and for branch offices from RMB 50 million ($6.03 million) to RMB 20 million ($2.41 million). These changes have been welcomed by some U.S. insurers, but others still consider them to be too high. The new rules also streamlined licensing application procedures and shortened approval times, although some procedures remained unclear. Meanwhile, the new rules did not adequately address branching rights, as many aspects of this issue remained vague.

In December 2004, in accordance with its WTO commitments, China lifted its geographic restrictions on foreign insurers on schedule. China also permitted foreign insurers to offer health and group insurance as well as pension/corporate annuities and increased the 50 percent ceiling on foreign ownership of joint venture insurance brokerages to 51 percent.

While China's lifting of geographic restrictions was a welcome development, U.S. and other foreign insurers are concerned that apparent discrimination in branching approvals may limit their ability to expand. In practice, it appears that established Chinese insurers are being granted new branch approvals on a concurrent basis, meaning more than one branch at a time. In contrast, foreign insurers so far have only received approvals on a consecutive basis, meaning one branch at a time. Meanwhile, a number of U.S. investors have taken significant minority equity stakes in major Chinese insurance companies as a means of accessing China's insurance market.

Banking and Securities Services

China put in place laws and regulations implementing its WTO commitments for banking and securities services during its first three years as a WTO member. Foreign banks and securities firms, however, continue to face a restrictive regulatory environment.

As part of its WTO accession agreement, China agreed to allow foreign banks to conduct local currency business with Chinese companies two years after WTO entry, and with Chinese individuals five years after WTO entry. The Chinese government also committed to opening four new cities every year where foreign banks could engage in local currency operations. All non-prudential market access and national treatment restrictions on foreign banks are to be lifted within five years of China's accession to the WTO.

China continues to have strict limitations, in particular, on foreign banks' participation in local currency operations, which are regulated by the People's Bank of China (PBOC). These restrictions are being gradually relaxed, but local currency transactions with individuals remain prohibited until December 11, 2006. Restrictions on the rights of foreign banks to raise RMB in the interbank market also inhibit the ability of foreign banks to build RMB loan portfolios necessary for profitable operations in China. Meanwhile, although foreign currency business with any customer, foreign or domestic, is now freely permitted, only a limited number of China banks are allowed to do forward foreign exchange contracts.

Under regulations issues in December 2001, foreign banks must meet stringent critieria such as having gross assets of $20 billion when opening new branches in China. Although China reduced capital requirements for foreign bank branches in December 2003, they remained excessively high, increasing local capital costs for foreign banks. Foreign bank branches must also place 30 percent of their operating capital in interest bearing assets designated by the PBOC. Foreign bank branch current assets (cash, local bank demand deposits, and PBOC deposits) must continue to be greater than 25 percent of customer deposits. In addition, the ration of customer deposits in foreign currency to domestic foreign currency assets may not exceed 70 percent, an increase from the 40 percent-level mandated previously. China calculates prudential rations and limits based on the local capital of foreign bank branches rather than on the global capital base of the bank, although more lenient rules apply in authorized cities in the northeastern and western regions of China.

In December 2003, the Chinese Government increased the stake a single foreign investor can take in a Chinese bank from 15 to 20 percent, with a total 24.9 percent allowed for all foreign investors. Several foreign (including U.S.) banks and financial institutions have since taken significant equity stakes in small and medium sized Chinese banks. Similar investments are expected when two of China's largest state-owned banks list in the market in 2005. As of December 2004, China had opened up five new cities – Kunming, Beijing, Xiamen, Xi'an and Shenyang – to foreign banks seeking to conduct local currency business, bringing the total number to 18.

Pursuant to the terms of China's WTO accession agreement, foreign securities firms were to receive the right to form joint ventures for fund management upon China's accession to the WTO, while joint ventures for securities underwriting were to be permitted within three years after accession. The China Securities Regulatory Commission issued regulations on the establishment of joint venture fund management companies and securities underwriting by Chinese-foreign joint ventures shortly after China's WTO accession. China's decision to limit foreign partners to a minority stake of these joint ventures, however, continues to limit their appeal to leading foreign firms. In addition, China continues to limit the security underwriting joint ventures to underwriting A-shares and to underwriting and trading government and corporate debt, B-shares and H-shares.

Since December 2002, China has allowed Qualified Foreign Institutional Investors (QFIIs) to trade in A-shares via special accounts opened at designated custodian banks. Stringent criteria currently make it difficult for foreign institutions to qualify as QFIIs, while other requirements limit the extent to which QFIIs can trade in A-shares.

Motor Vehicle Financing Services

China's WTO accession agreement required China to allow foreign non-bank financial institutions to provide motor vehicle financing immediately upon accession and without any limits on market access.

As a result of persistent U.S. engagement with China, both bilaterally and at WTO meetings, China issued regulations in October and November 2003 allowing foreign non-bank financial institutions to provide motor vehicle financing. The capital requirements set by these regulations are relatively high, with minimum registered capital at RMB 300 million ($36.2 million), and minimum paid-in capital at RMB 500 million ($60.3 million). In August 2004, CBRC granted licenses for one U.S. auto company and two other foreign auto companies to set up non-bank motor vehicle financing institutions.

Wholesaling Services and Commission Agents' Services

In its WTO accession agreement, China committed to provide national treatment and eliminate market access restrictions for foreign enterprises seeking to provide wholesaling and commission agents' services and related services, such as repair and maintenance services, through a local presence within three years of China's accession (or by December 11, 2004), subject to limited product exceptions. In the meantime, China agreed to progressively liberalize its treatment of these services pursuant to a set schedule. The phase-in of these services was supposed to start with minority foreign-owned joint ventures by December 11, 2002, followed by majority foreign-owned joint ventures by December 11, 2003.

Shortly after acceding to the WTO, China fell behind in its implementation of the required progressive liberalization, as foreign enterprises continued to face a variety of restrictions. It was not until mid-2004, following high-level U.S. engagement, that China began to take steps to liberalize. At that time, MOFCOM issued regulations providing national treatment and eliminating market access restrictions on joint ventures providing wholesaling services and commission agents' services. These regulations also established a timetable for extending this liberalization to wholly foreign-owned enterprises on December 11, 2004. However, MOFCOM's failure to clarify the procedures for securing the necessary approval certificates has delayed foreign enterprises' provision of these services.

Retailing Services

In 1999, the Chinese government broadened the scope for foreign investment in the retail sector. New regulations encouraged the entry of large international retailers (such as hypermarkets and warehouse-style stores) into China. China's subsequent WTO commitments were designed to further expand the ability of foreign retailers to enter the market through a much wider range of modalities. Smaller retail operations, some large retail operations, gas stations and even car dealerships may be wholly foreign-owned within three to five years of China's December 2001 WTO accession, although certain types of large retail operations may still face ownership limitations. In addition, franchising was to be permitted within three years of accession, or by December 2004.

As in the wholesale area, China fell behind in its implementation of the required progressive liberalization shortly after acceding to the WTO, as foreign enterprises continued to face a variety of restrictions. China only began to take steps to liberalize in mid-2004, when MOFCOM issued regulations providing national treatment and eliminating market access restrictions on joint ventures providing retailing services. These regulations also established a timetable for extending this liberalization to wholly foreign-owned enterprises on December 11, 2004. However, MOFCOM's failure to clarify the procedures for securing the necessary approval certificates has delayed foreign enterprises' provision of these services.

Sales Away From a Fixed Location

In 1998, China banned all direct selling (or sales away from a fixed location) activities after some foreign and domestic firms used direct selling techniques to operate pyramid schemes and other less-than-legitimate operations. Some large U.S. and other foreign direct selling firms were allowed to continue operating in China after altering their business models. In its WTO accession agreement, China committed to the full resumption of direct selling activities by December 2004. At the end of 2004, however, China was still drafting the necessary implementing regulations. Moreover, it appears that the latest version of the draft direct selling measures may contain several problematic provisions. For example, one provision raises serious national treatment concerns, as it apparently allows direct selling of domestically produced goods, but requires imported goods to be sold at a fixed location. Other provisions, meanwhile, impose operating requirements that may make direct selling commercially unviable.

Express Delivery Services

Beginning in December 2001, the State Postal Bureau (together with MOFTEC and MII) issued restrictive measures that could have jeopardized market access that foreign express delivery firms (which must operate as joint ventures with Chinese partners) enjoyed prior to China's accession. These measures threatened to curtail the scope of operations of foreign express delivery firms licensed prior to China's accession to the WTO, despite China's horizontal commitment on acquired rights. Specifically, Notice 629, issued in December 2001, required firms wishing to deliver letters to apply for entrustment with China Post. Notice 64, issued in February 2002, extended China Post's monopoly on letters by creating weight and rate restrictions on letter deliveries by private firms. Following high-level U.S. interventions, in September 2002, Notice 472 eliminated the weight and rate restrictions on letter deliveries and streamlined the entrustment application procedure. Two major U.S. express delivery firms subsequently applied for and obtained entrustment certificates from China Post.

In July 2003, however, China circulated draft amendments to its postal services law that generated two immediate concerns among U.S. companies. First, the draft amendments purported to give China Post a monopoly over the delivery of letters under 500 grams, which would have constituted a new restriction on the scope of activities of existing foreign-invested express delivery companies, contrary to China's horizontal acquired rights commitment. Second, the draft amendments did not address the need for an independent regulator. In September, October and November 2003, China circulated new sets of draft amendments. While each set of draft amendments included a different definition of the China Post monopoly, the most recent draft amendments continued to provide China Post with a monopoly on letters weighing less than 500 grams. They also included other problematic provisions. For example, they appeared to create a new, more burdensome licensing process, and they seemed to require express couriers to pay a percentage of their revenue from the delivery of letters into a universal service fund.

In April 2004, following high-level U.S. engagement urging China not to cut back on the scope of activities that foreign-invested express delivery companies had been licensed to provide prior to China's WTO accession, Vice Premier Wu Yi committed that old problems, like the weight restriction, would not resurface as new problems. In July 2004, however, the State Council circulated another set of draft amendments to the postal services law. Despite Vice Premier Wu's commitment, these draft amendments continued to include a weight restriction, now reduced from 500 grams to 350 grams and did little to address other U.S. concerns. No new sets of draft amendments were circulated during the remainder of 2004, as U.S. engagement continued.

Construction, Engineering, Architectural and Contracting Services

Since before China's WTO accession, U.S. construction, engineering and architectural firms and U.S. contractors have enjoyed a relatively cooperative and open relationship with the Chinese government. These firms have operated in the Chinese market through joint venture arrangements and have been less affected by regulatory problems than other service sectors. Nevertheless, they have also faced restrictions. It has been difficult for foreign firms to obtain licenses to perform services except on a project-by-project basis. Foreign firms have also faced severe partnering and bidding restrictions.

In September 2002, the Ministry of Construction and MOFTEC jointly issued Decrees 113 and 114, which opened up construction and related construction design services to joint ventures with majority foreign ownership and, two years ahead of schedule, wholly foreign-owned enterprises. At the same time, however, these decrees created concerns for U.S. and other foreign firms by imposing new and more restrictive conditions than existed prior to China's WTO accession, when they were permitted to work in China on a project-by-project basis pursuant to Ministry of Construction rules. In particular, these decrees for the first time required foreign firms to obtain qualification certificates, effective October 1, 2003. In addition, these decrees for the first time required foreign-invested firms supplying construction services to incorporate in China, and they impose high minimum registered capital requirements and foreign personnel residency requirements that are difficult for many foreign firms to satisfy. In consultation with U.S. industry, the United States, in a high-level intervention, pressed its concerns about Decrees 113 and 114 and sought a delay before the decrees' problematic requirements would become effective. In September 2003, the Ministry of Construction agreed to extend the implementation date from October 1, 2003 until April 1, 2004 so the concerns of foreign firms could be analyzed further.

In April 2004, Decree 113 went into effect. However, in September 2004, the Ministry of Construction and MOFCOM issued Circular 159, which permitted foreign providers of construction services and related construction engineering design services to continue operating on a project by-project basis until July 1, 2005, effectively extending the effective date of the incorporation-related requirements. After that date, U.S. and other foreign companies will face a great deal of uncertainty as they seek to participate in projects in China.

In late November 2004, the Ministry of Construction issued the Provisional Measures for Construction Project Management (known as Decree 200), scheduled to become effective on December 1, 2004. Among other things, Decree 200 appears to preclude the same company from providing construction services and related construction engineering design services if it is also providing project management services on the same project. This aspect of the decree raises concerns because U.S. companies often provide all of these services in combination when working on a project in a foreign market.

Meanwhile, foreign firms cannot hire Chinese nationals to practice engineering and architectural services as licensed professionals. Currently, Chinese architecture and engineering firms must approve and stamp all drawings prior to construction. There have also been instances in which U.S. architectural firms have had to pay Chinese domestic taxes on designs prepared in the United States for Chinese projects. China also sets extremely low design fees, rather than letting the market set prices. In addition, China does not have adequate lien laws to protect the rights of engineering and architectural firms from non-payment.

Transportation and Logistics Services

The transportation and logistics sector has in the past faced severe regulatory restrictions, high costs, dominance by government-invested agents, and limitations on permitted activities. The multiple government bodies responsible for this sector include: the Ministry of Communications, the Ministry of Railways, MOFCOM, NDRC and the Civil Aviation Administration of China. Overlapping jurisdictions, multiple sets of approval requirements, and opaque regulations hinder market access. In some areas, domestic firms have used government connections and investments to monopolize the sector.

Nevertheless, like China's own reform policies, China's WTO commitments support a broad opening of the transportation and logistics sector to foreign services providers, to be phased in over time. Foreign firms should be able to invest freely in warehousing, road freight transport, rail freight transport and freight forwarding companies within three to six years after WTO accession, depending on the sector.

In July 2002, MOFCOM's predecessor, MOFTEC, issued a Notice on Establishing Foreign-Invested Logistics Companies in Trial Regions. This notice allows foreign-invested logistics companies (with up to 50 percent foreign ownership and registered capital of $5 million) to establish in several designated cities. U.S. firms have expressed concern about the high capital requirement and the 50 percent cap on foreign ownership, which may conflict with China's WTO commitments for certain types of logistics services.

In November 2002, China issued regulations allowing majority foreign ownership of road transportation firms, as it was required to do within one year of its WTO accession. China was also obligated to issue regulations allowing majority foreign-owned joint ventures to enter the fields of packaging services, storage and warehousing, and freight forwarding one year after its accession; it issued timely regulations allowing 75 percent foreign-owned joint ventures in these fields.

Even though China made no WTO commitments covering aviation services sector, it took a significant step in July 2004 to increase market access for U.S. passenger and cargo carriers. China signed a landmark amendment to the aviation agreement with the United States that will more than double the number of U.S. airlines operating in China and that will increase by five times the number of flights providing passenger and cargo services between the two countries over the next six years. The agreement also allows each country's carriers to serve any city in the other country, provides for unlimited code-sharing between them, expands opportunities for charter operators, and eliminates government regulation of pricing as of 2008. U.S. passenger and cargo carriers have since obtained additional routes and increased flight frequencies, as envisioned by the agreement.

Similarly, in late 2003 China took steps to liberalize the maritime services sector despite having made no WTO commitment. The United States and China signed a far-reaching, five-year bilateral maritime agreement, which will give U.S.-registered companies the legal flexibility to perform an extensive range of additional shipping and logistics activities in China. U.S. shipping and container transport services companies, along with their subsidiaries, affiliates and joint ventures, will also be able to establish branch offices in China without geographic limitation.

Regulation of Internet Content and Restrictions on Encryption and Decryption

Chinese authorities routinely filter Internet traffic entering China, focusing primarily on the content they deem objectionable on political, social or religious grounds. In 2002, China lifted filters on most major western news sites. However, according to a Harvard University study, published in 2002, China has blocked 19,032 sites on multiple occasions. In addition to blocking sites related to Taiwan, the Falun Gong spiritual movement, Tibetan and Uighur support groups, and human rights organizations focusing specifically on China, university alumni homepages such as that for MIT, various Church and other religious-themed sites, and search engines such as Alta Vista, have been blocked repeatedly. Foreign news websites were also blocked for several weeks during the 16th National Congress of the Communist Party of China in March 2003. Few, if any, websites related to strictly economic and business matters are blocked. Changes to Internet filtering can occur without warning or public explanation. For example, the popular Internet search engine Google was blocked completely in China for a few weeks starting in late August 2002. When Google became available again in September 2002, its "cached pages" feature remained blocked; that feature had previously allowed users in China to access "snapshots" of some webpages that were otherwise blocked in China. There have been no significant changes to China's policies on Internet content since these developments in 2002.

Internet content restrictions are governed by a number of measures, not all of which are public. The most important of these measures was issued in September 2000 and cover Internet content providers, electronic commerce sites and application service providers. In March 2002, the Internet Society of China, a nominally private group affiliated with MII, established a "Public Pledge on Self-Discipline for the China Internet Industry." Signatories commit to "refrain from producing, posting or disseminating pernicious information that may jeopardize state security and disrupt social stability, contravene laws and regulations and spread superstition and obscenity." At least one Chinese subsidiary of a U.S. Internet firm has signed the pledge.

China generally prohibits foreign-developed encryption and decryption technologies. In the past, this prohibition has not applied to software and hardware for which encryption is only an incidental feature. However, in December 2003, China dramatically changed this precedent with the issuance of standards on encryption for WLAN, which have since been suspended (see the section on "Standards, Technical Regulations and Conformity Assessment Procedures" above).

Telecommunications

In its WTO accession agreement, China made important commitments in the area of telecommunications services. It agreed to permit foreign suppliers to provide a broad range of services through joint ventures with Chinese companies, including domestic and international wired services, mobile voice and data services, value-added services, such as electronic mail, voice mail and on-line information and database retrieval, and paging services. The foreign stake permitted in the joint ventures is to increase over time, reaching a maximum of 49 percent for most types of services. In addition, all geographical restrictions are to be eliminated within two to six years after China's WTO accession, depending on the particular services sector.

Importantly, when it acceded to the WTO, China also accepted key regulatory principles from the WTO Reference Paper. As a result, China became obligated to separate the regulatory and operating functions of MII (which had been both the telecommunications regulatory agency in China and the operator of China Telecom) upon its accession and to implement its regulations in an impartial manner. Since China's accession, MII has spun-off China Telecom, which now competes in the market with other telecom operators. While the formal separation of regulator and operator has occurred, evidence of continued MII influence over operational decisions of operators (e.g., relating to personnel and standards) suggest that regulatory independence is far from complete. The current regulator, MII, is not structured as an independent entity as it still bears the responsibility to help develop China's IT and telecom manufacturing industries.

China is also obligated to adopt pro-competitive regulatory principles, such as transparent licensing, cost-based pricing and the right of interconnection, which are necessary for foreign-invested joint ventures to compete against established operators. With practically no foreign participation in the market, it has been difficult to assess compliance with such commitments. This very lack of foreign participation, however. is indicative of a licensing regime that has not been conducive to foreign investment, in part due to lack of transparency.

China's Regulations on Foreign-Invested Telecommunications Enterprises went into effect January 1, 2002. They define registered-capital requirements, equity caps, requirements for Chinese and foreign partners, and licensing procedures. The regulations stipulate that foreign-invested telecommunications enterprises can undertake either basic or value-added telecommunications services. Foreign ownership may not exceed 49 percent in the case of basic telecommunications services (excluding wireless paging) and 50 percent in the case of value-added services (including wireless paging, which is otherwise categorized as a basic service). The entire process of forming a Sino-foreign joint venture for basic services pursuant to the new regulations is expected to be lengthy, lasting on average 9 to 12 months. While China committed to giving foreign applicants freedom to choose potential joint venture partners, it appears that MII is interpreting requirements regarding technical qualifications to effectively exclude all but incumbent operators, foreclosing additional competition in the market. For foreign operators interested in offering international services, requirements to use a gateway operated by a state-owned operator appear excessive and unjustified. The capitalization requirement established for new entrants, which exceed $200 million, is another major impediment to market access. There appears to be no justification for such a requirement, particularly for companies interested in leasing, rather than building facilities, while specific licensing terms for resale-based operators do not appear to exist. Meanwhile, MII continues to process applications very slowly for the few foreign-invested telecommunications enterprises that have attempted to satisfy MII's licensing requirements.

At times, MII has also changed applicable rules without notice and without transparency. For example, in February 2003, MII announced a reclassification of certain basic and value-added telecommunications services effective April 1, 2003. No public comment period was provided for. This move limited the ability of U.S. firms to access China's telecommunications market since basic services are on a slower liberalization schedule and are subject to lower foreign equity limits and higher capitalization requirements.

Little progress has been made in opening the market for value-added services, such as Internet service and content providers. MII announced moves toward convergence in voice, video and data services in 2000, but China considers information content sensitive, so foreign companies face significant barriers in the Internet services sector. Although more foreign companies are registering ".com.cn" websites in China, these sites are still often blocked, which hinders companies' abilities to maintain a stable Internet presence. The requirement that Internet Service Providers (ISPs) must provide user login information and transaction records to authorities upon request, without clear guidelines as to the circumstances and situations that warrant such actions, raises concerns about consumer privacy and prevention of data misuse. Meanwhile, the United States is not aware of a single application for a license to provide value-added services that has completed the MII licensing process.

Foreign equity investment limitations for ISPs and Internet Content Providers (ICPs) mirror the timetable for value-added services in the WTO agreement (30 percent upon accession, 49 percent within one year after accession and 50 percent within two years after accession). However, ICPs must still win the approval of MII and/or local telecom administrations depending on the geographic coverage of their services before they can receive foreign capital, cooperate with foreign businesses, or attempt domestic or overseas stock listings.

In 2004, a draft of the long-awaited Telecommunications Law began to circulate among Chinese ministries and agencies. If China takes the initiative, this law could be a vehicle for addressing existing market access barriers and other problematic aspects of China's current telecommunications regime.

Meanwhile, even though China committed in its WTO accession agreement that further liberalization of this sector would be discussed in the current round of WTO negotiations, China has yet to make an improved services offer. With the modest telecommunications commitments made by China in its WTO accession agreement having so far failed to facilitate effective market entry for foreign firms, further liberalization, bound through the current round of WTO negotiations, appears critical to improving market access prospects for this sector.

Audio-Visual Services (Including Film Imports)

China's Regulations on the Administration of Audio-Visual Products and Regulations on the Management of Film went into effect on February 1, 2002. They are designed to bring more order and transparency to the film and audio-visual industries, with an eye to moving toward greater commercial efficiency in accordance with domestic reform efforts and WTO commitments. Despite these positive moves, the desire to protect the revenues earned by the state-owned movie and print media importers and distributors, and China's concerns about politically sensitive materials, result in continued restrictions in audio-visual services. For example, distribution of sound recordings, videos, movies, books and magazines remains highly restricted. In addition news services remain wary that the government will impose new restrictions on their activities. Inconsistent and subjective application of censorship regulations further impedes market growth for foreign and domestic providers alike.

China issued a number of regulations in 2004 that should lead to expanded market access in the audio-visual services sector. In July, the State Administration for Radio, Film and TV (SARFT) issued the Rules for the Administration of China-Foreign Cooperation in Filmmaking. According to these rules, licenses are required for both the joint Chinese-foreign filmmaking cooperative and the cooperating domestic partner. In October, SARFT and MOFCOM issued the Provisional Rules on the Access Requirements for Film. These rules cover film production, distribution, screening and imports by domestic firms, and film production and screenings involving foreign firms. All firms engaged in these businesses are subject to SARFT licensing. Foreign firms are allowed to form joint ventures and cooperative firms engaged in film production, technology and equipment. Joint ventures or cooperative firms must have at least RMB 5 million ($603,000) of registered capital, and foreign capital cannot make up more than 49 percent of the total share. In October, SARFT and MOFCOM issued the Provisional Rules on the Administration of China-Foreign Joint Venture and Cooperative TV Program Production Firms. The rules establish capital requirements of RMB 2 million ($241,000) of registered capital, and mandate a share of no less than 51 percent for domestic partners.

China began importing foreign films on a revenue-sharing basis in 1994. The Chinese government limits the number of foreign films allowed to enter China. China allowed in only ten foreign films annually through much of the 1990s, but more recently allowed in twenty foreign films annually on a revenue-sharing basis under its WTO commitments. However, China treats its WTO commitment as a ceiling, rather than a floor, which artificially increases demand for pirated products. Although China is also obligated to open theaters and film distribution to foreign investment, currently there are only two authorized distributors of foreign films, the state-owned China Film Distribution Company and Huaxia. Furthermore, lengthy censorship reviews by Chinese authorities delay the arrival of legitimately imported foreign films on Chinese movie screens. When the films do make it to the screen, they have sometimes been subject to blackout viewing periods during national holidays. China's large black market for foreign films continues to grow because these market access restrictions not only create a demand for pirated DVDs in the absence of legitimately licensed films, but also diminish the incentive for foreign investment in movie theaters. Right holders who comply with Chinese law must forego marketing legitimate products, leaving the demand for movies to be satisfied almost entirely by pirates. This situation somewhat negates the apparent benefits of China's recent raising of the percentage of foreign investment allowed for movie theaters to 75 percent, thus allowing for majority ownership by foreign investors. Some progress was achieved in 2004 when MOFCOM approved a U.S.-invested film distribution joint venture and took steps to shorten the time required to bring films to market.

Tourism and Travel Services

Immediately following China's WTO accession, China issued new travel agency administration regulations to allow large foreign travel and tourism service providers to operate full-service joint venture travel agencies to promote foreign inbound tourism in the four major foreign tourist destinations in China: Beijing, Shanghai, Guangzhou and Xian. China subsequently issued the Provisional Measures for the Establishment of Foreign-controlled and Wholly Foreign-funded Travel Agencies, effective July 2003. For now, the travel agencies must have an annual worldwide turnover in excess of $40 million, and local registered capital of almost $500,000. In November 2003, Germany's Touristic Union International (TUI) signed a letter of intent with the China Tourism Agency to form the first joint venture travel agency controlled by a foreign interest since China's accession to the WTO. Japan Airlines has also established the first wholly foreign-funded travel agency.

Foreign firms, however, continue to be restricted from competing in the Chinese outbound tourist market. China requires all travel agents, airlines and other booking entities to use or connect into China's nationally owned and operated computer reservation system when booking airline tickets. Foreign computer reservation companies can only provide reservations by connecting with the Chinese system. The total number of visas issued to Chinese wishing to travel to the United States rose from approximately 85,000 in 2003 to more than 108,000 in 2004, a 27 percent increase. Most of this increase is accounted for by a resumption of normal travel patterns following the containment of the SARS outbreak in China in 2003.

Meanwhile, holders of Chinese official passports, nearly 23,000 of whom were issued U.S. visas in 2004, are required to use China's state-owned airlines or their code-share partners. Most of these individuals are state-owned enterprise employees, who would not be considered government employees in most countries. This represents a significant loss of business for U.S. airlines.

Education and Training Services

China faces a shortage of qualified teachers and clearly needs educators in inland regions. However, the Ministry of Education (MOE) continues to restrict participation by foreign educators and trainers. China permits only non-profit educational activities that do not compete with the MOE-supervised nine years of compulsory education, thereby inhibiting much-needed foreign investment in the education sector. In April 2000, MOE banned foreign companies and organizations from offering educational services via satellite networks. Foreign universities may set up non-profit operations, but must have a Chinese university host and partner to ensure that programs bar subversive content and localize imported information. Meanwhile, China's training market is unregulated, which discourages potential investors from entering the market.

In June 2004, the Ministry of Education issued the Implementing Rules for China-Foreign Cooperative Education Projects. Although formulated to implement the Regulations on China-Foreign Cooperation in Running Schools, issued in September 2003, the rules are only applicable to certain activities, including education offering academic certificates, supplementary education and pre-school education. These activities cannot take the form of actual educational institutions.

Legal Services

Prior to its WTO accession, China maintained various restrictions in the area of legal services. It prohibited representative offices of foreign law firms practicing Chinese law or engaging in profit-making activities with regard to non-Chinese law. It also imposed restrictions on foreign law firms' formal affiliation with Chinese law firms, limited foreign law firms to one representative office and maintained geographic restrictions. Chinese law firms, on the other hand, have been able to open offices freely throughout China since 1996.

As part of its WTO accession, China agreed to lift quantitative and geographical restrictions on the establishment of representative offices by foreign law firms within one year after accession. In addition, foreign representative offices are to be able to engage in profit-making business, to advise clients on foreign legal matters and to provide information on the impact of the Chinese legal environment, among other things. They also are to be able to maintain long-term "entrustment" relationships with Chinese law firms and to instruct lawyers in the Chinese law firm as agreed between the two law firms.

The State Council issued the Regulations on the Administration of Foreign Law Firm Representative Offices in December 2001, and the Ministry of Justice issued implementing rules in July 2002. While these measures removed some market access barriers, they also generated concern among foreign law firms doing business in China. In many areas, these measures were ambiguous. For example, it appeared that these measures created an economic needs test for foreign law firms that want to establish offices in China, which would be contrary to China's GATS commitments. These measures also seemed to take an overly restrictive view of the types of legal services that foreign law firms may provide. In addition, the procedures for establishing a new office or an additional office were unnecessarily time-consuming. For example, a foreign law firm may not establish an additional representative office until its most recently established representative office has been in practice for three consecutive years. Foreign attorneys may not take China's bar examination, and they may not hire registered members of the Chinese bar as attorneys. Although a number of U.S. and other foreign law firms have been able to open a second office in China in 2003 and 2004, little progress has been made on the other problematic aspects of these measures.

Accounting and Management Consultancy Services

Prior to China's accession to the WTO, foreign accounting firms could not choose their own Chinese joint venture partners freely or enter into contractual agreements that could fully integrate these joint ventures. In its WTO accession agreement, China agreed to allow foreign accounting firms to partner with any Chinese entity of their choice. China also agreed to abandon the prohibition on foreign accounting firms' representative offices engaging in profit-making activities. Foreign accounting firms can also engage in taxation and management consulting services, without having to satisfy the more restrictive requirements on form of establishment applicable to new entities seeking to provide those services separately.

Meanwhile, the Chinese Institute of Certified Public Accountants, a government body under MOF, has made significant progress in modernizing accounting in China. In 2002, MOF released four newly revised auditing statements covering inter-bank confirmation, capital verification, accounting estimates and the audit of commercial bank financial statements. Furthermore, MOF has been active in standardizing accounting procedures across a wide range of topics including investments, inventories, cash flow statements, and fixed assets. The Chinese Securities Regulatory Commission required listed companies to appoint a certified international CPA firm to conduct audits on prospectuses and annual reports in accordance with international standards. While specific numbers are not available, most observers agree that the demand for internationally qualified accountants will grow rapidly in coming years. Despite these positive changes, pervasive problems remain. Differing accounting regulations limit the comparability of data, and the accounting practices followed by many domestic firms do not meet international conventions.

Advertising Services

The State Administration of Industry and Commerce (SAIC) enforces China's 1995 Advertising Law. Among other things, the law bans messages "hindering the public or violating social customs." The law is subject to interpretation by the SAIC, which must approve all advertising campaigns. One additional difficulty for foreign advertising firms, as well as foreign manufacturers, is that China has strict regulations prohibiting comparative advertising as well as any advertising with claims about the relative superiority of one brand over another. Marketing strategies that are successful in some other countries are therefore illegal in China.

In the past, foreign firms had been restricted to representative offices or minority ownership of joint-venture operations. As part of its WTO accession commitments, however, China agreed to allow majority foreign ownership of joint venture advertising companies by December 11, 2003 and wholly foreign-owned subsidiaries by December 11, 2005. In March 2004, SAIC and MOFCOM issued rules governing joint venture, cooperative and wholly foreign-owned advertisement firms. To establish branches, a firm must have paid in full its registered capital and have at least RMB 20 million ($2.41 million) in annual advertising revenue. Foreign firms are currently limited to a 70 percent share of joint venture and cooperative firms. As of December 2005, wholly foreign-owned advertising firms will be allowed.

Movement of Professionals

Generally, there are no special entry restrictions placed on U.S. professionals who wish to work in China, such as doctors or engineers. However, like other foreign professionals, they must receive approval from the Foreign Experts Bureau. Prior to arrival, a prospective American job applicant may be asked to provide notarized copies of his or her professional credentials and a summary of past work experience. The credentials will be used by the employer to file for a "foreign experts residency permit" for the American employee. Once the "foreign expert" permit is authorized, the prospective employee can request a work visa (a "Z" visa) from a Chinese embassy or consulate. If the prospective employee arrives in China on a visitors' visa (an "L" visa) prior to commencing employment, the prospective employee is usually asked to depart China prior to starting work, and to apply for the appropriate work visa from a foreign entry point (usually Hong Kong). Local employers are responsible for all employment or income tax and other withholdings for these "foreign experts" while they are employed in China. Recent press reports indicate that the government is considering measures to liberalize access by issuing "permanent resident" visas to long-time foreign residents of China. Meanwhile, for long term foreign residents in China, the government is liberalizing access by replacing the "Residence Card" with the "Permanent Resident Visa."

INVESTMENT BARRIERS

Foreign investors continue to show great interest in China despite significant obstacles. According to the United Nations Conference on Trade and Development, China received $62 billion in FDI in 2004, making it the second largest destination for FDI after the United States. General barriers to investment that plague China include lack of transparency, inconsistently enforced laws and regulations, weak IPR protection, corruption and an unreliable legal system incapable of protecting the sanctity of contracts. China's leadership has reaffirmed its commitment to "further open" China to investment and to continue movement toward a rules-based economic system. Foreign (and domestic) companies have reported high profitability in 2004, indicating that challenges to doing business in China have been largely surmountable. Nonetheless, faster concrete progress toward removing investment barriers could spur even more investment, particularly in new, higher value-added manufacturing and services.

Investment Requirements

In addition to taking on the obligations of the WTO Agreement on Trade-Related Investment Measures, China committed in its WTO accession agreement to eliminate export performance, local content and foreign exchange balancing requirements from its laws and regulations and not to enforce any contracts imposing those requirements. China also agreed that it would no longer condition investment (or import) approvals on those requirements or on requirements such as technology transfer and offsets.

In anticipation of these commitments, China revised its laws and regulations on foreign-invested enterprises to eliminate WTO-inconsistent requirements relating to export performance, local content and foreign exchange balancing as well as technology transfer. China also revised "Buy China" policies that regulated procurement of raw materials and fuels, and removed requirements that joint ventures and wholly foreign-owned enterprises submit production/operation plans to Chinese authorities. However, some measures continue to "encourage" technology transfer, without formally requiring it. U.S. companies are concerned that this "encouragement" will in practice amount to a "requirement" in many cases, particularly in light of the high degree of discretion provided to Chinese government officials when reviewing investment applications. In addition, according to U.S. companies, some Chinese government officials still consider factors such as export performance and local content when deciding whether to approve an investment or to recommend approval of a loan from a Chinese policy bank, which is often essential to the success of an investment project. While the number of complaints declined in 2004, foreign investors still remain wary of potential violations, as central government commitments to WTO-compliant measures often do not translate into provincial practice.

Investment Guidelines

Foreign investment inflows continue to be controlled and channeled toward areas that support national development objectives. China has adjusted its investment guidelines a number of times over the last six years. The revisions have confused potential investors and added to the perception that the investment guidelines do not provide a stable basis for business planning. Uncertainty as to which industries are being promoted as investment targets and how long such designations will be valid undermines confidence in the investment climate. A new catalogue took effect January 1, 2005, listing sectors in which foreign investment would be encouraged, restricted or prohibited, replacing the April 2002 list. Unlisted sectors are considered to be permitted.

Encouraged sectors include ones in which China could benefit from foreign assistance or technology, such as in the construction and operation of infrastructure facilities. In addition, the April 2002 catalogue had implemented elements of openings in sectors to which China committed in its WTO accession agreement, including for banking, insurance, petroleum extraction, value-added telecommunications, and distribution. The new catalogue opens television program production, distribution and movie production to foreign investors through allowing minority participation in joint ventures. It also adds certain component production for large-screen color projection tubes, automobile electronics, industrial boilers and production of compact disc media to the list of encouraged investments, which benefit from duty-free import of capital equipment and VAT rebates on inputs.

Over the past five years, China has also introduced various incentives for foreign investment in certain encouraged sectors. China introduced incentives for investments in high-technology industries, such as a regulation issued in November 1999 that provided foreign-invested enterprises a tax deduction for contributions to non-affiliated research and development or educational institutions. In December 2001, China announced comprehensive new incentives for investment in the less-developed central and western parts of the country.

The government also announced a series of measures in August 1999 that began to decentralize investment approval decision-making authority and to create new incentives for investments in key sectors and geographic regions. These guidelines allowed authorities at the provincial level of government to approve "encouraged" foreign-invested projects and raised the investment value at which central government approval is required.

Meanwhile, the Chinese government restricts foreign investment projects in sectors not in line with "the needs of China's national economic development." In these sectors, foreign firms must form a joint venture with a Chinese company and restrict their equity ownership to a minority share in order to invest in the Chinese market.

The Chinese government also prohibits investment in certain sectors. China bans investment in the news media and broadcast citing national security interests. The production of arms and the mining and processing of certain minerals remain prohibited sectors. U.S. investors have expressed particular concerns about China's prohibition of investment in production and development of genetically modified plant seeds.

China is scheduled to release its 11th Five-Year Plan in mid-2005. The plan will outline policy objectives for the economy through 2010.

Other Investment Issues

Venture Capital

Regulations that took effect in March 2003 replaced earlier provisional regulations permitting the establishment of foreign-invested venture capital firms, including wholly foreign-owned enterprises, aimed at funding high-technology and new technology startups in industries open to foreign investment. The regulations lower capital requirements, allow these firms to manage funds directly invested from overseas, and offer the option of establishing venture capital firms under an organizational form similar to the limited liability partnerships used in other countries. April 2001 regulations bar securities firms (including foreign-invested firms) from the private equity business, while foreign private equity firms are permitted subject to limits on corporate structure, share issuance and transfers, and investment exit options. Investment exit problems, especially the difficulty of listing on China's stock exchanges, coupled with the bureaucratic approvals required to list overseas, have limited interest in establishing China-based venture capital and private equity investment. As a result, most foreign venture capital and private equity investments in China are actually housed in offshore investment entities, which, as with other offshore FDI, can be transferred without Chinese government approval.

Holding Companies

There has been some relaxation of restrictions on the scope and operations of holding companies, although minimum capital requirements normally make them suitable only for corporations with several sizeable investments to manage. Holding companies may manage human resources across their affiliated companies and provide certain market research and other services to their affiliates. However, some restrictions on services provided by holding companies and on their financial operations and their ability to balance foreign exchange internally will remain even after full implementation of China's WTO commitments. Profit and loss consolidation within holding companies also remains prohibited.

Access to Capital Markets

Foreign-invested enterprises in China remain largely unable to access domestic and international stock markets, to sell corporate bonds, to accept venture capital investment, to sell equity, or to engage in normal merger, acquisition and divestment activity. Foreign exchange transactions on the capital account can be concluded only with case-by-case official review, and approvals are subject to very tight regulatory control. These barriers to capital market access were not addressed by China's WTO accession agreement. China has begun to experiment with liberalization, such as the opening of domestic stock markets to listings by foreign-invested firms. Through the Qualified Foreign Institutional Investor (QFII) program, foreign securities firms can gain limited access to the RMB-denominated A share market by applying for QFII status with the Chinese government. As of December 2004, 27 foreign firms had been granted QFII status, and 24 of them had been issued QFII investment quotas totaling $3.425 billion.

GOVERNMENT PROCUREMENT

In accordance with the terms of its WTO accession agreement, China agreed to conduct its government procurement in a transparent manner and to provide all foreign suppliers with equal opportunity to participate in procurements opened to foreign suppliers. China also committed to become an observer to the WTO Agreement on Government Procurement (GPA), which it did in May 2002, and to table an offer and initiate negotiations for membership in the GPA "as soon as possible." In late 2003, MOF reportedly established a working group to study the possibility of initiating negotiations for accession to the GPA. In the interim, China agreed that all of its central and local government entities would conduct their procurements in a transparent manner, as reflected in its WTO accession agreement. China also agreed that, if a procurement were opened to foreign suppliers, it would provide MFN treatment by allowing all foreign suppliers an equal opportunity to participate in the bidding process.

In July 2002, China promulgated its first Government Procurement Law. In part, this was a response to the need to separate purchases by "state-owned enterprises," which China had agreed in its WTO accession agreement would be made on a commercial basis, from "government procurement." China also agreed that the government would not influence the commercial decisions of state-owned enterprises, although in practice this has not consistently been the case.

The Government Procurement Law, which became effective on January 1, 2003, attempts to follow the spirit of the GPA and incorporates provisions from the United Nations Model Law on Procurement of Goods. However, the law also directs central and sub-central government entities to give priority to "local" goods and services, with limited exceptions. China envisions that this law will improve transparency, reduce corruption and lower government costs. The law is also seen as a necessary step toward reforming China's government procurement system in preparation for China eventually becoming a Party to the GPA. In August 2004, MOF issued implementing rules stipulating that procurement of foreign goods, works and services, which are allowed in exceptional circumstances, are subject to review and approval by MOF.

In August 2004, MOF issued measures covering bidding procedures, publication of information and the handling of complaints related to government procurements. The bidding rules require all government procurements over a certain amount to be conducted through public bidding. According to the 2004 catalog for central-government financed government procurement, the threshold for public bidding is RMB 1.2 million, or $146,000. To be eligible to participate, suppliers must be domestic and provide "domestic goods and services." MOF is reportedly formulating the criteria for "domestic goods and services." The information publication rules require procuring entities and their agencies to make public all necessary information through media outlets designated by MOF. These rules define this information as statutes, data and other materials concerning government procurements, and also require the disclosure of detailed information concerning bid invitations and bidding. The complaint handling rules require MOF and local finance administrations to respond to complaints from suppliers regarding the conduct of procurements. Suppliers may apply for administrative review of a ruling or file an administrative suit in court.

Draft implementing rules governing the procurement of software products and services are of serious concern to U.S. companies. As initially drafted in 2003, when China's overall software market totaled $3.3 billion and was projected to grow by more than 50 percent annually, these rules reportedly contained guidelines mandating that central and local governments should purchase software developed in China to the extent possible. In November 2004, MOF and MII released a partial summary of draft measures that appear to define "domestic software" very restrictively and, as a result, would make it difficult for foreign software to qualify for a procurement. The United States has raised serious concerns about this aspect of the draft measures. By the end of 2004, final measures had not yet been issued.

ELECTRONIC COMMERCE

China has experienced dramatic growth in Internet usage since 1999. According to the 15th semiannual Internet survey recently published by the China Internet Network Information Center (CNNIC), the number of people in China with access to the Internet was approximately 94 million, an increase of 18 percent year on year, second only to the United States in terms of total users. Falling personal computer prices and the arrival of devices tailored for the Chinese market will further expand Internet access.

China has also experienced a dramatic increase in the number of electronic businesses established. An estimated 78 percent of all Chinese websites are now operated by "enterprises" and 5 percent by "businesses." By the end of June 2004, there were roughly 626,600 registered websites in China. Of this total, 382,216 were registered under ".cn". However, despite these developments, only 11 percent of Chinese "enterprise" websites and 45 percent of Chinese "business" websites offer "e-commerce services." Nevertheless, China is experiencing rapid development of on-line business such as search engines, network education, on-line advertisements, audio-video service, paid e-mail, short message, on-line job hunting, Internet consulting and on-line gaming.

The Chinese government recognizes the potential of electronic commerce to promote exports and increase competitiveness and has made some progress toward establishing a viable commercial environment. However, some Chinese ministries with responsibility for electronic commerce have excessively regulated the Internet, thereby stifling the free flow of information and the consumer privacy needed for electronic commerce to flourish. Content is still controlled and encryption regulated, as discussed more fully above (in the "Regulation of Internet Content and Restrictions on Encryption and Decryption" section).

A number of technical problems also inhibit the growth of electronic commerce in China. Rates charged by government-approved Internet service providers make Internet access expensive for most Chinese citizens. Slow connection speeds are another problem, although this is changing as broadband connections become more readily available. In 2004, nearly 46 percent of China's Internet users had broadband connections, representing an increase of 146 percent over 2003, and China Telecom is now reportedly the world's largest DSL operator, with subscribers expected to exceed 10 million in 2004.

Other impediments to Chinese businesses and consumers conducting online transactions include the paucity of credit payment systems, consumer reluctance to trust online merchants, the lack of secure online payment systems and inefficient delivery systems. China has also yet to develop a legal framework conducive to the rapid growth of electronic commerce. Laws recognizing the validity of "e-contracting" tools and stressing the importance of online privacy and security have been proposed, but not yet issued. Despite these obstacles, however, over 40 percent of Chinese Internet users surveyed in June 2003 said they had made an online purchase within the past year, and almost a third of them said they had paid online.

In a positive sign, China passed E-signature legislation on August 28, 2004, which will become effective on April 1, 2005. China is also in the process of drafting data privacy legislation.

ANTICOMPETITIVE PRACTICES

China continues to struggle with economic inefficiencies and investment disincentives created by local protectionism, pricing practices and preservation of industry-wide monopolies. Anticompetitive practices in China take several forms. In some cases, industrial conglomerates operating as monopolies, near monopolies, or authorized oligopolies (as in the telecommunications industry) have been allowed to fix prices, allocate contracts, and in other ways restrict competition among domestic and foreign suppliers. Regional protectionism by provincial or local authorities often blocks efficient distribution of goods and services inside China. These practices may restrict market access for certain imported products, raise production costs, and restrict market opportunities for foreign-invested enterprises in China.

There are several existing laws and regulations in China addressing competition matters. However, these measures are largely ineffective due to poor national coordination and inconsistent local and provincial enforcement. China is drafting a new anti-monopoly law that could be adopted as early as mid-to-late 2005.

Since November 2002, foreigners have been able to purchase traded and non-traded (designated state) shares of Chinese enterprises. In addition, regulations that took effect in April 2003 specify procedures for foreign acquisition of and merger with domestic enterprises. These regulations require pre-merger notification and allow for examination of antitrust considerations in some cases. By requiring approval of all owners of the domestic enterprise, the regulation implicitly prohibits hostile takeovers. The thresholds for notification are not straightforward, leaving open the possibility of abuse by officials or domestic competitors. Domestic competitors have the power under the regulations to call for public hearings on prospective mergers.

China also issued provisional regulations in November 2002, effective January 2003, on using foreign investment to reorganize state-owned enterprises. These reorganizations, however, require extensive approvals and full agreement of the domestic enterprise's labor union. These requirements are likely to limit the appeal of this type of investment.

OTHER BARRIERS

Transparency

Laws and regulations directly affecting international trade are increasingly becoming publicly available in China. Since 1992, China has published all trade laws and regulations in the "MOFCOM Gazette," available on a subscription basis, and MOFCOM maintains an updated list on its website. However, many measures that do not rise to the level of ministry-issued regulations or implementing rules continue to remain unavailable to the public. China's ministries routinely implement policies based on internal "guidance" or "opinions" that are not available to foreign firms. Experimental or informal policies and draft regulations, in addition, are regarded as internal matters and public access is tightly controlled.

China, in its WTO accession agreement, committed to publishing all laws, regulations and other measures that relate to trade matters, including those that affect imports, and generally to allowing its WTO trading partners an opportunity to comment on them before implementation. China also agreed to provide a copy of new trade-related laws, regulations and other measures to the WTO Secretariat in Geneva, translated into one or more of the WTO's official languages (English, French and Spanish) no later than 90 days after implementation. China further agreed to create various enquiry points for its WTO trading partners and foreign businesses to obtain information about these measures.

Various government-owned specialty newspapers routinely carry the texts of government regulations, implementing rules, circulars and announcements. Many government ministries also publish digests or gazettes containing the texts of these measures, both in written form and on their websites. In addition, there has been a proliferation of online news and information services that routinely offer up-to-date news about and texts of new laws and regulations. Some services even provide legal-quality English translations by subscription.

While positive in some respects, the sheer number of outlets through which these measures are published complicates the ability of interested parties to track their development and issuance. In its WTO accession agreement, China agreed to establish or designate an official journal for the publication of trade related measures. In late 2002, China designated the China Foreign Economic and Trade Gazette as the official journal for this purpose. Published by MOFCOM and replacing the MOFCOM Gazette, it came out on a trial basis in October 2002 and as an official publication in January 2003. However, this journal does not carry draft rules for comment, nor does it consistently carry trade related measures developed by ministries and agencies other than MOFCOM. The establishment or designation of a single comprehensive journal would enhance the ability of WTO members to track the drafting, issuance and implementation of trade related measures. Furthermore, the use of a single journal to request comments on proposed trade-related measures, as envisioned in China's WTO accession agreement, would facilitate the timely notification of comment periods and submission of comments.

In December 2001, the State Council issued regulations explicitly allowing comment periods and hearings. However, many of China's ministries and agencies continued to follow the practice prior to China's accession to the WTO. The ministry or agency drafting a new or revised law or regulation will normally consult with and submit drafts to other ministries and agencies, Chinese experts and affected Chinese companies. At times, it will also consult with select foreign companies, although it will not necessarily share drafts with them. As a result, only a small proportion of new or revised laws and regulations have been issued after a period for public comment, and even in these cases the amount of time provided for public comment has generally been short. In 2004, some improvements took place, particularly on the part of MOFCOM, which began following the rules set forth in its Provisional Regulations on Administrative Transparency, issued in November 2003. Those rules could potentially serve as a model for other ministries and agencies seeking to improve their transparency. Nevertheless, basic compliance with China's notice-and-comment commitment continued to be uneven. For example, China issued several major trade-related laws and regulations in 2004, including a revised Foreign Trade Law, insurance regulations, government procurement regulations and several sets of implementing rules, a new automobile industrial policy, regulations on rules of origin for imports and exports, and customs regulations on administrative penalties for IPR infringement. Encouragingly, drafts of the insurance regulations and most of the government procurement measures were circulated for public comment. However, drafts of the Foreign Trade Law, the automobile industrial policy, the rules of origin regulations, and the customs regulations were either selectively circulated or not circulated at all. Toward the end of 2004, a number of important measures, including direct selling regulations and government software procurement implementing rules were close to being finalized, without having been circulated for public comment.

U.S. industry continues to report instances where Chinese companies are provided unofficial guidance by Chinese regulators, guidance which is usually unavailable to foreign entities. In some cases, Chinese officials provided unpublished documents to interested parties, but this dissemination was ad hoc and based more on personal connections than formal procedures.

MOFCOM's predecessor, MOFTEC, in late 2001, established an enquiry point to provide information on new trade and investment laws, regulations and other measures. It is not clear whether this enquiry point is still functioning, however. Other ministries and agencies have also established formal or informal, subject-specific enquiry points. Since the creation of these various enquiry points, U.S. companies have generally found them to be responsive and helpful, and have generally received timely replies.

Legal Framework

Laws and Regulations

Laws and regulations in China tend to be more general and ambiguous than in other countries. While this approach allows the Chinese authorities to apply laws and regulations flexibly, it also results in inconsistency and confusion in application. Companies often have difficulty determining whether their activities contravene a particular law or regulation.

In China, regulations are also promulgated by a host of different ministries and governments at the central, provincial and local levels, and it is not unusual for the resulting regulations to be at odds with each other. Even though finalized regulations are now routinely published in China, they often leave room for discretionary application and inconsistencies, either through honest misunderstanding or by design. Indeed, government bureaucracies have sometimes been accused of selectively applying regulations. China has many strict rules that are often ignored in practice until a person or entity falls out of official favor. Governmental authorities can wield their discretionary power to "crack down" on foreign or disfavored investors or make special demands on such investors simply by threatening to wield such power.

This lack of a clear and consistent framework of laws and regulations can be a barrier to the participation of foreign firms in the Chinese domestic market. A comprehensive legal framework, coupled with adequate prior notice of proposed changes to laws and regulations, and an opportunity to comment on those changes, would greatly enhance business conditions, promote commerce and reduce opportunities for corruption. The U.S. Government has provided technical assistance, at the central and local levels of government in China, in an effort to promote improvements in China's legislative and regulatory drafting process.

In its WTO accession agreement, China committed to establish tribunals for the review of all administrative actions relating to the implementation of trade-related laws, regulations, judicial decisions and administrative rulings. These tribunals must be impartial and independent of the government authorities entrusted with the administrative enforcement in question, and their review procedures must include the right of appeal. China also committed, at all levels of government, to apply, implement and administer all of its laws, regulations and other measures relating to trade in goods and services in a uniform and impartial manner throughout China, including in special economic areas. In connection with this commitment, in 2002, China also established an internal review mechanism, now overseen by MOFCOM's Department of WTO Affairs, to handle cases of non-uniform application of laws. The actual workings of this mechanism still remain unclear, however.

Commercial Dispute Resolution

Both foreign and domestic companies often avoid seeking enforcement actions through the Chinese courts, as skepticism about the independence and professionalism of China's court system and the enforceability of court judgments and awards remains high. There is a widespread perception that judges, particularly outside of China's big cities, are subject to influence by local political or business pressures. Most judges are not trained in the law and/or lack higher education, although this problem decreases at the higher levels of the judiciary.

At the same time, the Chinese government is moving to establish consistent and reliable mechanisms for dispute resolution through the adoption of improved codes of ethics for judges and lawyers and increased emphasis on the consistent and predictable application of laws. The Judges' Law, issued by the Standing Committee of the National People's Congress in 1995, requires judges to have degrees in law or in other subjects where they have acquired specialized legal knowledge, and permits judges appointed before the law's implementation who do not meet such standards to undergo necessary training. In 1999, the Supreme People's Court began requiring judges to be appointed based on merit and educational background and experience, rather than through politics or favoritism. In August 2002, the Supreme People's Court issued rules designating certain higher-level courts to hear cases involving administrative agency decisions relating to international trade in goods or services or intellectual property rights. According to the Supreme People's Court, China's more experienced judges sit on the designated courts, and the geographic area under the jurisdiction of each of these designated courts has been broadened in an attempt to minimize local protectionism. The rules provide that foreign (or Chinese) enterprises and individuals may bring lawsuits in the designated courts raising challenges, under the Administrative Litigation Law, to decisions made by China's administrative agencies relating to international trade matters. The rules also state that when there is more than one reasonable interpretation of a law or regulation, the courts should choose an interpretation that is consistent with the provisions of international agreements to which China has committed, such as the WTO rules. The rules took effect in October 2002.

Despite initial enthusiasm, foreign observers have grown increasingly skeptical of the China International Economic and Trade Arbitration Commission (CIETAC) as a forum for the arbitration of trade disputes. Some foreign firms have obtained satisfactory rulings from CIETAC but other firms and legal professionals have raised concerns about restrictions on the selection of arbitrators and inadequacies in procedural rules necessary to ensure thorough, orderly and fair management of cases.

Finally, in cases where the judiciary or arbitration panels have issued judgments in favor of foreign-invested enterprises, enforcement of the judgments has often been difficult. Officials responsible for enforcement are often beholden to local interests and unwilling to enforce court judgments against locally powerful companies or individuals.

Labor Issues

In recent years, China has expanded the scope of its national labor laws and regulations so they now cover most, though not all, key labor areas. Even with these changes, China does not adhere to certain internationally recognized labor standards, such as the rights of freedom of association and collective bargaining. In addition, critics allege that China's household registration system is equivalent to a form of forced or compulsory labor, and there are many reports indicating that China does not enforce its laws and regulations concerning minimum wages, hours of work and occupational safety and health. There are also persistent concerns about the use of prison labor and child labor.

The Chinese government is slowly developing nationwide pension, unemployment insurance, medical insurance and workplace injury insurance systems that require substantial employer contributions. These systems are still rudimentary and characterized by serious funding shortfalls, in part due to widespread non-compliance among domestic firms. There is also inconsistent application and enforcement of labor regulations between Chinese-owned enterprises and foreign-invested enterprises.

The cost of labor, especially unskilled labor, is low in much of China. The existence of a large pool of surplus rural workers, many of whom seek work in urban areas, helps to keep unskilled wages low. Some companies offering substandard wages and working conditions have experienced shortages of unskilled labor. Where competition for workers is intense and the supply limited, as in the case of technical, managerial and professional staff in China's coastal areas, wages can be higher. However, restrictions on labor mobility distort labor costs. China is gradually easing restrictions under the country's household registration system, which has traditionally limited the movement of workers within the country, in part due to the recognition that labor mobility is essential to the continued growth of the economy.

Corruption

Many people expected that China's entry into the WTO, which mandated a significant reduction in tariffs, would in turn reduce incentives for smuggling-related corruption. While WTO membership has increased China's exposure to international best practices and resulted in some overall improvements in transparency, corruption remains endemic. Chinese officials themselves admit that corruption is one of the most serious problems the country faces, and China's new leadership has called for an acceleration of the country's anti-corruption drive with a focus on closer monitoring of provincial-level officials. According to Chinese state media sources, in 2004, Chinese prosecutors caught more than 42,000 officials for corruption and other offenses, reflecting a rise of one percent from 2003. Official graft was a leading offense, with prosecutors recovering a total of RMB 3.8 billion ($460 million) of misappropriated and embezzled funds.

In July 2004, China implemented a new Administrative Licensing Law. This law should increase transparency in the licensing process, an area that has long served as a source of official corruption. This law seeks to ensure the reasonable use of administrative licensing powers, to protect the interests of corporations and individuals, and to promote efficient administrative management by requiring government agencies to set up special offices for issuing licenses and to respond to applications within 20 days. It is too early to judge the effectiveness of this law, but some reports suggest that it has already resulted in the removal of numerous unnecessary administrative licensing requirements.

China issued its first law on unfair competition in December 1993, and the Chinese government continues to call for improved self-discipline and anti-corruption initiatives at all levels of government. While the government has pledged to begin awarding contracts solely on the basis of commercial criteria, it is unclear how quickly and to what extent the government will be able to follow through on this commitment. U.S. suppliers complain that the widespread existence of unfair bidding practices in China puts them at a competitive disadvantage. This dilemma is less severe in sectors where the United States holds clear technological or cost advantages. Corruption nevertheless undermines the long-term competitiveness of both foreign and domestic entities in the Chinese market.

Land Issues

China's constitution specifies that all land is owned in common by all the people. In practice, agricultural collectives, under the firm control of local Communist Party chairmen, distribute agricultural land to the rural poor, while city governments distribute land for residential and industrial use. The State and collectives can either "grant" or "allocate" land use rights to enterprises in return for payment of fees. Enterprises granted land-use rights are guaranteed compensation if the State asserts eminent domain over the land, while those with allocated rights are not. Granted land-use rights cost more, of course, than allocated rights. However, the law does not define standards for compensation when eminent domain supercedes granted land-use rights. This situation creates considerable uncertainty when foreign investors are ordered to vacate. The absence of public hearings on planned public projects, moreover, can give affected parties, including foreign investors, little advance warning.

The time limit for land-use rights acquired by foreign investors for both industrial and commercial enterprises is 50 years. A major problem for foreign investors is the array of regulations that govern their ability to acquire land-use rights. Local implementation of these regulations may vary from central government standards, and prohibited practices may occur in one area while they are enforced in another. Most wholly-owned foreign enterprises seek granted land-use rights to state-owned urban land as the most reliable protection for their operations. Chinese-foreign joint ventures usually attempt to acquire granted land-use rights through lease or contribution arrangements with the local partners.

China's current rural land law, which took effect in 2003, gives peasants fixed contracts for periods of 30 to 50 years, and permits peasants to exchange or rent out their land-use rights while their use contract remains in force. There is no immediate prospect for changing from land-use rights to direct ownership of rural land. However, in 2004, the leadership has pressed for sturdier land rights for farmers along with stricter controls over the legal process for converting farmland from agricultural to industrial or residential use. Local governments are no longer supposed to expropriate land for commercial use, as farmers are now supposed to be able to negotiate a compensation price for land directly with commercial users. However, implementation of these provisions lags.

COLOMBIA

TRADE SUMMARY

The U.S. trade deficit with Colombia was $2.8 billion in 2004, an increase of $157 million from $2.6 billion in 2003. U.S. goods exports in 2004 were $4.5 billion, up 19.9 percent from the previous year. Corresponding U.S. imports from Colombia were $7.3 billion, up 14.2 percent. Colombia is currently the 27th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Colombia in 2003 was $2.8 billion, up from $2.6 billion in 2002. U.S. FDI in Colombia is concentrated largely in the manufacturing, information and finance sectors.

FREE TRADE NEGOTIATIONS

In May 2004, the United States initiated free trade agreement (FTA) negotiations with three Andean nations -- Colombia, Peru and Ecuador. Bolivia is participating as an observer and is expected to become part of the agreement at a later stage. The U.S. Government will seek to address the issues described in this chapter within the context of these negotiations. The four Andean countries collectively represented a market of about $8.5 billion for U.S. exports in 2004, and were home to about $7.2 billion in U.S. foreign direct investment.

IMPORT POLICIES

Tariffs

Colombia has opened its economy considerably since the early 1990s. Customs duties were cut and many non-tariff barriers eliminated. Most duties have been consolidated into three tariff levels: zero to five percent on capital goods, industrial goods and raw materials not produced in Colombia; ten percent on manufactured goods with some exceptions; and fifteen to twenty percent on consumer and "sensitive" goods. The United States is seeking the elimination of Colombia's duties on U.S. exports in the FTA negotiations, upon entry into force of the agreement where possible and over time for the most sensitive products.

Some important exceptions include automobiles, which are subject to a 35 percent tariff, and agricultural products, which fall under a variable "price-band" import duty system. The price-band system includes 14 product groups and covers 154 tariff lines, which at times results in duties approaching or exceeding 100 percent for important U.S. exports to Colombia, including corn, wheat, rice, soybeans, pork, poultry, cheeses and powdered milk, and negatively affects U.S. access for products such as dry pet food, some of which is made from corn. When international prices surpass the price-band ceiling, tariffs are reduced; when prices drop below the price-band floor, tariffs are raised. The price-band system has affected local competitiveness and has dampened consumption by raising prices, and is a barrier to U.S. exports. Processed food imports from Chile and members of the Andean Community (Peru, Ecuador, Bolivia and Venezuela) enter duty-free.

Non-Tariff Measures

Other non-tariff barriers in Colombia include discretionary import licensing, which is used to ban imports of milk powder and poultry parts. Colombia removed the "absorption" requirements for all remaining agricultural products at the end of 2003, when the WTO waiver allowing them to link imports to local purchases expired. The Colombian government replaced this system with tariff-rate quotas for rice, yellow corn, white corn and cotton, with a requirement to purchase local production in order to import under the tariff-rate quota. The U.S. Government is seeking through the FTA negotiation to eliminate Colombia's barriers to trade in our agricultural products, while providing reasonable adjustment periods and safeguards for producers of import sensitive agricultural products.

Colombia treats remanufactured goods as used goods, thereby limiting the market access for major U.S. makers of high-quality remanufactured goods. Colombia also assesses a value-added tax (VAT) of 35 percent on whiskey aged for less than twelve years, which is more characteristic of U.S. whiskey, compared to a rate of 20 percent for whiskey aged for twelve or more years, most of which comes from Europe. Several Colombian states are engaged in practices that have restricted the ability of U.S. distilled spirits companies to conduct business in Colombia. For example, some states mandate the minimum quantity of a specific distilled spirit brand that a company must sell during the year. If a company does not meet the minimum sales requirement, the company is fined or its sales contract is revoked in that particular state. Some states also mandate the minimum price at which imported spirits may be sold. In certain cases, the minimum price is set above the price at which imported products can be sold competitively in the market. Other measures that are applied only to importers of distilled spirits include: assessment of a 7.5 percent tax on all contracts based on the minimum volume to be sold in the state; a requirement to share a percentage of profits with the state; and payment of a federal excise tax upon entry into Colombia instead of after the first sale as domestic producers are allowed to do.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Regarding pet food, Colombia requires companies not only to list the ingredients but the percentage of those ingredients on their products, which U.S. companies declare as proprietary information. In some cases, SPS measures have been implemented to restrict U.S. exports. For example, Colombia has maintained restraints on U.S. exports of cattle and beef that do not appear to be consistent with the Office of International Epizootics (OIE) recommendations. Since December 2003, U.S. beef has been banned in Colombia on the basis of BSE (Bovine Spongiform Encephalopathy). However, this ban continues to be enforced without adequate scientific justification.

U.S. companies retailing nutritional supplements in Colombia continue to experience problems due to the lack of legislation that establishes clear parameters for sanitary registration. Colombia does not have a specific classification for nutritional supplements.

GOVERNMENT PROCUREMENT

The Government Procurement and Contracting Law, Law 80/93 established procedures for the selection of suppliers, mainly through public tenders. In order to qualify as a potential supplier to the Government of Colombia, foreign firms must register with the local chamber of commerce and appoint a local representative. Registration must be renewed annually and includes certification of experience, finances, technical expertise and organization. The certifications are used to qualify and classify suppliers based on "bona fide" criteria. The registration requirements make the process particularly costly for foreign firms, which need to demonstrate a commercial presence in Colombia to participate in government procurement.

In July 2003, the Colombian government promulgated Law 816 to protect national industries in government procurement. Law 816 mandates that all public entities adopt criteria that support national industries and accords preferential treatment to bids that incorporate Colombian goods or services. Under Law 816, national companies are given a 10 percent to 20 percent "bonus" in their evaluation score, and companies using Colombian goods or services are given a 5 percent to 15 percent bonus. Bids without any Colombian component are scored between 5 percent and 20 percent lower than bids with such a component. Additionally, Law 816 requires foreign suppliers without local headquarters in Colombia to obtain certification from a Colombian mission in the suppliers' home country that government procurement laws in the suppliers' home country meet reciprocity requirements. To date, this new system, and specifically the lack of an established certification process, has proven to be a barrier against the participation of U.S. suppliers in government procurement contracts.

There have been complaints of non-transparency with respect to the awarding of major government contracts. The Colombian government has taken positive steps to fight corruption, such as working with non-governmental organizations to launch probity programs aimed at promoting entrepreneurial and public ethics. However, Colombia is not a signatory of the WTO Agreement on Government Procurement. According to industry analysts, the elimination of barriers in the government procurement sector could yield an increase of U.S. exports in the range of $100 to $500 million (U.S.). In the FTA negotiations the U.S. Government is seeking opportunities for U.S. companies to bid on Colombian government procurement.

EXPORT SUBSIDIES

Colombia has been working to eliminate export subsidies since its GATT accession. This process has continued under the WTO Agreement on Subsidies and Countervailing Measures. In December 2002, Colombia accepted the WTO Committee on Subsidies and Countervailing

Measures' decision to phase out all export subsidies in free trade zones by December 31, 2006. However, free trade zones and special import-export zones will maintain their special customs and foreign exchange regimes. In June 2003, the Colombian government announced that it would eliminate the tax benefits linked to exports and will replace them with other incentives for employment generation and investment in new technologies, but no decree has since been issued.

Colombia's tax rebate certificate program (CERT) is a tax reimbursement certificate, which represents a credit that can be applied to taxes on income, customs duties and certain other taxes. It also is freely negotiable and can be sold in a secondary market, although presumably at a discount. The CERT is intended to promote non-traditional export products (specifically excluded from the CERT program are coffee, petroleum and petroleum bi-products). The amount of the CERT is calculated as a flat percentage of the value of goods exported, and varies by product and destination. In late 2002, the Colombian government suspended use of the CERT, reducing it to zero percent. Although this means that the subsidy component has disappeared, the CERT has not been eliminated, and it could be increased in the future when Colombia's budgetary conditions improve.

The other export subsidy, known as the "Plan Vallejo," allows for duty exemptions on the import of capital goods and raw materials used to manufacture goods that are subsequently exported. In order to qualify for this tax exemption, in the case of capital goods, the producer must show that at least 70 percent of the volume of product produced by the newly imported capital good is exported. In the case of raw or partially finished materials, the producer must export a value equal to 1.5 times that of the value of the imported materials as valued upon their entry by Colombian government customs. In July 2004, the Colombian government proposed to eliminate the Plan Vallejo by December 31, 2006 in the hopes that a signed FTA between Colombia and the United States would be in place, providing for duty free importation of many capital goods.

Colombia also operates producer financed export subsidies under the "price stabilization" funds for sugar, palm oil, beef and dairy. The exports under the sugar and palm oil funds are in excess of Colombia's WTO export subsidy commitments of 223,608 tons for sugar and zero for palm oil.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Colombia has been on the Special 301 "Watch List" every year since 1991. Key concerns include lax customs enforcement and the inability to conclude legal cases against individuals arrested for trafficking or producing counterfeit goods. Colombia, which is a WTO member, has ratified its legislation to implement its obligations under the Uruguay Round Agreement on Trade-Related Aspects of Intellectual Property Rights. Colombia is a member of the World Intellectual Property Organization (WIPO), the Paris Convention for the Protection of Industrial Property, the Berne Convention for the Protection of Literary and Artistic Works, the Treaty on the International Registration of Audiovisual Works, and the 1978 Union for the Protection of New Plant Varieties, and a signatory to the Patent Cooperation Treaty.

In Colombia, the grant, registration and administration of intellectual property rights (industrial property and copyright) are carried out by four different government entities. The Superintendence of Industry and Commerce (SIC) acts as the Colombian patent and trademark office. This agency was given control of the government's IPR policy, effective January 2000. The agency suffers from inadequate financing and personnel, a high turnover rate, and a large backlog of trademark and patent applications, which has led to a large number of appeals. However, the SIC plans to provide electronic registration services for patents, industrial designs and trademarks. The Colombian Agricultural Institute (ICA) is in charge of the issuance of plant variety protection-related and agro-chemical patents. The Ministry of Social Protection is in charge of the issuance of pharmaceutical patents, while the Ministry of Justice is in charge of the issuance of literary copyrights.

Each of these entities suffers from significant financial and technical resource constraints. Moreover, the lack of uniformity and consistency in IPR registration and oversight procedures limits the transparency and predictability of the IPR enforcement regime.

The United States is currently negotiating IPR provisions under the ongoing Andean FTA negotiations to improve protection and strengthen enforcement of IPR. The U.S. Government is seeking to address specific U.S. industry concerns related to the protection and enforcement of copyrights and related rights, patents, proprietary data for pharmaceutical and agricultural products, trademarks and geographical indications.

Patents and Trademarks

The patent regime in Colombia currently provides for 20-year protection for patents and a ten-year term for industrial designs. Provisions covering protection of trade secrets and new plant varieties have improved Colombia's compliance with its TRIPS obligations. However, U.S. companies are concerned that the Colombian government does not provide patent protection for second uses.

In 2002, the Colombian government issued Decree 2085, which improved the protection of confidential data. Until 2002, Government of Colombia health authorities approved the commercialization of new drugs that were the bioequivalent of already-approved drugs, thereby denying the originator companies the exclusive use of their data. Decree 2085 prohibited this practice, thus providing improved protection for industrial information. Under the decree, data presented for health certification of pharmaceuticals is protected for a period of three years for registrations issued in 2002, four years in 2003, and five years in 2004 and beyond. In March 2003, the Agricultural Ministry promulgated Decree 502 that provides similar protection for agricultural chemicals. However, the subsequent passage of Law 822 on July 10, 2003 established additional norms in relation to the registration, control and sale of generic agrochemicals which, along with the related Resolution 770 of March 27, 2003, appear to significantly weaken the data protections established by Decree 502.

Counterfeit pharmaceutical products continue to be a major problem in Colombia. Recent surveys, such as the CRECER project, reveal that in rural areas there are more counterfeit pharmaceutical products than original products. The CRECER project found that ten percent of these counterfeit products are identical to the original product while 60 percent do not contain any active ingredient and 30 percent contain the wrong active ingredient or the wrong dosage.

Colombia is a member of the Inter-American Convention for Trademark and Commercial Protection. Enforcement of trademark legislation in Colombia is showing some progress, but contraband and counterfeiting are widespread.

Copyrights

Andean Community Decision 351 on the protection of copyrights has been in effect in Colombia since January 1, 1994. Colombia also has a modern copyright law: Law 44 of 1993. The law extends protection for computer software to 50 years but does not classify it as a literary work. Law 44 and Colombia's civil code include some provisions for IPR enforcement and have been used to combat infringement and protect rights. Colombia is a member of the Berne and Universal Copyright Conventions, the Convention on Literary and Artistic Copyright, Fourth International American Conference (Buenos Aires), the Inter-American Convention on Copyright and Literary Property (Washington), the Rome Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations, the Geneva Convention for Phonograms, the WIPO Copyright Treaty, and the WIPO Performances and Phonograms Treaty. It is not a member of the Brussels Convention relating to the Distribution of Programme-Carrying Signals Transmitted by Satellite.

Colombia's Criminal Code of 2001 includes copyright infringement as a crime, and significantly increased jail terms from three to five years. The code also contains provisions concerning technological protection measures and rights management information, both key obligations of the WIPO treaty. Colombia has also created a Special Investigative Unit within the Prosecutor General's Office dedicated to intellectual property rights issues. This unit began functioning in November 1999 and is currently working on a number of cases against pirate television programming broadcasters.

The International Intellectual Property Alliance estimates that in 2004 piracy levels in Colombia for recorded music reached 71 percent, with damage to U.S. industry estimated at about $52 million, while motion picture piracy represented 75 percent of the market, valued at a loss of an estimated $40 million. Piracy in both business software and book publishing continued to grow in 2004. Although the Colombian police have conducted raids, the judicial process is slow and cumbersome and fails to incarcerate copyright infringers.

The Motion Picture Association of America (MPAA), in conjunction with local attorneys, took 17 criminal actions against alleged television pirates in 2000, 16 such cases in 2001, and eight in 2002. However, MPAA's anti-piracy strategy relied on enforcement by the Colombian National Television Commission (CNTV), which largely failed in its efforts. Given the CNTV's poor results in suppressing piracy, MPAA has ceased initiating action against television broadcast or home video piracy. Colombia's Television Broadcast Law increased legal protection for all copyrighted programming by regulating satellite dishes, and enforcement has begun through a licensing process. However, an MPAA estimate suggests that 75 percent of the motion picture market in Colombia is pirated, while annual losses due to audiovisual piracy remained at $40 million in 2004. However, in 2004 CNTV launched an aggressive anti-piracy campaign and signed its first cooperation agreement with FOX Sports to combat piracy in the television market.

SERVICES BARRIERS

Liberalization has progressed furthest in telecommunications, accounting/auditing, energy and tourism. It has occurred to a lesser extent in legal services, insurance, distribution services, advertising and data processing. The provision of legal services is limited to law firms licensed under Colombian law. Foreign law firms can operate in Colombia only by forming a joint venture with a Colombian law firm and operating under the licenses of the Colombian lawyers in the firm.

Economic needs tests are required for foreign providers of professional services to operate temporarily in Colombia. Moreover, residency requirements restrict trans-border trade of certain professional services, such as accounting, bookkeeping, auditing, architecture, engineering, urban planning, and medical and dental services. For firms with more than ten employees, no more than ten percent of the general workforce and 20 percent of specialists may be foreign nationals.

A commercial presence is required to provide information processing services. Foreign educational institutions must have resident status in Colombia in order to receive operational authority from the Ministry of Education.

Trans-border transportation services are restricted in Colombia. Land cargo transportation must be provided by natural or legal persons with commercial presence in the country and licensed by the Ministry of Transportation. Colombia's law permits international cabotage companies to provide cabotage services "only when there is no national capacity to provide the service." Cargo reserve requirements in transport have been eliminated. However, the Ministry of Foreign Trade reserves the right to impose restrictions on foreign vessels of those nations that impose reserve requirements on Colombian vessels.

The U.S. Government is seeking through the FTA negotiations to secure greater access for U.S. providers of cross-border services to the Colombian market, including in the areas of financial and telecommunications services.

Financial Services

Colombia permits 100 percent foreign ownership of insurance firm subsidiaries. It does not, however, allow foreign insurance companies to establish local branch offices. Insurance companies must maintain a commercial presence in order to sell policies other than those for international travel or reinsurance. Colombia denies market access to foreign maritime insurers.

International banking institutions are required to maintain a commercial presence in Colombia through subsidiary offices and therefore must comply with the same capital and other requirements as local financial institutions. Colombian legislation has limits on the operation of banks and other financial institutions by separating fiduciary, investment banking, commercial loans, leasing and insurance services, from banking services. Current legislation (Law 389 of 1997) permits banking institutions to develop such activities in the same office/building, but the management of such services must be separate. Colombian legislation permits 100 percent foreign ownership in financial services, although the use of foreign personnel in the financial services sector remains limited to administrators, legal representatives and technicians. In April 2000, the Central Bank completely removed previous reserve requirements on foreign borrowing operations.

Further constraints on foreign financial institutions are found in Decree 2951, dated September 13, 2004. This decree requires foreign institutions to establish a commercial presence if their promotions target Colombian residents. A banking relationship with a Colombian resident and a financial entity abroad is permitted if the relationship was initiated by the Colombian resident without any publicity or promotion in Colombian territory. Industry experts estimate that the elimination of trade barriers in the financial services sector could create opportunities for U.S. firms to achieve $100 to $500 million in sales.

Basic Telecommunications Services

Significant barriers to entry include high license fees ($150 million for a long distance license), cross subsidies, commercial presence requirements and economic needs tests. The Telecommunications Regulatory Commission (CRT) may require an economic needs test for the approval of licenses in voice, facsimile, e-mail and other value-added services. The parameters that determine an "economic needs test", however, are not clearly established. In addition, lack of transparency in the interconnection and trunk access policies and guidelines applied by the regulatory authority further limit competition for the provision of local, long distance and mobile services.

In the WTO negotiations on basic telecommunications services, Colombia made fairly liberal commitments on most basic telecommunications services and adopted the WTO reference paper. However, Colombia specifically prohibited “callback” services, and excluded fixed and mobile satellite systems. Colombia also limited licenses or concessions for the supply of telecommunications services to enterprises legally established in Colombia. Most other restrictions on foreign participation in telecommunications services have been lifted and Colombia currently permits 100 percent foreign ownership of telecommunications providers.

In 2003, Colombia opened the mobile telecommunications market to Personal Communications Services (PCS) competition. The government issued a PCS license to new competitor Colombia Movil, effectively ending Colombia’s mobile telecommunications duopoly and opening the door for competition (Telefonica and Comcel share approximately 80 percent of the mobile market). Colombia Movil received a 10-year concession to develop the market and compete against the current cellular providers. The municipality-owned telephone companies, ETB (Empresa de Telecomunicaciones de Bogota) and EPM (Empresas Publicas de Medellin), own Colombia Movil.

Audiovisual and Communication Services

As part of the de-monopolization of Colombia’s government-owned television network, Colombia passed the Television Broadcast Law, Law 182/95, effective January 1995, which increased protection for all copyrighted programming by regulating satellite dishes and permitting private television broadcasters to compete with the government-owned broadcaster. The law increased restrictions on foreign content in broadcasting and imposed a burdensome system of sub-quotas for different hours of the day. The law requires broadcasters to transmit 70 percent nationally produced programming during prime time, 7:00 p.m. to 10:30 p.m., and 50 percent nationally produced programming from 10:00 a.m. to 7:00 p.m. and between 10:30 p.m. and midnight. Regional and local stations must also transmit 50 percent of nationally produced programming. According to Law 680, national production is defined as production that is made in all stages by Colombian artists and technicians, with the participation of national actors in starring and supporting roles while foreign actors’ participation is allowed as long as it does not exceed 10 percent of the starring roles. Retransmissions of local productions are considered to fulfill only part of the national content requirement.

Television, radio broadcasting and movie production and reproduction are subject to certain limitations. According to Law 680 and Law 80, ownership by foreign operators is limited to 40 percent for broadcast TV and 25 percent for radio broadcast. Law 29 requires Colombian nationals to be directors and managers of newspapers concerned with domestic politics. All motion picture exhibitions are charged a tax to finance the national Cinematographic Development Fund. Seventy percent of the resources from the Cinematographic Development Fund must be used to promote national film productions.

INVESTMENT BARRIERS

Colombian law requires that foreign investments be accorded national treatment. One hundred percent foreign ownership is permitted in most sectors of the Colombian economy; exceptions include activities related to national security and the disposal of hazardous waste. Investment screening has been largely eliminated, and the registration mechanisms that still exist are generally mere formalities and non-discriminatory. In the telecommunications, financial services, oil and mining sectors, for example, prospective foreign investors must comply with certain registration procedures, but there are no restrictions on the amount of foreign capital that may be invested in these sectors.

All foreign investment must be registered with the Central Bank’s foreign exchange office within three months in order to ensure the right to repatriate profits and remittances. All foreign investors, like domestic investors, must obtain a license from the Superintendent of Companies and register with the local chamber of commerce.

To promote the discovery and exploitation of new oil reserves, the government changed royalties from a flat 20 percent to a sliding scale, from 8 percent to 25 percent, depending on the size of the field. Colombia also implemented in June 2003 a new hydrocarbon policy, Law 1760, designed to attract foreign oil companies to Colombia. The new policy eliminated Ecopetrol's mandatory share in joint ventures, allowed private companies 100 percent control of exploration and production projects, and restructured Ecopetrol by creating the National Hydrocarbon Agency (ANH) in mid-2003. Although Ecopetrol is still state-owned, it is now an operating company similar to any other hydrocarbon company, while the ANH regulates the hydrocarbon sector and issues exploration and production contracts. The government is also extending existing contracts on a case-by-case basis.

Colombian television broadcast laws (Law 182/95 and Law 375/96) impose several restrictions on foreign investment. For example, foreign investors must be actively engaged in television operations in their home country, and their investments must involve a transfer of technology or know how. The National Planning Department issued a new Foreign Investment Regime – Decree 2080 of October 18, 2000 – that increased the cap on foreign investment in television network and programming companies from 15 percent to 40 percent.

The U.S. Government is seeking through the FTA negotiations a range of protections with respect to the treatment of U.S. investors, as well as a guaranteed right for those investors to have recourse to international arbitration in the event of disputes with the Colombian government.

ELECTRONIC COMMERCE

Colombia’s electronic commerce Law 527 of August 1999 provides electronic documents and signatures the same legal recognition as paper documents and provides a framework for their use. Law 527 allows for, and regulates, the issuance of digital certificates and grants enforcement and oversight responsibilities to the Superintendent of Industry and Commerce. Decree 1747 of September 2000, regulates Law 527 with regard to certificates and digital signatures, and establishes minimum capital and other requirements for agencies that have the authority to certify electronic documents and digital signatures. The Superintendent of Industry and Commerce must approve such agencies. In May 2000, the Colombian and U.S. Governments signed a joint declaration on electronic commerce to increase transparency in the sector.

However, Colombian electronic commerce is still an immature market because of the lack of capital for start-ups and consumer concerns over the safety of electronic transactions. The use of electronic business applications for customer relationship management, supply chain management or enterprise resource management is not widespread. Only a few large retail chains have established electronic commerce platforms to complement their businesses. Growth of these Internet-based endeavors is hampered by the need to validate credit card purchases over the telephone with local banks.

The U.S. is seeking in the FTA negotiations to include rules prohibiting duties on and discrimination against digital products, such as computer programs, videos, images, and sound recordings, based on where they are made or the nationality of the firms or persons making them.

COSTA RICA

TRADE SUMMARY

The U.S goods trade balance with Costa Rica went from a trade surplus in 2003 ($49.3 million) to a trade deficit of $29.2 million in 2004. U.S. goods exports in 2004 were $3.3 billion, down 3.2 percent from the previous year. Corresponding U.S. imports from Costa Rica were $3.3 billion, down 0.9 percent. Costa Rica is currently the 33rd largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Costa Rica in 2003 was $1.8 billion, the same as in 2002. U.S. FDI in Costa Rica is concentrated largely in the manufacturing sector.

IMPORT POLICIES

Free Trade Agreement

The United States engaged in free trade agreement negotiations with five Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) in 2003. The United States concluded negotiations with El Salvador, Guatemala, Honduras, and Nicaragua in December 2003 and with Costa Rica in January 2004. In May 2004, the six countries signed the United States – Central America Free Trade Agreement. During 2004, the United States and the Central American countries engaged in negotiations with the Dominican Republic to integrate that country into the free trade agreement. On August 5, 2004, the seven countries signed the Dominican Republic – Central America – United States Free Trade Agreement (CAFTA-DR). El Salvador ratified the Agreement in December 2004 and Honduras ratified in March 2005. Legislative approval is pending in the United States and the other signatories to the Agreement.

The CAFTA-DR will remove barriers to trade and investment in the region and will strengthen regional economic integration. The CAFTA-DR will also require the Central American countries and the Dominican Republic to undertake needed reforms to confront many of the problems noted below in areas including: customs administration; protection of intellectual property rights; services, investment, and financial services market access and protection; government procurement; sanitary and phytosanitary (SPS) barriers; and other non-tariff barriers.

Tariffs

As a member of the Central American Common Market (CACM), Costa Rica agreed in 1995 to reduce its common external tariff to a maximum of 15 percent. However, some industrial goods, such as new and used automobiles, are subject to much higher tariffs. Once the CAFTA-DR goes into effect, about 80 percent of U.S. industrial and commercial goods will enter the region duty-free, with the remaining tariffs phased out over ten years. Nearly all textile and apparel goods that meet the Agreement's rules of origin will be duty-free and quota-free immediately, promoting new opportunities for U.S. and regional fiber, yarn, fabric and apparel manufacturing. (The Agreement's tariff treatment for textile and apparel goods may be made retroactive to January 1, 2004.)

Most tariffs on agricultural products range from one percent to 15 percent. However, selected agricultural commodities currently are protected by tariffs that significantly exceed the 15 percent CACM common external tariff ceiling. These commodities include dairy products (40 percent to 65 percent) and poultry products (150 percent). Under the CAFTA-DR, Costa Rica will eliminate its tariffs on virtually all agricultural products within fifteen years (17 years for chicken leg quarters and 20 years for rice and dairy products). For the most sensitive products, tariff-rate quotas will permit some immediate zero-duty access for specified quantities during the tariff phase-out period, which will expand over time. Costa Rica will liberalize trade in fresh potatoes and onions through expansion of a tariff-rate quota.

The Agreement also requires transparency and efficiency in administering customs procedures, including the CAFTA-DR rules of origin. Costa Rica committed to ensure procedural certainty and fairness and all parties agreed to share information to combat illegal transshipment of goods.

Non-Tariff Measures

Costa Rica levies a sales tax of 13 percent on most goods and services, whether locally produced or imported. Costa Rica also applies a consumption tax (the level of which varies depending on the good) to many locally-produced goods and to about half of all imported goods. Among the highest taxed items are arms and ammunition (75 percent), costume jewelry (50 percent), fireworks (50 percent), new and used vehicles (variable), and wine and beer (40 percent). A bill currently in the Costa Rican Congress contemplates the enactment of a value-added tax including a rate of up to 79 percent on used autos.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The establishment of an electronic "one-stop" import and export window, and other recent improvements, have significantly reduced the time required for customs processing in Costa Rica. Nonetheless, procedures remain complex and bureaucratic. Sanitary and phytosanitary (SPS) requirements can often be cumbersome and lengthy. In addition, the Ministry of Agriculture and Livestock (MAG) enforces SPS measures that appear to be inconsistent with international standards and not based on science (e.g., zero tolerance for salmonella on raw meat and poultry products). Delayed entry of products into the country has resulted in lost earnings for U.S. exporters. In some cases, shipments have been destroyed.

Currently, all foods, pharmaceuticals, agricultural goods, and chemicals and cosmetics for human and animal consumption, locally produced or imported, must be tested and registered by the Ministry of Health before they can be sold. However, as implemented, this system appears to place greater burdens on imported than domestically produced goods. For example, a system of standards exists for local products, but lack of adequate laboratory testing equipment and funds prevents effective analysis on local products. In addition, Costa Rica requires that all imported products be certified safe and allowed for sale in the country of origin in order to be registered. Food traders express concern regarding the length of time it takes to register a product under this process, which can be months. Costa Rica requires extensive documentation to be notarized by the Costa Rican consulate in the country of origin for the importation of distilled spirits. These import licensing requirements are burdensome and costly to U.S. exporters. However, the five Central American countries, including Costa Rica, are in the process of developing common standards for several products, including distilled spirits, which should facilitate trade.

Effective December 24, 2003, Costa Rica temporarily banned imports of U.S. beef due to the single case of Bovine Spongiform Encephalopathy (BSE) in the United States. In May 2004, MAG indicated that imports of boneless beef from animals of less than 30 months of age could be imported; however, Costa Rica's inspection and certification requirements have prevented the resumption of imports. The United States is working to eliminate these plant by plant inspection requirements.

In May 2003, Costa Rica issued a decree allowing for the certification of an inspection system to replace a regulation that required poultry export plants to be inspected and approved by the Costa Rican Government. Amendments to Costa Rica's Law on Animal Health, which would provide statutory authority for Costa Rica to undertake an equivalency determination, are stalled in the Costa Rican Congress.

When the United States and Central America launched the free trade agreement negotiations, they initiated an active working group dialogue on SPS barriers to agricultural trade that met in parallel with the negotiations to facilitate market access. The objective was to leverage the impetus of active trade negotiations to seek difficult changes to the Central American countries' SPS regimes. Through the work of this group, Costa Rica has committed to resolve specific measures restricting U.S. exports to Costa Rica. In particular, for meat, dairy and poultry, Costa Rica agreed to undertake an equivalency determination for all plants inspected under the U.S. food safety and inspection system.

GOVERNMENT PROCUREMENT

Costa Rica is not a party to the WTO Agreement on Government Procurement. In recent years, a growing number of U.S. exporters and investors have reported unsatisfactory experiences when responding to Costa Rican government tenders. For example, the Government of Costa Rica (through the Comptroller General) and large state-owned enterprises have occasionally annulled and re-bid tenders after the financial analysis was completed and awards granted. The Government of Costa Rica has also substantially modified tender specifications midway through the procurement process. The bidders in these cases were forced to bear the costs associated with these changes.

The CAFTA-DR requires fair and transparent procurement procedures, including advance notice of purchases and timely and effective bid review procedures. Under the CAFTA-DR, U.S. suppliers will be permitted to bid on procurements covered by the Agreement for most Costa Rican government entities, including key ministries and state-owned enterprises on the same basis as Costa Rican suppliers. The anti-corruption provisions in the Agreement require each government to ensure that bribery in trade-related matters, including in government procurement, is treated as a criminal offense, or is subject to comparable penalties, under its law.

EXPORT SUBSIDIES

Tax holidays are available for investors in free trade zones, unless tax credits are available in an investor's home country for taxes paid in Costa Rica. Under the CAFTA-DR, Costa Rica may not adopt new duty waivers or expand existing duty waivers conditioned on the fulfillment of a performance requirement (e.g., the exportation of a given level or percentage of goods). Costa Rica may maintain existing duty waiver measures through 2009 provided such measures are consistent with its WTO obligations.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The United States continues to have concerns over Costa Rica's inadequate enforcement of its intellectual property laws. Therefore, Costa Rica remained on the 2004 Special 301Watch List. While many elements of Costa Rican intellectual property laws appear to be consistent with TRIPS obligations, the country's criminal codes have certain weaknesses that limit effective deterrence of intellectual property crimes.

The most significant step the Costa Rican government has taken to improve intellectual property protection is to increase raids on companies. However, other initiatives, including the formation of an inter-governmental intellectual property rights commission and the training of judges and prosecutors on intellectual property laws, have not produced significant improvements in the prosecution of IPR crimes.

Costa Rica is currently considering meaningful changes to its existing IPR laws to address limitations and loopholes that currently prevent effective enforcement. For example, there is a draft bill in Congress to modify the Intellectual Property Enforcement Law by deleting the "insignificance principle." According to industry, this threshold currently provides a loophole that prevents prosecution of retail-level piracy. This draft bill also recommends that intellectual property violators serve up to five years in prison. However, several proposals to strengthen IPR laws have languished in the Legislative Assembly during 2004, and IPR reforms are not likely to be enacted before the CAFTA-DR is considered by the Assembly.

CAFTA-DR obligations would strengthen Costa Rica's IPR protection regime to conform with, and in many areas exceed, WTO norms. CAFTA-DR obligations would also provide stronger deterrence against piracy and counterfeiting by criminalizing end user piracy and requiring Costa

Rica to authorize the seizure, forfeiture, and destruction of counterfeit and pirated goods and the equipment used to produce them. The CAFTA-DR text also mandates both statutory and actual damages for copyright and trademark infringement, which would ensure that monetary damages can be awarded even when it is difficult to assign a monetary value to the violation.

Copyrights

Costa Rica's copyright law is generally adequate, but not uniformly enforced. Long delays in copyright enforcement cases continue to be a serious problem. The copyright regime was revised in 1994 to provide specific protection for computer software and in 1999 to protect integrated circuit designs. In addition, the Legislative Assembly ratified the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty at the end of 1999.

Though piracy of satellite television transmissions by the domestic cable television industry has been curtailed, U.S. industry continues to express concern that some apartment buildings and hotels, particularly in areas not served by major cable service providers, continue to engage in satellite signal piracy. Unauthorized sound recordings, videos, optical discs, and computer software are also widespread, although some progress has been made in reducing their presence in the market. Efforts in copyright protection are significantly hindered by the lack of adequate funding and personnel committed to IP enforcement. The CAFTA-DR enforcement provisions are designed to help reduce copyright piracy.

Patents

The Legislative Assembly ratified reforms required by the Paris Convention for the Protection of Industrial Property in 1995. The patent law extended the term of protection for a patent from 12 years to 20 years from the date of the filing of the application for all inventions.

However, problems remain, for pharmaceutical and agricultural chemical companies seeking to protect undisclosed data submitted for regulatory approval, from unfair commercial use by unauthorized third parties.

Costa Rica has committed to protect such test data under the CAFTA-DR. This data will be protected against unfair commercial use for a period of 5 years for pharmaceuticals and 10 years for agricultural chemicals. In addition, there is no effective means of providing protection for plant varieties in Costa Rica’s current law. The CAFTA-DR obligations require that Costa Rica accede to the UPOV Convention (International Union for the Protection of New Varieties of Plants, 1991) by June 1, 2007.

Trademarks

Counterfeiting of well-known trademarks occurs frequently in Costa Rica. Legal recourse against these practices is available in Costa Rica, but may require protracted and costly litigation.

Accordingly, Costa Rican authorities have recently intensified efforts to raid businesses and confiscate property, especially clothing, which is infringing registered trademarks.

SERVICES BARRIERS

Costa Rica's insurance, telecommunications, electricity distribution, petroleum distribution, potable water, sewage, and railroad transportation industries are state monopolies. In addition, there are restrictions on the participation of foreign companies in some private sector activities, such as customs handling, medical services, prison operation, and other professions requiring Costa Rican registration and long-term residency of the persons providing the services. Under the CAFTA-DR, Costa Rica will accord substantial market access across their entire services regime, subject to very few exceptions.

For example, liberalization in insurance will be achieved through a phased-in approach with an initial opening at entry into force, an opening of the vast majority of the market by 2008, and a total opening by 2011. In addition, Costa Rica made specific commitments to gradually open its telecommunications market in three key areas – private network services and Internet services starting in 2006, and wireless services starting in 2007 – and committed to establishing a regulatory framework to help foster effective market access. Under the CAFTA-DR, Costa Rica agreed to enact a new legal framework to modernize telecommunications provider ICE.

Also, Costa Rica has ratified its commitments under the 1997 WTO Financial Services Agreement and accepted the Fifth Protocol of the GATS. Under this agreement, Costa Rica committed to allow foreign financial service providers to establish 100 percent-owned bank subsidiaries in Costa Rica to provide lending and deposit-taking services, leasing services, credit card services, and financial information services. Costa Rica made no commitments in the WTO for the provision of securities trading, underwriting services, or any type of insurance services. However, the CAFTA-DR will provide for openings in all these areas (insurance openings to be phased in as noted above).

Since 1995, private commercial banks have been permitted to offer checking accounts and savings deposits of less than 30 days and, since 1996, to access the Central Bank's discount window. However, private commercial banks are required to open branches in rural areas of the country or to deposit with the Central Bank 17 percent of their checking account deposits for state-owned commercial banks that have rural branches in order to qualify for the benefits of the law. The CAFTA-DR will ensure that foreign banks are treated under the same rules as domestic private banks.

Costa Rican regulations restrict the ability of certain professions to practice on a permanent basis in Costa Rica. For example, medical practitioners, lawyers, certified public accountants, engineers, architects, teachers, and other professionals must be members of an officially recognized association (colegio) which sets residency, examination, and apprenticeship requirements. However, under the CAFTA-DR, Costa Rica agreed to allow the provision of certain professional services on a reciprocal basis and also agreed to provide for temporary licensing of professional services.

INVESTMENT BARRIERS

Several U.S. investors have recently noted serious difficulties executing contracts made with the Costa Rican government, bringing into question the sanctity of contracts made with the Costa Rican government. For example, a U.S. company has expressed concern that the Government of Costa Rica failed to honor the company's petroleum exploration concession rights in Costa Rica and has not been willing to negotiate a settlement of the company's claims. Another U.S. company, operating under a Costa Rican joint venture, has suffered financial losses, as it has been denied the ability to fully exercise its concession rights to finance operations and capital improvements at Costa Rica's international airport while it works to negotiate a resolution with the Costa Rican government.

In addition, the slow pace of Costa Rica's legal system (a commercial dispute within the Costa Rican legal system can take an average of 10 years to be resolved) has been cited as an investment barrier by many U.S. investors. Another concern to existing and potential U.S. investors is the frequent use of "recursos de amparo" before the Costa Rican Constitutional Court, which are challenges to review the possible illegality of acts by the authorities or to review the constitutionality of legislation and regulations. Although these measures are generally seen as pro-investor, such challenges have been used at times to slow procedures and hinder the quick resolution of disputes.

Costa Rica's constitution and the expropriation law make clear that expropriations are to occur only after full advance payment is made. The law applies to Costa Ricans and foreigners alike.

While electricity generation and distribution remain a state monopoly, an electricity co-generation law enacted in 1996 allowed some private-sector participation (limited to 15 percent of the total market) in the production of electricity, but not in its transmission. This law has since been modified to permit the private construction and operation of plants under build-operate-transfer (BOT) and build-lease-transfer (BLT) mechanisms, but the operator must have at least 35 percent Costa Rican equity. Legislative proposals to open the electricity and telecommunications sectors to private investment and competition were abandoned in 2000 in the wake of large-scale demonstrations against reform and a Constitutional Court ruling against specific legislation under discussion. Existing private power producers have had their long-term, fixed-rate contracts challenged by certain Costa Rican governmental organizations, but these contracts have been honored.

Under the CAFTA-DR, all forms of investment will be protected, including enterprises, debt, concessions, contracts and intellectual property. U.S. investors will enjoy in almost all circumstances the right to establish, acquire and operate investments in Costa Rica on an equal footing with local investors. Among the rights afforded to U.S. investors are due process protections and the right to receive a fair market value for property in the event of an expropriation. Investor rights will be backed by an effective, impartial procedure for dispute settlement that is fully transparent. Submissions to dispute panels and panel hearings will be open to the public, and interested parties will have the opportunity to submit their views.

OTHER BARRIERS

The law regulating commercial representatives of foreign firms (Law No. 6209) grants local companies exclusive representation, without a signed agreement, for an indefinite period of time. In most cases, foreign companies must pay indemnity compensation in order to terminate an undesirable relationship with the local company.

Under CAFTA-DR, Costa Rica has committed to change its “dealer protection” regime. Under its existing regime, U.S. firms may be tied to exclusive or inefficient distributor arrangements. Costa Rica committed to establish a new legal regime that will give U.S. firms and their Costa Rican partners more freedom to contract the terms of their commercial relations and that will encourage the use of arbitration to resolve disputes between parties to dealer contracts.

COTE D'IVOIRE

TRADE SUMMARY

The U.S. trade deficit with Cote d'Ivoire was $597 million in 2004, an increase of $210 million from $387 million in 2003. U.S. goods exports in 2004 were $118 million, up 15 percent from the previous year. Corresponding U.S. imports from Cote d'Ivoire were $715 million, up 46 percent. Cote d'Ivoire is currently the 119th largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Cote d'Ivoire in 2003 was $237 million, up from $194 million in 2002. Cote d'Ivoire's international trade patterns – especially those involving trade in the West African region – have been significantly affected by the political instability and civil unrest that have gripped the country in the last few years.

IMPORT POLICIES

Cote d'Ivoire is a member of the WTO, the West African Economic and Monetary Union (known by its French acronym, UEMOA), and the Economic Community of West African States (ECOWAS). In January 2000, Cote d'Ivoire eliminated tariffs on imports from the eight member countries of UEMOA when UEMOA's Common External Tariff entered into effect. Imports from all other countries are subject to tariffs based on the Common External Tariff Schedule of five percent for raw materials and inputs for local manufacture, 10 percent for semi-finished goods, and 20 percent for finished products. In 2004, UEMOA suspended its practice of temporary duty-free status for imported goods destined for another country in the zone. This change means that goods entering UEMOA from non-member countries may no longer transit a UEMOA country duty-free en route to their final destination. Duties are now assessed at the first port of entry.

A one percent statistical fee is levied on the CIF (cost, insurance, and freight) value of imports except those destined for re-export, transit, or donations for humanitarian purposes under international agreements. Another tax on imports into Cote d'Ivoire is an ECOWAS community levy (solidarity tax), assessed at the rate of one percent of the CIF value of imported goods. There are special taxes on fish (20 percent), rice (between 5 percent and 10 percent based on category), alcohol, tobacco, cigarettes, certain textile products, and petroleum products. These special taxes are designed to protect national industries. The Customs office collects a value-added tax (VAT) of 18 percent on all imports, reduced from 20 percent in 2003. This tax computation is calculated on the CIF value added to the duty and the statistical fee.

Cote d'Ivoire reportedly continues to apply minimum import prices (MIPs) to imports of certain products, though the WTO waiver it once had allowing it to apply MIPs for some products has long since expired.

There are no quotas on merchandise imports, although the following items are subject to import prohibitions, restrictions, or prior authorization: petroleum products, animal products, live plants, seeds, arms and munitions, plastic bags, distilling equipment, pornography, saccharin, narcotics, explosives, illicit drugs, and toxic waste.

STANDARDS, TESTING, LABELING AND CERTIFICATION

All items imported into Cote d'Ivoire must have a certificate of compliance to clear customs. Two European companies are contracted to carry out all qualitative and quantitative verifications of goods imported into Cote d'Ivoire equal to or higher than CFA1.5 million (approximately $3,000). All merchandise packaging must be clearly labeled as to its origin. Manufactured food products must be labeled in French and have an expiration date. Standards generally follow French or European norms.

GOVERNMENT PROCUREMENT

The government of Cote d’Ivoire regularly and periodically issues notices of procurement tenders in the local press, in the form of documentation sent to the U.S. Embassy, or sometimes published in international magazines and newspapers. On occasion, there is a charge for the bidding documents. The implementing agency is usually the ministry making the request or the ministry under whose tutelage the office functions. The Bureau National d’Etudes Techniques et de Developpement (BNETD), the government’s technical and investment planning agency and think tank, sometimes serves as an executing agency representing ministries for major projects to be financed by international institutions.

The government has created a centralized office of public bids in the Finance Ministry to help ensure compliance with international bidding practices. While theoretically the procurement process is open, some well-entrenched foreign companies, through their relations with government officials, may retain a preferred position in securing bid awards. Many firms continue to see corruption as an obstacle that affects procurement decisions. Cote d’Ivoire is not a signatory to the WTO Agreement on Government Procurement.

SERVICES BARRIERS

Banks and insurance companies are subject to licensing requirements, but there are no restrictions on foreign ownership or establishment of subsidiaries. Foreign participation is widespread in computer services, education, and training. Prior approval is required for foreign investment in the health sector, travel agencies, and law and accounting firms; majority foreign ownership of companies in these sectors is not permitted, though foreign companies currently operate in all these sectors in partnership with local firms. Foreigners must associate with licensed Ivoirian practitioners to obtain permission to work in these sectors. One U.S. bank currently has branches in Cote d’Ivoire.

INVESTMENT BARRIERS

Cote d'Ivoire requires majority Ivoirian ownership in some sectors. The government actively encourages foreign investment, but in recent years political instability has substantially undermined investor confidence. The negative effects of the 1999 coup d'etat, the ensuing 10-month military rule, and the upheavals surrounding the elections in October 2001 had not dissipated when another attempted coup and rebellion gripped the nation in September 2002. The political crisis of November 2004, during which businesses were destroyed and looted, has further dampened near-term investment prospects. Ongoing efforts at national reconciliation have made little progress. There has been no progress on privatization since 2002.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The Ivoirian Civil Code protects the acquisition and disposition of intellectual property rights. Legal protection for intellectual property may fall short of TRIPS standards. Cote d'Ivoire is a party to the Paris Convention for the Protection of Industrial Property, its 1958 revision, and the 1977 Bangui Agreement covering 16 Francophone African countries in the African Intellectual Property Organization (OAPI). Effective February 2002, changes were made to the Bangui Agreement in an effort to bring it into conformity with TRIPS. Under OAPI, rights registered in one member country are valid for other member states. Patents are valid for ten years, with the possibility of two five-year extensions. Trademarks are valid for ten years and are renewable indefinitely. Copyrights are valid for 50 years.

In 2001, Ivoirian experts drafted a new law in an effort to bring Cote d'Ivoire into conformity with TRIPS. The new law adds specific protection for computer programs, databases, and authors' rights with regard to rented films and videos. However, the National Assembly has not yet approved this legislation and there appears little likelihood that it will do so in the near future.

The government's Office of Industrial Property is charged with ensuring the protection of patents, trademarks, industrial designs, and commercial names. The office faces an array of challenges, including resource allocation, political will, and the distraction of the ongoing political crisis. As a result, enforcement of IPR is largely ineffective. Foreign companies, especially from East and South Asia, flood the Ivoirian market with all types of counterfeit goods. Government efforts to combat piracy are modest. The Ivoirian Office of Author's Rights (BURIDA), established in 1998, has established a new sticker system, effective January 2004, to protect phonograph, video, literary and artistic property rights in music and computer programs. BURIDA's operations remain hampered by a long-running dispute over policy and who should direct the agency, but the agency does help to promote IPR enforcement with lawyers and magistrates.

ELECTRONIC COMMERCE

Electronic commerce is in its very early stages in Cote d'Ivoire but is expected to grow over time. There are a number of cultural barriers to growth, including the custom of paying with cash and the absence of widespread issuance and use of credit cards. However, a few individuals and small businesses have begun experimenting with electronic commerce, and interest in the medium continues to gain ground.

OTHER BARRIERS

Corruption

Many U.S. companies view corruption as an obstacle to investment in Cote d'Ivoire. Corruption has the greatest impact on judicial proceedings, contract awards, customs, and tax issues. It is common for judges who are open to financial influence to distort the merits of a case. Corruption and the recent political crisis have affected the Ivoirian government's ability to attract and maintain foreign investment. Some U.S. investors have raised specific concerns about the rule of law and the government's ability to provide equal protection under the law.

In 1997, the government of Cote d'Ivoire authorized the creation of an arbitration court. Since then, however, the court has examined only 40 cases. In July 2004, the governing body was strengthened with the added participation of local Chambers of Commerce, and the rules governing enforcement of arbitral awards were modified to allow for a quicker enforcement of awards. The business community has welcomed the 2004 revisions and hopes that the Arbitration Board can act as an alternative vehicle for businesses in dispute. In addition to its local arbitration board, Cote d'Ivoire is a member of the International Center for the Settlement of Investment Disputes.

DOMINICAN REPUBLIC

TRADE SUMMARY

The U.S. trade deficit with the Dominican Republic was $185 million in 2004, a decrease of $65 million from $250 million in 2003. U.S. goods exports in 2004 were $4.3 billion, up 3.3 percent from the previous year. Corresponding U.S. imports from the Dominican Republic were $4.5 billion, up 1.6 percent. The Dominican Republic is currently the 28th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in the Dominican Republic in 2003 was $860 million, down from $983 million in 2002. U.S. FDI in the Dominican Republic is concentrated largely in the manufacturing and wholesale sectors.

Much of the U.S. investment in the manufacturing sector is located in export processing zones, called Free Trade Zones (FTZs), which specialize in producing apparel, footwear, electronic products and medical goods using U.S. components and materials.

IMPORT POLICIES

Free Trade Agreement

The United States engaged in free trade agreement negotiations with five Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) in 2003. The United States concluded negotiations with El Salvador, Guatemala, Honduras, and Nicaragua in December 2003 and with Costa Rica in January 2004. In May 2004, the six countries signed the United States – Central America Free Trade Agreement. During 2004, the United States and the Central American countries engaged in negotiations with the Dominican Republic to integrate that country into the free trade agreement. On August 5, 2004, the seven countries signed the Dominican Republic – Central America – United States Free Trade Agreement (CAFTA-DR). El Salvador ratified the Agreement in December 2004 and Honduras ratified in March 2005. Legislative approval is pending in the United States and the other signatories to the Agreement.

The Dominican Republic and the Central American countries together already constitute the second largest U.S. export market in Latin America. The CAFTA-DR will remove barriers to trade with and investment in the region and will further regional economic integration.

The CAFTA-DR will also require the Central American countries and the Dominican Republic to undertake needed reforms to confront many of the problems noted below in areas including: customs administration; protection of intellectual property rights; services, investment, and financial services market access and protection; government procurement; sanitary and phytosanitary (SPS) barriers; and other non-tariff barriers.

Tariffs

Tariffs on imported agricultural and non-agricultural goods range from zero to 20 percent. However, tariffs on some agriculture items have increased in recent years to between 25 and 40 percent.

As a result of a progressive deterioration in the Dominican Republic's economy and the Government's efforts to meet fiscal targets, the Dominican Republic implemented an exchange surcharge (*Recargo Cambiario*), in the later part of 2003, which currently imposes a 13 percent duty on all imports into the Dominican Republic. U.S. industry has expressed concerns with this surcharge. Several countries, including others in the region, have also expressed their objections. In November 2004, in response to a complaint filed by Honduras, a WTO panel found the exchange surcharge to be inconsistent with the Dominican Republic's WTO obligations. The Dominican Republic (as well as Honduras) appealed certain panel findings to the WTO Appellate Body. A decision on the matter is expected in April 2005. In addition, a luxury tax (*Impuesto Selectivo al Consumo*), ranging from 15 percent to 60 percent, applies to non-essential goods. This consumption tax for luxury items applies to locally manufactured and imported "non-essential" goods, including perfume, alcoholic beverages, motor vehicles and tobacco.

Under the CAFTA-DR, tariffs on approximately 80 percent of U.S. industrial and commercial exports to the region would be eliminated immediately. Remaining tariffs on industrial goods will be eliminated within ten years. Nearly all textile and apparel goods that meet the Agreement's rules of origin will be duty-free and quota-free immediately, promoting new opportunities for U.S. and regional fiber, yarn, fabric and apparel manufacturing. (The Agreement's tariff treatment for textile and apparel goods may be made retroactive to January 1, 2004.)

Most tariffs on agricultural goods will be eliminated within 15 years and all tariffs will eventually be eliminated. The phase-out period for rice, chicken leg quarters, and dairy products is 20 years. For the most sensitive products, tariff rate quotas will permit some immediate zero-duty access for specified quantities during the tariff phase-out period, which will expand over time as the out-of-quota duties are eliminated.

Non-Tariff Measures

Entering goods into the Dominican Republic can be a slow and arduous process. Customs Department interpretations often provoke complaints by businesspersons, and arbitrary clearance procedures sometimes delay the importation of merchandise for lengthy periods. Furthermore, the Dominican Republic Government requires importers to obtain from a Dominican Republic Consulate in the United States a consular invoice and "legalization" of documents, with attendant fees and delays. Importers can pay a fine (approximately $400) if they lack these consular documents and some choose to do so rather than deal with Dominican Republic consulates in the United States. The use of "negotiated fee" practices to gain faster customs clearance continues to put some U.S. firms at a competitive disadvantage in the Dominican market. Under the CAFTA-DR, the Dominican Republic has committed to (i) provide greater transparency and procedural certainty in administering customs procedures; (ii) share information with other Parties to combat illegal transshipment of goods; and (iii) eliminate the consular invoice requirement.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Sanitary permits have been used in the Dominican Republic as import licenses to control import levels of selected commodities and products. The inability to apply for and receive sanitary permits in a timely manner in the Dominican Republic for shipments of U.S. meat and dairy products has been a serious problem for U.S. exporters and importers in the Dominican Republic. This situation has improved significantly in recent months. While sanitary permits remain mandatory for the importation of many products, they are no longer being used to the same degree to control imports.

GOVERNMENT PROCUREMENT

The CAFTA-DR requires fair and transparent procurement procedures, including advance notice of purchases and timely and effective bid review procedures. Under the CAFTA-DR, U.S. suppliers will be permitted to bid on procurements covered by the Agreement for most Dominican Republic government entities, including key ministries and state-owned enterprises on the same basis as Dominican Republic suppliers. The anti-corruption provisions in the Agreement require each government to ensure that bribery in trade-related matters, including in government procurement, is treated as a criminal offense, or is subject to comparable penalties, under its law.

EXPORT SUBSIDIES

The Dominican Republic does not have export promotion schemes other than the exemptions given to firms in the free trade zones. Under the CAFTA-DR, the Dominican Republic may not adopt new duty waivers or expand existing duty waivers conditioned on the fulfillment of a performance requirement (e.g., the exportation of a given level or percentage of goods). The Dominican Republic may maintain existing duty waiver measures through 2009 provided such measures are consistent with its WTO obligations.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Although the Dominican Republic has strong legislation to protect copyrights and has improved the regulatory framework for patent and trademark protection, U.S. industry representatives continue to cite lack of IPR enforcement as a major concern. As a result, the Dominican Republic remained on the Special 301 Watch List for 2004. The government has taken some steps to prosecute violators, but there is insufficient training or resources for enforcement, and the judicial process moves very slowly. While the Dominican Republic has ratified the World Intellectual Property Organization (WIPO) Copyright Treaty and the WIPO Performances and Phonograms Treaty, it has not deposited instruments of ratification for these two treaties with WIPO as of December 31, 2004.

CAFTA-DR obligations would strengthen the Dominican IPR protection regime to conform with, and in many areas exceed, WTO norms. CAFTA-DR obligations would also provide stronger deterrence against piracy and counterfeiting by criminalizing end user piracy and requiring the Dominican Republic to authorize the seizure, forfeiture, and destruction of counterfeit and pirated goods and the equipment used to produce them. The CAFTA-DR text also mandates both statutory and actual damages for copyright and trademark infringement which would ensure that monetary damages can be awarded even when it is difficult to assign a monetary value to the violation.

Patents and Trademarks

The United States government has continued to urge the Dominican Republic to bring the Industrial Property Law fully in line with its TRIPS Agreement obligations. Existing law and regulations have not yet been applied in legal proceedings, so the effectiveness of those measures has not been tested. The CAFTA-DR obligations would require that test data submitted to the Dominican government for the purpose of product approval be protected against unfair commercial use for a period of 5 years for pharmaceuticals and 10 years for agricultural chemicals.

Copyrights

Despite a strong copyright law passed in 2000, the appointment of a specialized IPR prosecutor with nationwide jurisdiction in 2003, and some improvement in enforcement activity, piracy of copyrighted materials is common. Audio recordings and software are being copied without authorization despite the government's efforts to seize and destroy such pirated goods. In addition, the U.S. Government continues to receive reports of television and cable operators re-broadcasting signals without compensating either the original broadcaster or the originator of the recording. U.S. industry representatives point to extended delays in the judicial process when cases are submitted for prosecution. While investigations and raids against broadcasting stations involved with the unauthorized transmission of copyrighted programming have been initiated, several high-profile cases against large cable companies were postponed repeatedly throughout 2004. The Dominican Republic court system remains a significant hurdle in providing effective, deterrent enforcement, due in part to antiquated criminal procedural rules.

The Dominican government has had some success in reducing both video and television broadcast piracy, including cooperation with administrative and criminal agencies. Nonetheless, industry remains concerned that the lack of effective enforcement against television and video piracy in the Dominican Republic continues to be a serious problem. Under CAFTA-DR, the Dominican Republic assumed several specific obligations with respect to broadcast piracy and the United States will continue to work them to strengthen enforcement measures for broadcast piracy.

SERVICES BARRIERS

Over the last few years, the Dominican Republic has taken steps to reform and liberalize the financial services sector. In October 2002, the Dominican Republic passed a monetary and financial law that provides for national treatment of investors in most of the financial services sector. The law establishes a regulatory regime for monetary and financial institutions, and provides for participation of foreign investment in financial intermediary activities in the Dominican Republic.

The Dominican Republic has ratified the 1997 WTO Financial Services Agreement and its monetary and financial law appears to go beyond the commitments of the WTO agreement. The Dominican Republic has committed itself to allow foreign banks to establish branches or local companies with up to 100 percent foreign equity to supply deposit-taking, lending, and credit card services. Branches of foreign banks have a phase in period of six years from 2004 to establish sufficient locally held capital to meet the same requirements applied to domestic banks.

A foreign insurance company can establish a wholly owned subsidiary. Under the CAFTA-DR, U.S. financial service suppliers would have full rights to establish subsidiaries, joint ventures or branches for banks and insurance companies. Furthermore, the Dominican Republic will allow U.S.-based firms to supply insurance (including reinsurance; reinsurance brokerage; marine, aviation and transport (MAT) insurance; and other insurance services) on a cross-border basis.

INVESTMENT BARRIERS

Existing Dominican legislation does not contain effective procedures for settling disputes arising from the government's actions. Dominican expropriation standards are not consistent with international law standards and numerous U.S. investors have had disputes related to expropriated property. Subsequent to U.S.-Dominican Trade and Investment Council meetings in October 2002, the Dominican government set out to examine outstanding expropriation cases for possible resolution under a 1999 law. With the help of a USAID contractor, the Boston Institute for Developing Economies (BIDE), the Dominican government was able to identify and analyze 248 cases, which were resolved, either by paying claimants with bond issues under Law 104-00 or by dismissing the claim. In an ongoing dispute, a U.S. firm is appealing a verdict from a Dominican Republic court which is inconsistent with the findings of the international arbiter identified in the original contract.

In 1999, privatization of the state electric company left control of the distribution system and most generating capacity in private hands. Beginning in 2003 the electricity sector in the

Dominican Republic began to deteriorate markedly, in part due to the government's decision to subsidize much of the rising cost of electricity. This subsidy program has proven unsustainable. The continuing problems in the sector are due to distributors' inability to collect sufficient funds from consumers and the Dominican government, and to the pricing formula that distributors must use to convert dollar-indexed electricity rates into peso charges to their customers, which has been exacerbated by rises in petroleum prices as the exchange value of the peso fell sharply. The total amount of government debt owed to generators and distributors is approximately $600 million and continues to grow. The U.S. Government through USAID has funded consultant studies of and coordination among participants in the sector, in order to elaborate the elements of a plan intended to stabilize the sector through December 2005, although this plan does not call for the reduction of the outstanding total of debt. Electrical sector problems threaten economic competitiveness and create wide-spread dissatisfaction with the government and private sector participants.

The Dominican Republic implemented the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention) in August 2002. The New York Convention provides courts a mechanism to enforce international arbitral awards.

Under the CAFTA-DR, all forms of investment would be protected, including enterprises, debt, concessions, contracts and intellectual property. U.S. investors would enjoy, in almost all circumstances, the right to establish, acquire and operate investments in the Dominican Republic on an equal footing with local investors. Among the rights afforded to U.S. investors would be due process protections and the right to receive a fair market value for property in the event of an expropriation. As in our other FTAs, these rights apply with respect to acts or facts that take place after the entry into force of the CAFTA-DR. Investor rights would be backed by an effective, impartial procedure for dispute settlement that would be fully transparent. Submissions to dispute panels and panel hearings would be open to the public, and interested parties would have the opportunity to submit their views.

ELECTRONIC COMMERCE

Law 126-02 enacted in 2002 regulates electronic commerce, documents and digital signatures. However, shipping costs, a non-existent public postal system, difficulties with customs, and import duties are practical constraints to the development of electronic commerce in the form of online merchandising. Major private air parcel express services serve the capital and provide generally speedy service. Under the CAFTA-DR, the Dominican Republic would agree to provisions on electronic commerce that reflect the issue's importance in global trade and the importance of supplying services by electronic means as a key part of a vibrant electronic commerce environment. The Dominican Republic would also commit to non-discriminatory treatment of digital products and agree not to impose customs duties on such products and to cooperate in numerous policy areas related to e-commerce.

OTHER BARRIERS

U.S. companies continue to complain about a lack of transparency and corruption in many sectors. Lack of predictability in the judicial process, which can also be lengthy, also presents problems for U.S. companies seeking to resolve contract disputes. The CAFTA-DR will enhance transparency, predictability, and the rule of law in virtually all areas of trade and investment. Further, the anti-corruption provisions in the Agreement require each government to ensure that bribery in trade-related matters is treated as a criminal offense, or is subject to comparable penalties, under its law.

Dealer Protection

U.S. companies have also expressed concern that the Dominican Dealer Protection Law 173, which applies only to foreign suppliers, makes it extremely difficult to terminate contracts with local agents or distributors without paying exorbitant indemnities. Several U.S. companies have lost lawsuits brought under this law and have suffered significant financial penalties. This law has had a negative impact on market access and on consumer welfare and has been a serious obstacle to distribution in the Dominican Republic. Under the CAFTA-DR, the Dominican Republic has committed to change its "dealer protection" regime. Under its existing regime, U.S. firms may be tied to exclusive or inefficient distributor arrangements. The Dominican Republic committed to provide U.S. firms and their Dominican Republic partners more freedom to contract the terms of their commercial relations and to encourage the use of arbitration to resolve disputes between parties to dealer contracts.

ECUADOR

TRADE SUMMARY

The U.S. trade deficit with Ecuador was $2.6 billion in 2004, an increase of $1.3 billion from $1.3 billion in 2003. U.S. goods exports in 2004 were $1.7 billion, up 15.2 percent from the previous year. Corresponding U.S. imports from Ecuador were $4.3 billion, up 57.4 percent. Ecuador is currently the 50th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Ecuador in 2003 was $1.4 billion, up from $1.28 billion in 2002. U.S. FDI in Ecuador is concentrated largely in the mining sector.

FREE TRADE NEGOTIATIONS

In May 2004, the United States initiated free trade agreement (FTA) negotiations with three Andean nations -- Colombia, Peru and Ecuador. Bolivia is participating as an observer and is expected to become part of the agreement at a later stage. The U.S. Government will seek to address the issues described in this chapter within the context of these negotiations. The four Andean countries collectively represented a market of about $8.5 billion for U.S. exports in 2004, and were home to about $7.2 billion in U.S. foreign direct investment.

IMPORT POLICIES

Tariffs

When Ecuador joined the WTO in January 1996, it bound most of its tariff rates at 30 percent or less. Ecuador's average applied tariff rate is 13 percent. Ecuador applies a four-tiered structure with levels of five percent for most raw materials and capital goods, 10 percent or 15 percent for intermediate goods, and 20 percent for most consumer goods. A small number of products, including planting seeds, agricultural chemicals and veterinary products are duty-free.

As a member of the Andean Community (CAN), Ecuador grants and receives exemptions from tariffs (i.e., reduced *ad valorem* tariffs and no application of the Andean Price Band System) for products from the other CAN countries (Bolivia, Colombia, Peru and Venezuela). Currently, these countries have an Andean Free Trade Zone and apply Common External Tariffs (CET), as stated in CAN Decision 370. There is a proposal for a new CET with a three-tiered structure, with levels of 5, 10 and 20 percent tariffs. The proposed structure has not been approved by the CAN. The United States is seeking the elimination of Ecuador's duties on U.S. exports in the FTA negotiations, upon entry into force of the agreement where possible and over time for the most sensitive products.

Ecuador maintains the Andean Price Band System (APBS) on 153 agricultural products (13 “marker” and 140 “linked” products) imported from outside the CAN. The 13 “marker” products are wheat, rice, sugar, barley, white and yellow corn, soybean, soybean meal, African palm oil, soy oil, chicken meat, pork meat and powder milk. Under this system, the *ad valorem* CET is adjusted (increased or reduced) according to the relationship between international reference prices, established floor and ceiling prices and the importation price of the commodity. Upon accession to the WTO, Ecuador bound its *ad valorem* tariffs (including the additional levy from the APBS) for these commodities at between 31.5 and 85.5 percent.

As part of its WTO accession, Ecuador committed to phase out its price band system, starting in January 1996, with a total phase out by December 2001. No steps have been taken to comply with this commitment. The U.S. Government is seeking through the FTA negotiation to eliminate Ecuador’s barriers to our trade in agricultural products, while providing reasonable adjustment periods and safeguards for producers of import sensitive agricultural products.

Non-Tariff Measures

Ecuador has failed to eliminate several non-tariff barriers since its WTO accession. Importers must register with the Central Bank through approved banking institutions to obtain an import license. Ecuador requires prior authorization from various government agencies, e.g., the Ministry of Agriculture (MAG), for importation of most commodities, seeds, animals and plants. Also, the Ministry of Health must give its prior authorization (i.e., sanitary registration) before the importation of processed, canned and packed foods, food ingredients, beverages, cosmetics and pharmaceutical products. Another administrative hurdle agricultural importers must overcome is the MAG’s use of “Consultative Committees.” These committees, mainly composed of local producers, often advise the MAG against granting import permits to foreign suppliers. The MAG often requires that all local production be purchased at high prices before authorizing imports.

Ecuador also continues to maintain a preshipment inspection (PSI) regime. Preshipment inspection by an authorized inspection company (both before shipment and after specific export documentation has been completed at the intended destination) results in delays far exceeding the time saved in customs clearance. Customs authorities sometimes perform spot-checks, causing further delays. These practices generally add six to eight weeks to shipping times.

Ecuador maintains bans on the import of used motor vehicles, tires and clothing. Ecuador applies a 27 percent markup on imported distilled spirits for excise tax purposes. As excise taxes on imports are calculated on CIF value plus import duties, the effective rate is higher for imports than domestic products. Ecuador has not equalized the application of excise taxes between imported and domestic products.

In December 1999, the MAG, through the Ecuadorian Animal and Plant Health Inspection Service (SESA), issued a requirement that all importers must present a certificate stating that imported agricultural products (plants, animals, their products or byproducts) have not been produced using modern biotechnology. In November 2002, the President issued Executive Decree 3399 creating the National Commission for Biosafety as an office of the Ministry of Environment. It is responsible for biotechnology-related products and regulations issues. However, no rules have yet been enacted.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Over the last two years, INEN has imposed unreasonable and costly certification requirements on imports of refrigerators, freezers and gas ranges of U.S. origin. These requirements have not been published in advance and have impeded market access for U.S. manufacturers. None of these certification requirements were notified to WTO members for comment as required by the WTO Agreement on Technical Barriers to Trade. In fact, Ecuador has never notified the WTO of any new or proposed changes in its technical regulations or conformity assessment procedures.

SESA is responsible for administering Ecuador's sanitary and phytosanitary controls. According to Ecuadorian importers, bureaucratic procedures required to obtain clearance still appear to discriminate against foreign products. Ecuador is bound by the WTO Agreement on the Application of Sanitary and Phytosanitary (SPS) Measures, yet denials of SPS certification often appear to lack a scientific basis and to have been used in a discriminatory fashion to block the import of U.S. products that compete with Ecuadorian production. This occurs most often with poultry, turkey and pork meats, beef, dairy products and fresh fruit. The ability to import some products, such as rice, corn, soybeans and soybean meal depends entirely on the discretion of the MAG, which will often look to the Consultative Committees for advice. Ecuador has yet to fulfill its notification obligations under the WTO SPS Agreement.

SESA follows the CAN’s “Andean Sanitary Standards.” Some standards applicable for third countries are different from those applied to CAN members. For example, there can be differences in the requirements for CAN and third countries for the importation of live animals, animal products, and plants and plant by-products. SESA also requires certifications for each product stating that the product is safe for human consumption or, in the case of live animals, that the animal is healthy and that the country of origin or the area of production is free from certain exotic plant or animal disease. Industry sources assert that this process has been used unreasonably by SESA to prevent entry of animal products -- especially poultry -- that compete with local producers.

Sanitary registrations are required for imported as well as domestic processed food, cosmetics, pesticides, pharmaceuticals, and syringes, as well as some other consumer goods. However, in a side agreement to its WTO Accession Agreement, Ecuador committed to accept the U.S. Certificate of Free Sale authorized by the U.S. Food and Drug Administration, instead of the Government of Ecuador’s Sanitary Registration. In August 2000, the Government of Ecuador passed a law (Ley de Promocion Social y Participacion Ciudadana, Segunda Parte – also known as Troley II), followed by regulations issued in June 2001, to reform the issuance of sanitary permits for food products. This is a step towards modernizing the issuance of sanitary registrations with new regulations that allow the acceptance of free sale certificates, require that the government issue sanitary permits within 30 days of the receipt of the request, and reduce the number of documents required to obtain a permit. However, it does not appear that these regulations are being applied consistently. U.S. firms report that the Izquieta Perez National Hygiene Institute (INHIP - the agency responsible for registering imported processed food products) office in Guayaquil has refused to accept U.S. Certificates of Free Sale and continues to apply the old regime for sanitary permits. In addition, non-transparent bureaucratic procedures and inefficiency have delayed issuance beyond 30 days and in some cases have reportedly blocked the entry of some imported products from the United States.

U.S. companies have expressed concerns regarding regulations issued by Ecuador's public health ministry requiring foreign food manufacturers to disclose confidential information such as formulas of imported food and pharmaceutical products. This requirement appears to go beyond the requirements of the Codex Alimentarius Commission on Internationals Standards and Labeling.

GOVERNMENT PROCUREMENT

Government procurement is regulated by the 1990 public contracting law. Foreign bidders must be legally represented in Ecuador. The law does not discriminate against U.S. or foreign suppliers. Bidding for government contracts can be cumbersome and insufficiently transparent. This can lead to multiple cancellations of bid solicitations, unnecessarily adding to the costs of submitting bids, and opens the process to possible manipulation by contracting authorities. Ecuador is not a signatory to the WTO Agreement on Government Procurement. In the FTA negotiations the U.S. Government is seeking opportunities for U.S. companies to bid on Ecuadorian government procurement.

EXPORT SUBSIDIES

Ecuador has created a semi-independent agency, the Corporation for the Promotion of Exports and Investments (Corpei), to promote Ecuadorian exports. Using a European Union loan, Corpei offers matching grants to exporters to help fund certain expenses, including international promotional events and export certifications.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

In 1998, Ecuador enacted a comprehensive law that significantly improved the legal basis for protecting intellectual property, including patents, trademarks and copyrights. The intellectual property law provides greater protection for intellectual property; however, it is deficient in a number of areas and the law is not being adequately enforced.

Ecuador's current intellectual property regime is provided for under its IPR law and Andean Pact

Decisions 486, 345 and 351. Ecuador is a member of the World Intellectual Property Organization (WIPO) and is a member of the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty. Furthermore, Ecuador has ratified the Berne Convention for the Protection of Literary and Artistic Works, the Geneva Phonograms Convention, the Paris Convention for the Protection of Industrial Property and the WIPO Patent Cooperation Treaty.

The United States is currently negotiating IPR provisions under the ongoing Andean FTA negotiations to improve protection and strengthen enforcement of IPR. The U.S. Government is seeking to address specific U.S. industry concerns related to the protection and enforcement of copyrights and related rights, patents, proprietary data for pharmaceutical and agricultural products, trademarks and geographical indications.

Copyrights

The Government of Ecuador, through the National Copyright Office's Strategic Plan against Piracy, has committed to take action to reduce the levels of copyright piracy, including implementation and enforcement of its 1998 Copyright Law. Enforcement of copyrights remains a significant problem, especially concerning sound recordings, computer software and motion pictures. The Government of Ecuador has taken no action to clarify Article 78 of the 1999 Law on Higher Education, which could be interpreted to permit software copyright violations by educational institutions.

Patents and Trademarks

Ecuador's 1998 IPR law provided an improved legal basis for protecting patents, trademarks, and trade secrets. However, concerns remain regarding several provisions, including a working requirement for patents, compulsory licensing and the lack of enforcement in the protection of test data. U.S. companies also are concerned that the Ecuadorian government does not provide patent protection to second uses, which would allow a company with a patented compound for one use to subsequently patent a second use of that compound.

Government of Ecuador health authorities continue to approve the commercialization of new drugs which are the bioequivalents of already approved drugs, thereby denying the originator companies the exclusive use of their data. In effect, the Government of Ecuador is allowing the test data of registered drugs from originator companies to be used by others seeking approval for their own pirate version of the same product.

Enforcement

There continues to be an active local trade in pirated audio and video recordings, computer software and counterfeit brand name apparel. The International Intellectual Property Alliance estimates that piracy levels in Ecuador for both motion pictures and recorded music has reached 95 percent, with estimated damage due to music piracy of $50 million to $60 million. At times, judges in IPR cases, before issuing a preliminary injunction, demand a guaranty and evidentiary requirements that exceed legal requirements and in effect limit the ability of rights holders to enforce their rights. Ecuador has made no progress in establishing the specialized IPR courts required by Ecuador's 1998 IPR law. The national police and the customs service are responsible for carrying out IPR enforcement but do not always enforce court orders. Some local pharmaceutical companies produce or import pirated drugs and have sought to block improvements in patent protection. U.S. industry estimates damage due to the failure to provide data exclusivity is at least $5 million.

SERVICES BARRIERS

Ecuador has ratified the WTO Agreement on Financial Services. The 1993 Equity Markets Law and the 1994 General Financial Institutions Law significantly opened markets in financial services and provided for national treatment for foreign suppliers. Foreign professionals are subject to national licensing requirements. The Superintendent of Banks must certify accountants.

In the area of basic telecommunications, Ecuador only subscribed to WTO commitments for domestic cellular services. It did not make market access or national treatment commitments for a range of other domestic and international telecommunications services, such as voice telephony and data. In addition, Ecuador does not adhere to the pro-competitive regulatory commitments of the WTO Reference Paper. Several U.S. telecommunications companies have had their international circuits disconnected without proper notice of alleged infractions. The Government has also used Ecuadorian courts to delay, on questionable grounds, implementation of an arbitral award in favor of a U.S. company.

The U.S. Government is seeking through the FTA negotiations to secure greater access for U.S. providers of cross-border services to the Ecuadorian market, including in the areas of financial and telecommunications services.

INVESTMENT BARRIERS

Ecuador's foreign investment policy is governed largely by the national implementing legislation for Andean Pact Decisions 291 of 1991 and 292 of 1993. Under Ecuadorian law, foreign investors are accorded the same rights of establishment as Ecuadorian private investors, may own up to 100 percent of enterprises in most sectors without prior government approval, and face the same tax regime. There are no controls or limits on transfers of profits or capital. The U.S.-Ecuador Bilateral Investment Treaty (BIT), which entered into force in May 1997, includes obligations relating to national and most-favored-nation treatment; prompt, adequate and effective compensation for expropriation; the freedom to make investment-related transfers; and access to binding international arbitration of investment disputes. U.S. companies are sometimes reluctant to resolve commercial disputes in the Ecuadorian legal system, fearing a prolonged process and a lack of impartiality, among other things.

In early 2005, Ecuador's Congress modified the Arbitration and Mediation Law to prohibit international arbitration if the national interest could be affected. Depending on how it is interpreted and applied, this modification of Ecuador's law could conflict with Ecuador's standing consent to binding arbitration under the U.S.-Ecuador BIT. At a minimum, the new law will create confusion among investors regarding their arbitration rights and may also reinforce negative impressions among investors of Ecuador's commitment to international arbitration.

Certain sectors of Ecuador's economy are reserved to the state. All foreign investment in petroleum exploration and development in Ecuador must be carried out under contract with the state oil company. U.S. and other foreign oil companies produce oil in Ecuador under such contracts. Several of these companies are involved in a dispute with the government of Ecuador relating to the refund of value-added taxes. In 2004, one of the disputing U.S. companies won a $75 million international arbitration award against the government of Ecuador. The Government has requested a judicial review of the arbitration award. After notice of the award, Ecuador's Solicitor General (Procurador General) initiated an investigation of the company for allegedly transferring assets to another foreign company without obtaining the required authorization from the state. The Ecuadorian government has since advocated the nullification of the company's contract and seizure of the company's considerable assets in Ecuador.

Foreign investment in domestic fishing operations, with exceptions, is limited to 49 percent of equity. Foreign companies cannot own more than 25 percent equity in broadcast stations. Foreigners are prohibited from owning land on the borders or the coast.

Effective compensation for expropriation is provided for in Ecuadorian law but is often difficult to obtain. The extent to which foreign and domestic investors receive prompt, adequate and effective compensation for expropriations varies widely. It can be difficult to enforce property and concession rights, particularly in the agriculture, oil and mining sectors. Foreign oil, energy and telecommunications companies, among others, have often had difficulties resolving contract issues with state or local partners. The transparency and stability of the country's investment regime are significantly weakened by the existence of numerous investment-related laws which overlap or appear to have mutually inconsistent provisions. This judicial complexity increases the risks and costs of doing business in Ecuador.

The U.S. Government has worked with the Government of Ecuador both before and in parallel with the FTA negotiations to ensure a fair resolution of U.S. investor disputes, consistent with Ecuadorian law. Some of those disputes have been resolved while others remain pending.

ELECTRONIC COMMERCE

Ecuador passed an electronic commerce law in April 2002 that makes the use of electronic signatures in business transactions on the Internet legally binding and makes digital theft a crime. Ecuador has initiated a program for e-government services and to promote public access to information technology through funding from international financial institutions. The U.S. is seeking in the FTA negotiations to include rules prohibiting duties on and discrimination against digital products, such as computer programs, videos, images, and sound recordings, based on where they are made or the nationality of the firms or persons making them.

EGYPT

TRADE SUMMARY

The U.S. trade surplus with Egypt was $1.8 billion in 2004, an increase of $311 million from $1.5 billion in 2003. U.S. goods exports in 2004 were $3.1 billion, up 19.1 percent from the previous year. Corresponding U.S. imports from Egypt were $1.3 billion, up 16.4 percent. Egypt is currently the 36th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Egypt were $3.3 billion in 2003 (latest data available), and U.S. imports were $1.7 billion. Sales of services in Egypt by majority U.S.-owned affiliates were $1.1 billion in 2002 (latest data available), while sales of services in the United States by majority Egypt-owned firms were $325 million.

The stock of U.S. foreign direct investment (FDI) in Egypt in 2003 was $3.0 billion, up from $2.9 billion in 2002. U.S. FDI in Egypt is concentrated largely in the mining sector.

IMPORT POLICIES

Over the past decade, the Government of Egypt (GOE) has gradually implemented a number of import policies to promote greater trade liberalization. The list of goods requiring prior approval before importation was eliminated in 1993. Egypt became a member of the World Trade Organization in 1995 and has pledged to be in full compliance with its trade commitments to the WTO by 2005. Progress in economic reform was halting during the last several years, but received renewed impetus with the appointment of Prime Minister and ministerial economic team in July 2004. Under the leadership of Prime Minister Nazif, the GOE has taken several positive steps (outlined below). Significant problems still remain and add to the cost of doing business. The GOE will have to continue efforts to reduce red tape, reform the cumbersome bureaucracy, and eliminate unreasonable and excessive Egyptian standards.

In January 2003, the government partly floated the Egyptian Pound (LE). Both government and business hoped the move to a flexible exchange rate would improve access to foreign exchange, but foreign exchange liquidity and turnover remained problems until a new Central Bank Governor was appointed in December 2003. During 2004 the foreign exchange market stabilized with increased availability of hard currency and the disappearance of backlogs in business requests. By December 2004 the parallel foreign exchange market, which had emerged in 2001, had largely disappeared and the official U.S. dollar exchange rate stabilized at LE6.25/$. Prime Ministerial decree 506 of 2003, which established a surrender requirement for all foreign exchange generating transactions, was annulled in December 2004 by a court decision and a Prime Ministerial decree. There are no reported delays in firms' requests for foreign currency for imports and loan repayment and imports have increased by 20 percent from fiscal year 2002/2003 to fiscal year 2003/2004.

Tariffs

Egypt significantly reduced tariffs in late 2004. In 1998 the GOE reduced the maximum tariff rate for most imports from a high of 50 percent to 40 percent. In keeping with most of its Uruguay Round commitments, over 98 percent of Egypt's tariffs are bound tariffs. Egypt's average weighted tariff rate was 27.5 percent, which was relatively high when compared with other developing countries with large internal markets and diversified industrial economies. In addition to tariffs, the GOE levied service fees on the value of imported shipments in exchange for inspection, listing, classification and reexamination of shipments. An inspection fee of one percent was levied on all imports. The GOE also applied an additional surcharge of two percent on goods subject to import duties of 5 percent to 29 percent, and a surcharge of three percent on goods subject to duties of 30 percent or more.

On September 8, 2004 the GOE announced a new tariff structure. The government removed services fees and import surcharges, reduced the number of *ad valorem* tariff rates from 27 to 6, dismantled tariff inconsistencies, including sharp escalation and reverse progression on tariff rates, and rationalized national sub-headings above the six-digit level of the Harmonized System (HS). The new tariff structure includes six tariff rates, pegged to the degree of processing, that range between 2 percent on raw materials, spare parts, and primary feeding products and 40 percent on durable consumer goods. The changes in tariffs brought down the officially announced weighted average tariff rate from 14.6 percent to 9.1 percent. The government also eliminated services fees and import surcharges ranging from 1 to 4 percent. The GOE replaced its 10-digit thirteen thousand-line tariff structure with a six-digit structure with less than six thousand tariff lines. This change should reduce disputes over product classification for customs purposes. Additionally, the GOE eliminated export duties on 25 products that were in short supply on the domestic market. A number of high tariffs still exist, including duties on imported alcoholic beverages, tobacco and cigarettes and passenger vehicles with cylinder capacity (CC) above 2000.

All goods are subject to sales tax ranging from 5 percent to 25 percent. Egypt applies a sales tax of 10 percent on high quality imported flour that is not applied to locally produced flour.

A ban on fabric imports was lifted in 1998, and a ban on apparel imports was lifted in January 2002. However, tariffs on textiles were well over 50 percent, and starting January 2002, garments were subject to a specific-rate, per-piece duty ranging up to 1,400 Egyptian pounds ($230) per item. In January 2004, the GOE formally repealed a long-standing ban on commercial clothing and fabric imports and replaced per-piece tariffs on clothing (which the U.S. had challenged in the WTO in December 2003) with *ad valorem* (percentage of value) tariffs consistent with Egypt's commitments to the WTO. (Currently rates are 40 percent for apparel.) A February 2004 ministerial decree required companies wishing to export to Egypt to register with the Egyptian General Organization for Import and Export Controls (GOIEC) and to certify their compliance with international labor, health, and environmental standards through a process which would have included visits to the their factories (at factory expense) by GOIEC inspectors. Although removal of the ban on apparel imports and change in nature of tariffs on imported apparel was a positive step, exporters considered the inspection process required for registration a non-tariff barrier that did not effectively allow importing of apparel. The registration regulation decree was amended in October 2004 to remove the inspection stipulation while maintaining registration with the GOIEC.

In December 2004 Egypt reduced tariffs for certain textile and apparel products and committed to a further round of tariff cuts for additional textile and apparel products in 2005.

Tariffs on passenger cars with engines under 1,600cc were reduced in September 2004 to a maximum of 40 percent, while engines over 1,600cc now have a tariff rate of 135 percent. The tariff rate on poultry was also reduced to 5 percent and on poultry parts to 32 percent. There is a 300 percent duty on wine for use in hotels, and a tariff ranging between 1,200 and 3,000 percent on alcoholic beverages for general importers. Foreign movies are subject to duties and import taxes of about 46 percent of the value of a film (32 percent for a copy of the movie, 12 percent on posters and 2 percent on the movie reel), as well as a 10 percent sales tax and a 20 percent box office tax (compared to a five percent box office tax for local films).

Soft drinks face a statutory excise tax of 50 percent to 60 percent (though various government-approved deductions result in an effective tax rate between 25 and 30 percent). By comparison, competing beverages such as bottled water, juices, teas and coffees are taxed at 10 percent**.** To address this issue, the GOE drafted amendments to the sales tax law and referred them to Parliament in the 2004/2005 round. Expected to be adopted in mid-2005, the amendments will decrease the statutory tax on soft drinks to 25 percent and the effective sales tax rate to 17 percent.

High tariffs restrict the competitiveness of U.S. food products such as U.S. apples and pears, which face a 40 percent *ad valorem* duty, and U.S. exporters report that Egypt's application of sanitary and phytosanitary measures to these products are non-transparent and burdensome.

Customs Procedures

Egypt announced implementation of the WTO customs valuation system in July 2001. The system has not been fully implemented, and importers sometimes face a confusing mix of the new invoice-based and old reference-price valuation systems depending on the type of imports. The Ministry of Finance is trying to assist customs officials by translating and simplifying the WTO valuation system, which uses seven valuation methods. The Ministry of Finance has committed to a comprehensive program to reform the customs system, and a priority is to implement the WTO Customs Valuation Agreement. USAID has funds available for a six-year, $30 million customs reform project to support the Ministry of Finance's efforts. The Ministry of Finance is working with other donors, including the European Union, on customs reform issues.

The September 2003 inauguration of the Model Customs and Tax Center (MCTC) was an important step in modernizing customs and tax administration in Egypt. The Cairo MCTC is a “one-stop shop” where taxpayers registered in Greater Cairo can settle income taxes, sales taxes and customs for goods passing through any of Egypt's ports. Another model customs center will be established in Alexandria in 2005.

In June 2002, the parliament approved a new Export Promotion Law (Law 155). The law reinforces the coordinating authority of the Ministry of Foreign Trade and Industry’s General Organization for Import and Export Control (GOIEC) for all import inspection procedures, though the Ministries of Health and Agriculture maintain their own inspection units and procedures. A focus of the law is to improve the duty drawback and temporary admission systems for exporters by establishing a central unit under the joint supervision of the Ministries of Finance and Foreign Trade to monitor and streamline the systems. The law also established an “export development fund” to promote Egyptian exports and increase their share of foreign markets with the assistance of the Egyptian Center for Export Development. The fund's specific activities are not clear. To date the fund has not been used to subsidize exports. As of December 2003 the law’s executive regulations were drafted but not yet issued.

In November 2002, the Ministers of Foreign Trade and Finance inaugurated the new temporary admissions unit at the Port of Alexandria, a first step in a plan to upgrade operation of the temporary admissions system at all ports of entry in the country. USAID assisted the Government of Egypt to set up three other sites for temporary admissions and duty drawback in Suez, Port Said, and Damietta. The three sites have begun operation.

Import Bans and Barriers

As noted earlier, Egypt lifted its ban on apparel imports on January 1, 2002, replacing it with high specific-rate duties. In January 2004 the GOE issued a decree replacing these specific-rate duties with *ad valorem* (percentage of value) tariffs that appear to be consistent with Egypt's commitments to the WTO.

In 1998, Egypt issued a decree stipulating that passenger vehicles can only be imported during their year of manufacture, effectively banning the importation of second-hand cars. In 2000 the decree was amended adding one year after the year of production to the period during which passenger vehicles can be imported.

Egypt maintains restrictions on the importation of health food products such as dietary goods. For example, import permits are not issued for such products that compete with local products.

In December 2003 Egypt suspended the issuance of import licenses for all U.S. ruminant and ruminant products, including beef and beef liver, due to a single case of BSE in an imported cow. Egypt still maintains a prohibition on U.S. beef, despite significant U.S. actions to ensure the safety of all beef. This fall the United States hosted a visit of Egyptian officials to review U.S. safeguards for BSE. The United States continues to vigorously press for the lifting of Egypt's import restrictions on these products.

Egypt continues to block imports of U.S. turkey and chicken parts based on reported concerns that U.S. industry cannot verify that it meets Egyptian Halal requirements. Despite technical meetings and a June, 2003 written submission on steps by U.S. industry to assure Halal treatment, Egypt has not addressed U.S. concerns.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Mandatory quality control standards and other non-tariff barriers appear to restrict imports of some U.S. products, thereby providing preferential treatment for domestic products over imports. Although the government stresses that standards applied to imports are the same as for domestically produced goods, in practice industry reports that imports are subject to different inspections by agencies from a number of ministries. Egypt currently has over 4,500 standards, seven percent of which are mandatory. There is little or no inter-agency coordination in the formulation and enforcement of standards. Standards are established by the Egyptian Organization for Standardization and Quality Control in the Ministry of Foreign Trade and Industry. However, verification of compliance is the responsibility of agencies affiliated with several ministries, including the Ministry of Health, the Ministry of Agriculture and, for imported goods, GOIEC in the Ministry of Foreign Trade and Industry.

Egypt has increased efforts to bring mandatory regulations into conformity with international standards. On February 22, 2005, the Minister of Industry and Foreign Trade issued decree number 130 for 2005, which obligates importers and producers of certain food products and commodities to comply with only essential Egyptian standards and specifications. However, many imports are still subject to burdensome quality standards and inspections. The import process remains opaque despite a 1999 Presidential decree designating GOIEC as the coordinator for all import inspections. Moreover, the number of imports subject to mandatory quality control has increased from 69 to 131 categories of items, including foodstuffs, appliances, electrical products, and spare parts.

Egypt has increased efforts to bring mandatory regulations into conformity with international standards. However, importers report that product testing procedures are not uniform or transparent and that inadequately staffed and poorly equipped laboratories often yield faulty test results. Efforts are underway to improve Egyptian standards and testing. USAID and the U.S. Department of Agriculture worked with GOIEC to develop a state-of-the-art food laboratory in Dekhaila port near Alexandria. The laboratory became operational in March 2004. The privately run port of Ain Sukhna also will soon have a qualified inspection laboratory on its premises.

Egypt is a key U.S. agricultural export market and is a major purchaser of U.S. wheat and corn. Trade in agricultural products could be expanded, however, through the elimination of tariff and non-tariff barriers. U.S. exporters report that Egypt's application of sanitary and phytosanitary measures on a number of agricultural products are non-transparent and burdensome, including beef, apples and pears.

Shelf-life standards required by the Government are rigid and do not appear to recognize quality, safety and technological differences between producers. Many imports (mainly foodstuffs) entering Egypt must have 50 percent or more of their shelf life remaining. Such standards may have the effect of blocking some U.S. exports, such as U.S. processed cheese products. Moreover, Egypt applies shelf life standards to certain non-food imports such as syringes and catheters.

Food imports are sometimes subject to quality standards that appear to lack technical and scientific justification. For example, Egyptian Standard 1522 of 1991 requires that frozen beef imported for direct consumption contain no more than seven percent fat, a requirement not imposed on domestically graded premium beef. As a result, U.S. exporters lose an estimated $2 million in sales annually. In early 2005, Egypt announced that it would issue a decree to eliminate this requirement.

Food imports face a number of burdensome labeling and packaging requirements. Poultry and meat products must be shipped directly from the country of origin to Egypt and sealed in packaging with details in Arabic both inside and outside the package. This requirement raises processing costs and discourages some exporters from competing in the Egyptian market.

In response to U.S. requests, Egypt in 2004 took steps to address barriers to imports of U.S. and other foreign textile and apparel, including removing costly and complicated labeling requirements. Egypt ended the requirement that the country of origin must be identified in a continuous band along the entire length of the imported fabric. In addition, fabrics are no longer subject to testing, and measures requiring that apparel labels be written in Arabic to include importer information were eliminated. Egypt also committed to expedite the customs clearance process for apparel and textile imports.

GOVERNMENT PROCUREMENT

Egypt is not a signatory to the WTO Agreement on Government Procurement. In 1998, Egypt passed a law setting new regulations for government procurement to make the tendering process more open and fair and to provide the Egyptian Government greater value for money in its procurements. The new law mandates that technical factors, not just price, be considered in awarding contracts. The preference shown to parastatal companies has diminished, but not been eliminated. Previously, publicly owned companies always received preference. Under the new law, this preference only applies when the bid of a publicly owned firm is within 15 percent of other bids. Contractors receive certain rights under the law, such as speedy return of their bid bonds and an explanation of why a competing contractor won the bid. Many concerns about transparency remain, however. For example, the Prime Minister can authorize the method of tendering for specific entities according to terms, conditions, and rules that he determines. In August 2004 the newly appointed Prime Minister issued a decree stipulating strict adherence by all government ministries to the provisions of the Tenders and Auctions law that limit direct orders to cases of national security or emergency. The United States and Egypt have a working group on government procurement established under the U.S.-Egypt Trade and Investment Framework Agreement Council, and Egypt supports discussion of transparency in government procurement in the WTO.

EXPORT SUBSIDIES

The GOE mandated a $43 million subsidy program for Egyptian cotton in October 2002 to encourage the use of local cotton by textile mills. The program ended during the first half of 2003, with no payments made to growers. There are no plans to renew this program. The government had imposed restrictions on the export of long and medium-long staple cotton to make these cotton varieties more available for local mills, presumably sold at lower prices than in foreign markets.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Though Egypt is a signatory to many of the international intellectual property (IP) conventions, intellectual property rights (IPR) protection was well below international standards until 2002. In 2002, Egypt took important steps to strengthen its IPR regime through improvements in its domestic legal framework and enforcement capabilities. In May 2002, the Egyptian Government passed a comprehensive IPR law to protect intellectual property and to attempt to bring Egypt into line with its obligations under the World Trade Organization Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS). The law addresses IPR protection in areas such as patents, copyrights (with enhanced protection for sound and motion picture recordings and computer software), trademarks, geographical indications, plant varieties, industrial designs, and semiconductor chip layout design. With respect to certain violations, the law stipulates higher fines and prison sentences for convicted violators. Although the law has certain shortcomings, its passage demonstrated a marked improvement in Egypt's IPR regime. In June 2003, the Executive regulations dealing with patents, trademarks, and botanical varieties were issued. The executive regulations covering copyright protections remain under review. Responding to Egypt's improved IPR protection, in May 2003 the United States Trade Representative (USTR) moved Egypt from the Special 301 "Priority Watch List" (a designation that Egypt had retained since 1997) to the "Watch List."

In 2004, however, Egypt lost ground in important areas of IPR protection. The U.S. government was deeply concerned by Egyptian government approval in late 2003 for local manufacturers to produce copies of several U.S. pharmaceutical products contrary to Egypt's obligations to protect the holder of the intellectual property rights of such products. As a result of these approvals, USTR in 2004 again elevated Egypt to the Priority Watch List. The data protection problem appeared to worsen in late 2004 when the Egyptian Ministry of Health apparently embarked on the approval of a significant number of copies of pharmaceutical products for marketing in Egypt. The U.S. Government is concerned that a number of these approvals would violate Egypt's obligations under TRIPS, its own IPR law, Prime Ministerial Decree 2211 and assurances it has given the U.S. Government on data protection. Other significant IPR problems in Egypt include lack of protection for new plant varieties and false licensing of some copyrighted works.

The United States has sought over the last ten years through USAID-funded projects to assist Egypt's efforts to build its capacities in intellectual property protection. Substantial and meaningful progress has been made in establishing and strengthening some of the government institutions necessary for an effective IP regime.

For example, in October 2004 the Ministry of Agriculture established a new plant variety registration office. However, articles in the Egyptian IPR law that require registration and certification by the plant variety registration office need to be modified to facilitate the process and provide adequate protection for new varieties. As of December 2004 no varieties have been registered with the office, prompting the Ministry of Agriculture to form a committee to resolve the problems associated with granting plant variety protection in Egypt. However, no action has yet been taken. Egypt's IPR law does not address "essentially derived varieties", thus leaving them without protection. U.S. companies are advised not to export new breeding material or new plant varieties to Egypt until the issues are addressed. Egypt is working on reforming administration of its IPR laws, including plant varieties, as part of its efforts to join the International Union for the Protection of New Varieties of Plants (UPOV).

A modern, computerized Egyptian Patent Office operating under the authority of the Ministry of Higher Education and State for Scientific Research now is capable of processing patent applications and granting patent protection. This office has significantly improved the quality and transparency of Egypt's trademark and industrial design registration system. Egypt has taken advantage of numerous technical assistance opportunities at the United States Patent and Trademark Office (USPTO) on topics such as computerized patent and trademark application searching, examination of trademark, and design applications, and the processing of applications under the Patent Cooperation Treaty (PCT). In preparation for the new WTO patent regime, in effect as of January 1, 2005, the Ministry began hiring new technical examination staff in 2003. It took appropriate steps to prepare for the processing of some 1,500 pharmaceutical patent applications that are expected to be in the "mailbox" when the new regime comes into effect. Egypt has become a receiving office under PCT for neighboring countries. This development should expand Egypt's regional role as a center for Arabic language training.

Counterfeiting and piracy adversely impact most of the intellectual property industries in Eygpt, including motion pictures (in video cassette format), sound recordings, books and other printed matter, textile designs, and computer software. The third chapter of the Egyptian IPR law's executive regulations covering copyrights and related issues has been under review by the Ministry of Culture for over two years. Regarding computer software protection, the GOE took steps to ensure the authorized use of legitimate business software by civilian government departments and in schools. Major U.S. software and computer companies operating in Egypt report a piracy rate in business software under 50 percent and improved enforcement in 2004. False licensing, where a local unauthorized distributor receives and is permitted to rely upon Ministry of Culture approval to distribute pirated software, music, and films, remains a problem and undermines copyright protection in Egypt. The Egyptian government, however, took steps to revoke such approvals for well-known pirates. Infringement of trademark, textile design and industrial designs remains problematic, though there are signs of improvement.

A USAID technical assistance program is working with several Egyptian Ministries to strengthen IPR enforcement and increase public awareness. Protection against false licensing is reported to be due to the government's inadequate human and physical resources. The USAID program is working with concerned government authorities to improve enforcement. Reports indicate an increase in police and Ministry of Culture involvement in IPR protection in 2004. The USAID program is working with the Ministry of Justice on IPR enforcement issues, including on efforts to increase the legal awareness of judges on IPR issues and to build institutional capacity to handle infringement cases. The program also works with law schools in five Egyptian universities to increase awareness and training on IPR issues. In addition, the program included cooperation with the Ministry of Internal Trade and Supply to set up a specialized IPR unit and modernize the trademark office that provide technical assistance to in-house inspectors. The Ministry of Foreign Trade and Industry established in mid-2004 a special unit for intellectual property rights protection.

SERVICES BARRIERS

Egypt participated actively in the Uruguay Round negotiations on services, but made commitments in only four sectors: construction, tourism, financial services, and international maritime transport. Egypt subsequently made commitments in the 1997 WTO agreement on financial services negotiations. Egypt is gradually implementing its General Agreement on Trade in Services (GATS) commitments. Egypt supported launching a new round of trade negotiations, including trade in services, at the WTO Ministerial meeting in Doha in November 2001.

Egypt has restrictions for most service sectors in which it has made GATS commitments. These restrictions place limits on foreign equity in construction and transport services (foreign capital equity should not exceed 49 percent of the total capital of some activities). Egypt restricts the employment of non-nationals to 10 percent of the personnel employed by a company.

Restrictions on the acquisition of land by foreigners for commercial purposes were amended in 2002 to allow the acquisition of land by non-Egyptians under certain criteria and procedures.

In 1998, the GOE passed legislation allowing privatization of Egypt's four state-owned insurance companies. The law removed the prohibition on majority foreign ownership of Egyptian private insurance firms, permitting up to 100 percent foreign ownership. In addition, the law eliminated the prohibition on foreign nationals serving as corporate officers of insurance companies. There are currently at least six foreign insurance companies operating in the market: Alico, AIG, ACE and ACE AIIC (U.S.), Legal and General (U.K.), and Allianz (Germany). There are eleven private sector insurance companies, three of which are joint ventures with U.S. firms. Plans to prepare the four state-owned insurance companies for privatization appear to have made little headway in the past two years. In December 2004 the Minister of Investment, who is responsible for privatization of public and joint venture companies, announced government plans to privatize public insurance companies. One public insurance company is expected to be privatized by the end of 2005.

There are 61 banks in Egypt, 22 of which are joint ventures with foreign participation. As a result of its 1997 WTO financial services commitments, Egypt does not limit foreign equity participation in local banks. Several foreign banks have majority shares in Egyptian banks, while other foreign banks are registered as branches of the parent bank (rather than subsidiaries). In all cases, these foreign banks can conduct all banking activities in Egypt. New foreign banking entrants face barriers, however. Because the government believes there are too many banks in Egypt, it has not issued a new banking license in at least ten years and announced it plans in the next five years to reduce the number of banks in Egypt to 21. As a result, the only way a foreign bank can enter the market in Egypt is to purchase an existing bank. In 2002, the Central Bank of Egypt (CBE) required that banks raise their capital adequacy ratios to meet Basel II standards. The 2003 banking law substantially raised minimum capital requirements for all banks mandating that banks unable to meet this requirement either merge with other banks or exit the market. Since early 2001 the government has advocated the merger of some smaller banks but little happened in this regard until late 2004 when two banks merged and three applied for CBE approval. More mergers are expected in 2005.

Also in 1998, legislation was passed to allow privatization of the four state-owned banks that control over 50 percent of the banking sector's total assets. Progress on privatization has been slow. In 2004, the government appointed new, western-trained senior management teams for the four banks. Government plans to privatize one public bank were announced following the appointment of a new Cabinet in July 2004, and this privatization is expected to be completed by the end of 2005. The downsizing and privatization of Egypt's banking sector should strengthen it and improve implementation of market-based financial operations.

Egypt's WTO financial services commitment in the securities sector provides for unrestricted market access and national treatment for foreign companies. International investors are permitted to operate in the Egyptian stock market largely without restriction. Several foreign brokers, including U.S. and European firms, have established or purchased stakes in brokerage companies. In May 2002, the Minister of Finance issued a decree to establish the Primary Dealers System which starting operating in July 2004. The new system allows financial institutions that are registered with the Ministry of Finance, currently including 13 banks, to underwrite primary issues of government securities and to activate trading in the secondary market through sale, purchase and repurchase of government securities. The government is using the primary dealers system to manage its public debt, secure non-CBE finance and create a market-based yield curve for public debt.

Telecommunications services have expanded rapidly in the past three years as the sector has been liberalized and opened to international competition. Telecom Egypt will continue to be a state-owned monopoly until the end of 2005. At that time, the GOE plans to offer up to 34 percent of the company to a strategic investor and additional shares on the stock exchange when market conditions are suitable. An initial public offering of Telecom Egypt stock was originally planned for late 2000, but it was delayed due to market conditions.

Private-sector firms participate actively in Internet services and cellular services. Foreign firms compete for contracts offered by Telecom Egypt to modernize its networks and switching equipment. Telecom Egypt has sought foreign participation in the management and operation of the national telecommunications grid, however no agreements have yet been signed. In February 2003, Egypt's parliament approved a new telecommunications law (Law 10). It stipulates, in compliance with Egypt's WTO commitments, that Telecom Egypt will relinquish its monopoly status as Egypt's domestic operator and sole international operator by January 2006 and provides for greater price flexibility for Telecom Egypt shares in a future public offering. In June 2002, Egypt acceded to the WTO Basic Telecommunications Agreement (BTA), which requires the liberalization of telecommunication services and full autonomy of the national telecom regulatory authority by January 2006. In April 2003, Egypt joined the WTO Information Technology Agreement (ITA), which requires the eventual phasing out of tariffs on all information technology imports from WTO members. Egypt has made significant progress in meeting its WTO telecommunications-related commitments. More progress is required to achieve full autonomy in National Telecommunication Regulatory Authority (NTRA) operations.

Maritime and air transportation services are being liberalized. A 1998 law ended the long-held government monopoly in maritime transport, and the private sector now conducts most maritime activities, including loading, supplying, ship repair, and, increasingly, container handling. The new Ain Sukhna port is the first privately owned and operated Egyptian port. Another port, East Port Said port, was inaugurated in October 2004. Egypt Air's monopoly on carrying passengers has been curtailed, and several privately owned airlines now operate regularly scheduled domestic flights and international charter services, although the national carrier remains by far the dominant player in the sector. Private and foreign air carriers may not operate charter flights to and from Cairo without the approval of the national carrier, Egypt Air. Egypt passed laws in 1996 and 1997 permitting private firms to build and operate new airports. Private concessions can operate businesses and provide services in airports, but private ownership of airports is still not permitted. Six new build-operate-transfer airports were under construction at the start of 2001. One of these, at Marsa Alam, opened at the end of 2001. The GOE plans to increase the number of airports in the country from the current 18 to 25 over the next decade.

Egypt maintains several other barriers to the provision of certain services by U.S. and other foreign firms. Foreign motion pictures are subject to a screen quota and distributors are allowed to import only five prints of any foreign film. The GOE applies to private express mail operators a postal agency fee of 10 percent of annual revenue from shipments under 20 kilos, a fee that negatively affects their competitiveness. Shipments weighing more than 20 kilos are treated as freight and are not subject to the 10 percent fee. According to the Egyptian labor law, foreigners cannot be employed as export and import customs clearance officers and tourist guides.

INVESTMENT BARRIERS

Under the 1992 U.S.-Egypt Bilateral Investment Treaty (BIT), Egypt committed to maintaining the critical elements of an open investment regime, including national and Most-Favored-Nation (MFN) treatment of investment (with exceptions specified in the treaty), the right to make financial transfers freely and promptly, and international law standards for expropriation and compensation. The BIT also establishes formal procedures to enforce the treaty, including international arbitration.

In 1999, Egypt and the U.S. signed a Trade and Investment Framework Agreement (TIFA) that established a TIFA Council designed to facilitate the discussion of bilateral trade and investment issues. The Council met most recently in October 2002 and established four working groups to review technical issues related to agricultural trade, customs administration, and government procurement. Other issues, including IPR, Egypt's foreign exchange regime, and specific commercial issues are discussed in the Council itself and in less formal meetings.

Egypt offers first-time investors expedited approval to establish operations, and special advantages and incentives are given to investors in 16 priority sectors (among them agriculture, housing, transportation, petroleum, and computer software). Many incentives are geographically based to encourage investors to locate outside of the greater Cairo area. For example, investors locating businesses in parts of Upper Egypt can receive 20-year tax holidays. A dozen new industrial zones have been built in satellite cities in the desert areas outside of Cairo and Alexandria. The government drafted a new income and corporate tax law which will be referred to parliament in the 2004/2005 session. The draft bill reduces income and corporate taxes by 50 percent, imposes flat rates, reforms tax administration, and eliminates tax holidays.

In 1995, Egypt notified the WTO about a measure inconsistent with its obligations under the Agreement on Trade-Related Investment Measures (TRIMS). The notified measure granted customs duty reductions to investments that met certain conditions with respect to resource exploitation, technology transfer, and export performance. By making this formal notification, Egypt qualified for a five-year transitional period for phasing out the relevant measure. In February 2001, Egypt submitted a request to the WTO for an additional five-year transition period. This request, which was received after the initial transition period had ended, was never formally granted by the WTO.

ANTICOMPETITIVE PRACTICES

The Government of Egypt has drafted a comprehensive competition and antitrust law that would prohibit monopolistic behavior that negatively impacts prices and quantities in local markets, and would call for monitoring companies that exceed a specific benchmark market share. The government circulated the draft law in the business community for discussion in the past year and made several amendments to accommodate international standards and the structure of the Egyptian economy. The law has been approved by the Egyptian Cabinet and is expected to be considered during the current session of parliament (November 2004-June 2005).

ELECTRONIC COMMERCE

Egypt issued the electronic signature Law 15 of 2004 which regulates authorization of electronic signatures and establishes the information technology industry development authority. Egypt is deferring a broader e-commerce law that will address such issues as domain names, customs and duties, and creation of a certificate authority to verify e-signatures. The development of e-commerce in Egypt has been impeded by concern about the lack of security on computer networks, the relatively high prices charged by Internet Service Providers, and the limited number of Internet users in the country.

OTHER BARRIERS

Pharmaceutical Price Controls

The Government controls prices in the pharmaceutical sector and does not have a transparent mechanism for pharmaceutical pricing. The Ministry of Health reviews prices of various pharmaceutical products and negotiates with companies to adjust prices of pharmaceuticals based on nontransparent criteria. The Ministry has not allowed complete adjustment of pharmaceuticals prices to compensate for general inflation and depreciation of the Egyptian pound since 2000. For example, although the Egyptian pound has fallen 80 percent in value against the U.S. dollar since June 2000, the government has granted price increases for only some pharmaceutical products. Because both domestic and foreign pharmaceutical companies rely heavily on imported inputs, profitability has dropped sharply and some companies claim to be operating at a loss. In September 2004 the government cut customs duties on most imports of pharmaceutical inputs and products from 10 percent to 2 percent. The government claims this step will allow local pharmaceutical companies to compensate for some of their losses from the devaluation. In November 2004 restrictions to export pharmaceuticals were removed to encourage pharmaceutical investment and exports. In November the Ministry of Health announced it will create a fund to stabilize prices of local pharmaceutical products. Some reports indicate the fund will mainly support local companies' research and development efforts. Details about the fund's operations are not available.

Export Restrictions

In August 2004 the Ministry of Agriculture removed restrictions on exporting cotton. The Minister of Foreign Trade and Industry then announced that all types of cotton will be available for exporting in the 2004/2005 season, and that the government will not interfere in cotton pricing. However, the U.S. Government continues to have concerns about Egypt's Alexandria Cotton Exporters' Association (ALCOTEXA), which controls all cotton export pricing and policies. The USG raised its concerns at the WTO's Working Party on STEs in November 2003 and awaits a response from the Egyptian government.

EL SALVADOR

TRADE SUMMARY

The U.S. trade deficit with El Salvador was $185 million in 2004, a decrease of $14 million from $199 million in 2003. U.S. goods exports in 2004 were $1.9 billion, up 2.6 percent from the previous year. Corresponding U.S. imports from El Salvador were $2.1 billion, up 1.6 percent. El Salvador is currently the 47th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in El Salvador in 2003 was $779 million, up from $684 million in 2002.

IMPORT POLICIES

Free Trade Agreement

The United States engaged in free trade agreement negotiations with five Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) in 2003. The United States concluded negotiations with El Salvador, Guatemala, Honduras, and Nicaragua in December 2003 and with Costa Rica in January 2004. In May 2004, the six countries signed the United States – Central America Free Trade Agreement. During 2004, the United States and the Central American countries engaged in negotiations with the Dominican Republic to integrate that country into the free trade agreement. On August 5, 2004, the seven countries signed the Dominican Republic – Central America – United States Free Trade Agreement (CAFTA-DR). El Salvador ratified the Agreement in December 2004 and Honduras ratified in March 2005. Legislative approval is pending in the United States and the other signatories to the Agreement.

The CAFTA-DR will remove barriers to trade with and investment in the region and will further regional economic integration. The CAFTA-DR will also require the Central American countries and the Dominican Republic to undertake needed reforms to confront many of the problems noted below in areas including: customs administration; protection of intellectual property rights; services, investment, and financial services market access and protection; government procurement; sanitary and phytosanitary (SPS) barriers; and other non-tariff barriers.

Tariffs

Most of El Salvador's tariffs do not exceed the maximum common external tariff of 15 percent established by the Central American Common Market (CACM), of which it is a member. There are several exceptions, however. Among these, tariffs on new and used finished clothing are generally 25 percent, while tariffs on fabrics which are not covered by CBI benefits can run 20 percent or more. Vehicles are assessed a 30 percent duty. Agricultural products face the highest tariffs. Dairy, rice and pork products are assessed a 40 percent duty, while the poultry tariff is higher. Alcoholic beverages are subject to a 30 percent duty, a specific tax based on alcoholic content, and an *ad valorem* 20 percent sales tax.

Under the CAFTA-DR, about 80 percent of U.S. industrial and commercial goods will enter the region duty-free, with the remaining tariffs being eliminated within ten years. Nearly all textile and apparel goods that meet the Agreement's rules of origin will be duty-free and quota-free immediately, promoting new opportunities for U.S. and regional fiber, yarn, fabric and apparel manufacturing companies. (The Agreement's tariff treatment for textile and apparel goods may be made retroactive to January 1, 2004.)

Under the CAFTA-DR, El Salvador will eliminate its tariffs on nearly all agricultural products within fifteen years (18 years for rice and chicken leg quarters and 20 years for dairy products). For the most sensitive products, tariff rate quotas will permit some immediate zero-duty access for specified quantities during the tariff phase-out period, which will expand over time. El Salvador will liberalize trade in white corn through expansion of a TRQ, rather than by tariff reductions.

The Agreement also requires transparency and efficiency in administering customs procedures, including the CAFTA-DR rules of origin. El Salvador committed to ensure greater procedural certainty and fairness and all Parties agreed to share information to combat illegal transshipment of goods.

Non-Tariff Measures

Rice and pork are both subject to import quota systems in addition to 40 percent duties. Rice millers are required to buy rice locally. When there is insufficient local supply, the Ministry of Agriculture allows imports under the quota, and if after the import quota has been exhausted, there is still a need for imported rice, rough or milled rice can be imported without limit, subject to a 40 percent duty. Pork importers face similar requirements to first buy locally and only import if a shortage remains after domestic supplies are exhausted, subject to a 40 percent duty. In addition, substantial tariff-rate quotas, which grow over time, were established under the CAFTA-DR for rice and pork to provide duty-free access for U.S. exports while the out-of-quota duties are phased-out.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Although sanitary standards have generally not been a barrier in El Salvador, practices with respect to raw poultry are a notable exception. Since 1992, the Ministry of Agriculture has imposed arbitrary sanitary measures on U.S. poultry imports. The Salvadoran government applies these standards in a discriminatory manner since domestic production is not subject to the same requirements as imports. As a result of these measures, the United States has been unable to export poultry to El Salvador. The industry estimates the value of lost U.S. poultry exports at

$5 million to $10 million per year. Resolution of this issue has been a priority for U.S. agencies, which continue to work with the Government of El Salvador.

In addition, the Salvadoran government requires that rice shipments be fumigated at importers' cost unless they are accompanied by a U.S. Department of Agriculture certificate stating that the rice is free of *Tilletia barclayana*. However, since there is no chemical treatment that is both practical and effective against *Tilletia barclayana*, USDA cannot issue these certificates. El Salvador failed to notify the WTO under the Agreement on the Application of Sanitary and Phytosanitary Measures when it imposed this requirement.

Importers must deliver samples of all foods for laboratory testing to the Ministry of Public Health, which, upon approval, issues the product registration numbers which allow them to be sold at retail outlets. Some U.S. processed foods that were approved in the United States were rejected after analysis in El Salvador, thereby barring their sale. The United States and the Ministry of Public Health initiated discussions on this issue in 2002. The U.S. Embassy has been able to obtain access for U.S. products rejected by the Ministry of Public Health testing on a case-by-case basis. At present, there is not yet a standard regulation allowing entry of U.S.-approved products. The CAFTA-DR provides an opportunity for the United States to engage El Salvador in several venues, including the SPS and Trade Capacity Working Groups established under the Agreement, and fosters significant movement toward the establishment of standard regulations for the import of foreign food products. A prime example is the work being done on the recognition of the equivalence of the U.S. inspection system for meat, dairy and poutry (see below).

All imports of fresh food, agricultural commodities, and live animals must have a sanitary certificate from the Ministry of Agriculture and the Ministry of Public Health. Basic grains must have import licenses from the Ministry of Agriculture, while dairy products require import licenses from the Ministry of Public Health. Consumer products require a certificate showing approval by U.S. health authorities for public sale.

The United States has raised concerns regarding the potentially discriminatory effects of a proposed Salvadoran technical standard for distilled spirits. U.S. industry has expressed concern with El Salvador's proposed standards for rum and *aguardiente*. However, the five Central American countries, including El Salvador, are in the process of developing common standards for several products, including distilled spirits, which could serve to increase market access and facilitate trade. U.S. industry also welcomes El Salvador's commitment under CAFTA-DR to explicitly recognize Bourbon and Tennessee whiskey as distinctive products of the United States.

When the United States and Central America launched the free trade agreement negotiations, they initiated an active working group dialogue on SPS barriers to agricultural trade that met alongside the negotiations to facilitate market access. The objective was to leverage the impetus of active trade negotiations to seek difficult changes to the Central American countries' SPS regimes. Through the work of this group, El Salvador has committed to resolve specific measures restricting trade between El Salvador and the United States. In particular, for meat, dairy, and poultry, El Salvador will move toward recognizing import eligibility for all plants inspected under the U.S. food safety and inspection system.

GOVERNMENT PROCUREMENT

El Salvador is not a party to the WTO Agreement on Government Procurement. However, government purchases and construction contracts are usually open to foreign bidders. The Legislative Assembly passed a new, more transparent procurement law in April 2000 that applies to the central government structure as well as to autonomous agencies and municipalities. The CAFTA-DR requires fair and transparent procurement procedures, including advance notice of purchases and timely and effective bid review procedures. Under the CAFTA-DR, U.S. suppliers will be permitted to bid on procurements covered by the Agreement for most Salvadoran government entities, including key ministries and state-owned enterprises on the same basis as Salvadoran suppliers. The anti-corruption provisions in the Agreement require each government to ensure that bribery in trade-related matters, including in government procurement, is treated as a criminal offense, or is subject to comparable penalties, under its law.

EXPORT SUBSIDIES

El Salvador gives a six percent tax rebate on exports shipped outside the Central American area based on the F.O.B port of exit value of the goods. The rebate is not granted to exports of coffee, sugar, or cotton unless these products have undergone a transformation process that adds at least 30 percent to the original value. Assembly plants outside of free trade zones (maquilas) are eligible if they meet the criteria for adding 30 percent Salvadoran value in the production process. Firms operating in free trade zones are not eligible to receive rebates as they already enjoy a 10-year exemption from income tax and duty-free privileges. Under the CAFTA-DR, El Salvador may not adopt new duty waivers or expand existing duty waivers conditioned on the fulfillment of a performance requirement (e.g., the exportation of a given level or percentage of goods). El Salvador may maintain existing duty waiver measures through 2009 provided such measures are consistent with its WTO obligations.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Criminal enforcement of IPR laws at the Attorney General's office is handled by the Crimes Against Private Property and Intellectual Property Unit, where 5 of the approximately 25 prosecutors are assigned to IPR cases, but not necessarily full time. The National Police established an IPR unit that supports the Attorney General's office, but also conducts its own investigations and raids. The National Health Council has administrative enforcement authority for cases involving pharmaceuticals and other intellectual property issues related to public health.

CAFTA-DR obligations would strengthen El Salvador's IPR protection regime to conform with, and in many areas exceed, WTO norms. CAFTA-DR obligations would also provide stronger deterrence against piracy and counterfeiting by criminalizing end user piracy and requiring El Salvador to authorize the seizure, forfeiture, and destruction of counterfeit and pirated goods and the equipment used to produce them. The CAFTA-DR text also mandates both statutory and actual damages for copyright and trademark infringement which would ensure that monetary damages can be awarded even when it is difficult to assign a monetary value to the violation.

Patents

The 1993 Intellectual Property Protection Law and El Salvador's acceptance of the disciplines in the TRIPS Agreement addressed several deficiencies in the patent regime. The 1993 law lengthened patent terms to 20 years from the application filing date. Although pharmaceutical patent terms were kept at 15 years, the Salvadoran government's Registry for Intellectual Property issues 20 year patents for pharmaceutical products in practice, which start on the filing date of the application. A major concern for U.S. pharmaceutical and agricultural chemical companies is the lack of data protection in El Salvador for undisclosed test data submitted for the marketing approval of a pharmaceutical or agricultural chemical product. Implementation of CAFTA-DR obligations will ensure adequate and effective protection of such data from disclosure and unfair commercial use.

Copyrights

After a sharp decline attributable to tough enforcement, video piracy in El Salvador returned to high levels in 2004. The main form of piracy is optical discs in DVD-R format offered by video clubs before the local theatrical release. Optical media imported from the United States by pirates is being used as duplication masters. While video piracy is the main concern, there has also been concern expressed about inadequate enforcement of cable broadcast rights and the competitive disadvantage it places on legitimate providers of this service.

Trademarks

In 2002, El Salvador's Legislative Assembly passed the Law of Trademarks and Other Distinctive Signs. The law provides for new protections against bad-faith registration of famous marks. Under the law, the National Registry of Intellectual Property requires that applicants show that they either own or have permission to register the famous mark. There were 25 complaints filed in 2004 with the Attorney General's office for counterfeiting or illegal use of trademarks. There were 54 raids to seize products with such trademarks. During 2003, there was progress in a significant intellectual property dispute involving trademark and copyright infringement by an ex-franchisee. The case, however, is still not fully resolved. Judicial enforcement continues to be the weakest pillar of intellectual property protection in El Salvador, but CAFTA-DR IPR enforcement provisions are expected to help reduce trademark infringement.

SERVICES BARRIERS

El Salvador maintains few barriers to services trade. El Salvador has accepted the Fifth Protocol to the WTO General Agreement on Trade in Services, which was necessary to bring its commitments on financial services into effect. Foreign investors are limited to 49 percent of equity in free reception television and AM/FM radio broadcasting. There are no such restrictions on cable television ownership. Notaries must be Salvadoran citizens. Under the CAFTA-DR, El Salvador will accord substantial market access in services across its entire services regime, subject to very few exceptions. In addition, U.S. financial service suppliers will have full rights to establish subsidiaries, joint ventures or branches for banks and insurance companies.

INVESTMENT BARRIERS

There are few formal investment barriers in El Salvador. However, U.S. investors complain that judicial and regulatory weaknesses limit their investment in El Salvador. The United States has raised concerns about the impact of re-regulation of the electric power sector on U.S. electric energy investors in El Salvador. A U.S. long distance telephone service provider complained that the dominant fixed-line telephone company refuses to sign an interconnection agreement with it on terms already extended to another market entrant, as required by Salvadoran law.

The first case of commercial arbitration in El Salvador involved a U.S. firm and the parastatal water company. The arbitration panel ruled in favor of the U.S-owned firm, but a legal challenge by the water company relating to the bidding process led the Supreme Court to suspend the proceedings pending a review of the case.

The United States and El Salvador signed a Bilateral Investment Treaty (BIT) in 1999. The United States and El Salvador each ratified the BIT in 2001 but did not exchange the instruments of ratification necessary to bring the treaty into force. When CAFTA-DR enters into effect, the investment chapter will provide for protection of U.S. investors comparable to those that were included in the 1999 BIT. Under the CAFTA-DR, all forms of investment will be protected, including enterprises, debt, concessions, contracts and intellectual property. U.S. investors will enjoy, in almost all circumstances, the right to establish, acquire and operate investments in El Salvador on an equal footing with local investors. Among the rights afforded to U.S. investors are due process protections and the right to receive a fair market value for property in the event of an expropriation. Investor rights will be protected by an effective, impartial procedure for dispute settlement that is fully transparent. Submissions to dispute panels and panel hearings will be open to the public, and interested parties will have the opportunity to submit their views.

EUROPEAN UNION

TRADE SUMMARY

The U.S. trade deficit with the European Union was $110 billion in 2004, an increase of $12.1 billion from $97.9 billion in 2003. U.S. goods exports in 2004 were $172.6 billion, up 11.2 percent from the previous year. Corresponding U.S. imports from the European Union were $282.6 billion, up 11.7 percent. The European Union ranked second behind Canada as an export market for the United States in 2004.

U.S. exports of private commercial services (i.e., excluding military and government) to the European Union were $101.3 billion in 2003 (latest data available), and U.S. imports were $85.8 billion. Sales of services in the European Union by majority American-owned affiliates were $197.7 billion in 2002 (latest data available), while sales of services in the United States by majority European-owned firms were $234.5 million.

The stock of U.S. foreign direct investment (FDI) in the European Union in 2003 was $856.3 billion, up from $759.8 billion in 2002. U.S. FDI in the European Union is concentrated largely in the manufacturing, finance, and wholesale sectors.

OVERVIEW

In most respects, the enormous U.S.-EU trade and investment relationship operates smoothly and to the great benefit of companies, workers, and consumers on both sides of the Atlantic. However, as outlined below, U.S. exporters in some sectors continue to face chronic barriers to entering the EU market. A number of these barriers (e.g., restrictions on U.S. poultry and beef exports) have been highlighted in this report for several years, despite repeated efforts to resolve them through bilateral consultations or, in some cases, the dispute settlement provisions of the WTO.

Although the enlargement of the EU in May 2004 to include ten new countries represents an important and positive political and economic achievement, it has resulted in new barriers for U.S. exports in some instances. This report highlights the U.S. determination to negotiate appropriate compensation arrangements or solutions related to the application by the new Member States of EU tariff, non-tariff, and services-related barriers to U.S. trade. In addition, systemic problems surrounding a lack of uniformity and transparency in the administration of EU customs law have assumed greater prominence in light of the addition to the EU of 10 new national customs authorities. The EU's longstanding policy of subsidizing the development, production, and marketing of large civil aircraft has had a distorting effect and has grown as a source of concern for U.S. trade policy. Other EU barriers cited in this report (for example, wine restrictions and agricultural biotechnology, including traceability and labeling requirements) are the result of restrictive regulatory approaches that often do not reflect a sound assessment of actual risks posed by the goods in question and that rely on ill-defined concepts of precaution. This year's report also outlines concerns of U.S. exporters with respect to a number of emerging EU policies that may threaten to disrupt trade in the future, such as the proposed new EU chemicals regulation.

IMPORT POLICIES

Customs Administration

EU customs law is set forth principally in the Community Customs Code and in implementing regulations promulgated by the Commission. However, the EU does not currently operate as a single customs administration. Application of the Community Customs Code to individual cases is the responsibility of EU Member State customs administrations, which do not have identical working practices, do not always interpret Code provisions on classification, valuation, and origin identically, and are not obliged to follow each other's decisions. In terms of day-to-day customs operations, differences from Member State to Member State exist in areas such as the type of automated systems used, risk criteria used by administrations to determine when to examine goods, VAT levels, and licenses required for food products, as well as disparities in certificate of origin requirements and treatment of express shipments. The difficulties presented by non-uniform procedures are increased by the absence of EU-wide administrative management of customs operations.

On some questions, where Member States administer EU law differently, the matter may be referred to the Customs Code Committee, an entity established by the Community Customs Code to assist the Commission. The Committee consists of representatives of the Member States and the Commission. While, in theory, the Committee exists to help reconcile differences and thereby help to achieve uniformity of administration, in practice its success in this regard has been limited. This is due in part to the fact that only a Member State or the Commission may refer a matter to the Committee; a private party has no right to refer matters to the Committee. Moreover, achieving consensus among Member States on particular issues is time-consuming with significant uncertainty to exporters. Even when a question of interest to a particular exporter is submitted to the Committee, there is no guarantee that the Committee will address all elements of the question.

This problem is further compounded by the absence of tribunals and procedures that would provide for the prompt review and EU-wide correction of administrative actions relating to customs matters, as is required by Article X:3(b) of the GATT 1994. Review by the European Court of Justice of national decisions regarding customs administrative matters may be available in some cases, but generally only after pursuit of the matter through Member State courts. Obtaining corrections with EU-wide effect for administrative actions relating to customs matters may take years.

The lack of access for traders to prompt review and correction by a tribunal with EU-wide jurisdiction is not a new phenomenon. However, the impact of this deficiency has grown with the May 2004 enlargement of the EU from 15 to 25 Members. The concern also has taken on new prominence in light of the focus of the Doha Development Agenda on trade facilitation.

Given the growing negative consequences of deficiencies in the EU's customs administration, the United States in September 2004 filed a WTO case, requesting consultations under the WTO's dispute settlement rules in an effort to address the systemic problems surrounding EU customs administration practices. The United States and the EU held consultations in Geneva on November 16, 2004. The panel will be established on March 21, 2005.

Changes to the EU Import Regime for Rice

On September 1, 2004, the EU implemented a new import tariff regime for rice, replacing the former "margin of preference" (MOP) mechanism. The MOP, which had been a significant trade concession negotiated between the United States and the European Union under WTO rules, provided for a variable rice tariff depending on the level of the world price compared to the internal EU intervention price. The MOP for rice was an important commitment on the part of the EU as a result of the Uruguay Round of multilateral trade negotiations. As part of the 2003 reform of the Common Agricultural Policy, which significantly lowered the EU's intervention price for rice, the European Commission replaced the MOP mechanism with a fixed tariff of 65 Euro/MT on husked rice and 175 Euro/MT on milled rice. The United States exports mainly brown (husked) rice to the EU, and has historically been the largest supplier of this type of rice to the EU market.

Under these new conditions, the United States risked losing its market for high-quality husked rice in Europe. As required by WTO rules, the EU entered into negotiations with trading partners, including the United States, to provide compensation to offset the change to the rice import regime. The United States had six months from September 1, 2004, within which to negotiate or assert its rights. On January 28, 2005, the United States initiated the necessary procedures to withdraw "substantially equivalent" concessions as allowed under WTO rules in the event that an agreement was not reached. On February 28, 2005, the United States announced that it had reached an agreement with the EU ensuring market access for U.S. brown (husked) rice exports to the EU. This avoided the need for the United States to withdraw tariff concessions by the March 1, 2005 deadline in connection with this issue.

EU Enlargement

The European Union expanded from 15 to 25 members on May 1, 2004, with the accession of 10 Central European and Mediterranean countries (Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, the Slovak Republic, and Slovenia). While this expansion of the single European market presents important opportunities for U.S. exporters, it has also resulted in negative commercial consequences in some instances.

Among U.S. concerns related to the recent enlargement (in addition to the concerns discussed under Customs Administration, above) are certain new Member States taking action to: (1) increase tariff rates as they apply the EU common external tariff; (2) withdraw or modify services market access commitments and changes to various GATS MFN exemptions to align them with the EU's existing GATS commitments; and (3) apply certain EU non-tariff barriers (such as sanitary and phytosanitary measures or other technical barriers). Further, there is continuing uncertainty surrounding how the EU will adjust import quotas and tariff-rate quotas applied to EU imports of agricultural and fish products to account for the expansion of the EU market as a result of enlargement. The United States has expressed concern about extension of EU antidumping and countervailing duty orders to new Member States without conducting appropriate economic or market analyses. In addition, the United States desires to ensure that the new Member States abide fully by the terms of trade agreements to which the European Community is bound, such as the WTO Agreement on Government Procurement, the WTO Agreement on Trade in Civil Aircraft, and various bilateral U.S-EU agreements.

The United States has entered into negotiations with the European Commission about enlargement-related concerns, including within the framework of GATT provisions relating to the expansion of customs unions. While pressing for a rapid and successful conclusion of negotiations to provide appropriate trade compensation, the necessary procedures have also been started to undertake retaliatory measures against the EU as allowed under WTO rules in the event that an agreement is not reached.

Restrictions Affecting U.S. Wine Exports

Since the mid-1980s, U.S. wines have been permitted entry to the EU market through temporary exemptions from certain EU wine regulations. One such regulation requires wines imported into the EU to be produced using only certain wine-making practices. Other regulations require extensive certification procedures for imported wines and prohibit the use of wine names and grape varieties as regulated in the United States. Without derogations from these regulations, many U.S. wines would be immediately barred from entering the EU. U.S. wines that are produced with practices for which there are no EU derogations are already barred. EU derogations for U.S. wines were set to expire in December 2003, but the EU has agreed to further extend the current arrangement until December 2005, pending U.S.-EU wine negotiations for an agreement addressing these issues.

Negotiations on a bilateral wine agreement continued throughout 2004. The United States is pressing the EU to provide U.S. wine makers equitable access to the EU wine market, particularly in light of Europe's considerable surplus in wine trade with the United States. A key U.S. objective is EU acceptance of U.S. wine-making practices, to obviate the need for future short-term derogations. The United States also continues to press for: (1) approval of future U.S. wine-making practices; (2) minimizing EU wine import certification requirements; and (3) allowing the use on U.S. wine labels of certain wine terms and names in the EU.

In 2002, the EU adopted a new wine labeling regulation (Commission Regulation No. 753/2002). This regulation entered into only limited enforcement in January 2003, after the United States, along with a number of other WTO Members, raised serious concerns about its lack of clarity and its WTO-consistency and urged the EU to withdraw the regulation. The regulation appears to be more trade restrictive than necessary to meet any legitimate objective, as it would prohibit the presentation on imported wine of information important for the marketing of wine unless certain conditions are met (e.g., the marketing information used must be regulated in the producing country). In addition, the EU imposes restrictions on the use of traditional terms listed in the regulation, in some instances granting exclusive use of a term to an EU wine in a manner akin to treating it like intellectual property. Traditional terms are, for the most part, terms used with certain other expressions (often geographical indications) to describe wine or liqueur, and in many cases the terms are merely descriptive (e.g., ruby and tawny). The United States does not recognize the concept of traditional terms as a form of intellectual property, nor is this a form of intellectual property recognized by the WTO Agreement on Trade-Related Intellectual Property Rights (TRIPS).

EU authorities began fully enforcing the new regulation in March 2004. Amendments to the original regulation fail to address key U.S. industry concerns, including restrictions on the use of certain wine terms, bottle shapes and labeling information on non-EU origin wines.

Whey Protein Tariff Reclassification

In October 2004, the Customs Code Committee of the European Union approved a tariff classification for whey protein isolate (WPI), a product that accounts for approximately 25 percent of annual U.S. dairy product exports to the EU. Previously, individual Member States had applied a different classification to WPI and had issued "binding tariff information" to particular importers confirming that classification. As a result of the decision by the Customs Code Committee, Member State binding tariff information applying the former classification had to be revoked. The effect of the Customs Code Committee's classification decision was to increase to 30 percent (from 3 percent) the rate of duty applied to U.S. exports of WPI, substantially eliminating meaningful access to the EU market. This decision was adopted despite the existence of valid binding tariff information issued by one EU Member State to classify WPI in the 3 percent duty classification. The information issued by that State should have been binding on all EU Member States with respect to the importer to whom it had been issued. The U.S. has raised concerns with the EU about the lack of transparency surrounding the decision and the factors behind the change in classification for this product. This is an example of one of the problems with EU customs administration as described above on which the United States requested consultations under WTO dispute settlement procedures.

Bananas

Under the terms of agreements that resolved the long-running U.S.-EU dispute regarding trade in bananas, the EU is required to institute a new import regime no later than January 1, 2006. This new regime is to replace the existing system of tariffs and license-based quota arrangements with a system based exclusively on tariffs. The EU's initial tariff proposals, tabled in late 2004, implied a significant increase in the tariff applied to non-preferential suppliers of bananas to the EU market. The United States is concerned that any new tariff-based import regime should uphold the EU's multilateral commitment to at least maintain total market access for non-preferential banana suppliers. While the United States does not directly export bananas to the EU, this is an issue of considerable importance to U.S. companies involved in the production, distribution, and marketing of bananas.

Market Access Restrictions for U.S. Pharmaceuticals

U.S. pharmaceutical companies encounter persistent market access problems throughout countries of the European Union, due to the price, volume, and access controls placed on medicines by national governments. In most cases, Member State governments administer medicine reimbursement programs as part of their healthcare programs that cover a significant segment of the market. The procedures for getting a product on the reimbursement list and the price controls for those that are on the list have a strong impact on U.S. exports. These price controls limit access by patients to innovative products and diminish the contribution of Europeans to pharmaceutical research and development.

While the EU's single market ensures that pharmaceuticals, like other goods, can move freely across borders among EU Member States, Member States' controlled prices vary greatly from one country to another, allowing intermediaries to buy medicines in countries where the price is lower and sell them in others where the price is set at a higher level.

Austria: A pharmaceutical firm seeking to include a product on the list of reimbursable drugs without prior authorization must first obtain the approval of the umbrella organization of social insurance funds (Hauptverband/HVB). This overly bureaucratic approval process limits market access for innovative pharmaceutical products. U.S. companies operating in Austria report cumulative losses between $25 million and $100 million due to these practices. The Austrian government is preparing a major health care reform that may bring Austria closer to European norms in pharmaceuticals pricing and the transparency of decision-making on reimbursement approvals.

Belgium: Pharmaceutical companies consider Belgium among the most inhospitable markets for their sector in Europe. Taxes, pricing policies, and patient access problems discourage investment in research and development. Despite promises by the Belgian government to industry in 2003 that pharmaceutical price controls would be lifted, prices on pharmaceuticals reimbursed through the Belgian healthcare system remain at well below European averages. There is also strong government pressure on doctors not to prescribe drugs under patent. Further, in addition to the turnover and profit taxes applied exclusively in this sector, pharmaceutical companies are required to reimburse most of the chronic gaps between budgeted and actual government spending on pharmaceuticals. In combination, these tax measures amount to a 10 percent to 11 percent additional levy on the sector.

Cyprus: Cyprus imposes strict price controls on local drug prices, including on non-prescriptive and over-the-counter drugs. In December 2004, the government announced that effective March 2005, it would reduce prices by 26 percent of pharmaceuticals sold in the private sector, which are consumed by 40 percent – 45 percent of the population.

Czech Republic: U.S. and European pharmaceutical companies complain that the process of setting reference prices for reimbursement of medicines prescribed by the national health insurance system lacks transparency and limits market access for patented medicines. Reimbursement levels are set at the price of the lowest-priced medicine in each therapeutic category, which is usually a generic, and is often a domestically produced product. In many cases, the entry of a generic drug onto the market immediately results in a sharply reduced reimbursement price. Low-priced pharmaceuticals from the Czech Republic are beginning to be sold in other EU Member States, affecting pharmaceutical companies' sales in those countries.

Denmark: The Danish government has failed to provide reimbursement for new innovative medicines; typically, new drugs do not appear on the list for at least five years after their introduction elsewhere in Europe. Within the context of the Danish socialized health system, this discourages the sale and use of such medicines. The Danish Medicines Agency is seeking to expand the use of restrictive reimbursement standards, apparently without objective and verifiable criteria, which increases U.S. industry's concerns about the lack of transparency and possibilities for discrimination. Industry estimates that if these barriers were lifted, U.S. exports would increase by around $10 million.

Finland: Innovative pharmaceutical companies in Finland have raised concerns that government regulations have resulted in an uncompetitive environment marked by pricing regulations that place low ceilings on pharmaceutical prices and limit the price differentials allowed between generic and innovative products. Further, industry claims that it takes more than three years for a pharmaceutical product to be approved for full reimbursement under the national insurance scheme.

France: The government that assumed office in 2002 has taken steps to accelerate the approval process and make prices for the most innovative medicines more comparable to those in other European markets. At present, however, France's health care provisions are still based on a 1997 law. The government is actively urging lower use of pharmaceuticals and the increased use of generics, and is imposing significant price cuts on pharmaceuticals.

Germany: As part of a broader health-care reform package, Germany introduced a reference pricing scheme on January 1, 2005. U.S. pharmaceutical companies have raised serious concerns about the transparency and fairness of the decision-making process and the new pricing scheme, which does not appropriately value innovative medicines. The U.S. Government has raised this issue with Germany.

Hungary: The Hungarian government and pharmaceutical companies signed a contract in June 2004 which ended a price freeze and returned prices to the March 2004 levels that existed before the last price cut. The government promised no more price freezes until December 31, 2006. In exchange, producers agreed to make payments into a subsidy fund, which were matched by funds from the government. The government also agreed to annual increases in its health budget by five percent in 2005 and 2006.

Italy: U.S. companies have raised concerns about Italian government measures that they believe will have a deleterious impact on their business there. Among these are: (1) an across-the-board decrease in reimbursement prices for almost 300 drugs now on the reimbursement list; (2) an increase in the amount that industry must "pay back" to the central government for regions' annualized overspending on pharmaceuticals; and (3) additional discounts on certain classes of drugs that will disproportionately disadvantage U.S. research-based companies. U.S. companies have been seeking a dialogue with the Italian government to improve transparency in Italy's cost-containment measures and to factor in the impact of those measures on U.S. industry.

Lithuania: The U.S. pharmaceutical industry has voiced concerns about Lithuania's low drug reimbursement rates. Lithuanian health insurance law requires that manufacturers' prices of medicines cannot exceed by more than five percent the price of the lowest "adequate" medicine in the European Union. The low reimbursement rates have driven several U.S. pharmaceuticals out of the market.

The Netherlands: U.S. pharmaceutical companies in the Netherlands have raised concerns about price ceilings in the Dutch pharmaceutical law and that the criteria used by the Dutch health insurance board (CVZ) to determine reimbursement levels often incorrectly classifies their new-to-market products. Industry has also voiced concerns that the CVZ procedures have resulted in considerable and unnecessary delays in classifying products for reimbursement.

Poland: The Polish government alleges that foreign pharmaceutical companies charged excessive margins for drugs and owe hundreds of millions of dollars in fines under a 2000 - 2002 ordinance related to pharmaceutical pricing. This ordinance was subsequently struck down by Polish courts. Poland has thus far ignored requests for EU arbitration of this issue, which could threaten the existing investments of foreign innovative pharmaceutical firms in Poland. In addition, the Health Ministry has not approved new drugs for the government reimbursement list since the late 1990s.

Portugal: Portugal's system for approving pharmaceuticals to be included in the reimbursement list is one of the slowest in Europe. Industry is also concerned about debt of more than $1 billion owed to the healthcare system by the government, which affects the timeliness of payments to patients.

Spain: Pharmaceuticals must go through an approval and registration process with the Ministry of Health that takes several years, unless previously registered in an EU Member State or with the London-based EU pharmaceutical agency, delaying entry of innovative pharmaceuticals into the Spanish market. Further delays are caused by a lengthy administrative pricing process plus onerous government reimbursement procedures. Many U.S. pharmaceuticals sold in Spain are still protected under the former pharmaceutical process patent regime, and thus effective patent protection for these drugs is limited.

A July 2002 regulation requires consumers to obtain special approval from a state inspector before pharmacies can fill prescriptions for two specific drugs produced by U.S. pharmaceutical manufacturers. This measure resulted in sharply decreased sales for both drugs. In 2003, the regional government of Andalucia followed suit and imposed a special approval requirement on all anti-psychotic drugs, which affected several U.S. pharmaceutical companies. Industry is further concerned that there may be an additional negative impact from the 2003 Spanish Law of Cohesion, which dictates which drugs will be covered by reference prices. It remains unclear how innovative drugs will be treated under this law.

Slovenia: A November 2003 regulation requires health professionals to prescribe medicines with the lowest price in their group as stated on a specific list. These are the only medicines that are fully reimbursed under the state insurance plan. This system creates significant advantages for local manufacturers of generic drugs.

Uranium Imports

The United States is concerned that EU import policies may restrict the import into the EU of enriched uranium, and possibly downstream goods such as nuclear fuel and nuclear rods and assemblies. Since 1992, the EU has maintained strict quantitative restrictions on imports of enriched uranium to protect its domestic producers. Since 1994, these restrictions have been applied in accordance with the terms of the Corfu Declaration, a joint European Council and European commission policy statement, which has never been made public or notified to the WTO. The Corfu Declaration appears to impose explicit quotas for imports of enriched uranium, limiting imports to only about 20 percent of the European market. The United States has raised concerns about the import quotas and the non-transparent nature of the Corfu Declaration and its application. Further, the United States is closely monitoring whether any future EU agreements with Russia under negotiation in the nuclear area will follow WTO rules on import quotas and transparency.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

Overview

With the decline of traditional transatlantic trade barriers, EU regulatory measures are increasingly viewed as impediments for U.S. exporters of manufactured and agricultural products. Compliance with divergent technical regulations and standards for products sold in the United States and the EU imposes additional costs on U.S. exporters (e.g., duplicative testing, product redesign) and increases the time required to bring a product to market. Such costs for U.S. exporters are compounded by lack of transparency in the development of EU regulations and a lack of meaningful opportunity for non-EU stakeholders to provide input on draft EU regulations and standards. To address these systemic concerns, the United States continues to promote greater U.S.-EU regulatory cooperation and enhanced transparency in the EU regulatory system.

Despite often sharing similar regulatory objectives, U.S.-EU dialogue frequently is unable to resolve promptly regulatory-based trade problems. In particular, the EU's growing use of a so-called precautionary principle to restrict or prohibit trade in certain products, in the absence of full scientific justification for doing so, is viewed by many U.S. exporters as a pretext for market protection. Further, EU regulatory barriers are often compounded by multiple and/or overlapping measures affecting particular products. Wine, poultry, and agricultural biotechnology products are examples of products that confront multiple layers of restrictive regulation in the EU marketplace. To illustrate:

- U.S. efforts to reopen the EU to U.S. poultry exports have been hindered by multiple obstacles. As a result, resolution of any one obstacle (e.g., the EU allowing the use of alternative antimicrobial treatments on poultry meat) would not necessarily result in reopening of trade due to the existence of other obstacles (e.g., requirements regarding on-farm practices for raising poultry).

- U.S. wine exporters are confronted not only by the uncertainty surrounding the EU's restrictions based on wine-making practices, but also by high tariffs, heavy subsidization of EU wine producers, and cumbersome certification and labeling requirements.

- U.S. exporters of agricultural biotechnology products have been harmed not only by the *de facto* moratorium on approving new products, but also by the existence of certain legally-questionable Member State prohibitions on products already approved for marketing within the European Community.

Standardization

Given the large volume of U.S.-EU trade, EU standardization work in regulated market segments is of considerable importance to U.S. exporters. A number of problems continue to impede U.S. exports, including: 1) delays in the development of EU standards; 2) delays in the drafting of harmonized legislation; 3) inconsistent application and interpretation by EU Member States of legislation; 4) overlap among Directives dealing with specific product areas; 5) gray areas between the scope of various Directives; and, in some cases, 6) reliance on design-based, rather than performance-based, standards. In addition, there are concerns related to the respective procedures, responsibilities (e.g., accountability, redress) and transparency in the Member States, the European Commission and the European standards bodies that require careful monitoring and more frequent advocacy efforts. The following examples illustrate the type of standards-related problems affecting U.S. exporters.

Gas Connector Hoses: The European Standardization organization, CEN, drafted a standard for gas connector hoses based on design specifications, which impedes access to the EU market for a U.S. product. The U.S. manufacturer has had considerable difficulties trying to participate in the standardization process. CEN has not been able to provide a credible technical basis for the requirement that only fixed and/or welded connections can be considered to be safe methods for gas hose connectors. Both U.S. industry and the U.S. Government have argued in favor of a performance-based standard for years, and the U.S. Government has persistently raised its concerns with national CEN members and Commission officials to press for more transparency and performance criteria in the CEN standardization process.

Pressure Equipment: In May 2002, the EU Pressure Equipment Directive (PED) entered into force, imposing new requirements on manufacturers of such equipment. Previously, pressure equipment manufacturers could demonstrate conformity based on standards for material specifications, including the U.S. ASME Code. Manufacturers using the ASME Code may now be excluded from the EU market because the European standards incorporate material specifications slightly different from those found in the ASME Code. In the absence of a full set of harmonized EU standards, the PED permits manufacturers to file for an EAM (European Approval of Materials); however, few requests for EAMs have been approved so far. Another option, the Particular Material Appraisal (PMA), is a costly process for which there are no clearly defined procedures in the PED. In light of these factors, U.S. manufacturers seek continued acceptance of ASME materials that have been widely used in Europe for decades prior to the PED. In an effort to bring the two sides closer together, the U.S., EU and stakeholders met during 2004. As a first step, both sides agreed to a pilot project to eliminate redundant testing requirements for materials. The two sides are aiming to make concrete progress on this issue during the first quarter of 2005.

Care Labeling Standard: The U.S. apparel industry has raised concerns about care labeling requirements for textile and apparel products sold within the EU. There is no harmonized EU legislation that requires care labeling when exporting to the EU, although individual Member

States may have specific requirements. However, if a care label is attached it should incorporate care symbols, which are published in the European standard EN 23758 (1994). These symbols are trademarked and their use is regulated by GINETEX, a European-based association. Requirements for the use of the GINETEX care symbols differ by EU Member State, and in some countries may require a membership fee or royalty payment. The fees involved with the use of the GINETEX care symbols can be costly to U.S. firms and the differing use requirements in Member States can be confusing and burdensome. At the same time, the use of care labels on textile and apparel products is recommended since the manufacturer can be held liable under the EU Product Liability Directive if a problem occurs.

Agricultural Biotechnology

Since 1998, it has proved impossible to assemble in the European Council a qualified majority of EU Member States in support of agricultural biotechnology product approvals, despite the lack of any legitimate health or safety reason to reject them. Therefore, after lengthy periods of consideration by the Council, in each case, approval applications have been sent back to the College of Commissioners for final adjudication. The Commission subsequently did approve these applications, the first in the EU since the 1998 approvals moratorium took hold.

In May 2003, the United States initiated a WTO dispute settlement process related to the EU's *de facto* moratorium on approvals of biotechnology products and on the existence of individual Member State marketing prohibitions on previously approved biotechnology products. Since that time, an initial round of consultations was held, followed by the formation of a panel to consider the case. The first panel meeting was in June 2004. A second panel meeting is expected in February 2005, with a final report expected in the spring or summer of 2005. Despite the individual produce approvals noted above, the United States sees no evidence that the *de facto* moratorium by certain Member States has been lifted.

Several Member States, including Austria, Luxembourg, and Italy, have imposed marketing bans on some biotechnology products despite existing EU approvals. After over five years in some cases, the European Commission has begun to take steps to overturn these bans. Despite the lack of scientific justification for these bans, the Council regulatory committee refused to lift them in December 2004. The proposal asking the Member States to lift the bans will be considered by the Council of Ministers in early 2005. The Council can either adopt or reject the Commission's proposal. If no decision is taken, the proposal returns to the Commission who can then adopt it. If adopted by the Commission, the Member States in question would have to repeal the national bans.

In accordance with DG Agriculture's guidance document on the co-existence of biotechnology and conventional crops, which recommends a regional approach to co-existence issues, a number of Member States, including Denmark, Germany, and three regions in Austria, have drafted new co-existence laws. These laws have taken a maximalist approach, requiring extensive liability systems be put in place and mandating extremely low thresholds for the presence of material derived from biotechnology. Once enacted, the European Commission may initiate infringement proceedings against a Member State's co-existence law if it is judged to be incompatible with EU law. However, there is no time limit on how quickly the Commission must act.

Traceability and Labeling: In April 2004, EC Regulations 1829/2003 and 1830/2003 governing the approval, traceability and labeling of biotechnology food and feed became effective. The regulations include mandatory traceability and labeling for all biotechnology and downstream products. Among the traceability rules are requirements that information that a product contains or consists of biotechnology products must be transmitted to each operator throughout the entire supply chain. Operators must have a standardized system in place to keep information about biotechnology products and to identify the operator by whom and to whom it was transferred for a period of five years from each transaction. The labeling requirements include an obligation to label appropriate products genetically modified and to indicate if the food is different from its conventional counterpart in composition, nutritional value, intended use or health implications. U.S. exporters fear that the practical effect of such labeling requirements will be to drive EU consumers away from such products. In some cases, these burdensome directives have already severely restricted market access for U.S. food suppliers, because food producers have reformulated their products to not use biotechnology products in them. Food producers have indicated concern about needing to find expensive or limited alternatives. The Directives generally are anticipated to have a negative impact on a wide range of U.S. exports, including processed food exports.

Austria: Recent amendments to the Austrian Biotechnology Law allow, in principle, the planting of biotechnology crops. However, strict and complicated rules on liability and compensation still represent a *de facto* barrier against all EU-approved biotechnology crops. National ordinances effectively prevent the planting of EU-approved biotechnology crops. Under current Austrian rules, unapproved biotechnology events must not be detected in conventional seeds ("zero tolerance"), but EU-approved events may be present in conventional and organic seeds up to 0.1 percent.

Cyprus: Cyprus has adopted increasingly tough standards, which in some cases exceed EU requirements, regarding biotechnology organisms and products. Biotechnology products that are already licensed in the EU may circulate in Cyprus freely. However, biotechnology organisms must be approved, even if they are already licensed in other EU countries.

France: France is in the process of implementing the new EU Regulations on "Genetically Modified Food and Feed" and Traceability and Labeling. However, it is applying standards that go beyond the EU regulations, for example, requiring additional standards for non-biotechnology labeling. The French government plans to present biotechnology legislation to the French Parliament in early 2005. This bill will include provisions on biotechnology and non-biotechnology co-existence and a proposal to create a new French biotechnology committee to assess biotechnology products at the national level.

Germany: Germany has suspended the approvals for planting certain biotechnology crops. In November 2004, Germany passed its new version of a law related to biotechnology, which went into effect on January 1, 2005. This law contains strict regulations for liability and requires the creation of co-existence regulations. The new law is expected to hinder the importation, use, and development of agricultural biotechnology products. Some biotechnology companies have already decided to stop their agricultural research efforts in Germany.

Greece: Greece has not been responsive to applications to introduce bioengineered seeds for field tests, despite support for such tests by Greek farmers and Greece's agricultural science community.

Hungary: Extensive biotechnology research is taking place in Hungary, and the Hungarian government has allowed field tests for herbicide resistant corn, wheat and other crops. Although Hungary is mandated to adopt all relevant EU biotech legislation, Hungary has not yet prepared the national application rules for the EU biotech regulations on food and feed and traceability and labeling. Hungary's considerable grain and seed business will not open for biotech varieties in the near future.

Italy: There are varying positions on agricultural biotechnology among Italy's Ministries of Health, Agriculture, and Environment. The Ministry of Agriculture is trying to minimize the presence of material derived from biotechnology by imposing extremely rigorous thresholds for seed purity, which further threaten U.S. exports of conventional corn and soybean seed. The stated objective of the Ministry of Agriculture is to disallow any bioengineered presence in seeds. In the case of soybeans used for animal feed, the Ministry of Agriculture allows imported biotechnology beans, since it is unable to meet Italian feed demand from non-biotechnology sources. Italy has not rescinded its ban on four EU-approved bioengineered corn varieties (BT11, MON 810, MON 809, and T25), though an Italian court revoked the decree in late November 2004. Also in November 2004 the Prime Minister's cabinet passed a decree-law on the coexistence of biotechnology, non-biotechnology, and organic crops that bans biotechnology cultivation in Italy through Dec. 31, 2005, by which time each of Italy's regions must devise a regional co-existence plan.

Luxembourg: A corn produced by Syngenta AG remains blocked from access to Luxembourg despite the product's approval by the European Commission in 1997.

Barriers Affecting Trade in Cattle, Beef, Poultry, and Animal By-Products

A variety of EU measures, outlined as follows, have the effect of severely restricting U.S. exports of livestock products to the European Union market.

EU Hormone Directive:

In 1988, the EU provisionally banned the use of substances that have a hormonal growth-promoting effect in raising food-producing animals. This action effectively banned the export to the EU of beef from cattle raised in the United States. The use of hormone implants is approved by the U.S. Food and Drug Administration and is a common practice in U.S. beef cattle production. The United States launched a formal WTO dispute settlement procedure in May 1996 challenging the EU ban. In 1999, the WTO ruled that the EU's ban is inconsistent with the WTO Agreement on Sanitary and Phytosanitary (SPS) Measures because it is imposed without a risk assessment based on scientific evidence of health risks and authorized the United States to impose sanctions on EU products with an annual trade value of $116.8 million.

In September 2003, the EU announced the entry into force of an amendment (EC Directive 2003/74) to its Hormone Directive (EC Directive 96/22). The new Directive recodified the ban on the use of estradiol for growth promotion purposes and extended the provisional bans on the five other growth hormones included in the original EU legislation. With enforcement of this new Directive, the EU argued that it was now in compliance with the earlier WTO ruling.

At present, the United States continues to apply 100 percent duties on $116.8 million of U.S. imports from the EU. In November 2004, the EU requested WTO consultations with the United States on this matter. The United States maintains its WTO-authorized sanctions on EU products, as to date, the United States fails to see how the revised EU measure could be considered to implement the recommendations and rulings of the DSB in this matter.

On December 16, 2004, the EU held consultations with the United States on this issue in Geneva. On January 13, 2005, the EU requested establishment of a panel to consider its complaint against the United States.

Animal By-Products Legislation:

In October 2002, the European Commission approved EC Directive 1774/2002, which strictly regulates the importation of animal by-products not fit for human consumption. The regulation was fully enforced in May 2004. During 2003, intensive technical discussions between U.S. and EU officials successfully addressed some issues and prevented trade disruption for a significant portion (at least $300 million) of U.S. exports to the EU of animal by-products. However, it is estimated that with the publication of the final text, about $100 million of U.S. animal by-product exports to the EU remain adversely affected to some degree. In particular, the United States remains concerned about various outstanding issues for which the EU has not provided risk assessments, such as a ban on the use of dead-in-transport poultry in pet food. The U.S. exports remaining most exposed to this regulation are dry pet food, other animal protein products, and some hides and skins. The regulation could also affect further downstream products such as certain in vitro diagnostic products that may use animal by-products and may not have available alternatives. Some derogations to the directive that facilitate trade also expire in 2005 and must be addressed.

Poultry Meat Restrictions:

U.S. poultry meat exports to the EU have been banned since April 1, 1997 because U.S. poultry producers currently use washes of low-concentration chlorine as an anti-microbial treatment (AMT) to reduce the level of pathogens in poultry meat production, a practice that is not permitted by the EU sanitary regime. U.S. concerns with respect to poultry intensified in 2004 as a result of EU enlargement and the application of EU restrictions in new Member States that had previously allowed entry of U.S. poultry and represented significant U.S. export markets.

In 2004, the United States made significant progress in its work with the EU to address differences between U.S. and EU food safety rules for poultry meat. The European Commission has accepted a U.S. residue program, U.S. water standards, and a U.S. proposal on use of alternative AMT substances. However, the Commission has linked the use of alternative AMTs with adoption by the United States of an integrated production control system that includes specific on-farm good management practices (GMPs). The Commission undertook an audit of the U.S. chicken and turkey meat system in June 2004 and USDA's FSIS responded to the audit, including the issue of GMPs, by December. The United States and the European Union continue to discuss the final details of a series of steps aimed at reopening as soon as possible the EU market to U.S. poultry and turkey meat.

Other Member State Measures:

Denmark: Following a Danish veterinary control regulation from March 2004, Denmark has imposed certification requirements for egg product imports. The Danish view is that the harmonized certificate provided for in Commission Decision 97/38/EC is insufficient for importing egg products to Denmark. According to the Danish Veterinary and Food Administration, Denmark is currently working to advance common EU certificate rules covering this specific area.

Finland and Sweden: The European Commission has granted both Finland and Sweden extensions of the derogations approved in their EU accession agreements, which allow both countries to continue to enforce stricter salmonella control and stricter border control for live animals (quarantine) than that of other EU Member States. These countries also impose strict requirements regarding the importation of fresh (including frozen) meat, ground meat, and meat preparations.

France: Poultry originating from countries that allow the use of compounds incorporating arsenic in poultry feed cannot enter France for human use. As the United States does not ban the use of such compounds, this decree creates a *de facto* ban on exports to France of U.S. poultry meat for human consumption. In addition, national standards impose restrictions on the import of enriched flour, bovine genetics, and exotic meats.

The Netherlands: A proposed Dutch requirement for certification and labeling of wood from sustainably managed forests could have a significant impact on U.S. trade because it requires assessment criteria to be equivalent to one particular certification program (Forest Stewardship Council - FSC) at the exclusion of others. FSC is only one of three certification programs that are widely used in the United States. The legislation also requires a declaration by the authority of the state where the wood is produced. This will be overly burdensome for both producers and governments, and will be extremely difficult, if not impossible, for manufacturers of panel products and other further processed wood products.

The estimated loss resulting from aforementioned certification and labeling requirements to U.S. exporters of wood panel products and processed wood products has been estimated by the industry at between $10 - 25 million annually.

Barriers Affecting Vitamins and Health Food Products

Denmark: A statutory order requires companies to conduct tests on nutrition products for content, including on individual ingredients, which is not required in other EU countries. The tests must be analyzed by a Danish Veterinary and Food Administration (DVFA)-accredited laboratory.

France: France does not apply the recently issued EU Directive on dietetics, and maintains its own restrictive policy and practices with regard to limits in vitamin and mineral composition.

Greece: In implementing the EU Food Supplement Directive, Greece restricted the sale of protein-based meal replacement products to pharmacies and specialized stores, limiting the ability of U.S. companies to sell such products through direct sales.

Spain: Spain has restrictive practices with respect to the use of vitamins and health food products. Since March 2002, Ministry of Health inspectors have raided health food shops and removed 227 different types of health food products from the market. Although the EU passed a new Directive on dietetics, Spain maintains its restrictive policy with regard to limits in vitamin and mineral composition.

Emerging Regulatory Barriers

In addition to the previously mentioned trade barriers arising from EU policies regarding standards, testing, labeling, and certification, the United States has serious concerns about the ongoing development of new regulations that would appear to have serious adverse consequences for U.S. exporters in the future. The United States is actively engaging the European Union with respect to the issues outlined below.

EU Directive on Wood Packaging Material (WPM):

The European Union (EU) was scheduled to implement on March 1, 2005 a new Directive on wood packaging material (wpm) that could affect up to $80 billion worth of U.S. agricultural and commercial exports to the EU that are shipped on wooden pallets or in wood packaging materials. The Directive, published by the European Commission on October 5, 2004, would place a debarking requirement in addition to heat treatment fumigation on wpm from the United States and other countries. The EU Directive, in the absence of a scientific justification, is more restrictive than the international standard established by the International Plant Protection Convention (IPPC), Guidelines for Regulating Wood Packaging Material in International Trade (IPSM-15).

At the October 2004 meeting of the WTO Committee on the Application of Sanitary and Phytosanitary Measures, the United States raised concerns with the EU's new directive on solid wood packing material. Several other Members added their concerns to those expressed by the United States. The EU representative indicated that they would take these concerns to Brussels for consideration. The EU has not provided the United States with any scientific basis for its more restrictive standard. WTO Members are obligated under the WTO Sanitary and Phytosanitary Agreement to have a scientific basis when they impose standards that are more restrictive than international standards. IPPC members, including the EU, approved ISPM-15 to harmonize and safeguard wpm requirements in world trade. IPPC members approved specific treatments and the marking of wpm, but did not support a debarking requirement in the absence of a scientific justification.

European Commission attempts to secure a suspension of the debarking requirement in technical level discussions with the Member States were not successful in 2004 and early 2005. The European Commission made a formal proposal to Member States on February 8, 2005, to suspend the debarking provision. On February 9, 2005, U.S. Trade Representative Robert Zoellick wrote to his counterparts in the 25 Member States encouraging them to support a suspension. The U.S. Department of Agriculture, the U.S. Department of Commerce and key Members of Congress also weighed in with senior European officials on the potential for a debarking requirement to be highly disruptive to U.S. trade with Europe. On February 28, 2005, the European Council of Ministers approved the Commission's proposal to delay the implementation of the wood packaging materials directive for one year (until March 1, 2006). The United States believes that the debarking requirement in the directive ultimately should be withdrawn until there is a science-based risk assessment to support debarking of wpm. The United States will continue to work with the EU on a long-term solution that is based on science and is applied only to the extent necessary to protect plant life or health.

Chemicals:

In October 2003, the European Commission approved its proposal for a massive overhaul of existing EU chemicals regulation. The proposal, called REACH (Registration, Evaluation, and Authorization of Chemicals), would be applicable to approximately 30,000 existing and new chemicals and chemical products. Under this proposed system, chemicals producers and downstream users would be responsible for registering and testing chemicals, conducting risk assessments, and reporting this information to a central agency. Virtually every industrial sector, from automobiles to textiles, could be impacted by the new policy, potentially affecting the majority of U.S. exports to the EU.

While the United States supports the EU's objectives of protecting human health and the environment, this approach appears to be unworkable and could have significant adverse implications for U.S. exports and U.S. jobs in a wide range of industrial sectors. The Commission's proposal could present significant obstacles to trade and innovation, possibly distorting global markets for thousands of products. Many of the EU's trading partners have expressed similar concerns.

The European Council and the European Parliament are in the early stages of examining the proposal under the EU's legislative co-decision process. The U.S. Government continues to underscore the importance of transparency, openness, and accountability throughout the EU regulatory process, as this will contribute to a balanced and cost-effective regulation.

Cosmetics:

In January 2003, the EU formally adopted the seventh amendment to Directive 76/768/EEC on Cosmetics. EU Member States were required to transpose the Directive into national law by January 1, 2004, at which time a series of amendments came into effect. The amended Directive calls for an EU-wide ban on animal testing within the EU for cosmetic products and an EU-wide ban on the marketing/sale of cosmetic products that have been tested on animals, whether such testing has occurred inside or outside the EU. It will prohibit the sale in the EU of U.S. cosmetics products tested on animals as of 2009 or 2013, depending on the type of test, or earlier if an alternative testing method is approved by the European Community. Some EU cosmetics could be prohibited from entering the U.S. market as well under U.S. Food and Drug Administration requirements.

To minimize possible trade disruption, the U.S. Government and the European Commission have embarked on a joint project to develop harmonized, alternative, non-animal testing methods. The project involves cooperation between the U.S. Interagency Coordinating Committee on the Validation of Alternative Methods and the European Center for the Validation of Alternative Methods (ECVAM). The aim is to develop mutually agreeable alternative testing methods that would be submitted to the OECD process for international validation. The validation of alternative methods is a long and expensive process, taking on average seven years. The EC is actively encouraging ECVAM to pursue alternative methods in the near term.

Waste Management (WEEE and RoHS Directives):

In January 2003, the European Union adopted a Directive that focuses on taking back and recycling Waste from Electrical and Electronic Equipment (WEEE). It also adopted a second Directive that addresses restrictions on the use of certain substances in electrical and electronic equipment, such as lead, mercury, cadmium, and certain flame retardants (known as Restrictions on the Use of Hazardous Substances or RoHS). Member States were required to transpose the legislation into national law by August 13, 2004 but so far only a minority of them has done it.

Under the WEEE Directive, producers will be held individually responsible for financing the collection, treatment, and recycling of the waste arising from their new products starting in August 2005. Producers will have the choice of managing their waste on an individual basis or by participating in a collective scheme. Waste from old products will be the collective responsibility of existing producers based on their market share. Under the WEEE Directive, Member States must ensure that a target of at least four kilograms of electrical and electronic equipment per inhabitant per year is being collected from private households. This target is to be met by December 31, 2006 at the latest. The policy is intended to create an incentive for companies to design more environment-friendly products.

Under the RoHS Directive, as of July 1, 2006, the placing on the European market of electrical and electronic equipment containing lead, mercury, cadmium, hexavalent chromium, polybrominated biphenyls, and polybrominated diphenyl ethers will be prohibited, with some limited exemptions. This list of exemptions from the RoHS Directive and the maximum concentration values of hazardous substances allowed under that Directive are currently being discussed by a technical adaptation committee (TAC) of Member States experts. Another issue being discussed by the TAC is the scope of the WEEE and RoHS Directives. This is of critical importance because it can have major financial implications for companies that fall in or out of the scope of the Directives. The United States supports the Directives' objectives to reduce waste and the environmental impact of discarded products, but has expressed concerns that a ban on substances with limited exemptions would adversely affect trade in products where viable alternatives may not exist. Further, the development and implementation of these Directives has lacked clarity, transparency and adequate opportunities for stakeholder input. As an additional concern, the U.S. testing industry argues that the EU has not yet developed test methods for use in conformity assessment of the products covered by these Directives.

Battery Directive:

On November 25, 2003, the European Commission proposed a new EU Battery Directive. The Commission's objective is the mandatory collection and recycling of all batteries that are placed on the EU market. The Commission proposal would not ban nickel-cadmium (NiCd) batteries, but it proposes strict collection and recycling targets for each Member State. For all types of batteries, Member States must ensure that producers finance collection, treatment, and recycling activities.

In April 2004, the European Parliament rejected the Commission's proposal and called instead for an EU ban on lead and cadmium in batteries, including NiCd rechargeable batteries. While MEPs allowed for some exemptions from a general ban, they rejected an exemption for NiCds in power tools. The Commission continues to oppose a ban, arguing that better collection would achieve the same environmental effect but at lower cost.

As of late 2004, the proposal was being discussed in the European Council. There is no agreement within the Council on the specific treatment of NiCd batteries. The Commission will issue a modified proposal, which is expected in the first half of 2005. The proposal will then return to the Parliament for consideration in a second reading.

Energy Using Products (EuP):

In August 2003, the European Commission issued a proposed directive establishing a regulatory framework for the setting of eco-design requirements for Energy Using Products (EuP). Moving rapidly though the legislative process and wider in scope than any related existing Community legislation, this directive has the potential to create burdensome procedures for manufacturers to prove their product designs are environmentally efficient. The electronics industry in particular has raised concerns with EuP, noting producers already face extensive new regulations on waste management and product design through the WEEE and RoHS Directives. Industry is most concerned about the need for product life cycle analysis, fearing adverse impacts on design flexibility, new product development and introduction, and increased administrative burdens.

Medical Devices: Reclassification of Joint Replacements:

The EC has proposed to reclassify ("up-classify") hip, knee and shoulder joint replacements from class II(b) to class III under Directive 93/42/EEC on medical devices. Such an action could significantly increase the cost and time necessary to obtain approval for these replacements in the EU. The U.S. medical device industry has expressed strong concerns about the lack of transparency in the development of this proposal, including the lack of a comprehensive scientific review of total joint replacements that substantiates the EC's planned up-classification of such products to class III. Industry also notes that the EC's proposed action diverges from regulatory treatment of some of these medical devices in the United States. U.S. orthopedic manufacturers account for approximately 75 percent of the knee implant device market and 50 percent of the hip and shoulder implant devices market in Europe. In light of these concerns, the United States has urged the EC to carefully consider comments from all interested stakeholders and to consult with the U.S. FDA and other international regulatory authorities.

Acceleration of the Phase-outs of Ozone-depleting Substances and Greenhouse Gases:

As part of a wider Climate Change program that started in 1991, Europe continues to try to reduce emissions of greenhouse gases to meet its Kyoto Protocol objectives (i.e., eight percent emission reduction) by 2010. In the fall 2004, EU environment ministers reached preliminary agreement on a legislative package limiting and, in some cases, banning the use of fluorinated greenhouse gases (f-gases). Final adoption will depend on approval by the European Parliament. The agreement was viewed as a step backwards by several Member States, which favor stricter controls. The package includes a regulation on f-gases used in stationary applications and a Directive on fluorinated hydrocarbons (HFCs) in vehicle air conditioning. The first measure will impact U.S. manufacturers of stationary air conditioning and refrigeration equipment and the companies that produce the chemicals used within them. The second will impact U.S. car and parts manufacturers. The stationary regulation seeks to improve containment of f-gases in other applications, by setting minimum standards for inspection and recovery, and, where containment is not feasible, will ban their marketing and use. Examples of banned products using f-gases include vehicle tires, non-refillable containers, windows, footwear, one-component foams, self-chilling drinking cans, novelty aerosols and fire extinguishers. While industry is encouraged by initial resistance to implement product bans, the issue will bear continued monitoring as the legislation is finalized.

The contentious issue in the vehicle air conditioning Directive is the timing of the phase-out of HFC 134a in vehicle air conditioning. Ministers agreed to begin the phase-out in 2011 with a view to securing a complete ban by 2017.

Both proposals will most likely be discussed in the European Parliament in spring 2005, with a view to reaching final adoption within Council and Parliament at the end of 2005. Member States will then have 18 months to transpose the Directive, whereas the regulation will enter into force unchanged. The United States will continue to closely monitor legislative developments and carefully examine the legislation for the impact on business.

Some EU Member States have their own national practices regarding standards, testing, labeling, and certification. A brief discussion of the additional national practices of concern to the United States follows:

Austria: Austria became the second EU country after Denmark to ban a range of uses of the three fluorinated gases controlled under the Kyoto protocol on climate change. An ordinance that took effect on November 22, 2002, prohibits the use in new sprays, solvents, and fire extinguishers of hydrofluorocarbons (HFCs), perfluorocarbons , and sulphur hexafluoride. The ordinance phases out their use in foams between mid-2003 and the end of 2007. It bans their use in new refrigeration and air-conditioning equipment by the end of 2007. The ban appears to exempt production of HFCs in Austria for the export market. If the upcoming EU f-gases regulation focuses on containment instead of bans, the government of Austria has indicated it will try to retain its own national HFC bans.

Finland: A ban on the importation and sale of new appliances containing hydrochlorofluorocarbons (HCFCs) was imposed on January 1, 2000, and remains in place. The importation of the chemical HCFC is allowed when used for maintenance of old appliances using HCFC. New HCFC compounds used for maintenance of refrigeration equipment will be banned as of 2010 and use of all HCFC compounds, including recycled compounds, will be banned as of 2015.

Germany: The German government has contemplated its own legislation to restrict the use of F-gases and is currently studying the European Commission's proposal, to determine whether to adopt this regulation directly into national legislation or to make national legislation on f-gases that is more restrictive than the EU proposal.

GOVERNMENT PROCUREMENT

In an effort to open government procurement markets within the Member States, the EU in 2004 adopted a revised Utilities Directive (2004/17), covering purchases in the water, transportation, energy, and postal services sectors. Member States must implement the new Utilities Directive by the end of January 2006.

This Directive requires open, objective bidding procedures (a benefit for U.S. firms) but still discriminates against bids with less than 50 percent EU content that are not covered by an international or reciprocal bilateral agreement. The EU-content requirement applies to U.S. suppliers of goods and services in the following sectors: water (production, transport, and distribution of drinking water), energy (gas and heat), urban transport (urban railway, automated systems, tramway, bus, trolley bus, and cable), and postal services. The Directive reportedly excludes the entire telecommunications sector, which would appear to waive the EU content requirement for U.S. suppliers of telecommunications equipment. U.S. Government agencies are analyzing the impact of the new Directive on U.S. complaints and retaliatory sanctions dating back to 1993 concering discrimination against U.S. firms in the EU telecommunications equipment market. The Directive's discriminatory provisions were waived for heavy electrical equipment manufactured in the United States under the May 1995 Memorandum of Understanding (MOU) on government procurement between the United States and the EU.

Member States have their own national practices regarding government procurement. In some cases, they require offsets, or obligations that require companies to provide services, create jobs, or purchase local goods as a condition for the contract's award. A brief discussion of some of the national practices of particular concern to the United States follows:

Austria: U.S. firms continue to report a strong pro-EU bias and pro-Austrian bias, in government contract awards and some privatization decisions. In major defense purchases, most government procurement regulations do not apply, offset requirements up to 200 percent of the value of the contract are common, political considerations remain important, and transparency remains limited. Austria's largest military procurement to date, the $2 billion purchase of fighter jets in 2002, continues to be a source of concern regarding its lack of transparency, an apparent bias against a U.S. proposal, and flawed offset deals related to the purchase.

France: France has a strong and extremely competitive aerospace and defense manufacturing base. Despite limited privatization, the French government continues to maintain shares in several major prime contractors. The French defense market remains generally closed to non-European competition, and even in the case of European competition, French companies are often selected as prime contractors. The Defense Ministry, which handles around 70 percent of the equipment budget, has a tendency to select a non-American solution even if it costs more and takes longer to market. These factors have made it difficult for U.S. defense firms to take part in French/European programs.

Greece: U.S. suppliers of defense material and services express concern that firms from other EU Member States are favored over U.S. firms in competitions for procurement contracts. U.S. firms believe that they are more likely to win defense procurement agreements if they partner with EU firms. Greece continues to insist on offset agreements as a condition for the purchase of defense items. A lack of transparency in procurement procedures and severe budgetary problems are also hampering U.S. firms' ability to win procurement awards. In the defense sector, in particular, U.S. companies have urged the Greek government to upgrade and extend the life of existing systems to save costs.

Ireland: Government procurements in Ireland generally are tendered under open and transparent procurement regulations. U.S. companies have raised concerns, however, that few of them have been successful in competing for infrastructure-related procurements under Ireland's National Development Plan (2000-2006) and regional government tenders. U.S. firms claim that procurements are delayed because budgetary decisions can take a long time and that unsuccessful bidders often have difficulties in getting fully debriefed on the rationale behind the tender outcome. Once awarded a contract, companies can experience significant delays in finalizing contracts and commencing work on the contract.

Italy: Italy's government procurement practices have created obstacles for U.S. firms. This is particularly true in the case of the Italian government's procurement of civilian helicopters, which a U.S. company has alleged favors a competing Italian supplier. This procurement has been challenged both in Italian administrative courts and at the EU level. Other cases under consideration by the European Commission have propelled Italy to make progress in increasing the transparency of its procurement laws and regulations and update its public procurement laws to be more in line with EU Directives.

An agency of Italy's Finance Ministry (CONSIP) manages procurements of all goods on behalf of public administration entities and issues tenders that stipulate framework agreements for specific products and services with suppliers that win the tenders. Framework agreements are executed between a supplier and CONSIP, but the eventual business transaction for a specific product or service is between the supplier and the ordering government entity. CONSIP monitors to ensure that transactions are carried out correctly. U.S. firms have mixed views on the effectiveness and transparency of CONSIP's operations. Reportedly, its role is gradually being diminished.

Lithuania: Lithuanian Government Resolution No. 918 of July 15, 2003 requires offset agreements as a condition for the award of contracts for procurement of military equipment exceeding $1.9 million.

Slovenia: U.S. companies continue to express concern about the transparency of the public procurement process in Slovenia. Many U.S. bidders report that European bidders are favored and usually win contract awards despite their higher bids and questions regarding those companies' ability to deliver on the terms of the tender. This has been a problem particularly in telecommunications and medical equipment procurements.

United Kingdom: There is an ongoing pattern in UK military procurements of engines and other propulsion systems of awarding contracts without competitions and overturning decisions that selected a U.S. supplier and the awarding of the contract to the domestic supplier, Rolls-Royce.

U.S. Participation in EU External Assistance Programs

The United States is concerned that, in most cases, U.S. companies and nationals are not eligible to compete to provide goods and services that are part of the extensive assistance programs that the EU provides to candidate countries such as Romania and Bulgaria, and soon to Croatia and Turkey. Participation in these tendering procedures is limited to EU Member State natural and legal persons and to natural and legal persons who are nationals of the beneficiary third country.

Among such programs are: (1) the Special Accession Programme for Agriculture & Rural Development (SAPARD), which finances agricultural and rural development measures; (2) PHARE, which aims to strengthen institutions and public administrations; and (3) Instruments for Structural Policy for Pre-Accession (ISPA), which finances major environmental and transport infrastructure projects. In addition, in Southeast Europe (Albania, Croatia, Bosnia Herzegovina, Federal Yugoslav Republic of Macedonia, Serbia, and Montenegro), the EU administers the Community Assistance for Reconstruction, Development and Stabilization (CARDS) program.

SAPARD, for example, had an overall budget of 560 million euros for the candidate countries until 2003. (Contracting is expected to continue in 2005 with payments due to run until 2006). For Romania and Bulgaria, SAPARD has an annual budget of 225 million euros. As part of the CARDS program, the EU has allocated 4.6 billion euro for projects in Southeast Europe through 2006.

EXPORT SUBSIDIES

Government Support for Airbus

Since the inception of Airbus in 1967, the governments of France, Germany, Spain, and the United Kingdom have provided billions of euros in subsidies to their respective Airbus member companies to aid in the development, production and marketing of Airbus civil aircraft. These governments have provided more than $15 billion in launch aid to finance all or a large portion of the development costs for all Airbus aircraft models and provided other forms of support, including equity infusions, debt forgiveness, debt rollovers, and marketing assistance, including political and economic pressure on purchasing governments. The EU's aeronautics research programs are driven significantly by a policy intended to enhance the international competitiveness of the European civil aeronautics industry. EU governments have spent hundreds of millions of euros to create infrastructure needed for Airbus programs, including 751 million euros from the City of Hamburg to create land that Airbus is using for the Airbus A380 "superjumbo" project and 182 million euros from French authorities to create the AeroConstellation site, which contains the Airbus facilities for the A380. With more than $6 billion in subsidies, the Airbus A380 is the most heavily subsidized aircraft in history.

After 30 years, the Airbus Integrated Company - successor to the original Airbus consortium and representing a partnership of the European Aeronautic, Defense, and Space Company (EADS) (80 percent equity share) and BAE Systems (20 percent equity share) - is now the second largest aerospace company in the world. With more than half of the new large civil aircraft sales worldwide over the last few years, Airbus is a mature company that should face the same commercial risks as its global competitors. The longstanding European rationale for Airbus subsidies – that they are necessary to bolster an infant industry – has clearly ceased to reflect marketplace realities.

In 2004, longstanding concerns over the past subsidization of Airbus and new concerns that Airbus would seek subsidies for yet another new Airbus plane led the United States to seek the negotiation of a new agreement to end subsidies for the development and production of large civil aircraft. After discussions over the spring and summer made it clear that the EU was reluctant to pursue such a goal, the United States requested consultations at the WTO with respect to the launch aid and other forms of subsidies that EU governments have provided to Airbus. Concurrent with the U.S. consultation request, the United States also exercised its right to terminate the 1992 U.S. – EU bilateral agreement on large civil aircraft. The U.S. concerns over the subsidization of Airbus were validated when Airbus executives subsequently declared publicly that Airbus was seeking additional launch aid subsidies to support a new aircraft program known as the A350.

In January 2005, the United States and the EU reached agreement on the terms for a bilateral negotiation that would end subsidies for the development and production of large civil aircraft. The negotiations have a three month time limit. The United States and the EU have agreed that, during the negotiations, neither side will commit any new government support for large civil aircraft (such as the proposed Airbus A350), and each side would refrain from taking additional steps in the WTO process.

The United States is committed to eliminating further subsidies to Airbus, either through the negotiation of a new agreement, or through WTO dispute settlement.

Government Support for Airbus Suppliers

Belgium: The Federal Government of Belgium, in coordination with the three regional governments, subsidizes Belgian aircraft component manufacturers that supply parts to the Airbus Integrated Company. In November 2001, the Belgian federal government reached an agreement with the three regional governments, usually responsible for R&D and investment promotion, on a 195 million euro package for aviation research and development for Airbus A380 components. Belgium claims the program was structured in accordance with the 1992 bilateral agreement, and covers non-recurrent costs. According to Belgian industry sources, about 160 million euros remains available of this amount, and the costs covered to date have netted orders worth 1.3 billion euros for the A380. The Belgian federal government says it has discontinued an earlier Belgian exchange rate subsidy program.

France: In addition to the 1.3 billion euros in reimbursable advances, spread out over several years, for development of the Airbus A380 super-jumbo aircraft, the government of France has committed to provide an additional 59 million euros in reimbursable advances to other aero-structure companies, which have concluded supplier partnership agreements with Airbus for development of the A380 airframe. France's 2005 government budget appropriates 330 million euros toward its A380 reimbursable advance program, to be disbursed to French companies Airbus, Latécoère, Socata and Aircelle. In addition to R&D, specific funds (32 million euros in 2005 and 34.5 million euros in ongoing programs) are earmarked for the development of on-board avionics and structural systems for the Airbus A380 and the Dassault Falcon F7X, a long-range business jet.

Spain: The recently completed Puerto Real factory in Spain's Andalucia region is responsible for constructing 10 percent of Airbus' new A380 aircraft. Spain's Ministry of Science and Technology currently subsidizes A380 construction through its agreement to provide 376 million euros in direct assistance through 2013. To date, the ministry has provided 92.5 million euros of that obligation. Furthermore, the regional government of Andalucia has channeled an additional 13 million euros of State General Administration regional incentive funds and 17.5 million euros of its own funds to subsidize the A380 project.

Government Support for Aircraft Engines

United Kingdom: Since 1988, the UK government has committed 949 million pounds to direct product development of Rolls-Royce civil aircraft engines. Despite Rolls-Royce's substantial market share during this period, the UK government has been repaid only 314 million pounds. This amount would not appear to cover the cumulative interest expense on equivalent commercial debt over the period, let alone provide a return on the loan's principal.

In February 2001, the UK government announced its intention to provide up to 250 million pounds to Rolls-Royce to support development of two additional engine models for large civil aircraft, the Trent 600 and 900. The UK government characterized this engine development aid as an "investment" that would provide a "real rate of return" from future sales of the engines.

The European Commission announced its approval of a 250 million pounds "reimbursable advance" without opening a formal state investigation into whether the advance constituted an illegal (under EU law) state aid. According to a European Commission's statement, the "advance will be reimbursed by Rolls-Royce to the UK government in case of success of the program, based on a levy on engine deliveries and maintenance and support activity." Detailed terms of the approved launch aid were not made public. To date, none of the launch aid for the Trent 600 and 900 has been repaid.

As the United States noted in last year's NTE report, continuing UK government support of Rolls-Royce raises serious concerns about UK and EU adherence to the WTO SCM Agreement. U.S. engine suppliers have lost sales of engines and claim that they have encountered suppressed prices in the United States and world markets.

France: The French government-owned engine manufacturer SNECMA will receive 102 million euros in support under a royalty-based system authorized by the European Commission for SNECMA's development work on a family of large engines.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The EU and its Member States support strong protection for intellectual property rights (IPR), and the importance of protecting IPR was highlighted at the U.S.-EU summit in June 2004. During 2004, the European Commission approved a commendable strategy for the enforcement of IPR in third countries through a number of mechanisms including multilateral and bilateral agreements, political dialogue, technical cooperation, and dispute settlement. There is scope for increased U.S. – EU cooperation on the protection of IPR in third countries.

There are several Member States with whom the United States has raised concerns either through the U.S. Special 301 process or through WTO Dispute Settlement procedures about their failure to fully implement the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). The United States continues to be engaged with the EU and individual Member States on these matters.

In April 2004, the EU adopted a Directive on the enforcement of intellectual and industrial property rights, such as copyright and related rights, trademarks, designs, or patents. This

Directive requires all Member States to apply effective and proportionate remedies and penalties that form a deterrent against those engaged in counterfeiting and piracy. Member States are required to have a similar set of measures, procedures, and remedies available for right holders to defend their IPR. The Directive includes procedures covering evidence and measures such as injunctions and seizures. Remedies available to right holders include the destruction, recall, or permanent removal from the market of illegal goods, as well as financial compensation, injunctions, and damages. There is a right to information allowing judges to order certain persons to reveal the names and addresses of those involved in distributing illegal goods or services, along with details of the quantities and prices involved. Under the Directive, Member States will have to appoint national correspondents to cooperate and exchange information with other Member States and with the Commission. The Directive takes on additional importance because of the expansion through EU enlargement of the EU's borders to the east, which moves them closer to countries such as Russia that have been a persistent source of pirated CDs and DVDs. Member States, including the ten new Member States, have until April 2006 to implement the Directive.

Copyrights

In April 2001, the EU passed a Directive (known as the Copyright or "Information Society" Directive) to harmonize aspects of the copyright law and implement the WIPO Internet Treaties. Some Member States, such as Belgium and Spain have failed to meet the December 2002 deadline to implement the directive. In July 2004, the European Commission published a working paper on the EC's legal framework in the field of copyright and related rights. This working paper will frame the debate for possible amendments to European copyright law during 2005.

Designs

The EU adopted a Regulation introducing a single Community system for the protection of designs in December 2001. The Regulation provides for two types of design protection, directly applicable in each EU Member State: the registered Community design and the unregistered Community design. Under the registered Community design system, holders of eligible designs can use an inexpensive procedure to register designs with the EU's Office for Harmonization in the Internal Market (OHIM). The holders will then be granted exclusive rights to use the designs anywhere in the EU for up to twenty-five years. Unregistered Community designs that meet the Regulation's requirements are automatically protected for three years from the date of disclosure of the design to the public. Protection for any registered Community design was automatically extended to the 10 new EU Member States on May 1, 2004.

The European Commission has proposed amending the legal protection of designs Directive (98/71) by removing Member States' option to maintain design protection for "visible" replacement vehicle parts, such as hoods, bumpers, doors, lamps, rear protection panels, windscreens and wings. The proposal would allow independent part manufacturers –not linked to the producers of finished vehicles - to compete throughout the EU market for visible replacement parts. Neither non-visible parts, like engine or mechanical parts, nor components in new vehicles would be affected by the proposal.

Patents

Patent filing and maintenance fees in the EU and its Member States are significantly higher than in other countries. Fees associated with the filing, issuance, and maintenance of a patent over its life far exceed those in the United States.

In October 2004, the European Commission proposed a regulation to allow manufacturers of generic pharmaceuticals to produce medicines under patent for export to countries in need that cannot produce sufficient quantities themselves. The regulation would implement within the EU an August 2003 WTO decision, under which national authorities can grant compulsory licenses for such production if certain conditions are fulfilled. One requirement is that the destination country must have notified the WTO that it is seeking the medicine covered by the license. To help ensure that medicines get to the patients who need them and to protect patent holders, customs authorities will be able to prevent the re-importation into the EU of medicines produced under the system. The proposed regulation would set up a system for companies that wish to manufacture medicines for export to apply to national authorities for the grant of a compulsory license from a patent holder that has exclusive rights over the manufacture and sale of the products concerned. Before coming into effect, the proposed regulation would have to be discussed and approved by EU Member States and the European Parliament.

In some countries, such as Slovakia and Portugal, copies of medicines which are still under patent are allowed on the market by the ministries of health which fail to coordinate with their domestic patent offices.

Data Exclusivity: In some of the new Member States in particular, there is a lack of protection for data submitted to obtain marketing approval for pharmaceutical and agricultural chemical products. Such protection is required by Article 39.3 of the Trade-Related Aspects of Intellectual Property (TRIPS) Agreement.

Hungary: Hungary's 2001 ministerial decree related to the protection of test data took effect on January 1, 2003. Retroactive protection exists for pharmaceutical products that received first marketing authorization in the EU or Hungary on or after April 12, 2001. The decree is only retroactive to April 12, 2001, not January 1, 2000, as required by TRIPS.

Poland: Although Poland is required to implement the EU data protection regime as part of its entry into the European Union, concerns remain over its request to delay implementation for 15 years. In addition, while the government has signaled that it is considering implementation of a coordination mechanism between the Health Ministry and the patent agency, no concrete actions have been taken to do so.

Portugal: Pharmaceutical firms continue to be adversely affected because there is no cross-check for pre-existing patents before market access for drugs is granted. Due to significant back-logs in the court system, legal recourse is time consuming and expensive. It can take several months to obtain an injunction against continued production of a copy of a patented pharmaceutical product. Final rulings can take years, resulting in high legal fees and lost income for U.S. firms.

Slovakia: The Ministry of Health (MOH) has approved for sale a generic version of a U.S. company's drug that was protected by a patent. Further, the confidential product information that must be submitted to the MOH to have drugs registered for sale in Slovakia is stored in the facilities of a local generic drug competitor. Despite requests by U.S. companies for MOH to identify a secure location, the MOH has allowed the confidential data to remain on the premises of the competitor.

Patenting of Biotechnological Inventions

A 1998 EU Directive (98/44) on the legal protection of biotechnological inventions harmonizes EU Member State rules on patent protection for biotechnological inventions. Although Member States were required to bring their national laws into compliance with the Directive by July 2000, at the end of 2004, some had not yet fully met that obligation, and the European Commission has started legal proceedings at the European Court of Justice against them.

Austria: In January 2004, the European Commission sued Austria for not implementing the 98/44 Directive. The Austrian government has sent a draft bill to the Parliament that would implement the Directive, but it is uncertain when Parliament will pass the bill.

France: France has not yet brought its national law into compliance with Directive 98/44. The French government's draft bill transposing the Directive into national law was presented to the Senate in October 2001, but was not brought to debate until late 2004, only after the European Court of Justice condemned France in July 2004 for not taking action. The French proposal allows plant breeders making varietal selections to freely use (protected) plant varieties to create new varieties.

Trademarks

Registration of trademarks with the European Union's Office for Harmonization in the Internal Market (OHIM) began in 1996. OHIM issues a single Community trademark that is valid in all 25 EU Member States.

Madrid Protocol: On October 1, 2004, the European Community acceded to the World Intellectual Property Organization (WIPO) Madrid Protocol, establishing a link between the Madrid Protocol system, administered by WIPO, and the Community Trademark system, administered by OHIM. Community Trademark applicants and holders now are allowed to apply for international protection of their trademarks through the filing of an international application under the Madrid Protocol. Conversely, holders of international registrations under the Madrid Protocol will be entitled to apply for protection of their trademarks under the Community trademark system.

Geographical Indications: The United States has long had concerns that the EU's system for the protection of geographical indications, reflected in Community Regulation 1493/99 for wines and spirits and Regulation 2081/92 for certain other agricultural products and foodstuffs, appears to fall short of what is required under the TRIPS Agreement.

In a report issued on December 21, 2004, a WTO panel agreed with the United States that the EC's regulation on food-related geographical indications (GIs) is inconsistent with the EC's obligations under the TRIPS Agreement and the GATT 1994. This report results from the United States' long-standing complaint that the EC GI system discriminates against foreign products and persons - notably by requiring that EC trading partners adopt an "EC-style" system of GI protection - and provides insufficient protections to trademark owners. In its report, the panel agreed that the EC's GI regulation impermissibly discriminates against non-EC products and persons and agreed with the United States that the regulation could not create broad exceptions to trademark rights guaranteed by the TRIPS Agreement. The panel recommended that the EC amend its GI regulation to come into compliance with its WTO obligations. The United States requested WTO dispute consultations on this regulation in June 1999. On August 18, 2003, the United States requested the establishment of a panel, and panelists were appointed on February 23, 2004. The panel's report was circulated to WTO Members and the public on March 15, 2005.

Member State Practices:

Belgium: Domestically pirated and parallel-imported DVDs are a growing problem in Belgium. An industry trade association estimates that 250,000 illegal downloads of DVDs occur daily, and illegal copies on VHS, CD-R and DVD-R media are distributed by specialty stores, retail outlets, and local and international Internet sites. The recording industry estimates that 85 percent of blank digital media sold in Belgium are used for illegal downloads of music or videos. Annual losses to the U.S. motion picture industry through IPR piracy in Belgium are estimated at over 15 million euros. The Belgian Anti-Piracy Foundation (BAF) has focused chiefly on the purchase of hard goods, but increasingly works to combat illegal Internet distribution. It reports that Belgium's 1994 Copyright Law provides deterrent penalties for piracy, but that legal procedures are cumbersome and the court system is overburdened, discouraging action to combat IPR fraud. Obtaining a judicial restraining order against Internet piracy, for example, takes two to three months. Belgian judicial action appeared to increase in 2004, and judgments in favor of IFPI and rights collectors may provide helpful precedents. The Belgian government has still not implemented with Belgium the EU Copyright/"Information Society" Directive.

Cyprus: IPR legislation in Cyprus is, on the whole, modern and comprehensive, although enforcement should be further improved. Cyprus has harmonized its IPR regime with EU requirements as part of its accession to the EU in 2004. Optical media piracy can be described as moderate but rising, characterized by in-house duplication by DVD rental shops. Audio piracy (mainly CDs) remains fairly constant. Software piracy, largely fueled by small PC assembly and sale operations paying little attention to software licensing regulations, has reached 55 percent.

France: Although the French government has stepped up its efforts to fight piracy, video piracy and unauthorized parallel imports continue to impose significant losses on U.S. industry, and cable piracy and Internet piracy present further problems in this area. In June 2004, the government launched: 1) an ambitious plan to collaborate with Asian countries on combating piracy; 2) a customs national action plan that beefs up customs training and places French government anti-piracy personnel in embassies abroad; and 3) an interagency "tracking center" called "Tracfin" that gathers information on sales and manufacturing of counterfeit products and their links with organized crime. The government also is funding a large-scale public anti-piracy and counterfeiting campaign aimed at businesses and consumers.

Finland: In early 2004, Finland's Ministry of Social Affairs and Health (MoSAH) began preparing legislation that would extend the time that brand name drugs are protected from competition by generic alternatives. Research based pharmaceutical companies, legislators and civil servants at MoSAH and Ministry of Trade and Industry are working closely together to produce a report to the Minister of Social Affairs and Health by the end of 2004. Some forward movement is expected in early 2005.

Germany: Non-retail outlets (Internet, print media, mail order, open-air markets) represent Germany's major piracy problem. Pirated videos, VCDs, and DVDs are sold primarily by residential mail-order dealers who offer the products via the Internet, newspaper advertisements, or directly sell them in flea markets. German copyright legislation allows the making of private copies, which, although it does not include sharing or downloading of music, has been sometimes misunderstood as being a broader exception than it actually is. German authorities in several cases have prosecuted pirates who download music and videos from the Internet and then distributed burned CDs or DVDs and made a major arrest of four persons in October 2004 who ran a major ring selling pirated videos on the Internet. The German government in July 2003 enacted amendments to the German Copyright Act intended to bring it in line with the EU Copyright/"Information Society" Directive. The Ministry of Justice has introduced additional amendments to the copyright law that are likely to be considered by parliament in 2005. U.S. publishers have expressed a concern that these amendments might result in insufficient protections for the copyrights of works, particularly in digital format. The United States is watching this issue closely

Greece: Although Greece has made progress in reducing the illegal broadcast of unlicensed films, problems involving copyrighted products and trademarks still exist, especially in the sound recording and software sectors. The United States looks to the Greek government to strengthen its enforcement of laws governing the protection of copyrights and trademarks and is encouraged by recent efforts, particularly in Thessaloniki, to conduct raids and seize pirated CDs and DVDs.

Hungary: On January 1, 2003, Hungary acceded to the European Patent Convention and has amended the Hungarian Patent Act accordingly. Act CII of 2003 modified the Hungarian Copyright Act and the Hungarian Design Act in order to bring all these laws fully in line with the relevant European legislation. The Hungarian Patent Office implemented the EU Copyright/"Information Society" Directive. In October 2004, Hungary implemented Council Regulation 1383/2003 concerning customs action against goods suspected of infringing certain intellectual property rights. Further, a government decree established a customs task force to accept claims from producers whose trademarks or copyrights were violated or infringed.

Italy: Although Italy has a robust set of anti-piracy laws on the books, the lack of enforcement remains a serious concern. There is still no coordination of anti-piracy efforts at the national level. As a whole, Italy's judiciary has failed to impose meaningful sanctions against pirates and counterfeiters. This has discouraged local police and prosecutors from pursuing cases of IPR theft. Despite occasional crackdowns, street vendors openly sell pirated CDs, DVDs, and computer software in Italian cities. The sale of counterfeit designer handbags and other merchandise is also very common, particularly in tourist areas.

In 2004, the Italian Parliament approved a government decree known as the Urbani Decree to criminalize the unauthorized sharing of copyrighted material over the Internet. The decree introduced criminal penalties for illegal file sharing and levies on reproduction equipment. It also creates a certification of legality to be posted by Italy's collecting society SIAE on legal Internet sites, which is strongly opposed by the software industry. As of March 2005, Italy's parliament was considering revisions to the Urbani Decree that would eliminate the levies and the certification requirements, but would also weaken the Decree's criminal provisions against file sharing. In response to film and music industry concerns that such a change would encourage more Internet piracy. The parliament was also considering a measure to write the criminalization of unauthorized file sharing into Italy's main copyright law.

Lithuania: Although Lithuania amended its Copyright Law in 2003 to bring it in line with the EU Copyright/"Information Society" Directive, penalties for confiscated pirated software and media worth less than $4,800 remain low and the investigative process remains slow. The CD piracy rate in 2003 was already high at 55 percent - 85 percent of all sales. Ineffective border enforcement also remains a serious concern because Lithuania, given its geographical location, is a major transshipment area for pirated goods. However, to Lithuania's credit, the number of pirated CDs seized in 2004 increased fourfold. The software piracy rate in 2003 (58 percent) was also high. Lithuania has not yet brought its national law protecting biological inventions into compliance with EU Directive 98/44.

Poland: Poland has shown progress on several elements of IP protection. As a result of EU accession, Poland published amendments to its copyright law on April 30, 2004 and the amendments contained several improvements which had been proposed by the copyright-related industries. Poland also published an Optical Disc Decree on June 2, 2004, although concerns over the lack of criminal sanctions remain. The Polish government has increased antipiracy efforts, improving enforcement at the Warsaw Stadium and invigorating its Interministerial Antipiracy Group. Poland has also made some progress in strengthening border enforcement, although problems remain particularly along the Eastern borders.

Spain: Copyright infringement has become an increasing problem in Spain's major urban centers. Street piracy remains a serious issue, although authorities are conducting raids. With respect to copyright, industry representatives stress the importance of Spain passing implementing legislation for the WIPO Internet treaties and the EU Copyright Directive because Internet piracy is becoming an increasingly serious problem. There is also a need to improve the tracking of imports of blank CDs.

Sweden: U.S. copyright industries have raised concerns about a provision in Swedish copyright law that denies to authors and producers of U.S. audiovisual works, and to the performers that appear in those works, the right to be compensated for private reproductions. Taxes collected by a levy on blank tapes are distributed to Swedish authors and producers but not authors and producers from the United States. U.S. industry questions the consistency of this practice with Sweden's national treatment obligations under the Berne Convention and its national treatment and MFN obligations under the TRIPS Agreement. The Swedish government has promised to rectify this issue (the so-called blank-tape levy issue) through the process of adopting the EU Copyright/"Information Society" Directive. The Swedish Parliament will most likely address this issue in the spring of 2005, with a first possible date of entry into force on July 1, 2005.

SERVICES BARRIERS

Concerns Related to EU Enlargement

On May 28, 2004, the European Commission notified members of the World Trade Organization of a proposed consolidation of the EU's schedule of specific commitments under the General Agreement on Trade in Services (GATS) pursuant to GATS Article V to reflect both the 1995 accession to the European Union of Austria, Finland, and Sweden, and the 2004 accession of Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, the Slovak Republic, and Slovenia. As a result of this proposed consolidation, a number of previous GATS commitments by these countries have been modified in a way that may reduce sector-specific or horizontal market access commitments. Although not within the scope of the GATS Article V notification, the consolidation also entails the extension of most-favored nation exemptions reflected in the EU's schedule of GATS commitments. As provided for under GATS rules, the United States has engaged in initial consultations with the European Commission to evaluate possible adverse consequences to U.S. services trade of the consolidation and the potential for EU compensation to the United States for such consequences. The two sides plan to consult further on this issue.

Television Broadcast Directive (Television without Frontiers Directive)

The 1989 EU Broadcast Directive (also known as the Television without Frontiers Directive) includes a provision requiring that a majority of television transmission time be reserved for European-origin programs “where practicable and by appropriate means.” All EU Member States, including the ten new Member States, have enacted legislation to implement the Broadcast Directive. It remains important to ensure that the flexibility built into the Directive is preserved and that individual broadcasting markets are allowed to develop according to their specific conditions and needs.

The European Commission is currently reviewing the Directive. As a result of consultations held with stakeholders in 2003, the Commission adopted in April 2004, a communication on the future of the European regulatory audiovisual policy, calling for more legal certainty on television advertising and an update on the protection of minors, among other issues.

Several EU Member States have specific legislation that hinders the free flow of some programming. A summary of some of the more salient restrictive national practices follows:

France: France continues to apply its more restrictive version of the EU Broadcast Directive, which was first introduced into French legislation and approved by the European Commission in 1992. In implementing the Directive, France chose to specify a percentage of European programming (60 percent) and French programming (40 percent), which exceeded the requirements of the Broadcast Directive. Moreover, these quotas apply to both the 24-hour day and prime time slots, and the definition of prime time differs from network to network. The prime time rules are a significant barrier to access of U.S. programs to the French market.
In addition, the United States continues to be concerned that broadcasts of American music are limited by radio broadcast quotas (40 percent of songs on almost all French private and public radio stations must be Francophone), which have been in effect since 1996.

Italy: 1998 legislation making Italy’s TV broadcast quota stricter than the EU Broadcast Directive remains in effect. It makes 51 percent European content mandatory during prime time, and excludes talk shows from the programming that may be counted toward fulfilling the quota. A 1998 regulation requiring all multiplex movie theaters of more than 1,300 seats to reserve 15 percent to 20 percent of their seats, distributed over no fewer than three screens, to showing EU films on a stable basis also remains in effect. In May 2004, Italy enacted controversial media reform through the so-called Gasparri Law, under which the media/communications market is viewed broadly as one sector. Under this law, no single operator may receive more than 20 percent of overall revenues from the entire sector. In addition, the law provides for the gradual privatization of the state-owned radio and television broadcasting conglomerate, RAI.

Spain: Spain's theatrical film system has been modified sufficiently in recent years so that it is no longer a major source of trade friction. Government regulations issued in 1997 require exhibitors to show one day of EU-produced film for every three days of non-EU-produced film. Spanish law requires that the quotas issue be reviewed in 2006.

Postal Services

United States express and package service providers remain concerned that postal monopolies in many EU Member States restrict their market access and create unfair conditions of competition with the incumbents. In October 2001, EU Member States agreed to open additional postal services to competition beginning in 2003, including all outgoing cross-border mail. Depending upon the results of a European Commission study (scheduled to be completed by the end of 2006), full liberalization of the EU postal market could occur by 2009.

Belgium: U.S. companies continue to express concern that the government-owned Belgian Railways and Belgian Post cross-subsidize their divisions that provide package and express delivery services. The future of these publicly-owned companies remains unclear. The European Commission continues to examine a 140 million euro bridging loan that Belgian government extended to one of the companies.

Germany: In October 2004, the European Commission initiated a treaty infringement procedure against Germany for failing to mandate that the German postal monopoly, Deutsche Post, offer unbundled access to competitors. Some U.S. companies have indicated they might be interested in providing services such as sorting.

Professional Services

In the area of professional services, there are significant variations among EU Member State requirements for foreign lawyers and accountants intending to practice in the European Union. While many of these are not outright barriers, disparities among Member State requirements can complicate access to the European market for U.S. lawyers and accountants.

Legal Services

Austria: U.S. citizens can only provide legal advice on U.S. law and public international law (excluding EU law) on a temporary basis. Only an Austrian or other EU national can join the Bar Association. U.S. nationals cannot represent clients before Austrian courts and authorities and cannot establish a commercial presence in Austria. However, informal cooperation with Austrian partners is possible.

Finland: Foreigners from non-EU countries cannot become members of the Finnish Bar Association and receive the higher law profession title of Asianajaja (Attorney at Law). Persons holding the title of Asianajaja are subject to Asianajaja Law as well as bar regulations. While the title gives added prestige and helps solicit clients, it is not essential to practice domestic or international law or to represent a client in court.

France: Non-EU firms are not permitted to establish branch offices in France under their own names. Also, non-EU lawyers and firms are not permitted to form partnerships with or hire French lawyers.

Germany: U.S. lawyers that have joined the German Bar Association under their home title may practice international law (but not EU law) and the law of their home country. To be admitted to the bar to practice German law, individuals generally have to complete five years of study and two years of practical training.

Hungary: Foreign non-EU lawyers may provide legal advice on legislation of their own country and international law. Lawyers registered in the EU may be admitted to the bar. Foreign lawyers from non-EU countries may establish a partnership with a Hungarian legal firm and provide legal services under a "cooperation agreement."

Ireland: In general, lawyers with non-Irish qualifications who wish to practice Irish law and appear before Irish courts must either pass transfer examinations or retrain as lawyers under the direction of the Law Society of Ireland. Only lawyers who have either been admitted to the Bar of England, Wales, or Northern Ireland, practiced as an attorney in New York, California, Pennsylvania (with five years experience required in Pennsylvania), or New Zealand, or have been admitted as lawyers in either an EU or EFTA Member State are entitled to take the transfer examination.

Italy: In 2001, Italy passed a law implementing EU Directive 98/5 on EU lawyers' freedom to establish themselves EU-wide and enabling Italian lawyers to practice jointly, including with EU lawyers, through a limited liability partnership or through the Italian branch of a partnership formed in another EU Member State, as long as the limited liability partnership is composed exclusively of Italian and EU lawyers. The status of non-EU lawyers is not explicitly addressed by the law. This omission leaves the status of international law firms with offices in Italy uncertain, insofar as they have Italian and non-EU lawyers as partners.

Lithuania: U.S. attorneys face higher licensing requirements in Lithuania than their EU counterparts. To practice in Lithuania, a U.S. lawyer must pass the Lithuanian bar examination in the Lithuanian language. EU lawyers, by contrast, have only to enroll in the Lithuanian bar, provide proof of nationality and qualifications in their home countries, and work in association with Lithuanian lawyers on Lithuanian cases during their initial three years of practice in-country.

Slovakia: Effective January 1, 2004, Act No. 586/2003 (the Advocacy Act) forces non-EU-based law firms to change their legal status from a branch partnership to a limited liability company (LLC). An LLC must be owned by an EU advocate registered in Slovakia or a Slovak national. As a result, non-EU law firms cannot market themselves under their internationally recognized corporate identities and incur extra costs to comply with the special rules.

The law also requires non-EU-based lawyers and law firms to register with the Slovak Bar Association to practice law in Slovakia. In 2004, no U.S. attorneys have been able to register. The United States is concerned that the Slovak Bar consistently has tried to limit foreign lawyers' ability to practice law in Slovakia; the Advocacy Act appears to facilitate their ability to deny them registration.

Accounting and Auditing Services

France: There is a nationality requirement for the establishment of a practice, which can be waived at the discretion of the French authorities. An applicant for such a permit, however, must have lived in France for at least five years.

Greece: U.S. access to the Greek accounting market remains limited. A 1997 Presidential decree established a method for fixing minimum fees for audits and established restrictions on the use of different types of personnel in audits. It also prohibited auditing firms from doing multiple tasks for a client, thus raising the cost of audit work. The Greek government has defended these regulations as necessary to ensure the quality and objectivity of audits.

Hungary: Only a Hungarian-certified accountant may conduct audits, but this individual may work for a foreign-owned firm.

Architectural Services

The U.S. National Council for Architectural Registration Boards and the E.U. Architect's Council of Europe are currently working to develop a foreign diplomat recognition agreement that would be valid for all 25 EU Member States.

Austria: Only citizens from EU and EEA Member States are eligible to obtain a license to provide independent architectural services in Austria. The European Communities' Schedule of Specific Commitments under the GATS does not list any limitations on the supply of architectural services on a cross-border basis or through a commercial presence. Austria's refusal to permit the licensing process to proceed for non-EU/EEA citizens seeking to establish a commercial presence appears to be inconsistent with Austria's GATS commitments on market access and national treatment.

France: To operate in France, architects are required to obtain French architectural degrees recognized by the French government or obtain equivalency.

Insurance Services

Estonia: The Estonian Insurance Activities Act, which requires branches of non-EU insurance companies to keep committed assets in Estonia, may form an obstacle for U.S. companies seeking to open branch operations in Estonia. Estonia presents particular limitations because of the small size of the local market and the lack of government debt there.

Commercial Air Services

The United States currently has liberalized bilateral open skies agreements with 15 of the 25 EU Member States: Austria, Belgium, the Czech Republic, Denmark, Finland, France, Germany, Italy, Luxembourg, Malta, Netherlands, Poland, Portugal, Slovakia, and Sweden. The U.S. has no agreement with Cyprus, Estonia, Latvia, Lithuania, and Slovenia; more limited agreements with Greece, Hungary, Ireland and Spain; and a particularly restrictive agreement with the United Kingdom. In the absence of a broader, comprehensive agreement with the European Union, the United States will continue to seek more liberalized arrangements with willing and like-minded EU partners.

Ireland: The U.S.-Ireland Air Transport Services Agreement requires U.S. and Irish carriers to match every flight to/from Dublin with a flight to/from Shannon. This arrangement compels U.S. airlines that serve Dublin to bear the costs associated with additional mandatory service to Shannon. These costs have deterred a number of U.S. carriers from entering the Irish market.

The United Kingdom: Under the highly restrictive 1977 "Bermuda II" agreement between the United States and the UK, the UK limits access to London's Heathrow airport to only two U.S. carriers, United and American Airlines, and two British carriers, British Airways and Virgin Atlantic. The agreement further limits U.S. cities eligible for non-stop service to London and caps entry in most markets to one U.S. and one UK carrier, making the U.S.-UK agreement one of the most restrictive agreements the United States has with any aviation partner.

Telecommunications Market Access

Both the WTO Basic Telecommunications Agreement and the EU's regulatory framework for telecommunications services have spurred liberalization and competition in the European telecommunications sector. Under the WTO Agreement, for example, all EU Member States made commitments to provide market access and national treatment for voice telephony and data services. However, liberalization and harmonization have been uneven across the Member States. In many markets, significant problems remain with the provisioning and pricing of unbundled local loops, line sharing, co-location, and the provisioning of leased lines. Partial government ownership of some Member States' incumbent telecommunications operators also has the potential to raise problems for new entrants.

In 2002, the EU issued a new regulatory framework for electronic communications that includes a Framework Directive, which defines the role of National Regulatory Authorities (NRAs). It also promulgated four specific Directives on: (1) licensing; (2) access and interconnection; (3) universal service and user rights; and (4) data protection. Member States were required to implement the new rules in 2003.

This new regulatory framework updates and adapts European legislation to account for converging technologies and for future technological and market developments. It applies to all forms of electronic communications networks and associated services, not just traditional fixed telephony networks. The long-term goal is to phase out sector-specific, *ex-ante* regulation (for all but public interest reasons) in favor of reliance on general competition rules. The Commission has identified 13 Member States that need either primary or secondary legislation to implement the new regulatory framework.

Member State Practices: Enforcement of existing legislation by the National Regulating Authorities (NRAs) appears hampered by unnecessarily lengthy and cumbersome procedures in France, Italy, Austria, Portugal, among others. The European Commission also found that incumbents in Germany, Greece, Spain, Italy, Ireland, Austria, Finland, and Sweden have slowed the arrival of competition by systematically appealing their national regulators' decisions despite the fact that in most cases the appeals are not successful.

Austria: In general, Austria has moved toward a more open and competitive telecommunications market and has transposed the relevant directives. There are several outstanding concerns related to the: (1) wholesale leased line market; (2) the market for PSTN transit services; (3) phone spectrum allocation; (4) interconnection fees; (5) lack of definition for the wholesale broadband access market (including bitstream access); and (6) restricted telecommunications infrastructure access to buildings. Generally, the NRA provides timely initial decisions, but follow-up on NRA decisions, including the appeals process for such decisions, remains uncertain and slow.

Belgium: Belgium has not yet transposed the new EU Regulatory Framework mentioned above. The legislation is pending in Parliament and is expected to be passed by May 2005. Businesses complain of excessively high Mobile Termination Rates (MTR). The NRA sets the MTRs for the two mobile providers with the largest market share, but does not regulate the smallest provider. Implementation of the new Regulatory Framework will give BIPT the authority to regulate MTRs from all three mobile providers.

Finland: The Finnish government implemented a comprehensive reform effort, called the Communications Act, in July 2003, which aimed to improve the legislative environment for competition and the development of communications technology and innovations. The Act implements four new Directives on electronic communications. Internet Service Providers are also included in the scope of the Act. According to the Act, specific requirements will be applied to telecommunications operators with significant market power. Regulation of smaller operators is less stringent. The NRA will determine if there is not enough competition within a particular market and institute what it sees as remedial requirements.

France: The French NRA adopted a new organization structure in February 2004. France also implemented the EU Telecommunications Framework Directive in June 2004. This should increase competition and remove barriers in the French market. The new law substantially increases the powers of the NRA, by allowing it to impose greater fines and take action to gather evidence.

The French government continued to further privatize France Telecom, bringing state ownership of the company to below 50 percent. The company still dominates the fixed line market and is a major player in mobile services and Internet services through its subsidiaries Orange and Wanadoo.

Questions about fair competition still beset France's impressive growth in unbundled broadband connections. The NRA and France Telecom are still sparring over pricing at the retail and wholesale levels, with the NRA complaining of predatory pricing at the retail level and overpricing at the wholesale level. This pricing has made market entry difficult for new players.

French unbundled shared local loop tariffs are the lowest in Europe, but high fixed-to-mobile (F2M) rates still subsidize mobile telephony and the building of fiber optic networks for broadband. The NRA recently mandated a 25 percent cut in F2M rates. However, this reduction does not include calls initiated in other countries. In addition, France Telecom, the dominant fixed line carrier, is challenging this in court.

Germany: Germany has made slow progress in introducing competition to some sectors of its telecommunications market. However, new entrants continue to face difficulties competing with the partially state-owned incumbent Deutsche Telekom AG (DT), which retains a near-monopoly in a number of key services, including local loop and broadband connections. On the positive side, since 2003 implementation of carrier selection and pre-selection for local calling has helped competitors gain close to 20 percent of the local calling market. The revised Telecommunications Act entered into force in June 2004 and most competitors to DT believe that it allows a structure that should provide for enhanced competition. Currently, the NRA is studying how it should regulate individual market segments.

Throughout 2004, competitors charged that DT continued to engage in a variety of anticompetitive practices. In January 2004, several telecommunications trade associations and private firms filed complaints with the U.S. Government under Section 1377 of the Omnibus Trade and Competitiveness Act of 1988. The submissions asserted, *inter alia,* that: 1) timely interconnection remained a problem; 2) DT's unbundled rates were not cost-oriented; 3) DT's broadband monopoly remains unchallenged; and 4) DT and other mobile providers charge excessive termination charges when fixed-line users call mobile phones. In June 2004, DT and other mobile producers agreed on a voluntary reduction of these fixed-to-mobile termination charges over 2004 and 2005. While other providers welcomed this as a step in the right direction, some questioned if the reductions go far enough.

Hungary: The Hungarian telecommunications market is almost fully liberalized. However, legal obstacles, as well as lack of investors do not help competition. The Deutsche Telekom owned Matáv Group managed to keep its leading position in all areas of telecommunications (including mobile). UPC and TELE2, as new-fixed line providers, launched their services offering lower tariffs than Matav. The number of fixed line subscriptions is constantly decreasing. Mobile phone penetration reached 80 percent with three providers on the market (T-Mobile, Pannon GSM, Vodafone).

Ireland: The government privatized the state monopoly, Telecom Eireann, in 1999, but the new company, Eircom, retains an 80 percent share of the fixed lines in Ireland and dominates leased line services and national interconnection. Thus, while there are currently 48 operators authorized to provide publicly available telephone services/fixed telephony in the Irish market, these new entrants only account for a total of 20 percent of the fixed line market. Competition has significantly reduced prices for international business and residential calls, while the price for local service remains high, discouraging both broadband development and Internet use. Only 2 percent of the population has broadband, and the government has cited the need for Eircom to reduce local loop unbundling charges further to promote competition and innovation in the DSL market.

Significant competition is now emerging in the mobile phone market, with three licensed and active operators. The mobile penetration rate in Ireland in 2004 was 89 percent; there are 3.5 million mobile subscribers. Ireland has adopted EU local loop unbundling legislation, committed to full liberalization of access to and the tariff rates for the last mile of telephone lines in 2001.

Italy: Despite the progress in liberalizing the overall telecommunications market, and even though it sold off its residual three percent share in the Telecom Italia, the Italian government is still able to maintain influence. The State also exerts influence over other companies, as well. For example, the government holds a controlling interest in ENEL, the national electricity conglomerate that in turn owns Italy’s second largest telecommunications company WIND.

Lithuania: The Lithuanian government may soon issue a tender for a two-way radio system to guard Lithuania's external border that would require use of the EU's TETRA standard. The selection of TETRA may block some potential U.S. companies from competing in the tender, although others manufacture compatible equipment.

Luxembourg: Luxembourg has yet to adopt the EU’s Electronic Communications legislation. Infringement proceedings in the European Court of Justice have been brought against Luxembourg. Luxembourg’s state-owned Post and Telecommunications company continues to dominate its telecommunications market. Despite a 1998 court ruling opening Luxembourg's small mobile phone market to competition, the market remains dominated by only two companies, one of which is partially-owned by the state company.

Slovenia: Slovenia has harmonized its telecommunications legislation with EU law, but it has failed to properly implement the EU Communications Framework, citing the need to introduce new Slovenian by-laws. This underscores the lack of efficiency and transparency in the domestic legal process. These factors, combined with late or non-responses from regulating bodies and lengthy appeal procedures have disadvantaged a U.S. wireless provider. The company claims that the unfair pricing practices of Mobitel, the subsidiary of state-owned Telekom Slovenije, has hampered its ability to compete. The company has filed claims of unfair competition and violations of the Slovenian Telecommunications Act with the Competition Protection Office and the Slovenian Telecommunications Agency. To this date the company has not received a reply.

Spain: Leased lines in Spain remain problematic because rates are not based on actual cost. Despite actions by the NRA, wholesale prices are still above the European average and approximately 100 percent above U.S. prices. This has allowed the incumbent operator Telefónica to offer services to customers at substantially lower rates than competitive carriers, which must lease lines from Telefonica at a higher wholesale rate.

Spanish mobile operators charge excessive mobile termination rates. U.S. operators active in this market are squeezed out from the fixed-to-mobile communications markets, because mobile operators offer their subscribers mobile-to-mobile and fixed-to-mobile calls at below wholesale rates. Spanish anti-trust authorities are considering penalizing these providers.

Evolution of the broadband market has been slow and problematic, and many operators have ceased offering these services. Although Telefónica's market share is slowly being reduced, their continued dominance precludes new entrants from operating on a commercially viable basis in Spain. Competitors attempting to negotiate nondiscriminatory access directly with Telefónica have been met by refusal from the incumbent, and at times disinterest by the regulator.

Sweden: Sweden implemented the EU Directive on local loop unbundling in 2001. Companies that compete with national incumbent Telia Sonera in the market for broadband access via fixed lines depend on that company for copper access. There have been complaints that Telia Sonera does not conform to the Directive and that competitors have been discriminated against in favor of Telia's subsidiaries. As a consequence, the National Post & Telecommunications Agency (PTS) has ordered Telia Sonera to provide copper access to other players in the same manner as it provides access to its subsidiaries.

United Kingdom: There is limited competition in advanced data services over fixed-line incumbent British Telecom's (BT) infrastructure. The UK's new NRA, Ofcom, was launched in late 2003. Ofcom is seeking to increase BT's competitors' access to BT's wholesale products.

Given the current roll-out of BT's "21st Century Network" – which aims to provide BT customers with converged, multimedia communications services over an all-IP-based network by 2009 – Ofcom believes that expanding access to the network and the operations that support it has additional urgency. Further, Ofcom believes that the UK's initial attempts at local loop unbundling were unsuccessful and is actively seeking a new approach. Ofcom is undertaking a Strategic Review, which is expected to conclude in 2005 with a series of regulatory and policy recommendations for the telecommunications industry.

INVESTMENT BARRIERS

Overview

The European Commission's mandate on investment issues is evolving. Still, in many instances, Member State practices are of more direct relevance to U.S. firms. Under the 1993 Maastricht Treaty, free movement of capital became an EU responsibility, and capital controls both among EU Member States and between EU members and third countries were lifted. A few Member States barriers remain in effect, although in particular cases EU law may supercede these. Right of establishment issues, particularly regarding third countries, is a shared competence between the EU and the Member States. The division of this shared competence varies from sector to sector, based on whether the EU has issued regulations in that sector. Direct branches of non-EU financial service institutions remain subject to individual Member State authorization and regulation. EU Member States negotiate their own bilateral investment protection and taxation treaties and generally retain responsibility for their investment regimes. The EU requires national treatment for foreign investors in most sectors. EU law, with a few exceptions, requires that any company established under the laws of one Member State must, as a Community undertaking, receive national treatment in all Member States, regardless of its ultimate ownership. However, some restrictions on U.S. investment do exist under EU law and others have been proposed (see below).

Ownership Restrictions and Reciprocity Provisions

The right to provide maritime transport services within certain EU Member States is restricted. EU banking, insurance, and investment Directives include reciprocal national treatment clauses, under which financial services firms from a third country may be denied the right to establish a new business in the EU if the EU determines that the investor's home country denies national treatment to EU financial service providers. The right of U.S. firms to national treatment in this area was reinforced by the EU's GATS commitments. The EC Hydrocarbons Directive similarly provides that an investor may be denied a license if its home country does not permit EU investors to engage in activities under circumstances comparable to those in the EU.

Member State Practices

Austria: While European Economic Area (EEA) Member States' banks may operate branches on the basis of their home country licenses, banks from outside the EEA must obtain Austrian licenses to operate in Austria. However, if such a non-EEA bank has already obtained a license in another EEA country for the operation of a subsidiary, it does not need a license to establish branch offices in Austria.

Cyprus: Non-EU residents are restricted to buying only a single piece of real estate for private use not exceeding three donums (around one acre). Exceptions can be made for projects requiring larger plots of land (i.e. beyond that necessary for a private residence) but are difficult to obtain and are rarely granted. A law prohibiting investment in tertiary education by non-EU residents or entities is still in force. However, it is expected that the government will soon lift this restriction as part of its continuing overhaul of tertiary education legislation. Cyprus also restricts non-EU ownership of local mass media companies to five percent or less.

France: Generally, there are no screening or prior approval requirements for non-EU foreign investment. However, as part of a November 2004 law that streamlined the French Monetary and Financial Code, the State Council was directed to define a number of sensitive sectors that would require prior approval for acquisition of a stake (no threshold limit). These areas have yet to be defined, but are expected to include national defense, public safety, nuclear energy, cryptology and nanotechnologies. France continues to apply reciprocity requirements to non-EU investments in a number of sectors. For the purpose of applying these requirements, the French government generally determines a firm's residency based on the residency of its ultimate owners rather than on the firm's place of business or incorporation.

Germany: Germany's takeover law, which came into effect in 2002, has reintroduced measures that allow firms to ward off hostile takeover bids: first, at the stockholder level, where management may be given authority at the annual shareholders' meeting to take measures deemed necessary to guard against unwanted interest; and, second, at the management level, where the managing board can take protective measures upon approval by the supervisory board bypassing the need for stockholder approval altogether. These provisions may have negative consequences for outside investors and stockholders.

Germany passed legislation in July 2004 requiring notification of planned investments by foreign entities to obtain 25 percent or more in German manufacturers of armaments and cryptology technology used for classified government communications. Planned share acquisitions meeting the threshold must be notified to the Federal Economics Ministry for inter-ministerial review. The government can veto such sales within one month of receipt of a notification. The legislation could seriously restrain U.S. and other foreign investors.

Greece: Greek authorities consider local content and export performance when evaluating applications for tax and investment incentives. However, such criteria are not prerequisites for approving investments.

Greece, which previously restricted foreign and domestic private investment in public utilities (except for cellular telephony and energy from renewable sources, e.g., wind and solar), has recently opened its telecommunications market and is in the process of gradually liberalizing its energy sector.

U.S. and other non-EU investors receive less advantageous treatment than domestic or other EU competitors in the banking, mining, maritime, and broadcast industries (which were opened to EU citizens under EU single market rules). There are restrictions for non-EU investors on land purchases in border regions and on certain islands (on national security grounds).

Italy: In conformity with EU Treaty Article 43, Italy provides national treatment to foreign investors established in Italy or another EU member state, except in a few instances. The exceptions include limits on access to government subsidies to the film industry and additional capital requirements for banks from non-EU countries. U.S. and other firms from non-EU countries may operate based on authorization from Italy's equivalent of the U.S. Securities and Exchange Commission (CONSOB). CONSOB may deny authorization to firms from countries that discriminate against Italian firms. Finally, foreign insurance firms must prove that they have been active in life and property insurance for not fewer than ten years and must appoint a general agent domiciled in Italy.

Malta: Maltese law requires that anyone buying residential or commercial real estate must obtain a permit from the Minister of Finance. EU citizens and returning Maltese migrants who have lived in Malta for more than five years receive a waiver from these permits. Non-EU citizens are not entitled to this waiver. Despite the restriction, permission to purchase land for commercial or residential purposes is normally granted. We are not aware of any U.S. businesses that were discouraged from investing in Malta because of these restrictions. The restrictions have, however, delayed certain business investment projects involving American businesses.

Portugal: Most foreign investments in Portugal are only subject to *post facto* registration. However, Portugal retains the discretion to limit foreign investment, on a case-by-case basis, in state-owned companies that are being privatized. To date, this prerogative has not been exercised.

ELECTRONIC COMMERCE

U.S. businesses and the U.S. Government continue to monitor potential problems related to data privacy regulation and legal liabilities for companies doing business over the Internet in the EU.

Exports of Personal Data from the EU

The EU's Data Protection Directive (1995/46) allows the transmission of EU data to third countries only if those countries are deemed by the European Commission to provide an adequate level of protection. U.S. companies can only receive employee and customer information from the EU by using one of the exceptions to the Directive's adequacy requirement, or by demonstrating they can provide adequate protection for the transferred data. These requirements can be burdensome for many U.S. industries that rely on data exchange across the Atlantic.

The U.S. Department of Commerce negotiated the Safe Harbor framework to provide U.S. companies with a simple, streamlined means of complying with the adequacy requirement.
The agreement allows U.S. companies that commit to a series of data protection principles (based on the Directive), and that publicly state their commitment by "self-certifying" on a dedicated website, to continue to receive personal data from the EU. Signing up is voluntary but the rules are binding on those who do. The ultimate means of enforcing Safe Harbor is that failure to fulfill the commitments will be actionable as an unfair and deceptive practice under Section 5 of the FTC Act, or under a concurrent Department of Transportation statute for air carriers and ticket agents.

The USG actively supports the Safe Harbor agreement and encourages the European Commission and Member States to continue to use the flexibility offered by the Data Protection Directive to avoid unnecessary interruptions in data-flows to the United States. Furthermore, we expect the European Commission and EU Member States to fulfil their commitment to inform us if they become aware of any actions that may interrupt data flows to the United States.

Brussels Regulation

The EU adopted a regulation on December 22, 2000, the so-called Brussels Regulation, which allows consumers to sue companies in the court of their country of residence, "when the website is directed to [his/her] Member State or to several countries, including that Member State." Industry claims that the practical effect of this is that companies doing business on the Internet in the EU risk being sued in every EU Member State, as opposed to being subject to the jurisprudence of their country of origin.

OTHER BARRIERS

Agricultural Subsidies

EU shipments of heavily subsidized canned peaches continue to distort world markets to the detriment of U.S. producers. Similarly, EU subsidies for the production of apples, prunes, grapes, wine, cherries, and citrus affect U.S. exports to the EU and globally. Although a 1985

U.S.-EU Canned Fruit Agreement brought some discipline to processing subsidies, significant fraud and abuse have undermined the discipline imposed by the Agreement. Growers and producers of peaches receive a range of assistance from producer aid, market withdrawal subsidies, sugar export rebates, producer organization aid and regional development assistance. The United States will continue to monitor EU subsidies to this sector, evaluate their trade-distorting effects, and monitor other areas of interest to our agricultural sector, for example, horticulture, grains, pork, and beef.

Wood Industry Subsidies

Several EU Member States and regional governments within them provided state aid to pulp, paper and wood processing projects. Germany, in particular, has given aid in the form of grants, loans and loan guarantees for pulp and paper and wood products capacity building, especially in former Eastern Germany. This has added substantial new capacity and has contributed to a substantial drop in U.S. pulp and paper exports to the EU and globally and to a rise in European paper and wood exports to the U.S. and third country markets.

GHANA

TRADE SUMMARY

The U.S. trade surplus with Ghana was $161 million in 2004, an increase of $34 million from $127 million in 2003. U.S. goods exports in 2004 were $306 million, up 46.3 percent from the previous year. Corresponding U.S. imports from Ghana were $145 million, up 77.1 percent. Ghana is currently the 87th largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Ghana in 2003 was $249 million, down from $266 million in 2002.

IMPORT POLICIES

Ghana has progressively eliminated or reduced its import quotas, tariffs, and import licensing requirements through the structural adjustment program it initiated in the early 1980s. The import licensing regime was eliminated in 1989, but some imports, such as pharmaceuticals, mercury, gambling machines, handcuffs, condensed or evaporated milk, arms and ammunition, and live plants and animals require special permits. The tariff system has been simplified and harmonized to match the four tariff levels of the Economic Community of West African States (ECOWAS) trade liberalization program. Under this system, there are four *ad valorem* import duties: 0 percent, 5 percent, 10 percent, and 20 percent. The standard rate of duty is 20 percent. The zero-rate duty continues to apply to agricultural and industrial machinery, solar, wind, and thermal energy, and educational materials. A one percent processing fee applies to duty-free goods, except on education, health, and agriculture sector goods. In 2002, the government increased the duty from 0 percent to 5 percent for imported fish, selected commercial vehicles, and selected building materials. Also in 2002, an additional one percent examination fee was levied on imported used vehicles. Importers are charged 0.04 percent of the sum of the free on board (FOB) value of goods and the value-added tax (VAT) for the use of the automated clearing system, the Ghana Community Network (GCNet). Importers have indicated that they would prefer a flat fee on each transaction.

In 2000, Ghana imposed an additional 0.5 percent ECOWAS duty on all goods originating from non-ECOWAS countries. In 2001, under the Export Development and Investment Fund Act (Act 582), Ghana instituted a 0.5 percent duty on all non-petroleum products imported in commercial quantities. Since the end of 1998, a 12.5 percent VAT has been added to the duty-inclusive value of all imports, with a few selected exemptions. In August 2004, Ghana introduced the National Health Insurance Levy of 2.5 percent, which in effect increases the VAT to 15 percent. Additional excise taxes ranging between 5 percent and 140 percent are applied to malt drinks, water, beer, and tobacco products.

In August 2002, Ghana abolished its 10 percent tax on selected “non-essential” imports in an effort to bring its tariff structure into harmony with ECOWAS and WTO provisions. In February 2003, the government considered adding 20 percent to the existing import duty on rice and poultry products but decided against it following consultations with its trading partners.

However, the government did increase import duties from 10 percent to 20 percent on some imported finished products for which locally manufactured products are available, such as cement, doors, windows and their frames, corrugated iron sheets, and nails. In August 2002, the ban on importing used vehicles that are more than 10 years old was replaced with a system of penalties ranging from 5 percent to 50 percent of the C.I.F. (cost, insurance, freight) value of the used vehicles. All communications equipment is subject to import restrictions. Each year between May and October, there is a temporary ban on the importation of fish, except canned fish, to protect local fishermen during their peak season.

In May 2002, the WTO and Ghana’s Customs Excise and Preventive Service (CEPS) signed an agreement on customs valuation and trade facilitation to simplify customs procedures and facilitate swift clearance of goods. In April 2000, Ghana transitioned from using pre-shipment inspection to a destination inspection scheme. Four inspection companies currently have contracts with the government to perform the destination inspection.

In order to develop competitive domestic industries with exporting capabilities, the Ghanaian government continues to support domestic private enterprise with financial incentives and tax holidays. Nevertheless, Ghanaian manufacturers and producers contend that the country’s relatively low tariff structure puts them at a competitive disadvantage vis-à-vis imports from countries that enjoy greater production and marketing economies of scale. While tariff reductions have increased competition for local producers, the reductions have also reduced producer costs for imported raw materials and inputs. So there is, in fact, some local demand for further tariff reductions, especially on inputs used by local businesses. Ghana has responded by reducing the import duty on livestock ingredients and inputs for textiles production. Tariff information is available on the CEPS website (www.cepsghana.org).

The government has indicated its intention, along with other ECOWAS countries, to begin the phased implementation of the Common External Tariff on January 1, 2005. This will entail immediately harmonizing 5,100 tariffs (93 percent of all tariff lines) with little or no variation from the ECOWAS values. For the remaining seven percent of tariff lines, Ghana will likely pursue one or all of the following options: (1) phase in over a period of three years the remaining 400 tariff lines (constituting a large percentage of Ghana’s overall customs revenues) to the slightly higher ECOWAS rates; (2) try to negotiate with ECOWAS a permanent exception to some or all of these disputed rates; or (3) agree to harmonize the rates over time, but in practice hold on to national rates.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Ghana has issued its own standards for most products under the auspices of its testing authority, the Ghana Standards Board (GSB). The GSB has promulgated more than 250 Ghanaian standards and adopted more than 3,057 international standards for certification purposes. The GSB determines standards for all products. Authority for enforcing standards for food, drugs, cosmetics, and health items lies with the Food and Drugs Board. Ghana intends to adopt more internationally-recognized standards and move away from its mandatory domestic standards, except for products that raise environmental or human health or safety concerns.

Ghana prohibits the importation of meat with a fat content by weight greater than 25 percent for beef, 42 percent for pork, 15 percent for poultry, and 35 percent for mutton. It also restricts the importation of condensed or evaporated milk with less than 8 percent milk fat by weight, with the exception of imported skim milk in containers. Imported turkeys must have their oil glands removed. Industry reports that products with coded expiration dates, though accepted by the GSB, can cause delays at the border because of the lack of bar-code-reading devices.

GOVERNMENT PROCUREMENT

Ghana is not a signatory to the WTO Agreement on Government Procurement. However, in December 2003, Parliament passed a public procurement law that codified guidelines to enhance transparency and efficiency and give administration of procurement to a central body. In August 2004, the government inaugurated the Public Procurement Board. Tender committees and tender review boards are being formed and national dailies are publishing more public procurements. Section 60 of the procurement law allows procurement entities to give preference to domestic suppliers of goods and services. However, the government has not yet determined the margin of preference or passed procurement regulations.

EXPORT SUBSIDIES

The Ghanaian government uses preferential credits and tax incentives to promote exports. The Export Development Investment Fund administers financing on preferential terms using a 15 percent rate of interest, which is lower than market rates. Agricultural export subsidies were eliminated in the mid-1980s. The Export Processing Zone (EPZ) Law, enacted in 1995, leaves corporate profits untaxed for the first ten years of business operation in an EPZ, after which the tax rate climbs to 8 percent (the same as for non-EPZ companies); however, business producing traditional exports, e.g. cocoa beans, logs and lumber, remain untaxed. The tax rate for non-exporting companies is 32.5 percent.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Ghana is a party to the Universal Copyright Convention and a Member of the World Intellectual Property Organization (WIPO), the African Regional Industrial Property Organization, and the World Trade Organization. In December 2003, Parliament passed five of the six bills designed to bring Ghana into compliance with TRIPS requirements. The new laws are: Trade Marks, Patents, Layout-Designs (Topographies) of Integrated Circuits, Geographical Indications, and Industrial Designs. The government expects Parliament to pass the remaining Copyright bill in 2005. In cases where trademarks have been misappropriated, the price and quality disparity is usually readily apparent. Piracy of protected goods is known to take place, though there is no reliable information on the scale of this activity. Holders of intellectual property rights have access to local courts for redress of grievances, although few trademark, patent, and copyright infringement cases have been filed in Ghana in recent years. Government-initiated enforcement is virtually non-existent.

SERVICES BARRIERS

The investment code excludes foreign investors from participating in four economic sectors: petty trading, the operation of taxi and car rental services with fleets of fewer than ten vehicles, lotteries (excluding soccer pools), and the operation of beauty salons and barber shops. Provision of services by professionals such as lawyers, accountants, and doctors requires membership in a professional body. Requirements for membership are identical for both Ghanaians and non-Ghanaians.

Ghana has committed to offering access to foreign telecommunications providers for most basic services but has required that these services be provided through joint ventures with Ghanaian nationals. The government has allowed a duopoly to dominate both domestic and international services but in 2004 announced plans to open up the market by allowing additional carriers. The government has adopted a reference paper on regulatory principles, which obliges Ghana, among other things, to ensure cost-oriented interconnection with its major suppliers. The National Communications Authority, established to regulate the market, has yet to become an effective mechanism to resolve complaints of anticompetitive practices by Ghana Telecom, the partially state-owned national telecommunications operator.

Ghana allows up to 60 percent foreign ownership in the insurance sector. This cap does not apply to auxiliary insurance services. Ghana requires a high capital requirement for foreign firms to participate in the insurance sector but allows them to provide a full range of services.

There are no limits on foreign participation in banking and other financial services. However, shares held by a single non-resident foreigner and the total number of shares held by all non-resident foreigners in one security listed on the Ghana Stock Exchange may not exceed 10 percent and 74 percent, respectively. The Central Bank must issue licenses for banking and leasing. For securities trading, a license is required from the Securities Regulatory Commission. Foreign-owned banking businesses face higher capital requirements than Ghanaian-owned banks (50 billion cedis versus 25 billion cedis, approximately \$5.6 million and \$2.8 million, respectively).

INVESTMENT BARRIERS

The 1994 Investment Code (Act 478) eliminated the need for prior approval of foreign investment projects by the Ghana Investment Promotion Center. Investment registration, which the government undertakes essentially for statistical purposes, is supposed to be accomplished within five working days. However, according to the "Administrative and Regulatory Cost Survey" conducted by the World Bank and IFC-funded Foreign Investment Advisory Service in

2003, the actual time reported by respondents averaged two weeks. The World Bank reported in its "Doing Business 2004" report that the total time to start a business in Ghana was 85 days, an improvement from 129 days prior to 2003 but still significantly longer than in many other countries at a similar level of development.

Investment incentives are no longer subject to official discretion; they have been made automatic through incorporation into the corporate tax and customs codes. Incentives include exemption from import tariffs for manufacturing inputs and equipment and generous tax breaks. Work visa quotas for businesses, though relaxed, remain in effect. The following minimum equity requirements apply, in the form of either cash or its equivalent in capital goods, for non-Ghanaians who want to invest in Ghana: (1) $10,000 for joint ventures with a Ghanaian; (2) $50,000 for enterprises wholly-owned by a non-Ghanaian; and (3) $300,000 for trading companies (firms that buy/sell finished goods) either wholly or partly-owned by non-Ghanaians. Trading companies must also employ at least ten Ghanaians.

The Ghanaian government at one point controlled more than 350 state-owned enterprises, but nearly 300 had been privatized by the end of 2000 under the privatization program of former President Rawlings. The Kufuor government has reconstituted the Divestiture Implementation Committee; by the end of 2003, total divestiture transactions numbered 318. Thirty-six remaining state-owned enterprises are slated for divestiture. However, the divestment of Ghana Commercial Bank, which is Ghana's largest bank and represents a contingent liability for the government, has yet to materialize.

U.S. direct investment in Ghana is predominantly in the mining and energy sectors, but there is also significant U.S. investment in the seafood, telecommunications, chemical, and wholesale trade sectors. Wage rates in the mining sector are substantially higher than in other industries. U.S. and other foreign firms in Ghana are required to adhere to Ghanaian labor laws, including restrictions on the number of expatriates employed.

Several U.S. investors operating in Ghana continue to struggle with longstanding and costly investment or trade disputes with the government. However, most investors do not encounter such difficulties.

ELECTRONIC COMMERCE

Barriers to electronic commerce are mainly due to a financial infrastructure that is inadequate for electronic commerce to thrive. The payment system in Ghana is largely cash-based. The legalization of foreign exchange bureaus has made foreign currency readily available for small transactions. Local banks can facilitate the transfer of foreign payments abroad. Transfers of large quantities of foreign currency, however, can run into significant delays.

OTHER BARRIERS

U.S. businesses interested in Ghana should also be aware of other barriers, such as limited and costly credit facilities for local importers and freight rates that are higher than those for potential European competitors. There are frequent problems related to the complex land tenure system, and establishing clear title can be difficult. Non-Ghanaians can have access to land on a leasehold basis. Frequent backlogs of cargo at the port hurt the business climate. The Customs Service is still phasing in an automated customs declaration system that was established in the last quarter of 2002 to facilitate customs clearance. It has not yet had the desired impact because complementary services from government agencies, banks, destination inspection companies, and security services are not up to speed.

The high cost of local financing (with short-term interest rates currently above 25 percent) is a significant disincentive for local traders, inhibiting the expansion of most Ghanaian businesses from their current micro-scale operations and constraining industrial growth. The high cost of credit in Ghana is a function of the oligopolistic structure of the banking sector and inefficient directed lending to state-owned enterprises. Ghanaian banks are among Africa's most profitable due to wide interest/deposit rate spreads of up to 20 percentage points. The residual effects of a highly regulated economy and occasional lack of transparency in government operations create an element of risk for potential investors. Bureaucratic inertia is sometimes a problem in government ministries, and administrative approvals take longer than they should. Entrenched local interests sometimes have the ability to derail or delay new entrants, and securing government approvals may depend upon an applicant's local contacts. The political leanings of the Ghanaian partners of foreign investors are often subject to government scrutiny.

Corruption historically has been an issue with which foreign firms have had to contend. President Kufuor has instituted a policy of "zero tolerance" for corruption, and has confirmed his commitment to free markets and trade.

GUATEMALA

TRADE SUMMARY

The U.S. trade deficit with Guatemala was $607 million in 2004, a decrease of $77 million from $683 million in 2003. U.S. goods exports in 2004 were $2.5 billion, up 12.6 percent from the previous year. Corresponding U.S. imports from Guatemala were $7.1 billion, up 4.3 percent. Guatemala is currently the 40th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Guatemala in 2003 was $294 million, down from $303 million in 2002.

IMPORT POLICIES

Free Trade Agreement

The United States engaged in free trade agreement negotiations with five Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) in 2003. The United States concluded negotiations with El Salvador, Guatemala, Honduras, and Nicaragua in December 2003 and with Costa Rica in January 2004. In May 2004, the six countries signed the United States – Central America Free Trade Agreement. During 2004, the United States and the Central American countries engaged in negotiations with the Dominican Republic to integrate that country into the free trade agreement. On August 5, 2004, the seven countries signed the Dominican Republic – Central America – United States Free Trade Agreement (CAFTA-DR). El Salvador ratified the Agreement in December 2004 and Honduras ratified in March 2005. Legislative approval is pending in the United States and the other signatories to the Agreement.

The CAFTA-DR will remove barriers to trade with and investment in the region and will further regional economic integration. The CAFTA-DR will also require the Central American countries and the Dominican Republic to undertake needed reforms to confront many of the problems noted below in areas including: customs administration; protection of intellectual property rights; services, investment, and financial services market access and protection; government procurement; sanitary and phytosanitary (SPS) barriers; and other non-tariff barriers.

Tariffs

Guatemala's tariffs on most goods from outside the Central American Common Market (CACM) are currently within the zero to 15 percent range. There are exceptions, however, including tariffs of up to 40 percent for alcoholic beverages and up to 20 percent for precious and semiprecious stones, various types of vehicles, watches, and firearms and munitions. Other exceptions include the higher tariffs applied to agricultural commodity imports in excess of any applicable tariff rate quota (TRQ). The average applied rate on all products is approximately 5 percent to 6 percent. Guatemala also applies minimum import values (MIVs) on used auto parts and used clothes. Once the CAFTA-DR goes into effect, about 80 percent of U.S. industrial and commercial goods will enter the region duty-free, with the remaining tariffs phased out over ten years.

Nearly all textile and apparel goods that meet the Agreement's rules of origin will be duty-free and quota-free immediately, promoting new opportunities for U.S. and regional fiber, yarn, fabric and apparel manufacturing. (The Agreement's tariff treatment for textile and apparel goods may be made retroactive to January 1, 2004.)

Under the CAFTA-DR, Guatemala will eliminate its tariffs on nearly all agricultural products within 15 years (18 years for rice and chicken leg quarters and 20 years for dairy products). For the most sensitive products, tariff rate quotas will permit some immediate zero-duty access for specified quantities during the tariff phase-out period, which will expand over time. Guatemala will liberalize trade in white corn through expansion of a TRQ.

The Agreement requires transparency and efficiency in administering customs procedures, including the CAFTA-DR rules of origin. Under the CAFTA-DR, Guatemala committed to ensure greater procedural certainty and fairness in the administration of these procedures, and all Parties agreed to share information to combat illegal transshipment of goods.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Guatemalan law requires that food products sold in the domestic market be tested, registered and labeled in Spanish, although stick-on labels are permitted. Products sold in bulk are exempt from the labeling requirement unless they are to be sold at the retail level as an individual unit. Enforcement of product registration and labeling requirements has been inconsistent but is improving.

When the United States and Central America launched the free trade agreement negotiations, they initiated an active working group dialogue on SPS barriers to agricultural trade that met alongside the negotiations to facilitate market access. The objective was to leverage the impetus of active trade negotiations to seek difficult changes to the Central American countries' SPS regimes. Through the work of this group, Guatemala has committed to resolve specific measures affecting U.S. exports to Guatemala. In particular, for meat, dairy and poultry, Guatemala will move toward recognizing import eligibility for all plants inspected under the U.S. food safety and inspection system. For distilled spirits, U.S. industry welcomes the trade-facilitative initiative of the five Central American countries, including Guatemala, to develop common standards for distilled spirits products. However, outstanding concerns remain, such as alcohol content, brand registration and certification requirements.

GOVERNMENT PROCUREMENT

Guatemala is not a party to the WTO Government Procurement Agreement. Currently, Guatemala's Government Procurement Law requires most government purchases over $113,000 to be submitted for public competitive bidding. Contracts may be awarded when there is only one bidder. The government occasionally declares certain projects a matter of national emergency, thereby avoiding the competitive bidding process. Foreign suppliers must submit their bids through locally registered representatives, a bureaucratic process that can place foreign bidders at a competitive disadvantage. Additionally, U.S. companies have long alleged that significant corruption exists in the public procurement process and is a barrier to entry. However, in March 2004, the new Berger Administration made mandatory the use of Guatecompras, an Internet-based electronic system to publicize Guatemala's procurement needs, which is improving transparency in the government procurement process.

The CAFTA-DR requires fair and transparent procurement procedures, including advance notice of purchases and timely and effective bid review procedures. Under the CAFTA-DR, U.S. suppliers will be permitted to bid on procurements covered by the Agreement for most Guatemalan government entities, including key ministries and state-owned enterprises on the same basis as Guatemalan suppliers. The anti-corruption provisions in the Agreement require each government to ensure that bribery in matters affecting trade and investment, including in government procurement, is treated as a criminal offense, or is subject to comparable penalties, under its law.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

CAFTA-DR obligations for IPR will strengthen Guatemala's IPR protection regime to conform with, and in many areas exceed, WTO norms. CAFTA-DR obligations would also provide stronger deterrence against piracy and counterfeiting by criminalizing end user piracy and requiring Guatemala to authorize the seizure, forfeiture, and destruction of counterfeit and pirated goods and the equipment used to produce them. The CAFTA-DR text also mandates both statutory and actual damages for copyright and trademark infringement which would ensure that monetary damages can be awarded even when it is difficult to assign a monetary value to the violation.

Patents

Guatemala's 2000 Industrial Property Law made improvements to the protection afforded to patent holders, increasing the term of protection for a patent to 20 years from the date of filing the patent application. It also increased the number of products and services that are considered patentable, including living organisms, commercial plans and chemical compounds or compositions. This law provided patent protection for pharmaceutical and agricultural products for the first time and established a mailbox system to process cases filed since 1995.

Copyrights

Piracy of copyrighted material, including videos, optical discs (CD-R & DVD-R formats), and software, remains widespread, and enforcement of existing legislation remains a concern. Some progress has been achieved in concluding valid licensing agreements with copyright holders and in reducing the incidence of pay television piracy (though rural operators still remain outside the legitimate system). Guatemala has ratified the WIPO Copyright Treaty (WCT) and the WIPO Performances and Phonograms Treaty (WPPT). CAFTA-DR enforcement provisions are designed to help reduce copyright piracy.

Trademarks

Exclusive rights for trademarks are granted on a first-to-file basis, thus permitting third parties to register and gain exclusive use of well-known or famous trademarks. A dispute resolution system has been established in the event that a well-known or famous trademark is granted to a third party. The local Internet domain name registrar does not accept applications for well-known and famous names from applicants who are not the trademark holders as frequently as it once did. Additionally, when receiving an Internet domain name registration, the domain name owner is required to submit the registration to the WIPO online dispute resolution system in the event of a challenge by a third party. CAFTA-DR enforcement provisions are designed to help reduce trademark infringement.

SERVICES BARRIERS

Currently, international telephone traffic must be routed through the facilities of an enterprise licensed by the Guatemalan Superintendence of Telecommunications. U.S. companies have raised allegations of anti-competitive behavior, including unilateral changes of interconnection rates, by the country's dominant fixed line telephone service provider, Telgua, which is a subsidiary of Telmex of Mexico. Guatemala's courts have ruled against Telgua in those cases where a verdict was reached, but the anticompetitive practices continue. The CAFTA-DR will require that Guatemala further open its telecommunications market to competition on a nondiscriminatory basis.

Foreign banks may open branches or subsidiaries in Guatemala subject to the conditions of the Monetary Board, including capital and lending requirements based exclusively on the balance sheet of the local entity. Branches and subsidiaries must be inscribed in the Mercantile Registry, as is the case with any business.

Some professional services may only be supplied by professionals with locally recognized academic credentials. Notaries public must be Guatemalan nationals. Under the CAFTA-DR, as with banks, U.S. insurance companies would have full rights to establish subsidiaries and joint ventures upon entry into force of the agreement, with branching rights phased in. U.S. insurance suppliers would also be able to provide insurance cross-border in areas such as Marine, Aviation and Transportation insurance, goods in international transit, reinsurance as well as services auxiliary to insurance such as claims settlement, actuarial, risk assessment and consulting. Foreign enterprises may provide licensed professional services in Guatemala through a contract or other relationship with an enterprise established in Guatemala.

INVESTMENT BARRIERS

Guatemala's 1998 investment law generally provides for national treatment of foreign investment. However, specific restrictions remain in several sectors of the economy, including auditing, insurance and forestry, although these restrictions are not always enforced. Complex and confusing laws, regulations, red tape, and corruption constitute practical barriers to investment. When the CAFTA-DR is implemented, the agreement will establish a more secure and predictable legal framework for U.S. investors operating in Guatemala.

The CAFTA-DR will establish a more secure and preditable legal framework for U.S. investors operating in Guatemala. All forms of investment will be protected, including enterprises, debt, concessions, contracts and intellectual property. U.S. investors will enjoy, in almost all circumstances, the right to establish, acquire and operate investments in Guatemala on an equal footing with local investors. Among the rights afforded to U.S. investors are due process protections and the right to receive a fair market value for property in the event of an expropriation. Investor rights will be backed by an effective, impartial procedure for dispute settlement that is fully transparent. Submissions to dispute panels and panel hearings will be open to the public, and interested parties will have the opportunity to submit their views.

OTHER BARRIERS

Past allegations of official corruption, security concerns and an anti-business attitude under the previous administration (there was a change in administration in January 2004) may have weakened investors' confidence and affected investment and trade decisions related to Guatemala. The anti-corruption provisions in the Agreement require each government to ensure that bribery in matters affecting trade and investment is treated as a criminal offense, or is subject to comparable penalties, under its law.

HONDURAS

TRADE SUMMARY

The U.S. trade deficit with Honduras was $565 million in 2004, an increase of $78 million from $486 million in 2003. U.S. goods exports in 2004 were $3.1 billion, up 8.9 percent from the previous year. Corresponding U.S. imports from Honduras were $3.6 billion, up 9.9 percent. Honduras is currently the 37th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Honduras in 2003 was $270 million, up from $181 million in 2002. U.S. FDI in Honduras is concentrated largely in the manufacturing sector.

IMPORT POLICIES

Free Trade Agreement

The United States engaged in free trade agreement negotiations with five Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) in 2003. The United States concluded negotiations with El Salvador, Guatemala, Honduras, and Nicaragua in December 2003 and with Costa Rica in January 2004. In May 2004, the six countries signed the United States – Central America Free Trade Agreement. During 2004, the United States and the Central American countries engaged in negotiations with the Dominican Republic to integrate that country into the free trade agreement. On August 5, 2004, the seven countries signed the Dominican Republic – Central America – United States Free Trade Agreement (CAFTA-DR). El Salvador ratified the Agreement in December 2004 and Honduras ratified in March 2005. Legislative approval is pending in the United States and the other signatories to the Agreement.

The CAFTA-DR will remove barriers to trade with and investment in the region and will further regional economic integration. The CAFTA-DR will also require the Central American countries and the Dominican Republic to undertake needed reforms to confront many of the problems noted below in areas including: customs administration; protection of intellectual property rights; services, investment, and financial services market access and protection; government procurement; sanitary and phytosanitary (SPS) barriers; and other non-tariff barriers.

Tariffs

Honduras' tariffs on most goods from outside the Central American Common Market (CACM) are currently within the zero to 15 percent range. Once the CAFTA-DR goes into effect, about 80 percent of U.S. industrial and commercial goods will enter the region duty-free, with the remaining tariffs phased out over ten years. Nearly all textile and apparel goods that meet the Agreement's rules of origin will be duty-free and quota-free immediately, promoting new opportunities for U.S. and regional fiber, yarn, fabric and apparel manufacturing. (The Agreement's tariff treatment for textile and apparel goods may be made retroactive to January 1, 2004.)

Honduras maintains a combination price band and absorption agreement for corn, grain sorghum, and corn meal. Under the price band mechanism, duties can vary from 5 percent to 45 percent, depending on the import price. The duty for these products drops to 1 percent if the end users agree to first purchase a predetermined amount of corn and sorghum from domestic farmers; otherwise, the higher tariffs of the price band mechanism remain in effect. The tariff reduction only takes place during non-harvest season (March through August), and only end-users who have previously signed the absorption agreement may apply for this preferential treatment. A similar absorption agreement exists for rough rice, with duties of 1 percent for signers of the agreement and 45 percent for everyone else. The United States has strongly opposed the Honduran policies on these grains as limiting access for U.S. agricultural products.

Under the CAFTA-DR, Honduras will eliminate its tariffs on nearly all agricultural products within 15 years (18 years for rice and chicken leg quarters and 20 years for dairy products). For the most sensitive products, tariff rate quotas will permit some immediate zero-duty access for specified quantities during the tariff phase-out period, which will expand over time. Honduras will liberalize trade in white corn through expansion of a TRQ. Accordingly, when implemented, the CAFTA-DR will lead to the elimination of market access barriers, including the price band and absorption agreement system, for all products other than white corn.

The Agreement also requires transparency and efficiency in administering customs procedures, including the CAFTA-DR rules of origin. Honduras committed to ensure greater procedural certainty and fairness in the administration of these procedures and all Parties agreed to share information to combat illegal transshipment of goods.

Honduras implemented the WTO Customs Valuation Agreement in February 2000.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

Application of SPS requirements is sometimes lacking in transparency, resulting in uncertainty among U.S. suppliers and Honduran importers. The Honduran government requires that sanitary permits be obtained from the Ministry of Health for all imported foodstuffs, and that all processed food products be labeled in Spanish and registered with the Division of Food Control (DFC) of the Ministry of Health. A U.S. and a regional supermarket chain have complained that delays in the process of granting these permits have hampered their ability to import into Honduras. The Ministry of Health agreed to accelerate the process by focusing most closely on products considered to be at high risk for sanitary concerns (such as raw meat) and simplifying the procedures for low-risk products. However, during 2004, concerns remained: that these regulations were not being strictly enforced for Honduran competitors, and that imports into

Honduras could grow significantly, with a more transparent and efficient process of granting sanitary permits.

In 2002 and 2003, Honduran importers had initial difficulty receiving permission to import turkey into Honduras, though permission was eventually granted. The Honduran government has also cited SPS concerns in periodically denying applications for the importation of pork and dairy products.

Since 2002, Honduras has imposed a ban on poultry products from a number of U.S. states, due to concerns over low-pathogenic avian influenza (LPAI). The ban was revised and renewed in March 2004 in spite of World Organization for Animal Health (OIE) guidelines that the presence of LPAI does not justify trade restrictions, and despite information provided to Honduran officials by the U.S. Department of Agriculture (USDA) indicating the dates on which testing was completed in the affected states. The USDA estimates that if Honduran restrictions on U.S. raw poultry and poultry parts were lifted, U.S. producers could export an additional $10 million of poultry products to Honduras annually.

When the United States and Central America launched the free trade agreement negotiations, they initiated an active working group dialogue on SPS barriers to agricultural trade that met alongside the negotiations to facilitate market access. The objective was to leverage the impetus of active trade negotiations to seek difficult changes to the Central American countries' SPS regimes. Through the work of this group, Honduras has committed to resolve specific measures affecting U.S. exports to Honduras. In particular, for meat, dairy, and poultry, under CAFTA-DR Honduras will move toward recognizing import eligibility for all plants inspected under the U.S. food safety and inspection system.

GOVERNMENT PROCUREMENT

Honduras is not a party to the WTO Government Procurement Agreement. Under the Government Contracting Law, which entered into force in October 2001, all public works contracts over one million lempiras (approximately $53,850 as of December 2004) must be offered through public competitive bidding. Public contracts between 500,000 and one million lempiras ($26,925 and $53,850) can be offered through a private bid, and contracts less than 500,000 lempiras ($26,925) are exempt from the bidding process. Currently, to participate in public tenders, foreign firms are required to act through a local agent (at least 51 percent Honduran-owned).

While foreign firms are granted national treatment for public bids, some still complain of mismanagement and lack of transparency in the bid processes. One way that the government of Honduras has tried to improve transparency and fairness in government procurement is by contracting with the United Nations Development Program (UNDP) to manage procurement for an increasing number of ministries and state-owned entities. However, U.S. companies have expressed concerns about the way UNDP has managed major procurements for the government, such as complaints that bid requirements were written so narrowly that they favored a particular company from the outset and that UNDP management of invitation-only, limited-bid process, was not transparent.

The CAFTA-DR requires fair and transparent procurement procedures, including advance notice of purchases and timely and effective bid review procedures. Under the CAFTA-DR, U.S. suppliers will be permitted to bid on procurements covered by the Agreement for most Guatemalan government entities, including key ministries and state-owned enterprises on the same basis as Guatemalan suppliers. The anti-corruption provisions in the Agreement require each government to ensure that bribery in matters affecting trade and investment, including in government procurement, is treated as a criminal offense, or is subject to comparable penalties, under its law. In addition, the CAFTA-DR would eliminate the local agent requirement for participation in public tenders.

EXPORT SUBSIDIES

Honduras does not have export subsidies or export-promotion schemes other than the tax exemptions given to firms in free trade zones. Under the CAFTA-DR, Honduras may not adopt new duty waivers or expand existing duty waivers conditioned on the fulfillment of a performance requirement (e.g., the exportation of a given level or percentage of goods). Honduras may maintain existing duty waiver measures provided such measures are consistent with its WTO obligations.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Honduras largely complied with the Trade Related Aspects of Intellectual Property Rights (TRIPs) Agreement by the January 1, 2000, deadline. In December 1999, the Honduran Congress passed two laws to reform previous legislation concerning copyrights, patents, and trademarks. However, the Honduran Congress has yet to pass laws governing the protection of integrated circuit designs and plant varieties. In the CAFTA-DR, Honduras agreed to ratify or accede to the International Convention for the Protection of New Varieties of Plants by January 1, 2006, or provide effective patent protection for plants by the date of entry into force of the agreement.

CAFTA-DR obligations will also strengthen Honduras' IPR protection regime to conform with, and in many areas exceed, WTO norms. CAFTA-DR obligations would also provide stronger deterrence against piracy and counterfeiting by criminalizing end user piracy and requiring Honduras to authorize the seizure, forfeiture, and destruction of counterfeit and pirated goods and the equipment used to produce them. The CAFTA-DR text also mandates both statutory and actual damages for copyright and trademark infringement, which would ensure that monetary damages can be awarded even when it is difficult to assign a monetary value to the violation.

Copyrights

Honduras' copyright law, updated in 1999, added more than twenty different criminal offenses related to copyright infringement and established fines and suspension of services that can be levied against offenders. However, the piracy of books, sound and video recordings, compact discs, and computer software is still widespread in Honduras, due to limited enforcement capacity. A spot survey by an industry-sponsored IPR advocacy group found that nearly 75 percent of all compact discs for sale in Honduras' markets were pirated. U.S. software companies are also pushing for ministries and state-owned entities to ensure their own use of only authorized licensed software. A major U.S. software company has estimated that it loses $5 million annually due to software piracy in Honduras.

The piracy of cable television signals is also a problem in Honduras. During 2004, two different U.S. companies claimed that their competitors were broadcasting pirated cable television signals from the United States, and that the Honduran authorities do not vigorously investigate and prosecute these activities. The CAFTA-DR enforcement provisions are designed to help reduce copyright piracy.

Patents and Trademarks

Honduras ratified the Paris Convention for the Protection of Industrial Property in 1994. The Honduran Congress enacted a 1999 Law of Industrial Property to provide improved protection for both trademarks and patents. To be protected under Honduran law, patents and trademarks currently must be registered with the Ministry of Industry and Trade. The CAFTA-DR will eliminate cumbersome registration requirements.

Modifications to the Patent Law of 1993 included patent protection for pharmaceuticals, and extension of the term of protection for a patent from seventeen to twenty years from the date of filing, to meet WTO standards. The term for cancellation of a trademark for lack of use was extended from one year to three years. Trademarks are valid for up to ten years from the registration date. The illegitimate registration of well-known trademarks has, however, been a persistent problem in Honduras. The CAFTA-DR enforcement provisions are designed to help reduce trademark infringement.

A major concern for U.S. pharmaceutical and agricultural chemical companies is the lack of effective data protection in Honduras for undisclosed test data submitted for the marketing approval of a pharmaceutical or agricultural chemical product. Implementation of CAFTA-DR obligations will ensure adequate and effective protection of such data from disclosure and unfair commercial use.

SERVICES BARRIERS

Currently, special government authorization must be obtained to invest in the tourism, hotel, and banking services sectors. Foreigners may neither hold a seat on, nor provide direct brokerage services in, Honduras' stock exchange. Honduran professional bodies heavily regulate the licensing of foreigners to practice law, medicine, engineering, accounting, and other professions.

Under the CAFTA-DR, Honduras will accord substantial market access in services across their entire services regime, subject to very few exceptions. In addition, U.S. financial service suppliers would have full rights to establish subsidiaries, joint ventures or branches for banks and insurance companies. Honduras will allow U.S.-based firms to offer cross-border services in areas such as financial information and data processing, and financial advisory services. In addition, Honduran mutual funds will be able to use foreign-based portfolio managers. The right to provide professional services will be granted on a reciprocal basis depending on the requirements in individual U.S. states.

INVESTMENT BARRIERS

Currently, the government of Honduras must approve any foreign investment in sectors including telecommunications, basic health, air transport, insurance and financial services, private education, and most sectors related to natural resources and farming. Foreigners are barred from small-scale commercial and industrial activities with an investment less than 150,000 lempiras (about $8,078). Foreign ownership of land within 40 km of the coastlines and national boundaries is constitutionally prohibited, although tourism investment laws allow for certain exceptions. Inadequate land title procedures, including overlapping claims and a weak judiciary, have led to numerous investment disputes involving U.S.-citizen landowners.

In 2001, a Bilateral Investment Treaty (BIT) between the United States and Honduras entered into force. The treaty provides, among other things, for equal protection under the law for U.S. investors, with limited exceptions, and permits expropriation only in accordance with international legal standards and accompanied by adequate compensation. U.S. investors in Honduras also have the right to submit an investment dispute to binding international arbitration.

Under current Honduran law, the government-owned telephone company Hondutel maintains monopoly rights over all fixed-line telephony services. However, in 2003 the government began to allow foreign investors to participate in fixed-line telephony services as "sub-operators" in partnership with Hondutel. At present, approximately 40 firms have entered into "sub-operator" contracts with Hondutel, of which five firms are already providing services to the public. By law, Hondutel's monopoly expires in December 2005, and the government of Honduras has announced plans for full privatization of Hondutel thereafter. Both foreign and domestic firms already enjoy full rights to invest in cellular telephony services.

In July 2004, the Minister of Natural Resources and the Environment issued a decree calling for a new national policy on mining and ordered the government agency responsible for granting mining permits and concessions, DEFOMIN, to stop granting any new mining concessions. This review is ongoing and has blocked plans of some U.S. investors, including the expansion plans of a U.S. company operating in Honduras, which is experiencing a delay in obtaining an environmental permit necessary to operate.

Under the CAFTA-DR, U.S. investors will enjoy in almost all circumstances the right to establish, acquire and operate investments in Honduras on an equal footing with local investors. In the investment chapter of the CAFTA-DR, Honduras will commit to provide a higher level of protection for U.S. investors than under the existing BIT. Among the rights afforded to U.S. investors are due process protections and the right to receive a fair market value for property in the event of an expropriation. Investor rights will be backed by an effective, impartial procedure for dispute settlement that is fully transparent. Submissions to dispute panels and panel hearings will be open to the public, and interested parties will have the opportunity to submit their views. The CAFTA-DR requires that all forms of investment be protected, including enterprises, debt, concessions, contracts and intellectual property. Upon entry into force of the CAFTA-DR, the BIT will be suspended. For a period of 10 years, however, current U.S. investors may choose either dispute settlement under the BIT or the FTA.

ELECTRONIC COMMERCE

Honduras currently has no domestic legislation concerning electronic commerce, as the sector is still not developed in the Honduran market. The Electronic Commerce System Directorate (DISELCO), a joint project of the Chamber of Commerce and Industry of Tegucigalpa (CCIT), the Chamber of Commerce and Industry of Cortés (CCIC), and the National Industry Association (ANDI), is the institution in charge of establishing the policies and norms pertaining to electronic commerce in Honduras.

Although improving, the country still lacks adequate basic telecommunications infrastructure and Internet bandwidth capacity to effectively support significant electronic commerce. Except for web page promotional material, companies are not utilizing computer-based sales as a substantial distribution channel in Honduras.

The CAFTA-DR includes provisions on electronic commerce that reflect the issue’s importance in global trade and the importance of supplying services by electronic means as a key part of a vibrant electronic commerce environment. Under the Agreement, Honduras has committed to provide non-discriminatory treatment of digital products and not to impose customs duties on such products and to cooperate in numerous policy areas related to electronic commerce.

OTHER BARRIERS

Historically, U.S. firms and private citizens have found corruption to be a problem which seriously complicates doing business in Honduras. Corruption appears to be most prevalent in the areas of government procurement, the buying and selling of real estate, particularly land title transfers, performance requirements, and the regulatory system. Honduras' judicial system is subject to influence, and the resolution of investment and business disputes involving foreigners is largely non-transparent. With considerable U.S. help, the government is reforming Honduras' judicial system and fighting corruption, though progress has been very slow and serious problems remain. During 2004, Honduras had the distinction of being chosen as eligible to apply for Millennium Challenge Account (MCA) assistance. MCA countries are deemed to have shown a commitment to ruling justly (including by tackling corruption), investing in their people, and encouraging economic freedom. The anti-corruption provisions in the CAFTA-DR require each government to ensure that bribery in matters affecting trade and investment is treated as a criminal offense, or is subject to comparable penalties, under its law.

Anti-Competitive Practices

U.S. industry has expressed concern that investors who set up business in Honduras have at times found themselves subject to forms of competition that, in the United States, would be considered anticompetitive. In 2003, a U.S.-Japanese joint venture established a cement company in Honduras, challenging the duopoly enjoyed by the two Honduran companies in the market. The new joint venture investment was critical of the two established companies accusing them of predatory pricing that brought cement prices below the cost of production. After the U.S.-Japanese venture dropped out of the market, prices returned to their earlier level. There is currently no law against predatory pricing in Honduras. However, a draft competition law, which would address certain types of anti-competitive behavior, is currently before a congressional committee.

HONG KONG

TRADE SUMMARY

The U.S. trade surplus with Hong Kong was $6.5 billion in 2004, an increase of $1.8 billion from $4.7 billion in 2003. U.S. goods exports in 2004 were $15.8 billion, up 16.9 percent from the previous year. Corresponding U.S. imports from Hong Kong were $9.3 billion, up 5.2 percent. Hong Kong is currently the 13th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Hong Kong were $3.2 billion in 2003 (latest data available), and U.S. imports were $3.0 billion. Sales of services in Hong Kong by majority U.S.-owned affiliates were $8.6 billion in 2002 (latest data available), while sales of services in the United States by majority Hong Kong-owned firms were $1.3 billion.

The stock of U.S. foreign direct investment (FDI) in Hong Kong in 2003 was $44.3 billion, up from $41.6 billion in 2002. U.S. FDI in Hong Kong is concentrated largely in the finance, wholesale, and manufacturing sectors.

On June 29, 2003, Hong Kong and China signed the Closer Economic Partnership Arrangement (CEPA), a free trade agreement granting Hong Kong's manufacturers and service suppliers preferential access to the PRC market. CEPA was implemented on January 1, 2004, providing tariff-free treatment for Hong Kong-origin goods in 374 product categories as well as preferential access to 18 service sectors. Preferential access for five types of value-added telecommunications services was implemented on October 1, 2003.

On August 27, 2004, Hong Kong and China signed the second phase of CEPA to further liberalize trade in goods and services. Effective January 1, 2005, Hong Kong-origin goods in 529 additional product categories are exported to China tariff-free; as of January 1, 2006, another 184 products will enjoy this treatment. Additionally, effective January 1, 2005, Hong Kong service providers enjoy preferential treatment in eight new service sectors.

IMPORT POLICIES

The Hong Kong government pursues a market-oriented approach to commerce. Hong Kong is a duty-free port, with few barriers to trade in goods and services and few restrictions on foreign capital flows and investment. However, Hong Kong does maintain excise duties on certain goods, including alcoholic beverages and wine. Duties on alcoholic beverages and wine range from 40 percent to 100 percent *ad valorem* and have been identified as a significant concern for U.S. exporters and producers. The Hong Kong government issued a consultation paper in December 2004 proposing reductions in these duties.

Hong Kong banned imports of U.S. beef in December 2003 following the detection of one positive case of Bovine Spongiform Encephalopathy (BSE) in the state of Washington. As of the publication of this report, the U.S. Government is continuing to work with the Hong Kong government to re-open the market as quickly as possible. In addition, the United States is working in the International Organization for Epizootics to revise international standards related to BSE to reflect current scientific knowledge. U.S. beef exports to Hong Kong in 2003, prior to the import ban, were valued at approximately $82 million. At that time, Hong Kong was the fifth largest export market for U.S. beef. For the past eleven months, the U.S. Government estimates that the Hong Kong government's import ban has cost U.S. beef exporters nearly $75 million.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The Hong Kong government continues to maintain a robust IPR protection regime. Hong Kong has strong laws in place, a dedicated and effective enforcement capacity, and a judicial system that supports enforcement efforts by sentencing those convicted of IPR violations to prison. However, there are vulnerabilities to some forms of infringement, and the U.S. Government continues to monitor the situation to ensure that Hong Kong's IPR protection efforts are sustained and that problem areas are addressed.

The Hong Kong government has sustained public education efforts to encourage respect for intellectual property rights and has re-launched its "no fakes" campaign with local retailers who pledge to sell no counterfeit or pirated goods. Hong Kong authorities also continue to conduct aggressive raids at the retail level and to act against vendors who advertise illegal products over the Internet. In the first eight months of 2004, there were 783 piracy-related arrests. During the same period, the judiciary handed down 924 copyright and trademark convictions, the majority of which led to prison sentences of six to twelve months. Hong Kong Customs intelligence operations and raids on underground production facilities have closed most large-scale pirate manufacturing operations, prompting many producers of pirated optical media to switch to computers or CD burners to produce illicit copies and forcing retailers to rely increasingly on smuggled goods. In July 2004, Hong Kong Customs used the Organized and Serious Crimes Ordinance (OSCO) to freeze the assets of a pirating syndicate worth $2.7 million. This is the first time OSCO has been applied to an IPR case.

Despite the crackdown on large-scale illicit manufacturing, there is still concern about Hong Kong's licensed optical media production lines, which give the territory an overcapacity that must be carefully monitored. The volume of openly-marketed pirated optical media found in retail shopping arcades has decreased significantly but sales of infringing products remain a problem. U.S. officials have encouraged the Hong Kong government to sustain the pace of its ongoing enforcement activities aimed at local producers and vendors of infringing products.

Hong Kong's IPR enforcement efforts have helped reduce losses by U.S. companies, but end-use piracy, the rapid growth of peer-to-peer downloading from the Internet, and the illicit importation and transshipment of pirated and counterfeit goods, including optical media and name brand handbags and apparel from China and elsewhere in the region, are continuing problems. The software industry estimates that Hong Kong's software piracy rate was 52 percent in 2003, placing Hong Kong well above the software piracy rates in other advanced economies and resulting in losses of approximately $102 million to rights-owners. According to the U.S. film industry, in November 2004 it found 2,446 Hong Kong IP addresses from which Internet users could download infringing movies for free, as opposed to only 107 such IP addresses in 2003. The Hong Kong government has taken some steps against each of these problems. In September 2004, Hong Kong authorities took to court a software end-use piracy case for the first time in almost two years, attaining guilty pleas from two of the defendants. Hong Kong Customs made numerous seizures of cross-border shipments of IPR infringing products from China in 2004. Hong Kong officials have also established a joint task force with copyright industry representatives to track down on-line pirates using peer-to-peer networks for unauthorized file-sharing. However, end-use piracy, Internet piracy, and the cross-boundary flow of infringing products continue to result in significant losses to American companies, and U.S. officials have urged Hong Kong authorities to intensify efforts against these problems.

U.S. pharmaceutical companies are concerned that the Hong Kong Department of Health continues to issue marketing authorizations for patent-infringing pharmaceutical products. The local pharmaceutical industry association (which represents a number of U.S. and other international firms) submitted a proposal to the Hong Kong government in June that would give patent holders an opportunity to commence legal action against infringing generics before their marketing authorization applications are processed by the Department of Health. However, the Department of Health claims it cannot adopt this proposal without amending its pharmaceutical registration law. In addition, the industry has concerns about sales of counterfeit pharmaceuticals, which threaten consumer safety and brand reputation, and it seeks more vigorous enforcement and tougher penalties to deter this kind of illicit trade. The U.S. Government continues to urge the Hong Kong government to address both the patent protection and counterfeiting issues as they pertain to pharmaceutical products.

In February 2004 the Hong Kong government enacted an amendment to the Copyright Ordinance that provided tougher measures against illicit copy shops. These provisions took effect on September 1, 2004. In December 2004 the Hong Kong government initiated public consultations on another proposed amendment to the Copyright Ordinance that will deal with various aspects of end-use piracy. At present, Hong Kong law provides end-user criminal liability only for four categories of works: computer software, movies, television dramas, and sound recordings. Printed works are not protected by criminal liability.

SERVICES BARRIERS

Hong Kong completed its liberalization of the fixed-line telecommunications network services market on January 1, 2003. There are no limits on the number of licenses issued and no time limit for submitting license applications. In July 2004, the Hong Kong government announced that it would withdraw its interconnection policy for local fixed-line telecommunications services by June 30, 2008. Interconnection charges will then be subject to commercial negotiation between the operators concerned. In October 2004, the Hong Kong government began a 2-month public consultation on the regulation of Internet Protocol (IP) Telephony. The objectives of the consultation were to seek views on whether the existing regulatory requirements for traditional voice telephony service should be applied to the new services and whether Internet Service Providers should be allowed to operate IP Telephony services. In November 2004, the government decided to revoke in 2008 a CDMA (code division multiple access) license and a TDMA (time division multiple access) license from two local operators. The government will conduct a spectrum review in 2005 in which it will examine whether a more free-market approach, like spectrum trading, would better fit Hong Kong's needs. Under the current scheme, operators of second-generation mobile phone services cannot change the way they use their spectrum once it is assigned, although they may transfer the license with government approval.

In November 2004, the Bank of China began providing clearing arrangements that permit Hong Kong-licensed banks to conduct personal Renminbi (RMB) business. The scope of RMB business is limited to deposit-taking, exchange, remittances and credit cards. U.S. banks licensed in Hong Kong are able to provide RMB services.

The October 2002 U.S.-Hong Kong civil aviation agreement significantly expanded opportunities for U.S. carriers. The agreement allows cooperative marketing arrangements between U.S. and Hong Kong and third-country carriers (codesharing) and also increases the ability of U.S. carriers to operate cargo and passenger services between Hong Kong and third country points. However, restrictions on frequencies and routes for these services remain, as the agreement fell well short of creating "open skies." Bilateral talks aimed at further liberalization are scheduled for April 2005.

Foreign law firms that practice foreign law in Hong Kong are barred from practicing Hong Kong law and from employing or joining into partnership with Hong Kong solicitors. Foreign law firms that wish to provide both foreign and Hong Kong legal services may do so only by establishing a Hong Kong legal practice in which all partners are Hong Kong-qualified solicitors and the number of registered foreign lawyers employed does not exceed the number of Hong Kong solicitors. Such firms may be associated with, or even be branches of, overseas law firms if they meet certain criteria, e.g., at least one partner of the Hong Kong firm must also be a partner in the overseas firm.

Hong Kong has no general competition law that prohibits incumbents from using their market dominance to keep out new entrants. There are several domestic service sectors where one firm, or a handful of firms, dominate market share.

ELECTRONIC COMMERCE

Hong Kong places great importance on its role as an information technology and electronic commerce hub. In June 2004, the Legislative Council passed amendments to the Electronic Transactions Ordinance to update and improve the legal framework for the use of electronic transactions. The ordinance mandates a technology-neutral approach regarding electronic signatures for satisfying legal signature requirements. It also removes unnecessary legal impediments to electronic transactions and streamlines the operation of a voluntary recognition scheme for certification authorities.

As part of its electronic-government initiative, Hong Kong launched the Multi-Application Smart Identity Card in June 2003. In addition to providing access to various government services, the card also features an embedded digital certificate that enables secure on-line bank, stock trading, or tax return transactions.

In January 2004, the Hong Kong government opened the Government Electronic Trading Services (GETS) market to a second company for the electronic submission and processing of import and export trade documents and dutiable commodities permits.

OTHER BARRIERS

Pharmaceuticals

U.S. industry has expressed concerns about lengthy approval procedures for new pharmaceuticals, which shorten the effective patent life of new products by six months. In addition, the U.S. industry is concerned about the lack of transparency in the Hong Kong Hospital Authority's approval process for new drugs. These cumbersome procedures also inhibit the patent owners' ability to market their products on a timely basis.

INDIA

TRADE SUMMARY

The U.S. trade deficit with India was $9.5 billion in 2004, an increase of $1.4 billion from $8.1 billion in 2003. U.S. goods exports in 2004 were $6.1 billion, up 22.4 percent from the previous year. Corresponding U.S. imports from India were $15.6 billion, up 19.2 percent. India is currently the 24th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to India were $3.7 billion in 2003 (latest data available), and U.S. imports were $2.2 billion. Sales of services in India by majority U.S.-owned affiliates were $1.2 billion in 2002 (latest data available), while sales of services in the United States by majority India-owned firms were $261 million.

The stock of U.S. foreign direct investment (FDI) in India in 2003 was $3.6 billion, up from $3.3 billion in 2002. U.S. FDI in India is concentrated largely in the manufacturing, utilities, and banking sectors.

IMPORT POLICIES

India's tariffs remain remarkably high, especially in the agricultural sector. U.S. producers encounter tariff and non-tariff barriers that impede their exports. This is despite the fact that beginning with its economic reform program initiated in 1991, India has taken noteworthy steps to open its markets. A progressively more open and transparent trade regime stimulated a strong increase in U.S.-India trade and investment in the first half of the 1990s. U.S exports to India stagnated in 1996 as the reform process stalled, but have shown a positive growth trend since 2001. While U.S. exports continued to grow in 2004, substantial expansion in U.S.-India trade will be unlikely without significant additional Indian liberalization.

The government of India (GOI) has made substantial progress in restructuring the tariff applied to non-agricultural goods. In January 2004, the GOI reduced from 25 percent to 20 percent the tariff applied to most non-agricultural goods. The GOI applies higher tariffs to petrochemicals, automobiles, and finished steel products. On February 28, 2005, the GOI stated its intention to reduce the peak applied non-agricultural duty by another 5 percentage points.

According to a September 2004 World Bank study on Trade Policies in South Asia, India's simple average applied duty rate is 22.2 percent, down from 24.8 percent in 2003. India also reduced applied duties in 2004 on certain selected imports, including: coal; nickel and nickel articles; power transmission and distribution project equipment; electricity meters; certain raw materials and inputs for optical fibers and cables; capital goods for manufacturing electronic goods; certain telecommunication infrastructure equipment; cellular telephones; VCDs and

DVDs; lifesaving bulk drugs, formulations, and medical equipment; parts of artificial limbs and certain rehabilitation aids; medical, surgical, dental, and veterinary furniture; mosquito nets treated with pesticide; aviation turbine fuel; and equipment for industrial and agricultural water supply projects. According to the U.S. textile industry, India continues to maintain numerous textile trade barriers, and India remains one of the most heavily protected textile markets in the world. In addition, reductions to India's agricultural tariffs continue to be negligible.

The GOI assesses a one percent customs handling fee on all imports in addition to the applied customs duty. In January 2004, the GOI eliminated a four percent Special Additional Duty (SAD), which had been levied on virtually all imports since the 1998/99 budget. In July 2004, a newly elected government imposed a new two percent education fund assessment that must be paid in addition to customs duties. The GOI includes tariffs in calculating the value upon which to assess additional duties.

The United States has actively sought market-opening opportunities in India, both bilaterally and multilaterally in the Doha Development Round. U.S. Trade Representative Robert B. Zoellick and his Indian counterpart, Minister of Commerce and Industry Kamal Nath, held several meetings in 2003-2004. The AUSTR for South Asia regularly visits India and meets with Indian diplomatic and trade officials, as well as U.S. and Indian private sector representatives, to identify ways to open India's markets. As part of the United States-India Economic Dialogue, the United States-India Trade Policy Working Group meets regularly to discuss the full range of bilateral trade and investment issues.

In the World Trade Organization (WTO), India has bound tariffs on 68 percent of its industrial goods tariff lines. The majority of these bindings exceed India's applied rates of duty. In agriculture, India's WTO bound tariffs range from 100 percent to 300 percent, also higher than the applied rates in many product areas.

The Indian government publishes tariffs and additional tax rates applied to imports, but there is no single official publication that includes all information on tariffs, fees, and tax rates on imports. The system is characterized by a lack of transparency. Importers must consult separate tariff and excise tax schedules, as well as any applicable additional public notifications and notices, to determine current tariff and tax rates. Furthermore, official Indian publications use different classification nomenclatures for tariffs and excise taxes, which cause confusion. Each Indian state also levies taxes on interstate commerce, which creates additional confusion. The government has taken steps to implement a Value-Added Tax (VAT) on April 1, 2005 that is meant to replace inter-state taxes, but previous deadlines for VAT implementation have not been met.

Import Licensing

As a result of a WTO dispute settlement action the United States initiated in 1997, India has eliminated its import licensing requirements for most consumer goods. Importers of vehicles of any type, however, face restrictive and trade-distorting import practices. For example, the GOI requires special licenses for importing motorcycles that are virtually impossible to obtain. Import licenses for motorcycles are granted only to foreign nationals: (1) permanently residing in India; (2) working in India for foreign firms that hold greater than 30 percent equity; or (3) working at embassies located in India. Certain domestic importers are eligible to import vehicles without a license, but only if these imports are offset by exports attributable to the same importer.

In addition, India continues to maintain a negative import list. The negative list is currently divided into three categories: (1) banned or prohibited items (e.g., tallow, fat, and oils of animal origin); (2) restricted items which require a non-automatic import license (e.g., livestock products, certain chemicals); and (3) "canalized" items (e.g., petroleum products, some pharmaceuticals, and bulk grains) importable only by government trading monopolies subject to cabinet approval regarding timing and quantity.

India has liberalized many restrictions on the importation of capital goods. The government allows imports of all second-hand capital goods by the end-users without requiring an import license, provided the goods have a residual life of five years. Refurbished computer spare parts can only be imported if an Indian Chartered Engineer certifies that the equipment retains at least 80 percent of its residual life.

Fertilizer Subsidy Regime

The Indian government subsidizes di-ammonium phosphate (DAP) fertilizer. Under the current system, which the current government says it will revise by April 1, 2006, the GOI sets a maximum retail price that can be charged to farmers for DAP. This price is not adequate to cover the cost of producing or importing DAP. The excess costs for domestic producers and importers were subsidized, at different levels that favored domestic DAP over imports. Since July 2004, subsidies have been equalized but at a level insufficient to allow for regular commercial import transactions. Prior to 2000, the subsidy differential was minimal and encouraged both the import of finished DAP and domestic production. Beginning in 2000, the subsidy differential between domestically produced DAP and imports put DAP importers at a competitive disadvantage. U.S. imports shrunk by 75 percent from a high of $414 million in 1999, to approximately $100 million in 2004, even though Indian domestic production could not keep pace with rising demand. The United States continues to press India to end its costly, trade-distorting treatment of DAP fertilizer.

Customs Procedures

The GOI appears to apply discretionary customs valuation criteria to import transactions. Valuation procedures issued on September 7, 2001, allow Customs to reject the declared transaction value of an import because a particular sale: (a) was not undertaken "in the ordinary course of trade under fully competitive conditions;" or (b) involved a "reduction from the ordinary competitive price." U.S. exporters have reported that India's customs valuation methodologies do not reflect actual transaction values and effectively increase tariff rates. The United States is working through the WTO Committee on Customs Valuation to obtain further information from India on the operation of these amendments, and will continue to examine the customs valuation procedures for consistency with India's obligations under the Customs Valuation Agreement.

Indian Customs requires extensive documentation, which inhibits the free flow of trade and leads to frequent processing delays. In large part these delays are a consequence of India's complex tariff structure and multiple exemptions, which may vary according to product, user, or specific Indian export promotion program.

India introduced a reference price system for soybean oil in September 2002 to address alleged under-invoicing. The reference price is the basis upon which India assesses its 45 percent customs duty. When the GOI reference price for soybean oil rises above the transaction price, the effective rate of duty may also increase above India's 45 percent WTO-bound tariff. The GOI states that the reference price is reviewed as frequently as weekly and adjusted, if published world prices differ by plus or minus 10 percent from a calculated three week moving average. India has not formally defined this procedure, making it non-transparent and unpredictable. Exports of U.S. crude soybean oil to India were negligible in 2003 after accounting for $25 million in 2002. The U.S. Government continually raises this issue with India, but has not received a response from the Indian government that clarifies its policy and the reference price scheme's relationship to India's WTO commitments.

Certain customs procedures impede importation of automotive products. Motor vehicles may be imported through only three specific ports and only from the country of manufacture. Declared transaction values of automotive products may be rejected, insofar as legitimate reductions in the wholesale price of such products are ignored.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The GOI has identified 109 specific commodities (including food preservatives and additives, milk powder, infant milk foods, certain types of cement, household and similar electrical appliances, gas cylinders and multi-purpose dry cell batteries) that the Bureau of Indian Standards (BIS) must certify before the products are allowed to enter the country. A system now exists by which foreign companies can receive automatic certification for products made outside India provided BIS has first inspected the production facility (at the manufacturers expense). Licensing fees include the cost of the initial inspector's visit and tests, an annual fee of approximately $2,000 and a marking fee that ranges from 0.2 to 1 percent of the value of certified goods imported into or produced in India.

In 2004, Indian Customs began to require registration or an exemption certificate for imported boric acid. The Ministry of Agriculture's Central Insecticides Board and Registration Committee has not yet published criteria and procedures for obtaining this documentation. Imports of boric acid are, therefore, effectively blocked. Indian government rule making has been *ad hoc* and confusing. India may be the only country that requires registration of boric acid intended for non-insecticide use. U.S. industry is required to register, although it asserts that 90 percent of all boric acid imports into India are for non-insecticide uses and should qualify for an exemption. India's boric acid producers are not, according to U.S. industry, subject to the same constraints. We have sent a demarche addressing this issue to the GOI and are awaiting a response.

India's procedures for establishing emissions standards are vague and non-transparent. The emissions standards seem to favor small displacement four-stroke motorcycles that are primarily manufactured by Indian producers. Even the latest low-emission technology used by U.S. manufacturers fails to meet India's requirements.

In 2001, India banned textile and apparel imports that contain certain dyes. In January 2004, the GOI relaxed its textile-testing requirement by announcing that it would accept, as proof of the absence of azo-dye, certification that the exporting country had banned azo-dyes in textiles.

Sanitary and Phytosanitary (SPS) Measures

The U.S. Government has raised with India concerns regarding its failure to notify certain SPS measures. Bilateral technical level discussions are ongoing and have resulted in a short-term agreement for important U.S. export commodities, such as almonds. The U.S. government continues to impress upon India the need to base its SPS measures on science, including those affecting apples, dairy products, pulses, poultry, pet food, and forest products. The United States will continue to seek a long-term solution regarding almonds and other outstanding SPS issues.

In 2003, the Ministry of Health implemented amendments under its Prevention of Food Adulteration Act (PFA) which could potentially restrict Indian imports of several agricultural products. In addition, at the end of 2003, the Ministry of Agriculture issued a set of new phytosanitary regulations and quarantine requirements for imports of agricultural products. These are entitled the "Plant Quarantine (Regulation of Import into India) Order, 2003". GOI implementation of these measures prior to notifying them to the WTO SPS Committee jeopardized Indian imports of U.S. almonds, pulses, fresh fruits and vegetables. Furthermore, new requirements affecting solid Wood Packaging Material (SWPM), as they were initially drafted, threatened adversely to impact U.S. exports of nonagricultural products. Bilateral discussions led the Ministry of Agriculture to amend its quarantine requirement for wood packaging materials to make it compatible with international standards, thereby resolving the market access problem.

The Indian government has implemented several sanitary restrictions, which do not appear to coincide with the Office of International Epizootics (OIE) and CODEX recommendations. The OIE and CODEX are the global standard setting bodies for animal health issues and food products respectively. Such restrictions have affected Indian imports of poultry and poultry products, and pet food and dairy products. Until February 2004, the Indian pet food market had been a rapidly growing and promising market for U.S. exports. U.S. government officials have regularly called upon Indian sanitary authorities in an effort to resolve this problem.

The GOI reports that it is currently reviewing its policy for evaluating the safety of biologically engineered foods. In 2002, the Genetic Engineering Approval Committee (GEAC), the Indian government's regulatory body for biotechnology products, conditionally approved the import of refined soy oil and crude de-gummed soy oil. It declined, however, to consider importation of a corn-soy blend (CSB) without a special U.S.-issued certification. Even if a satisfactory certificate were available, the GEAC has not specified the criteria upon which it would evaluate the safety of CSB. In the absence of a policy framework for assessing the safety of biotechnology commodities and foods, the decision-making process within the GEAC is slow, non-transparent and arbitrary. Meanwhile, Indian researchers themselves are engaged in the domestic development of agricultural products derived from biotechnology such as mustard seed, potatoes, tomatoes, cabbage, cauliflower, chilies, groundnuts, and rice.

GOVERNMENT PROCUREMENT

India is not a signatory to the WTO Agreement on Government Procurement. Indian government procurement practices and procedures are non-transparent. Foreign firms rarely win Indian government contracts. In 2004, the GOI extended until April 2005 a policy giving preference to public sector companies whose offers are within 10 percent of the lowest bidder and are willing to match that price. As this applies to procurements by India's numerous public sector enterprises as well as government agencies, the policy seriously restricts the ability of US firms to compete in the Indian market.

EXPORT SUBSIDIES

As part of its Foreign Trade Policy announced in August 2004, the GOI committed to revise its export-based import-duty drawback scheme to address WTO inconsistencies. The GOI continues, however, to maintain a number of "incentive" programs that effectively subsidize exports. In 2004, 30 percent of export profits could be deducted from a company's gross taxable income. The tax exemption for profits from export earnings is being phased out over five years ending March 31, 2005. Tax holidays will continue for Export Oriented Units and exporters in Special Economic Zones. The GOI purchases wheat and rice on the local market at support price levels. At times the government has exported its stocks at prices well below the domestic price.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Intellectual property protection in India is weak but likely to improve as a result of expanded patent coverage effective January 1, 2005. USTR placed India on the "Priority Watch List" as part of the 2004 "Special 301" review.

Patents

On December 27, 2004, the GOI issued a Patent Amendment Ordinance just ahead of India's January 1, 2005 WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) deadline to enact product patent protection. The ordinance extends product patent protection to pharmaceuticals and agricultural chemicals. To make these changes permanent, the Indian Parliament must ratify this ordinance or pass substitute legislation before the six-month ordinance period expires. While a positive step, these changes do not address several important weaknesses in India's patent law. For example, as currently written, the new ordinance does not clarify some ambiguities regarding the scope of patentable inventions.

In December 2003, the GOI issued regulations to implement the Protection of Plant Varieties and Farmers' Rights Act, passed in August 2001. As a result, India provides protection for plant varieties.

Indian law does not provide for protection against unfair commercial use of test or other data that companies submit to the government in order to obtain marketing approval for their pharmaceutical or agricultural chemical products. Since 2003, the GOI has been debating the provision of such protection, but has taken no action. Without specific protection against unfair commercial use of clinical test data, companies in India are able to copy certain pharmaceutical products and seek immediate government approval for marketing based on the original developer's data. Recognizing the role that TRIPS-consistent protection plays in fostering innovation and investment, a small, but growing, domestic Indian constituency, comprised of Indian pharmaceutical companies, technology firms and educational and research institutions, favors changes to improve protection of data.

Copyrights

U.S. industry estimates that, in 2003-2004, lost sales resulting from piracy in India of U.S. motion pictures, sound recordings and musical compositions, computer programs, and books totaled about $500 million.

In 2000, India amended and substantially weakened the software provisions of its Copyright Act which, since 1995, had been one of the most progressive in the developing world. Nevertheless, the Information Technology Act of 2000 includes penalties for the unauthorized copying of computer software. Penalties of up to $240,000 can be applied to unauthorized copying. Also, the penalty affords no immunity from prosecution under other laws. But, to our knowledge, no successful prosecutions have emerged from the Indian court system.

The GOI is not a party to either the 1996 WIPO Copyright Treaty (WCT) or the WIPO Performances and Phonograms Treaty (WPPT). For several years a "core group" of GOI officials, local industry representatives, academics and lawyers has been discussing amendments to the Indian Copyright Act which would enable India to implement these treaties. The core group has yet to introduce the necessary amending legislation. United States' attempts to provide useful input into this process continue to be disregarded.

The Indian Constitution delegates enforcement responsibility to the state governments. The central government can pass laws but the states are responsible for implementing them. The Central Bureau of Investigation (CBI), for example, which has inter-state jurisdiction, does not pursue IPR-related cases. The state, municipal or local police forces - although untrained - are charged with enforcing IPR laws.

Piracy of copyrighted materials (particularly software, films, popular fiction works and certain textbooks) remains a problem for both U.S. and Indian producers. Pirated semiconductors are sold in violation of copyright and semiconductor mask laws. India has not adopted an optical disc law to deal with optical media piracy, although inter-ministerial consultations to examine this option are now underway. Classification of copyright and trademark infringements as "cognizable offenses" has expanded police search and seizure authority. The law provides for minimum criminal penalties, including mandatory minimum jail terms. If implemented, these penalties, U.S. industry believes, could effectively deter piracy. The establishment of a copyright enforcement advisory council with responsibility for policy development and coordination, as well as the initiation of a program for training police officers and prosecutors concerned with enforcement of copyright laws, has not been vigorously pursued. Due to backlogs in the court system and documentary and other procedural requirements, few cases recently have been prosecuted. U.S. and Indian industry report that piracy levels in all sectors remain high.

Cable television piracy continues to be a significant problem, with estimates of tens of thousands of illegal systems in operation in India. Copyrighted U.S. product is transmitted over this medium without authorization, often using pirated videocassettes, VCDs, or DVDs as source materials. This widespread copyright infringement has a significant detrimental effect on all motion picture market segments in India - theatrical, home video and television. For instance, pirated videos are available in major cities before their local theatrical release. The proliferation of unregulated cable TV operators has led to pervasive cable piracy. The United States continues to press for effective copyright enforcement and has found pockets of positive movement.

Trademarks

The Government of India has pledged to upgrade its trademark regime. Upgrades include national treatment for the use of trademarks owned by foreign proprietors, statutory protection of service marks, and clarification of the conditions under which the cancellation of a mark due to non-use is justified. In December 1999, after four years of debate, India passed new trademark legislation. It provides protection for service marks for the first time. Implementing regulations to put the new law into effect were not published until September 2003. Although enforcement is improving, protection of foreign marks in India remains difficult.

The required registration of a trademark license (described by U.S. industry as highly bureaucratic and time-consuming) can be refused on such grounds as "not in the public interest," "will not promote domestic industry," or for "balance of payments reasons." The Foreign Exchange Management Act 1999 (FEMA) restricts the use of trademarks by foreign firms unless they invest in India or supply technology.

The United States continues to press for adequate and effective protection of trademarks and looks forward to India fulfilling its pledge to upgrade its trademark regime.

Enforcement

India's criminal justice system does not effectively support the protection of intellectual property. India's criminal IPR enforcement regime, including border protection against counterfeit and pirated goods, remains weak. There have been few reported convictions for copyright infringements resulting from raids, including raids against recidivists. Adjudication of cases is extremely slow. Police action against pirates of motion pictures has improved somewhat since 2003. No criminal software end-user piracy cases have resulted in convictions to date. Obstruction of raids, leaks of confidential information, delays in criminal case preparation and the lack of adequately trained officials have further hampered the criminal enforcement process.

Recent amendments to the Code of Civil Procedure requiring that civil cases must be completed within one year may provide more expeditious disposition of the civil cases brought by U.S. industry in Indian courts.

SERVICES BARRIERS

Indian government entities run many major services industries either partially or entirely. Nevertheless, both foreign and domestic private firms play a large role in advertising, accounting, car rental, and a wide range of consulting services. There is a growing awareness of India's potential as a major services exporter and increasing demand for a more open services market. While India has submitted an initial WTO GATS offer to provide further services liberalization in the context of the WTO Doha Development Agenda, it does not go far enough in removing existing restrictions in its services market in key sectors such as professional services, telecommunications and financial services. The United States will continue to press India for further market opening in these sectors and its services market overall to provide additional export opportunities for U.S. services providers.

Insurance

Prior to 2000, all insurance companies were government-owned, except for a number of private sector firms providing reinsurance brokerage services. The Insurance Regulatory and Development Authority (IRDA) bill ended the government monopoly and established an insurance regulator. The law opened India's insurance market to private participation with a limit on foreign equity of 26 percent of paid-up capital. In July 2004, the GOI announced its intention to amend the IRDA law to increase that cap to 49 percent. Intense domestic political debate has delayed action.

Banking

Most Indian banks are government-owned, and entry of foreign banks remains highly regulated. State-owned banks control 80 percent of the banking system. The Reserve Bank of India has granted operating approval to 25 new foreign banks or bank branches since issuing new guidelines in 1993. As of September 2004, 35 foreign banks with 217 branches were operating in India. Five U.S. banks now have a total of 16 branches in India. They operate under restrictive conditions including tight limitations on their ability to add sub-branches. Foreign direct investment (FDI) in banking is slowly being liberalized and the foreign equity ceiling has been raised to 74 percent from 49 percent for investment in private banks. FDI in state-owned banks remains capped at 20 percent. Foreign investor voting rights are capped at 10 percent in private banks and one percent in state-owned banks Foreign banks may operate in India through only one of three channels; branches, a wholly owned subsidiary, or up to 74 percent ownership in a private Indian bank.

Audiovisual and Communications Services

The Indian government has removed most barriers to the import of motion pictures, although U.S. companies have experienced difficulty in importing film/video publicity materials and are unable to license movie-related merchandize due to royalty remittance restrictions.

Legislation passed in December 2002 allowed the GOI to put in place the Conditional Access System (CAS) for cable television whereby television subscribers would be required to install set-top-box decoders to view premium channels. By providing tighter regulation of the cable industry as a whole, CAS was expected to help reduce the problem of pirated broadcasts. In March 2004, in the face of considerable distributor and consumer resistance, as well as confusion surrounding pricing issues and other rules, the GOI suspended implementation of CAS pending review by a regulatory authority.

The government of India permits FDI of up to 49 percent in Indian cable networks and companies that uplink from India. Total foreign investment in Direct to Home (DTH) broadcasting has been restricted to 49 percent, with an FDI ceiling of 20 percent on investments by broadcasting companies and cable companies. At present, news channels are permitted to have up to 26 percent foreign equity investment. As of August 2003, they must also ensure that a dominant Indian partner holds at least 51 percent equity. In addition, operational control of the editorial content must be in Indian hands. The Indian government has also announced other minimum capitalization requirements. In December 2004, the Telecom Regulatory Authority of India (TRAI) implemented regulations requiring (1) all pay television content providers to make their content available to all cable and satellite television system operators; and, (2) requiring 30 days public notification before content providers can cut off their signals to non-paying system operators.

Accounting

Only graduates of an Indian university can qualify as professional accountants in India. Foreign accounting firms can practice in India, if their home country provides reciprocity to Indian firms. Internationally recognized firm names may not be used, unless they are comprised of the names of proprietors or partners, or a name already in use in India. This limitation applies to all but the two U.S. accounting firms that were established prior to the imposition of this rule. Effective July 1, 1998, the Institute of Chartered Accountants of India (ICAI) banned the use of logos of accounting firms. Only firms established as a partnership may provide financial auditing services. Foreign accountants may not be equity partners in an Indian accounting firm.

Construction, Architecture and Engineering

Many construction projects are offered only on a non-convertible rupee payment basis. Only government projects financed by international development agencies permit payments in foreign currency. Foreign construction firms are not awarded government contracts unless local firms are unable to perform the work. Foreign firms may only participate through joint ventures with Indian firms.

Legal Services

The Indian Bar Council has imposed restrictions on the activities of foreign law firms in recent years that have sharply curtailed U.S. participation in the Indian legal services market.

Telecommunications

India has one of the fastest growing telecommunications markets in the world and has taken positive steps towards liberalizing the market and introducing private investment and competition in basic telecommunications services. Concerns remain regarding interconnection charges for new entrants, India's weak multilateral commitments in basic telecommunications, and the apparent bias of telecommunications policy towards government-owned service providers.

The national telecommunications policy allows private participation in the provision of basic (including cellular) and value-added telecommunications services. Foreign equity in value-added services is limited to 51 percent. For basic services, the limit was 49 percent, but was raised to 74 percent in February 2005. Private operators can provide services within regional "circles" that roughly correspond to the borders of India's states.

Private competitive carriers are concerned about the neutrality and fairness of government policy. The Indian government retains a significant ownership stake and interest in the financial health of the dominant telecommunications firms, all of which formerly enjoyed monopoly status in their areas of operation. The government holds a 26 percent position in the international carrier, VSNL, a 56 percent position in MTNL, which primarily serves the Delhi and Bombay metropolitan areas, and a 100 percent position in BSNL, which provides domestic services throughout the rest of India. The government has indicated it will privatize MTNL and BSNL in the future but has not established a timetable.

American telecommunications companies have complained about the restrictive polices adopted by incumbent Indian international service provider VSNL on international submarine cable access and landing stations in India. They complained about the discriminatory and monopolistic practices of VSNL and requested the Indian government to intervene to ensure VSNL makes available submarine cable capacity to other suppliers on a reasonable and non-discriminatory basis. In mid-2004, VSNL reached agreement with then-U.S.-based Flag Telecom, allowing the latter to sell international bandwidth through a VSNL landing station; however, overall capacity constraints and artificially higher prices persist in the market.

In October 2003, the Indian cabinet approved the introduction of a unified license regime for cellular and basic telecommunications services. India continues to modernize its regulatory framework, with a draft "convergence" bill which is pending parliamentary consideration. The bill will consolidate authority over telecommunications, the Internet, and broadcasting in a single, super regulator.

In January 2003, TRAI implemented an interconnection Access Deficit Charge. Although revised in October 2003 and lowered further in late 2004, this charge appears inconsistent with India's legal and regulatory requirements that such charges be cost-based, completely neutral, and nondiscriminatory.

Internet telephony became legal in India in 2002, but this long-awaited liberalization came with several restrictions. Only Internet Service Providers (ISPs) are allowed to offer Internet telephony within their service areas, and telephone-to-telephone communications through the Internet remain illegal within India.

Distribution Services: Direct Selling

U.S. direct selling firms have been misclassified as retail instead of wholesale companies, and have also been mischaracterized as illegal pyramid schemes. Current Indian law does not sufficiently differentiate between legitimate direct selling operations and pyramid schemes.

INVESTMENT BARRIERS

Equity Restrictions

Most sectors of the Indian economy are now partially open to foreign investment, with certain exceptions. The Indian government continues to prohibit or severely restrict FDI in certain politically sensitive sectors, such as agriculture, retail trading, railways, and real estate. At the same time, the GOI has liberalized other aspects of foreign investment and eliminated various government approvals. Automatic FDI approval in many industries, including bulk manufacturing activities, is now allowed. Some sectors still require government approval.

Foreign industries have expressed concern with the Indian government's stringent and non-transparent regulations and procedures governing local shareholding. Current price control regulations have undermined incentives to increase equity holdings in India. Some companies report forced renegotiation of contracts in the power sector to accommodate government changes at the state and central levels. Press Note 18, promulgated in 1998 by the Ministry of Industry, poses major impediments to investment in India by requiring prior approval of the Indian party to a joint venture before the foreign partner can pursue other investment opportunities in India. This provision had been widely abused, holding foreign partners hostage, even for failed joint ventures. In January 2005, the GOI partially lifted Press Note 18 by eliminating its application to all new joint ventures and relaxing the hold local firms have on the future business plans of foreign partners for existing joint ventures.

Investment Disputes

Although the new government wants to increase infrastructure investment, high-profile commercial disputes in the power sector, such as the Dabhol power project, dampen investor sentiment. The U.S. Government is taking the GOI to state-to-state international arbitration because OPIC has been unable to resolve a $300 million to $400 million claim - including a $110 million expropriation claim - against the GOI under the Dabhol project. This is the first time that the U.S. Government has had to file a claim on behalf of OPIC. This dispute is one of many involving U.S. and other investors in India's power sector. The United States continues to try to persuade the GOI that, to attract investment, India needs to provide a secure legal and regulatory framework for the private sector.

ANTICOMPETITIVE PRACTICES

India suffers from a slow bureaucracy and regulatory bodies that reportedly apply monopoly and fair trade regulations selectively. With little or no fear of government action and with a clogged court system where cases linger for years, Indian firms face few if any disincentives to engage in anticompetitive business practices.

Although the Indian Parliament approved competition legislation in 2002 that provided for a new regulatory authority, the Competition Commission of India (CCI) has yet to be constituted due to disagreement over its leadership and its relationship to the judicial system. The new law does not prohibit monopolies but does charge the CCI with regulating unfair practices and promoting policies that favor competition.

OTHER BARRIERS

India has an unpublished policy that favors countertrade (a form of trade in which imports and exports are linked in individual transactions). The Indian Minerals and Metals Trading Corporation is the major countertrade body, although the State Trading Corporation also handles a small amount of countertrade. Private companies are encouraged to use countertrade. Global tenders usually include a clause stating that, all other factors being equal, preference will be given to companies willing to agree to countertrade. The exact nature of offsetting exports is unspecified, as is the export destination. The Indian government does try, nonetheless, to eliminate the use of re-exports in countertrade.

India's medicines policy is an issue of concern for U.S. pharmaceutical companies. While the scope of the rigid government-controlled pricing system has been reduced, final steps to eliminate it have stalled and some politicians and GOI officials continue to call for expanding price controls as the preferred means to confront inflationary trends.

Indian states fail to apply consistently certain national laws and regulations. This creates uncertainty for U.S. companies exporting to, and investing in, India. U.S. companies affected by such inconsistency include: cable television content providers of programming subject to conditional access system rules, pesticide manufacturers whose products have been approved at the national level and banned at the state level, and distilled spirits producers who face non-uniform state-level taxes despite the national government’s directive to harmonize such taxes. In addition, taxes on inter-state trade and conflicting regulations continue to hamper the free flow of goods within India.

India’s implementation of its antidumping regime has raised concerns in key areas such as transparency and due process. India continued aggressively to apply its antidumping law over the past year. From the second half of 2003 through the first half of 2004, which is the most recent 12-month period for which WTO statistics are available, India imposed 38 final antidumping measures, more than any other WTO Member, and ranked second in the number of initiations. Of the newly initiated investigations, six of which involved U.S. exports, chemical products were the leading target of investigation. The United States will continue to seek clarification and address concerns both bilaterally and multilaterally. Most recently, the United States participated in a technical exchange with Indian antidumping administrators to obtain a better understanding of India’s trade remedies laws and their compliance with India’s WTO obligations.

INDONESIA

TRADE SUMMARY

The U.S. trade deficit with Indonesia was $8.1 billion in 2004, an increase of $1.1 billion from $7.0 billion in 2003. U.S. goods exports in 2004 were $2.7 billion, up 6.1 percent from the previous year. Corresponding U.S. imports from Indonesia were $10.8 billion, up 13.6 percent. Indonesia is currently the 39th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Indonesia were $1.1 billion in 2003 (latest data available), and U.S. imports were $278 million.

The stock of U.S. foreign direct investment (FDI) in Indonesia in 2003 was $10.4 billion, up from $10.3 billion in 2002. U.S. FDI in Indonesia is concentrated largely in the mining, utilities, and manufacturing sectors.

OVERVIEW

Although Indonesia's economy weathered the 2002 global economic slowdown relatively well, the country still has not fully recovered from the effects of the 1997-98 financial crisis. The government of former President Megawati Soekarnoputri maintained a measure of political stability during its tenure, despite an ongoing conflict with separatists in the gas-rich province of Aceh. In 2004, Indonesians elected a new President, Susilo Bambang Yudhoyono, who took office in October pledging fundamental reform as part of his "100-Day Plan." President Yudhoyono has announced an ambitious economic reform program that focuses on reducing poverty by raising Indonesia's GDP growth rate, eliminating corruption, and improving the business climate. The earthquake and tsunami that struck Sumatra and the Indian Ocean region on December 26, 2004, left over 150,000 dead in Indonesia alone and caused incalculable human suffering as well as losses in property and infrastructure. As of the end of 2004, it was unclear what effect this natural disaster would have on Indonesia's economy and President Yudhoyono's reform plans.

The Indonesian government generally has adhered to its long-term trade liberalization program, although some backsliding occurred under the Megawati administration between 2002 and 2004. Indonesia fully implemented the final stage of its commitments under the ASEAN Free Trade Agreement (AFTA) on schedule on January 1, 2002. However, during its tenure, the Megawati administration expressed reservations about the pace of liberalization within AFTA, and noted an interest in pursuing emergency exit clauses from AFTA commitments in general.

Indonesia has a mixed record in the WTO. In the current Doha multilateral negotiations, Indonesia continues to advocate special product exemptions for rice, sugar, soybeans, and corn. 2002 textile regulations favor domestic textile fabrics over imports, and we have raised our concerns in the WTO. However, in 2003 the government used WTO-compliant mechanisms, like safeguards, as an alternative to protectionist measures.

Indonesia's garment sector suffers from poor capital investment and low productivity. Some observers predict the industry may lose half of its four percent world market share following the expiration of the Multi Fiber Agreement at the end of 2004.

The new Yudhoyono administration has pledged to reassert Indonesia within multilateral trade organizations like the WTO, APEC and ASEAN. The new government has also committed itself to improving Indonesia's trade competitiveness by streamlining bureaucracy, improving competitiveness, and rectifying ill-conceived policies of the past.

Indonesia's relationship with the International Monetary Fund (IMF) provided the framework for the country's economic policies since November 1997. IMF-supported economic reforms helped stabilize the macro economy, restructure the financial sector, and reinforce policies of trade and investment liberalization. Indonesia concluded its IMF program at the end of 2003.

President Yudhoyono has proposed creating an economy characterized by efficient resource allocation, open markets and free trade, the protection of property rights, and a stronger rule of law that is applied transparently and free from corruption and that diffuses knowledge broadly. He has also proposed increasing Indonesia's competitiveness in priority sectors including: electronics, textiles, automotive, fisheries, wood-based and rubber-based industries, as well as key service sectors such as air travel, tourism, health care and electronic commerce, and small- and medium-sized businesses. The economic goals expressed by President Yudhoyono touch on U.S. industry's continuing concerns over the wide range of business problems it encounters in Indonesia, including the lack of contract enforceability, discriminatory taxation, the absence of a transparent and predictable regulatory environment, arbitrary and inconsistent interpretation and enforcement of laws, irregularities in government procurement tenders, and ineffective enforcement of intellectual property rights. These business problems cause great uncertainty, which combined with widespread corruption, an ineffective judicial system, non-existent credit reporting, and underdeveloped capital markets, hinders commercial dealings in Indonesia.

IMPORT POLICIES

Tariffs

As of January 2003, about 70 percent of Indonesia's tariff lines were assessed import duties ranging between zero percent and five percent. Indonesia's unweighted tariff average is 7.3 percent, compared to 20 percent in 1994.

In the late 1980s the Indonesian government began long-term trade reform to wean the economy away from its dependence on oil and gas and to increase Indonesia's industrial competitiveness. In the early 1990s, it began a series of annual deregulation packages designed to gradually lower applied tariff rates, convert non-tariff barriers into tariffs, and remove restrictions on foreign investment. The January 11, 2001, tariff reduction package cut five percentage points on 1,279 tariff lines. The majority, 769 lines, had tariff rates reduced to 10 percent or below. Effective January 1, 2002, Indonesia, along with the other five original ASEAN members, implemented the final phase of the ASEAN Free Trade Agreement (AFTA). Indonesia has reduced tariffs for all products included in its original commitment (7,206 tariff lines) to five percent or less for products of at least 65 percent ASEAN origin. The government released a new tariff reduction package in January 2004. The new tariff book categorizes tariffs into International Non-ASEAN Tariffs and ASEAN Tariffs. Most Non-ASEAN tariffs fall into 0 percent, 5 percent, and 10 percent tiers, except for sensitive items such as automotive goods and alcohol. ASEAN tariffs fall into three tiers, 0 percent, 2.5 percent, and 5 percent, for all goods covered by the ASEAN Free Trade Agreement (AFTA).

In the Uruguay Round market access negotiations, Indonesia committed to bind 94.6 percent of its tariff schedule; most tariffs are bound at 40 percent. Products for which tariff bindings exceed 40 percent, or which remain unbound include automobiles, iron, steel, and some chemical products. Indonesia committed to remove import surcharges on items bound in the Uruguay Round by the year 2005, and had done so by the end of 1996. In accordance with the WTO Agreement on Agriculture, Indonesia agreed to eliminate non-tariff barriers on agricultural products, and replace them with tariffs. In the agricultural sector, 1,341 tariff lines have bindings at or above 40 percent, including the most sensitive and heavily protected sectors. In the current WTO Doha negotiations, Indonesia has been advocating special products exemptions from tariff reductions for rice, sugar, soybeans, and corn.

Beginning in 2002 and intensifying through 2004, domestic agricultural interests put pressure on the Indonesian government for protection from international competition. However, with some notable exceptions, the Indonesian government has resisted such pressure. Since late 1999, rice imports have been subject to a specific tariff of 430 rupiah per kilogram (5.1 cents per kilogram or approximately 30 percent on an *ad valorem* basis). In 2004, the Indonesian government instituted bans on imports of rice, sugar and salt. Local agriculture interests continue to lobby the government to increase tariff rates above the levels bound in the WTO on sensitive agricultural products, such as sugar, soybeans and corn. However, the Yudhoyono administration has announced plans for a review of all rules and regulations related to imports and exports and business licensing. The stated intention of the review is to identify and rectify onerous bureaucracy and ill-conceived trade policies.

Non-Tariff Barriers

Since 1997, Indonesia has dismantled many formal non-tariff barriers. In September 1998, the Indonesian government sharply curtailed the role of the National Logistics Agency (Bulog), which had a monopoly on importing and distributing major bulk food commodities, such as wheat, rice, sugar, and soybeans. Bulog now maintains the status of a state-owned enterprise with responsibility for maintaining stocks for distribution to military and low-income families, and for managing the country's rice stabilization program. The agency has floated the idea of again becoming a state trading enterprise with monopoly import rights for some products, but the Indonesian government has not taken action on this proposal. Bulog is no longer entitled to draw on Bank Indonesia credit lines, a privilege it long enjoyed under the Soeharto regime, and must use commercial credit and pay import duties. In conjunction with the minimization of Bulog's authority and role, some designated private companies are now permitted to import rice, wheat, wheat flour, soybeans, garlic, and sugar.

The Indonesian government continues to maintain a ban on imports of chicken parts originally imposed in September 2000 by the Directorate General of Livestock Services in the Ministry of Agriculture. The U.S. government has raised concerns about this issue, but the Ministry of Agriculture continues to insist on the necessity to assure consumers that imports are halal (produced in accordance with Islamic practices). U.S. imports comply with Indonesia's established requirements for halal certification, and several ministries have unsuccessfully sought to repeal the ban. U.S. industry estimates the value of lost trade from this ban at roughly $10 million per year.

Indonesia's government also imposes *de facto* quantitative restrictions on imports of meat and poultry products by requiring an Importer Letter of Recommendation ("Surat Rekomendasi Importir"). In approving requests for such letters the government can arbitrarily alter the quantity allowed to enter, raising concerns that these Letters of Recommendation are being used to limit imports. U.S. industry estimates the annual trade impact of this restriction to be between $10 million and $25 million.

The government imposed a rice import ban in February 2004 just prior to the rice harvest season (February - May). The ban is supposed to be in effect one month before and two months after the planting season. The Ministry of Agriculture, however, requested that the ban be extended through the end of 2004. Meanwhile, U.S. rice exports increased from $5 million in 2001 to $18.5 million in 2002. Most of these exports were linked to two P.L. 480 Title I concessional loan programs in each respective year. Although the Indonesian government rejected the program for 2003, U.S. rice exports reached $16.3 million (mostly for humanitarian purposes), 12.2 percent lower than in 2002.

In June 2004, the Ministry of Trade banned the importation of salt during the harvest season from July through the end of the year. Under the regulations, salt importing companies must be registered and source 50 percent of their raw materials locally. A September 2004 Ministry of Industry and Trade decree allows five companies to import sugar. It also states that the Ministry of Trade decides which companies can import sugar and how much.

The U.S. government has received reports that Indonesia's Customs Service uses a schedule of arbitrary "check prices" rather than actual transaction prices on importation documents for assessing duties on food product imports. While Indonesia's government officials defend this practice on the basis of combating under-invoicing, they do not publicize the list or the methods used to arrive at those prices. As a result, although most food product import tariffs remain at five percent, the effective level of duties can be much higher.

Other quantitative limits apply to wines and distilled spirits. In addition to the regular import duty of 170 percent, a 10 percent VAT and 35 percent luxury tax, Indonesia's government restricts imports of alcoholic beverages to three registered importers, including one state-owned enterprise.

Import Licensing

Indonesia's government has continued to reduce the number of products subject to import restrictions and special licensing requirements. Currently, 141 tariff lines are subject to import licensing restrictions, down from 1,112 tariff lines in 1990. Alcoholic beverages, lubricants, explosives, and certain dangerous chemical compounds, among other items, are subject to these requirements.

In March 2002, the Minister of Industry and Trade issued a decree on Special Importer Identification Code Numbers (NPIK). This decree requires importers of certain product categories to apply for a special importer identity card, without which products can be detained at port. These goods include: corn, rice, soybeans, sugar, textile and related products, shoes, electronics and toys.

On October 23, 2002, the Minister of Industry and Trade issued a decree concerning Textile Import Arrangements. Only companies that have production facilities to use imported fabrics as inputs for finished products, such as garments or furniture, may obtain import licenses. The United States has raised serious concerns that the import licensing requirements severely restrict and distort trade. Indonesia's government insists the regulations are designed to help curb smuggling. The U.S. Government has recommended that the decree be rescinded.

STANDARDS, TESTING, LABELING AND CERTIFICATION

In July 2000, the Indonesian government began to implement the Consumer Protection Law of 1998 by requiring registration of imported food products. Importers must apply for a registration number from the Agency for Drug and Food Control (BPOM). After complaints from Indonesian importers and retailers of overly complex, time consuming, and costly requirements, BPOM drafted revised procedures that would simplify the process. However, those draft regulations have stalled in the President's Office without approval or further comment.

All imported food products must be tested by BPOM. Fees for such testing range from Rp 50,000 ($6.00) to Rp 2.5 million ($300) per item, and between Rp 1 million ($120) to Rp 10 million ($1200) per product. Some U.S. producers have expressed concerns that the extremely detailed information on product ingredients and processing they must provide may infringe upon proprietary business information. This has led some U.S. exporters to discontinue sales.

However, the government has not fully implemented these regulations, and enforcement is weak and inconsistent. If fully implemented the annual level of trade adversely affected by this requirement is estimated by U.S. industry at between $10 million and $25 million.

Indonesia's government also has been gradually implementing a strict food labeling law that requires labels written only in the Indonesian language on all consumer products. Labels may not include any other languages. U.S. companies, which generally design labels to accommodate several export markets (often in several languages), have concerns about this requirement because it makes it cost ineffective to export smaller volume products. However, as of December 2004, the government had not issued implementing rules or enforced the food labeling requirement. The United States is closely monitoring this situation.

Beginning January 2001, Indonesia's regulations required labels identifying food containing "genetically engineered" ingredients and "irradiated" ingredients. However, the government has not implemented these new requirements because it has yet to establish minimum threshold-presence levels. U.S. industry estimates that the new regulation could affect sales of approximately $411 million annually in soybeans and soybean meal from the United States. The United States is closely monitoring the situation.

GOVERNMENT PROCUREMENT

Indonesia is not a party to the WTO Government Procurement Agreement (GPA). Indonesia's government procurement regime is governed by a number of overlapping laws, regulations, and presidential decrees. Most important is a presidential decree issued in February 2000, which updated the Law on Government Procurement of 1994. The decree simplified procurement procedures and enhanced transparency, but also granted special preferences to domestic sourcing. In addition, Construction Law 14/1999 governs procurement of civil engineering services and related consulting services. Regional decentralization also may introduce additional barriers as local and provincial governments adopt their own procurement rules.

Bilateral or multilateral donors finance many large government contracts and often impose special procurement requirements. For large, government-funded projects, international competitive bidding practices must be followed. The Indonesian government seeks concessional financing for most procurement projects. Since late 1999, the Indonesian government has conducted audits of the state-owned electricity company (PLN), the state oil and gas company (Pertamina), and the State Logistics Agency (Bulog), which identified serious irregularities in procurement. However, no legal action has been taken.

Foreign firms bidding on high value government-sponsored construction or procurement projects have been asked to purchase and export the equivalent value in selected Indonesian products. Government departments, institutes, and corporations are expected to utilize domestic goods and services to the maximum extent feasible, with the exception of foreign aid-financed goods and services procurement projects. State-owned enterprises that publicly offer shares through the stock exchange are exempted from government procurement regulations. The new oil and gas upstream authority, BP Migas, regulates the import of all materials used by the oil and gas sector.

EXPORT SUBSIDIES

In 2004, the Indonesian government ended several credit programs that offered subsidized loans to agriculture and small and medium sized businesses to support exports.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The United States placed Indonesia on the "Priority Watch List" again in 2004, due to continued weak IPR enforcement. Previous Special 301 Annual Reviews in 2003, 2002 and 2001 identified a range of IPR concerns, including rampant software, audio, video disk and book piracy; pharmaceutical patent infringement; counterfeiting; trade secret protection; data protection; apparel trademark counterfeiting; an inconsistent and corrupt law enforcement regime; and an ineffective judicial system. The lack of effective IPR protection and enforcement are major disincentives to foreign investment in Indonesia, particularly in high technology sectors.

The government agency responsible for IPR legislation, the Ministry of Justice Directorate General for Intellectual Property Rights, works closely with industry groups. However, prosecution of violators has been difficult due to inadequate police action, prosecutor and judge unfamiliarity with the new law, as well as the Indonesian public's limited understanding of the importance of IPR protection, and rampant corruption. In 2001, the Indonesian judiciary began consideration of certain IPR cases in the Commercial Courts. In a landmark case that year, a U.S. software company won a civil suit against five retailers for selling computers bundled with pirated software. In their first two years, the Commercial Courts have concluded over 150 cases. Nonetheless, U.S. companies often find the Indonesian court system unpredictable in practice and ineffective in punishing violators. Industry representatives say the vast majority of criminal prosecutions must be dropped due to poor evidence documentation and maintenance, as well as widespread corruption within the justice system. The few cases that are concluded by the courts often result in minimum sentences and/or fines being imposed which are not sufficient to act as a deterrent.

Indonesia is a member of the WIPO and has acceded to numerous international conventions on IPR. These include the Paris Convention for the Protection of Industrial Property, the Berne Convention for the Protection of Literary and Artistic Works, the WIPO Copyright Treaty, the Patent Cooperation Treaty, the Trademark Law Treaty, the Nice Agreement for the International Classification of Unclassified Goods and Services, and the Strasbourg Agreement Concerning International Patent Classification. Despite well-publicized raids on pirate operations in the last few years, industry sources report that Indonesia ranks very poorly when compared to its peers in ASEAN in its record for payment of IPR royalties.

Copyrights

The new copyright law came into force in July 2003, one year after it passed Parliament. The law contains a number of important provisions long sought by U.S. and Indonesian copyright holders, including provision for the issuance of an implementing regulation on optical disks (OD), criminal penalties for end-user piracy and the ability of rightholders to seek civil injunctions against pirates. President Megawati signed the OD regulation into law in October 2004. The outgoing Minister of Industry and Trade issued two ministerial decrees required to implement the OD regulation. These new regulations include a six-month transition grace period and will become effective in April 2005.

The Copyright Law establishes rights to license, produce, rent or broadcast audiovisual, cinematographic, and computer software. It also provides protections for neighboring rights in sound recordings and for the producers of phonograms. It stipulates a 50-year term of protection for many copyrighted works, meeting TRIPS Agreement requirements. A 1989 copyright agreement between the United States and Indonesia extends national treatment for copyright protection to works created by citizens of each country.

The government's enforcement of copyrights is uneven, although it periodically intensifies actions against copyright piracy and officials regularly consult with copyright holders and associations. However, piracy of video compact disks in Indonesia is widespread, undermining the sale and rental of legitimate products. Periodic raids result in the seizure of sizable caches of pirated OD products. However, none of these cases has resulted in meaningful penalties or permanent impoundment or destruction of equipment used to manufacture pirated products. In recent years, movies on high-quality pirated digital video disks (DVDs) have become increasingly available alongside video compact disks (VCDs). According to U.S. industry estimates, total losses from copyright piracy in Indonesia during 2002 were nearly $260 million, the last year for which consolidated losses are available.

Patents

Indonesia enacted its Patent Law on August 1, 2001. The law consolidated three previous laws covering patents, and established an independent commission to rule on patent disputes and appeals. The law transferred jurisdiction over IPR civil cases to the Commercial Court from the District Court and raised the maximum fine for patent violations to Rp 500 million ($60,000). The term of protection remains 20 years with a possible two-year extension. A patent is subject to cancellation only in the event the patent holder fails to pay annual fees within specified periods. Unauthorized use of a product or process invention that is the subject of a pending application constitutes patent infringement.

Despite these measures, a lack of effective enforcement of patent rights continues. The patent law does not correct some of the weaknesses that concern foreign rights holders. Chief among these is the requirement that an inventor must produce a product or utilize a process in Indonesia to obtain a patent for the product or process. The standard for excluding inventions contrary to the public interest from patentability appears broader than the standards enumerated in the TRIPS Agreement.

Trademarks

Indonesia enacted its trademark law on August 1, 2001. The trademark law consolidated three prior laws enacted over 20 years. The law raised the maximum fine for trademark violations to Rp 1 billion ($120,000) and slightly reduced the maximum possible prison term. The government justified this move by claiming that financial penalties were a greater deterrent to IPR violators than imprisonment. Foreign rights holders, arguing that most IPR cases never result in the maximum sentence, had pushed for minimum sentencing guidelines rather than higher fines.

The trademark law provides for the determination of trademark rights by priority of registration, rather than by priority of commercial use. The law also provides for the protection of well-known marks, but offers no administrative procedures or legal grounds under which legitimate owners of well-known marks can cancel pre-existing registrations. Indonesia’s trademark officials’ requirement that all trademark modifications be registered raises concerns under the TRIPS Agreement and the Paris Convention. Currently, the only avenue for challenging existing trademark registrations in Indonesia is through the courts, an often-burdensome undertaking that must be initiated within five years from the date of the disputed registration. Faster processing (within 180 days) of trademark cases by the Commercial Courts has benefited some trademark holders. However, industry representatives had hoped courts additionally would use injunctions, especially in cases where a lower court eventually invalidates a false trademark registration.

SERVICES BARRIERS

Despite relaxation of some restrictions, particularly in the financial services sector, trade barriers to services continue to exist in many sectors.

Legal Services

A few local law firms currently dominate the legal market, and foreign law firms cannot operate directly in Indonesia. In order to practice legally, lawyers must hold Indonesian citizenship and a degree from an Indonesian legal facility or other recognized institution. Foreign lawyers can only work in Indonesia as "legal consultants" and must first obtain the approval of the Ministry of Justice and Human Rights. A foreign law firm seeking to enter the market must establish a relationship with a local firm.

Distribution

In 1998-99, Indonesia liberalized portions of the distribution services sector under terms of its agreements with the IMF. The Indonesian government eliminated restrictive marketing arrangements for cement, paper, plywood, cloves and other spices. Indonesia has opened the wholesale and retail trade sectors to foreign investment. Since 1998, it has allowed up to 100 percent foreign equity in the distribution and retail sectors, with the condition that the investor enter into a "partnership agreement" with a small-scale Indonesian enterprise. This partnership agreement need not involve an equity stake in the project. The film sector is not covered by this regulation. There is a ban on all foreign investment in media businesses, including cinema construction or operation, video distribution and broadcast services. Presidential decrees issued in July and August 2000 prohibit foreign investment in broadcast and media sectors, including the film industry (film making, film technical service providers and movie house operations). The decrees also prohibit foreign investment in the provision of radio and television broadcasting services, radio and television broadcasting subscription services and media print information services.

In October 2001, Indonesia passed a new Oil and Gas Law to deregulate downstream activities. Presidential Decree 86/2002 and Government Regulation 67/2002 establish a new Oil and Gas Downstream Business Regulating Board (Badan Pengatur Kegiatan Usaha Hilir Migas, or BPH Migas) to control downstream activities. Although the day-to-day activities of the board must still be defined through implementing regulations, BPH Migas will be an independent government institution that reports directly to the President. Its primary functions include regulating the supply and distribution of oil fuel, allocating sufficient fuel oil to meet national fuel oil reserves, stipulating conditions on fuel oil transportation and storage, setting tariffs for natural gas pipeline use, setting the price of natural gas for households and small consumers, and regulating the transmission and distribution of natural gas.

Financial, Accounting and Banking Services

Under the WTO Financial Services Agreement, Indonesia committed to allow 100 percent foreign ownership for non-bank financial services companies that are publicly listed, including insurance and securities firms. Indonesia also guarantees the access of existing financial services firms in its market. It lifted restrictions on branching and sub-branching for joint venture banks and foreign branches in 1998.

Paid-in capital requirements are twice as high for multi-finance companies with foreign partners than for domestic multi-finance companies. However, in November 1998, Parliament passed amendments to the 1992 banking law that allow 100 percent foreign ownership of Indonesian banks. All insurance policies in Indonesia must be purchased from either domestic or joint venture companies unless specific coverage is unavailable in Indonesia or if the insured is a wholly foreign-owned entity. Under an Insurance Industry Association rule, supported within the GOI, Insurance companies are required to purchase a percentage of their reinsurance for earthquake coverage (5 percent for West Java and Jakarta and 25 percent elsewhere) from the local firm MAIPARK. There is discussion about soon expanding that requirement to coverage of floods.

Accounting Services

Foreign firms cannot practice under international firms' names, although terms such as "in association with" are permissible. Foreign accounting firms must operate through technical assistance arrangements with local firms. Foreign agents and auditors may act only as consultants and cannot sign audit reports. Licensed accountants must hold Indonesian citizenship.

Audio-Visual

Indonesia prohibits foreign film and videotape distributors from establishing branches or subsidiaries. Under the Film Law, provision of importation and distribution services is limited to wholly-owned Indonesian companies. The film law contains a screen quota that gives priority to the showing of local Indonesian language films. However, this has not proven to be a serious barrier as few local films have been produced in recent years.

Construction, Architecture and Engineering

Foreign consultants working under government contract are subject to government billing rates. Foreign construction firms are only permitted to be subcontractors or advisors to local firms in areas where the government believes that a local firm is unable to do the work. In addition, for government-financed projects, foreign companies must form joint ventures with local firms.

Telecommunications Services

The provisions of Indonesia's Telecommunications Law 36, which came into force in 2000, have guided reforms to end monopolies and open basic telecommunications services to majority foreign ownership. Telecom Law 36 lays out goals that exceed many of the modest commitments Indonesia agreed to under the WTO Basic Telecommunications Agreement (maximum foreign investment limit of 35 percent for telecommunications services companies) and the WTO Pro-Competition Annex in 1997 (transparent regulatory procedures, nondiscriminatory licensing, and competitive safeguards for companies operating in Indonesian markets).

In 2002, subsequent implementing regulations for Telecom Law 36 established conditions for a new policy of duopoly and accelerated reforms. The government ended the exclusive rights of PT Telkom for domestic long distance service and local fixed-line service in August 2003, and of PT Indosat and Satelindo for international calling service in 2003. The requirement for a foreign satellite operator to have an Indonesian partner, however, perpetuates inefficiency, raises costs to Indonesian consumers, and constitutes a serious trade barrier. Indonesia also formed a telecommunications regulatory body in July 2004 to improve transparency in regulation development and dispute resolution.

Telecom Law 36 removed previous requirements that prospective foreign investors partner or enter into a revenue-sharing arrangement with a state-owned enterprise. In January 2002, to attract investors the government committed to raise telephone tariffs each year for three years to achieve market levels. Popular resistance, however, prevented the second round of price increases in 2003. Indonesia has undertaken partial privatizations of its telecommunication companies. In July 2002 government ownership of PT Telkom was reduced to 51 percent, after a public offering of 3.1 percent. In December the same year, the government reduced its ownership of PT Indosat to 15 percent, after it sold 41.9 percent to Singapore Technologies Telemedia.

Despite the autonomous liberalization that Indonesia has implemented, the government has yet to submit a revised telecommunications offer in the Doha Development negotiations in the WTO.

INVESTMENT BARRIERS

Indonesia's investment climate is poor. The World Economic Forum's 2003 competitiveness rankings scored Indonesia 97th of 102 countries. Foreign direct investment (FDI) has declined steeply since the 1997-98 financial crisis and in the last few years the numbers have been inflated by the inclusion of state-owned firms that were partially privatized. Government approvals for investment proposals reached $14.6 billion in 2003, $9.8 billion in 2002, an adjusted $9 billion in 2001, and $16 billion in 2000. Investment proposals from Asia, North American and Europe - traditionally large investors - declined from 2002. Most of this investment is never realized.

On January 1, 2001, Indonesia began to implement a large-scale decentralization of authority and budget from the central government to the provincial and district-level governments. Differences of opinion between the central and local governments about which has authority on certain issues has added to the level of uncertainty facing foreign investors. In many areas, even though contrary to law, local governments have instituted revenue-raising measures ("retribusi"), which are trade-distorting.

Decentralization has complicated government efforts to improve Indonesia's investment climate and reduce burdensome bureaucratic procedures and other requirements on foreign investors. Indonesian law provides for both 100 percent FDI projects and joint ventures with a minimum Indonesian equity of five percent. Currently, BKPM and other relevant agencies in certain sectors must approve proposed foreign investments, but under the proposed law, BKPM would be responsible for approvals in all sectors, including licenses, tax incentives, and business registrations. The Government is considering proposing a revised investment law to Parliament in 2005 that would streamline foreign investment approval procedures.

Indonesia blocks or restricts foreign investment in some sectors in addition to those service sectors mentioned above. These restricted sectors are described in the "negative list." The most recent version, issued in August 2000, is based on Presidential decree 96, which opened some sectors, particularly certain medical services, to foreign investment. The negative list restricts foreign investment in industries producing marijuana, certain environmentally harmful chemicals, chemical weapons, and alcoholic drinks, and it closes to foreign investment casino and gambling facilities, air traffic and marine vessel certification and classification systems, and radio frequencies. However, various infrastructure, airline, medical services, marine and fisheries, industrial, and other trade sectors are open to investment subject to joint venture or other conditions.

ELECTRONIC COMMERCE

Despite the proliferation of Internet service providers in recent years, several factors hinder the growth of electronic commerce in Indonesia. These include the lack of a clear policy in support of an open telecommunications infrastructure, monopoly provision of fixed landline service by PT Telkom, a low level of computer ownership by both businesses and individuals, lack of funding, and weak IPR protection. U.S. industry has identified the lack of a legal framework for ensuring security of online transactions as a particularly significant impediment. Indonesia's government expects to complete drafting of cyber crime and electronic transactions legislation in early 2005.

OTHER BARRIERS

Transparency

President Yudhoyono has stated repeatedly that eliminating corruption will be one of his Administration's top priorities. Nonetheless, a lack of transparency and widespread corruption are significant problems for companies doing business in Indonesia. Corruption was endemic under the former Soeharto regime, and still remains an enormous problem for foreign companies. These companies are concerned about demands for irregular fees to obtain required permits or licenses, government awards of contracts and concessions based on personal relations, and an often arbitrary legal system.

Many laws passed since late 1997 have established new institutions and agencies to respond to popular demands to address corruption, collusion, and nepotism, but poor implementation has undermined that effectiveness. Indonesia's government established stiffer penalties for corruption as well as an independent commission to investigate and audit the wealth of senior government officials. In December 2003, the government also established an Anti-Corruption Commission.

Automotive Policies

On June 24, 1999, the Indonesian government announced a major revision of its national automotive policies in order to rely on market forces to foster a more efficient and globally competitive automotive industry. The new policy eliminated extensive tariff and tax incentives for local content. The Indonesian government reduced the maximum tariff on automobiles from 200 percent to 80 percent. Tariffs on passenger car kits imported for assembly, which had ranged from zero percent to 65 percent, were reduced to 25 percent, 35 percent, 40 percent, or 50 percent depending on engine size. Tariffs on non-passenger car kits were reduced to a uniform 25 percent. Tariffs on auto components and parts imported for local assembly of passenger cars and minivans were changed to a uniform rate of 15 percent. Imports of motor vehicles are no longer restricted to registered importers or sole agents of foreign automakers, but are open to any licensed general importer. U.S. motorcycle manufacturers are concerned about the high tariff of 60 percent (25 percent on knockdown kits), the luxury tax of 75 percent, and the prohibition on motorcycle traffic on tollways as barriers to the Indonesian market.

In December 2000, Indonesia's government restructured the way luxury sales taxes are imposed on motor vehicles. The luxury sales tax on 4,000cc sedans and 4x4 Jeeps or vans was raised from 50 percent to 75 percent. The luxury tax on automobiles with engine capacity between 1,500cc and 3,000cc was increased from 15 percent to between 20 percent to 40 percent, depending on the size of the engine. This decision had a significant negative impact on the market since 65 percent of the market share belongs to automobiles with engine sizes between 1,500cc and 3,000cc.

ISRAEL

TRADE SUMMARY

The U.S. trade deficit with Israel was $5.3 billion in 2004, a decrease of $548 million from $5.9 billion in 2003. U.S. goods exports in 2004 were $9.2 billion, up 33.5 percent from the previous year. Corresponding U.S. imports from Israel were $14.5 billion, up 13.8 percent. Israel is currently the 19th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Israel were $2.3 billion in 2003 (latest data available), and U.S. imports were $1.8 billion.

The stock of U.S. foreign direct investment (FDI) in Israel in 2003 was $6.2 billion, up from $5.6 billion in 2002. U.S. FDI in Israel is concentrated largely in the manufacturing sector.

The United States-Israel Free Trade Area Agreement

Under the United States-Israel Free Trade Area Agreement (FTA), signed in 1985, the United States and Israel agreed to phased tariff reductions culminating in the complete elimination of duties on all products by 1995. In practice, most tariffs between the United States and Israel have been eliminated as agreed, although tariff and non-tariff barriers continue to affect a certain portion of U.S. agricultural exports.

Israel continues to restrict market access for certain U.S. agricultural products. To temporarily and partially address the differing views between the two countries over how the U.S.-Israel FTA applies to trade in agricultural products, in 1996 the United States and Israel signed an Agreement on Trade in Agricultural Products (ATAP), establishing a program of gradual and steady market access liberalization for food and agricultural products effective through December 31, 2001. Negotiation and implementation of a new ATAP was successfully completed in 2004. The new agreement is effective through December 31, 2008, and provides improved access to selected U.S. agricultural products. The agreement provides U.S. food and agricultural products access to the Israeli market under one of three different categories: unlimited duty-free access; duty-free tariff-rate quotas (TRQs); or preferential tariffs, which are set at least 10 percent below Israel's most-favored nation (MFN) rates. The ATAP also provides for annual increases in TRQs.

IMPORT POLICIES

Tariffs

Under the 1985 FTA, the United States and Israel agreed to eliminate duties on all products by January 1, 1995, the end of the implementation period. Israel removed duties on U.S. non-agricultural products according to the FTA schedule, but substantial tariffs remain on some U.S. agricultural products.

Agriculture

Approximately 90 percent of U.S. agricultural exports (by value) enter Israel duty- and quota-free as a result of Israel's implementation of commitments under the WTO, the FTA, and the new ATAP. However, remaining U.S. agricultural exports consisting largely of consumer-oriented goods face restrictions such as a complicated tariff-rate quota system and high tariffs. In addition, the ability of U.S. exporters to utilize available quota volumes can be hampered by problems with the administration and transparency of Israel's TRQs. TRQ-related problems include lack of data on quota fill rates and license allocation issues such as small non-commercially viable quota quantities and difficulties in obtaining licenses for within-quota imports. The Israeli government has committed to taking steps to improve the administration of TRQs, including engaging in regular bilateral consultations through a review mechanism created by the new ATAP.

U.S. agricultural exports without free access to Israel primarily consist of high value goods which are important to the Israeli agricultural sector such as dairy products, fresh fruits, fresh vegetables, almonds, wine, and some processed foods. According to industry estimates, elimination of levies on processed foods could result in increased sales by U.S. companies in the range of $25 million to $50 million (with appropriate market development efforts). Removal of quotas and levies on dried fruits could result in increases in sales by U.S. exporters of up to $10 million. U.S. growers of apples, pears, cherries and stone fruits estimate that elimination of Israeli trade barriers would lead to an increase of $5 million to $25 million in export sales of these products. It is estimated that free trade in agriculture could result in U.S. almond exports growing by as much as $10 million.

Labeling Requirements

Imported food products face rigid labeling requirements. For many products, the labeling required by Israel is far more detailed than that required in the United States. The cost of additional labeling has acted as a deterrent for many U.S. companies who have considered marketing their products in Israel. The loss of sales of American products is difficult to estimate due to the variety of products affected by these regulations.

Customs Procedures

Some U.S. exporters have reported difficulties in claiming preferences under the U.S.-Israel Free Trade Agreement. Israeli concerns about the U.S. methods for issuing certificates of origin have sometimes delayed entry of, or delayed preferential tariff treatment to, U.S. goods going into Israel.

Meat Imports and Kosher Certification

Israel prohibits the importation of any meat or meat product that is not certified as kosher by Israel's chief rabbinate, a policy that presents significant challenges for U.S. meat exporters. There is strong demand in Israel for quality kosher beef. However, the process for granting kosher certificates is expensive and complex. In 2002 the U.S. meat industry and the two governments attempted, but were unable to develop, steps to facilitate U.S. compliance with Israel's kosher requirements. Industry estimates that kosher certification for U.S. meat could result in an annual increase in U.S. meat exports of $15 million in the medium term and more than $25 million in the long-term. In addition, work on an agreement on veterinary certificates of health for live animal imports was suspended after the announcement of the discovery of a single U.S. case of BSE involving an imported animal.

Israel permits the domestic production and marketing of non-kosher meat, but bans its importation. The ban on the import of non-kosher meat raises questions in terms of the 1985 FTA requirement that any religious-based restrictions be applied in accordance with the principle of national treatment. U.S. firms estimate that elimination of the prohibition on non-kosher imports could result in increased sales of less than $10 million.

Wine Imports

The 2004 Agreement on Trade in Agricultural Products for the first time grants U.S. wine exporters an annual tariff-rate quota of 200,000 liters of wine, with preferences over Israel's MFN rate for exports over and beyond that level. However, other impediments to U.S. wine exports remain. Wine importers also note that the government of Israel does not require Israeli wine producers to follow the detailed labeling requirements of the official Israel Standard for Wine, while these rules are strictly enforced on imported wines.

Rabbinical regulations for kosher certification also pose challenges for the wine industry. For example, rabbinical regulations do not permit use of the same company name on kosher and non-kosher wines. To keep their kosher certification, importers of kosher wines are not permitted to import non-kosher wines. Kosher wines cannot be stored in the same warehouse as non-kosher wines.

Sales of U.S. wines to Israel are about $700,000 per year. The industry estimates that the elimination of trade barriers could result in increased exports worth up to $10 million per year.

Purchase Taxes

In February 2004, the GOI announced a series of cuts in purchase taxes as part of a wide-ranging plan to reduce taxes to help benefit weak sectors in the economy. This included reducing taxes on televisions, videos, and DVDs from 45 percent to 15 percent, and reducing taxes from 15 percent to 5 percent on household appliances, such as refrigerators, ovens, dishwashers, washing machines, and dryers. In April 2004, purchase taxes on raw materials and building materials were eliminated. In December 2004, the Ministry of Finance announced a tax increase on cigarettes.

Textiles

Israel restricts imports of used clothing, and bans the importation of seconds fabrics. There has been an increased enforcement effort by the Israeli Customs Authority regarding its inspection of textile products entering Israel under the auspices of the U.S.-Israeli FTA. For apparel shipped from, but assembled outside, the United States, the Customs Authority requires a statement from the U.S. exporter with a complete breakdown of the value for each type of item in the shipment by design, cutting, assembly, etc., to determine whether the goods qualify to enter Israel under the FTA rules of origin.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Technical standards are increasingly becoming a prominent non-tariff barrier limiting U.S. exporters' access to the Israeli market. Since 1999, Israeli law mandates that the Standards Institution of Israel (SII) adopt multiple international technical standards whenever possible. However, the SII has not implemented this concept. In addition, SII's formal process for adopting or developing technical standards appears to be a significant market-access obstacle to U.S. exporters despite concerted U.S. Government efforts to address the underlying issues of access and transparency. Moreover, each government ministry may adopt mandatory new regulations that can prevent the importation of U.S.-made products and services to Israel. This procedure has also created difficulties for U.S. exporters who contend that transparency and due process are frequently lacking, most notably for food imports. In addition, industry has said that requirements for technical standards are often not uniformly enforced. In some instances, domestic products appear to have an advantage over imports because enforcement of standards on domestic producers has been inconsistent, while standards requirements are more strictly applied to imported goods. U.S. companies that have been doing business in Israel for many years have increasingly been confronted by new, often EU-based, standards. In addition, the SII does not recognize U.S. testing or accreditation of electrical components and products without the product undergoing additional and often costly tests in Israel.

GOVERNMENT PROCUREMENT

Israel is a signatory to the WTO Agreement on Government Procurement (GPA), which covers most Israeli government entities and government-owned corporations. Most of the country's open international public tenders are published in the local press. However, government-owned corporations make extensive use of selective tendering procedures. In addition, the lack of transparency in the public procurement process discourages U.S. companies from participating in major projects and disadvantages those that choose to compete. Enforcement of the public procurement laws and regulations is not consistent. Poor design and unfair management of public tenders discourages U.S. bidders.

In accordance with the Israel public tendering law, all international public tenders with a value of at least $500,000 contain requirements for "industrial cooperation" (IC) with Israeli entities. Under the IC agreements, foreign companies offset their income from Israel by agreeing to invest in local industry, co-develop or co-produce, subcontract to local companies, or purchase from Israeli industry. The current IC offset percentage for industries covered under the WTO GPA is 30% of the value of the contract; for industries excluded from the GPA, including most military procurements and El Al, it is 35%. U.S. suppliers have found the size and nature of their IC proposals to be a decisive factor in tight tender competitions, despite a court decision that prohibits the use of offset proposals in determining award of a bid. Small and medium-size U.S. exporters are often reluctant to commit to make purchases in Israel in order to comply with the IC requirements and refrain from participation in GOI tenders. At Israel's request, the WTO Committee on Government Procurement granted Israel an additional year (until the end of 2005) to reduce the level of its offsets from 30 percent to 20 percent. Israel is now required to reduce the level of its offsets to 20 percent by January 1, 2006.

In addition, the inclusion of unlimited liability clauses in many government tenders discourages American firms from competing. When faced with the possibility of millions of dollars in legal costs for unforeseeable problems resulting from a government contract, most American firms are forced to insure against the risk, which raises their overall bid price, and reduces their competitiveness.

For civilian local currency procurement by the Ministry of Defense (MOD), a U.S.-Israeli Memorandum of Understanding (MOU), extended in 1997, gives U.S. competitors equal status with domestic suppliers. This MOU applies to procurements that are not connected with U.S. military assistance programs. Despite this MOU, U.S. suppliers have expressed concern about the lack of transparency and apparent lack of justification for excluding U.S. suppliers from MOD tendering opportunities. The MOU, which has had a favorable effect on the Israeli defense industries by opening up the U.S. market to their products, has not resulted in an open market for U.S. suppliers competing on MOD's local currency procurements. Efforts by U.S. manufacturers or their agents to win military tenders for food have invariably met with failure.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Israel is a member of the World Trade Organization (WTO) and the World Intellectual Property Organization (WIPO). It is a signatory to the Berne Convention for the Protection of Literary and Artistic Works, the Universal Copyright Convention, the Paris Convention for the Protection of Industrial Property, and the Patent Cooperation Treaty. Israel was fully obligated to implement the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) in 2000. The United States would like to see Israel accede to the WIPO Copyright Treaty and the WIPO Performance and Phonograms Treaty (commonly known as the WIPO

Internet Treaties), particularly in view of the importance of Israel's high-technology software and telecommunication industries.

Although Israel has been obligated since January 1, 2000 to protect undisclosed test data from unfair commercial use, it has failed to do so. This lack of protection places it at odds with other OECD-level economies and many of its neighbors that have met their TRIPS Article 39.3 obligations. Israel does not deny that it relies, or allows a third party without authorization to rely, on data submitted by U.S. pharmaceutical firms when approving marketing applications from domestic generic competitors of U.S. innovator firms. The impact of Israel's failure to provide data protection is already being felt within the country. Research and development, as well as clinical trial expenditures made by international pharmaceutical companies, have fallen in recent years as these companies have moved these activities to countries with more favorable data protection regimes. The U.S. Government has urged the Israeli government and the Knesset to enact TRIPS-consistent legislation that will provide a reasonable period of non-reliance on confidential data similar to that granted in OECD countries and many neighboring countries. In March 2004, an inter-ministerial Israeli government commission issued findings that support the adoption of protection for confidential test data in Israel; however, legislation submitted by the Israeli Government for Knesset consideration in December would fall short of providing adequate data protection. At U.S. urging, the Israeli Government in early 2005 withdrew the legislation from consideration to allow the two sides additional time to seek a resolution of the data protection issue.

At the same time, Israel has increased its budgetary, educational, police, and judicial resources devoted to the enforcement of the country's copyright and trademark laws. In addition, Israel passed amendments to its copyright laws that should make it easier for law enforcement officials, prosecutors, and judges to pursue, prosecute, and punish copyright crimes. In 2003, the U.S. Trade Representative (USTR) recognized the country's efforts by moving Israel from the Special 301 Priority Watch List to the Watch List. While noting Israel's efforts, USTR said that it is essential that progress continue to be made in copyright and trademark enforcement, such as providing the Israeli police, prosecutors and courts with sufficient resources to fully meet enforcement requirements. In 2004, U.S. industry estimates the loss due to inadequate intellectual property protection $113 million.

In 2004, the government of Israel prepared new draft legislation intended to update and consolidate the country's copyright laws. This draft may exclude end-user piracy from criminal liability, a step that may lead to weaker protection for business software. In addition, a separate law concerning writable media threatens to legalize the downloading of protected content from the Internet, and compensating rights holders through a tax on the media itself.

In October 2004, the government of Israel assured the United States that it would continue to provide U.S. music rights-holders' with national treatment protection.

SERVICES BARRIERS

Audiovisual and Communications Services

Israel has made progress in liberalizing its telecommunications sector. Foreign companies are now able to participate in joint ventures providing cellular and international telephone service, DBS satellite broadcasts, cable television, and Internet service. Israel officially opened domestic telephone service to domestic and foreign competition in 2000.

The State of Israel now owns less than 50 percent of Bezeq, the telephone parastatal, after it sold off shares of the company in July and November 2003. Privatization of the remainder of Bezeq is moving ahead, with an information room opened for potential bidders in November 2004 and the Government Companies Authority monitoring the tender process.

In 2001, Bezeq received a license to provide high speed Internet service with the condition that it permits other Internet service providers to have access to its infrastructure. The Knesset amended the telecommunications law to permit cable television providers (including firms with U.S. ownership) to provide fast Internet and other telecommunications services.

The international telephone market expanded in 2004 with two of the Internet companies, Netvision and Internet Gold Lines, receiving licenses to provide international telephone service.

Only selected private Israeli television channels are allowed to air advertising. These channels received broadcast licenses and the advertising privilege in exchange for certain investment commitments. Israeli law largely prohibits other channels, both public and private, from airing advertising. The government funds the country’s public channels, whereas the remaining private channels generate revenues via subscription fees. In 2002, the Israeli government developed regulations that allow foreign channels aired through the country’s cable and satellite networks to broadcast a limited amount of advertising aimed at a domestic Israeli audience. Currently, the regulations allow foreign channels to use up to 25 percent of their total advertising time to target the Israeli market. The regulations allow a foreign channel to apply for more than 25 percent advertising time if the channel can prove that it has a sizable viewing audience outside of Israel. The U.S. Government worries that any restrictions on advertising might inhibit the economic viability of U.S. firms’ participating in the Israeli broadcasting sector.

INVESTMENT BARRIERS

The Israeli government actively solicits foreign private investment, including joint ventures, especially in industries involving exports, tourism, telecommunications, and high technology. Foreign firms are accorded national treatment in terms of taxation and labor relations, and are eligible for incentives for designated "approved" investments in priority development zones. There are generally no ownership restrictions, but the foreign entity must be registered in Israel.

Profits, dividends, and rents generally can be repatriated without difficulty through a licensed bank.

Over 750 U.S. companies have subsidiaries in Israel. Estimates for the number of Israeli companies with subsidiaries in the United States range from 300 to 500. Investment in regulated sectors, including electronic commerce, banking, insurance, and defense industries, requires prior government approval. Israel is a member of the International Centre for Settlement of Investment Disputes (ICSID) and a party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

In an attempt to increase competition in the very concentrated banking sector and prevent conflicts of interest, the Government approved the Bachar capital market recommendations in November 2004. The two largest banks, Hapoalim and Leumi, control 61% of the banking sector's assets, and the 5 largest banks control 95% of the banking sector's assets.

The main aspects of the Bachar reforms include removing from the banks' ownership and management the Provident funds, which are private retirement funds, and mutual funds. This is to be done gradually over the next few years. In return, banks will be able to enter the insurance market, and sell life insurance. However, these reforms require Knesset approval.

ELECTRONIC COMMERCE

Israel generally supports U.S. efforts to ensure that electronic transmissions will not be subject to tariffs. U.S. industry has not reported any barriers to electronic commerce in Israel. Israel still lacks a clear body of regulations and tax laws covering electronic commerce-specific transactions. As a disincentive to online businesses, loopholes in the laws dictate that a consumer can decline to pay for any merchandise for which they did not physically sign. In August 2000, an Electronic Signature Bill was passed to regulate signatures on electronic media. The Ministry of Justice maintains a register of authorizing entities to issue electronic certificates attesting to the signature of the sender of an electronic message. Also under their jurisdiction is the Registrar of Data Bases, which by law must issue licenses to any firm or individual holding a client database. This measure is designed to protect client information from unwanted third party intrusion. It remains to be seen how the bill is being enforced, and whether businesses and consumers have increased confidence in electric commerce due to these measures.

JAPAN

TRADE SUMMARY

The U.S. trade deficit with Japan was $75.2 billion in 2004, an increase of $9.2 billion from $66.0 billion in 2003. U.S. goods exports to Japan in 2004 were $54.4 billion, up 4.6 percent from the previous year. Corresponding U.S. imports from Japan were $129.6 billion, up 9.8 percent. Japan is currently the 3rd largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Japan were $29.8 billion in 2003 (latest data available) and U.S. imports were $17.4 billion. Sales of services in Japan by majority U.S.-owned affiliates were $38.3 billion in 2002 (latest data available), while sales of services in the United States by majority Japan-owned firms were $22.3 billion.

The stock of U.S. foreign direct investment (FDI) in Japan in 2003 was $73.4 billion, up from $65.9 billion in 2002. U.S. FDI in Japan is concentrated largely in the finance, manufacturing, and wholesale sectors.

REGULATORY REFORM OVERVIEW

Japan's efforts to achieve meaningful structural and regulatory reform have begun to bear concrete results. Broadband utilization in Japan has increased greatly and can now be enjoyed at some of the fastest speeds and lowest costs in the world. Energy sector reform is creating greater opportunities for competition and paving the way for more efficient use of electricity and natural gas in Japan. In the financial sector, Japan has made significant progress in dealing with its non-performing loans and deflation. And there are now hundreds of Special Zones for Structural Reform up and running throughout Japan, spurring growth and innovation at the local level. The United States welcomes all this reform activity and the growth it is generating to put the Japanese economy back on track.

If Japan is to sustain this growth, however, it must hold firm in its determination to continue its bold reform agenda. The United States therefore welcomes Prime Minister Koizumi's unwavering commitment to a meaningful structural and regulatory reform agenda. In particular, the United States welcomes the Prime Minister's decision to establish the Council for the Promotion of Regulatory Reform (CPRR) to carry on the important work of the Council for Regulatory Reform. Structural and regulatory reform not only contributes to growth, but also plays an enormous role in increasing market access opportunities for U.S. companies.

The U.S. Japan Regulatory Reform and Competition Policy Initiative

The Regulatory Reform and Competition Policy Initiative (Regulatory Reform Initiative) is one of six components of the U.S.-Japan Economic Partnership for Growth (Partnership), which President Bush and Prime Minister Koizumi launched in June 2001. The Initiative addresses key sectors, including telecommunications, information technologies, energy, medical devices and pharmaceuticals, financial services, and agriculture. It also addresses crosscutting sectoral issues, including competition policy, transparency, privatization, legal system reform, revision of Japan's commercial law, and distribution. Through the Regulatory Reform Initiative, the United States continues to advocate the reform of laws, regulations, administrative guidance and other measures, formal and informal, that impede access to the Japanese market for U.S. goods and services.

Progress achieved in the third year of this Initiative was detailed in the Third Report to the Leaders and presented to President Bush and Prime Minister Koizumi at the G-8 Summit in Sea Island, Georgia, in June 2004. Kicking off the fourth year of the Regulatory Reform Initiative, the United States submitted its recommendations to Japan in October 2004 in Washington. This was followed by a first round of Working Group meetings held in early December. After convening another round of Working Group meetings and a deputy-level meeting in the spring of 2005, the two Governments intend to conclude a Fourth Report to the Leaders on the margins of the next G-8 Summit in Perthshire, Scotland, in early July.

SECTORAL REGULATORY REFORM

Telecommunications

Under the Regulatory Reform Initiative, the United States seeks regulatory changes to promote competition, innovation, and choice in Japan's telecommunications sector. The competitive and regulatory environment in this sector has evolved over the past several years, resulting in the rollout of numerous innovative technologies and competitively priced advanced services, including Digital Subscriber Line, Fiber-to-the-Home, and Voice Over Internet Protocol. Nevertheless, maintaining, and in some cases strengthening, dominant carrier regulation and competitive safeguards will be critical if competing carriers (both domestic and foreign-invested) are to offer viable alternatives to NTT's regional carriers and mobile operator.

Through its October 2004 Regulatory Reform submission and in bilateral consultations, the United States has asked Japan to take measures to address specific market access impediments related to a wide range of policies in this sector. If undertaken, these measures should help address important market access and regulatory barriers. Nevertheless, ensuring effective competition in Japan, especially in the local telecommunications markets, will require an independent regulator committed to ensuring equitable opportunities for new entrants and unbiased treatment of all operators. The United States continues to request that Japan develop a plan to move regulatory functions outside the purview of a ministerial agency, where it is subject to direct political control, to a fully independent organization. It is also important for Japan to establish and exercise meaningful sanction authority by the regulator (imposition of fines, payments of damages, license restrictions) to punish anticompetitive behavior.

Interconnection and Pricing: One of the most significant examples of insufficient safeguards on dominant carriers impeding competition is the high cost and onerous conditions that NTT regional operators are allowed to impose on their competitors for interconnection. In JFY 2003, the key interconnection rate was increased by 21 percent, and the revised rate for 2004 was increased an additional 6 percent in 2004. As a result, Japan continues to have some of the highest interconnections rates among OECD countries. The Ministry of Internal Affairs and Communications (MIC) is currently conducting another review to determine the rate system to be put in place from JFY 2005. The United States will continue to press Japan to correct the fundamental flaws of the methodology that caused the increased rates (primarily, inclusion of non-traffic sensitive costs in the rate calculation), as well as to address its lack of regulatory independence and accountability, which make it vulnerable to political influence throughout the rate-setting process.

Dominant Carrier Regulation: NTT has maintained its market dominance through a number of measures, such as denial of access to emergency services by interconnecting carriers and proposals for higher interconnection charges on carriers competing with alternative technologies (e.g., for DSL services). NTT also has been pressing MIC to remove fiber optic cable from the list of unbundled items they are required to make available to competitive carriers at non-discriminatory rates. The United States continues to monitor whether MIC is taking sufficient steps to ensure that NTT East and West will not take advantage of their dominant position to inhibit competition.

Mobile Termination: New entrants to Japan's telecommunications market have also expressed concern about the high access rates charged by NTT DoCoMo, the dominant wireless service provider. While DoCoMo reduced rates significantly in 2003, rate reduction in 2004 was barely four percent. Following reforms to the Telecommunications Business Law in 2001, DoCoMo was recognized as a dominant carrier in 2002, but MIC has not required DoCoMo to explain how its rates are calculated.

New Mobile Wireless Licenses: MIC’s role in limiting the mobile wireless market to three main competitors, dominated by NTT DoCoMo with a market share of over 50 percent, is problematic – particularly given the high mobile rates prevalent in the market, evidence that operators are warehousing spectrum, and opposition by one incumbent to any new market entry (a position inconsistent with Japan’s WTO commitments). MIC could greatly improve the competitive environment in the mobile wireless market by expanding market access opportunities through a more transparent and pro-competitive approach to spectrum allocation and assignment. Interest by U.S.-affiliated operators in new licenses makes this a priority issue.

Rights-of-Way: New competitors in Japan find it time-consuming and expensive to build competing networks in Japan because of high costs and difficulties related to access to "rights-of-way." A labyrinth of restrictions reportedly increase construction costs by roughly ten times and can result in digging that takes six times longer than in other major markets. Japan's e-Japan Strategy, which is designed to make Japan a global information technologies leader by 2005, includes measures to relieve these problems on an experimental basis (in particular, relaxing certain restrictions on the laying of fiber optic cable). The United States continues to urge mandatory rights-of-way access for new competitors and has proposed that Japan establish pro-competitive rules to ensure non-discriminatory, transparent, timely, and cost-based access for telecommunications carriers and cable television operators.

Information Technologies

Japan has made important progress over the last few years in removing numerous regulatory barriers as part of its efforts to become a world leader by 2005, a goal the Japanese government first outlined in a bold plan called the e-Japan Strategy. This progress has helped transform the landscape in Japan into one where broadband utilization is widespread and can be enjoyed at some of the fastest speeds available and at the lowest costs in the world. Japan has also increased the use of IT and online processes in the private and public sectors and is now one of the largest e-commerce markets in the world. The "e-Japan Priority Policy Program 2004" (2004 Priority Policies) reaffirms Japan's goals and prioritizes steps to achieve them, such as ensuring secure and reliable networks, focusing on IT adoption, protecting intellectual property, encouraging content development, and increasing use of e-government. The 2004 Priority Policies also acknowledge the private sector's leadership role in promoting IT usage, and the global nature of e-commerce.

The United States supports Japan's efforts to remove these barriers. The U.S. Government's recommendations in its October 2004 Regulatory Reform submission support Japan's goals by focusing on: 1) removing persistent legal and other barriers that hinder e-commerce; 2) allowing maximum private-sector flexibility, innovation, self-regulation, and leadership; 3) expanding private-sector input into the development of IT-related policy, regulations, and procurement reforms; 4) creating a legal structure that enhances efficiency and security and facilitates online transactions in all areas of the economy; 5) developing coordinated policies compatible with international practice; and 6) protecting and promoting intellectual property. The U.S. Government also urges Japan to ensure that new strategies, laws, ordinances, and guidelines to implement the 2004 Priority Policies do not promote, mandate, or unduly favor specific technologies (technological neutrality), in order to provide maximum flexibility and encourage innovation within the private sector.

Regulatory and Other Barriers: While Japan has made great strides in promoting e-commerce and increasing the use of online processes in the private and public sectors, legal and other regulatory barriers remain that prohibit Japan from fully realizing its IT potential. In its October 2004 Regulatory Reform submission, the United States is therefore urging Japan to: (1) remove barriers in existing laws and regulations that hinder e-commerce, such as permitting e-notification under the Money Lending Business Law and amending the Road Transportation Vehicle Law to allow registered owners of fleet vehicles to use online e-government systems to change fleet vehicle registrations; (2) create a flexible legal framework for digital storage and exchange of data in various sectors, including medical services, through the "e-Document Law" and its implementing regulations; and (3) implement measures to strengthen the ability of the IT Strategic Headquarters to produce coordinated, effective IT policymaking that meets the needs of the private sector.

Personal Data Regulation (Privacy): Since the Diet passed the Law on the Protection of Personal Information on May 23, 2003 (Privacy Law), several ministries and agencies have formulated implementation guidelines that must be finalized before the Law goes into effect in April 2005. The United States urges Japan to ensure the following: that any forthcoming privacy implementation guidelines are developed in a transparent and coordinated manner; that all final guidelines are consistent, complement existing international regulations, and not be overly burdensome; and that guidelines be enforced consistently and fairly. The United States suggests that implementing agencies issue authoritative government regulations and/or guidelines and examples for educational purposes, as had been discussed at the public/private privacy roundtable organized by the two Governments and held in Tokyo in May 2004. To further support Japan's efforts to establish privacy guidelines, the U.S. Government has been suggesting the co-sponsoring of a second privacy roundtable, where the ministries could further explain the implementation of their guidelines, as well as address industry's concerns regarding compliance and enforcement.

Alternative Dispute Resolution: Online dispute resolution is the only practical tool for consumers and online businesses to resolve the inevitable disputes that arise in business to consumer transactions. International practice allows for dispute resolution providers to be of the parties' choosing. Japan has been an outlier in this area as only members of Japan's bar have been permitted to profit from ADR services. This discouraged the development of online and offline dispute resolution in Japan. Late in 2004, Japan passed legislation to create a government certification system for ADR providers. This certification system, although voluntary, has the potential to actually discourage parties from choosing non-certified ADR providers. Given the impracticality of using an ADR provider certified by the Japanese government, the new legislation may not further the use of online dispute resolution in the cross-border context. (*See also Legal System Reform section in this chapter.*)

Strengthening Intellectual Property Rights (IPR) Protection: The October Regulatory Reform submission includes a number of recommendations to Japan intended to strengthen IPR, such as: (1) extending the term of copyright for sound recording and all other subject matter protected under Japan's Copyright Law; (2) adopting a statutory damages system that would act as a deterrent against infringing activities, ensure that right holders are fairly compensated for the losses suffered by infringement, and enhance judicial efficiency by eliminating the costly burden of having to establish and calculate actual damages and profits; and (3) actively working with the

United States to develop ways to promote greater protection of intellectual property rights worldwide, especially in Asia. (*See also Intellectual Property Rights Protection in this chapter*.)

Digital IPR: Japan's liability rules for Internet Service Providers (ISPs) went into effect in May 2002 along with implementing guidelines drafted by a private sector-led working group. The United States remains concerned that the liability rules: remain unclear; do not provide the appropriate balance among the interests of telecommunication carriers, ISPs, right holders, and website owners; and fail to provide adequate protection for right holders. The lack of adequate protection for right holders prevents them from obtaining appropriate remedies when infringement has occurred, adversely affects the financial stability of several creative industries such as the audio-visual and game software industries, and may hinder the development of creative works and new products that could be subject to online piracy. The United States urges Japan to monitor compliance with the implementing guidelines for ISP liability rules and their effectiveness for ensuring that infringing materials are removed from websites quickly and adequate remedies are provided for any injuries suffered. The United States also continues to urge Japan to support the continued existence of the private sector working group, and any revisions of the guidelines and/or the law for ISP liability rules that may be necessary to ensure an effective "notice and take down system" and the appropriate balance of the rights and interests of all parties.

The Japanese government took a significant step forward in protecting temporary copies (e.g., digital copies made in the RAM of a computer) by recognizing that "temporary storage" implicates the reproduction right. However, the scope of protection for temporary copies remains vague, which could erode the ability to protect copyrighted materials in Japan. Given the importance of this new interpretation, the United States will continue to monitor developments in this area.

Network Security: Japan's Ministry of Economy, Trade and Industry (METI) issued network security guidelines in April 2003 for its own use. MIC released similar guidelines in late 2003 for use by local governments. In addition, the Cabinet Secretariat in conjunction with various ministries is currently developing central government-wide network security guidelines. Ministries are also scheduled to begin development of guidelines for key industrial sectors as well. The United States is urging Japan to ensure that any network security standards and guidelines developed for use by the Japanese government or the private sector be coordinated so as to provide predictability in the private sector, consistent to the extent practicable with standards developed by voluntary industry consensus standards bodies, developed in a transparent manner, and technology neutral and non-trade restrictive. The United States also urges Japan to take into account the input of all stakeholders on any forthcoming network security guidelines via a public comment process of at least 30 days.

Information Systems Procurement: The U.S. Government supports Japan's information systems procurement reforms. To ensure that these reforms are producing the intended results, the United States urges the Japanese government to monitor and evaluate the implementation and effectiveness of measures listed in the memorandum of agreement adopted by the ministries on March 30, 2004, and create additional measures to strengthen the reforms. The U.S. Government welcomes Japan's efforts to disclose more complete information about procurement awards by posting information to the electronic version of the government gazette (*kanpo*) and providing additional data, including Overall Greatest Value Method (OGVM) technical points and lifecycle costs, on the Internet. The United States encourages Japan to continue making procurement information even more accessible.

Energy

As Japan moves to further liberalize its energy sector, the United States has viewed ongoing bilateral discussions as a key means of providing input into this process and to support Japan's goals of improved energy efficiency and lower energy costs, which are among the highest in the world. Japan has made important progress since both governments began to discuss this sector as part of their bilateral deregulation/regulatory reform work – in particular with the passage in June 2003 and subsequent steps to implement the Law for the Partial Revision of the Electricity Utility Industry Law and Gas Utility Industry Law.

Electricity: Key elements of the 2003 legislative reforms in the electricity sector include: (1) securing fairness and transparency of transmission and distribution systems through information firewalls, monitoring, and prevention of cross-subsidization; (2) abolishing the transmission pancaking system; (3) organizing and strengthening the governmental structure responsible for market monitoring and dispute resolution; and (4) establishing a plan and schedule for greater retail choice, with discussions on full liberalization to begin in April 2007. The reforms also paved the way for the planned launch in April 2005 of two new key institutions: a nationwide wholesale power exchange and a neutral transmission system organization (NSO) to set transmission and distribution rules.

To support Japan's electricity reform efforts, the United States continues to share its own experiences on reform of this sector and has made numerous recommendations under the Regulatory Reform Initiative. Among the recommendations discussed during Working Group talks in December 2004 were the establishment of procedures to supervise and enforce rules and fairness in the NSO; stronger steps to ensure reliable third-party access to the transmission grid; regulatory reforms to provide meaningful opportunities to operators of co-generation or other small-scale sources of excess power to sell electricity into the market; and securing sufficient resources to develop and implement effective regulatory and market monitoring functions.

Natural Gas: Japan's 2003 energy reform legislation also includes numerous important changes in the natural gas sector, such as: (1) special measures to increase incentives for pipeline investment and the promotion of pipeline interconnection; (2) steps to secure fair and transparent competition between the gas companies that maintain and operate the network and other companies that use the pipelines; (3) measures to separate accounts and prohibit discriminatory treatment towards certain businesses to which gas companies supply gas; (4) steps to promote third-party usage of liquefied natural gas (LNG) terminals by, for example, establishing rules for resolving disputes over negotiations; and (5) a plan and schedule for greater retail liberalization. As in the electricity sector, the United States continues to share its own experiences on reform of its natural gas sector and has made numerous recommendations to Japan under the Regulatory Reform Initiative. These include establishing a regulatory framework, including a tariff structure, that provides non-discriminatory, transparent, and reliable third-party access to LNG terminals and pipelines; ensuring adequate assessment and monitoring mechanisms to ensure gas liberalization is having a meaningful, pro-competitive impact on the market; establishing and strengthening a mechanism to conduct more rigorous rate approval examinations and audits; and conducting neutral and fair ex-post facto monitoring of the industry.

In addition to raising these and other recommendations during Working Group talks in December 2004, the United States stressed the importance of meaningful, reliable third-party access to LNG terminals and gas pipelines in Japan on the degree of competition and new market entry in the electricity and natural gas sectors. In order to give confidence to new entrants, the United States urged METI to take steps to ensure strong enforcement of the government's new conduct guidelines for third-party access to LNG terminals. The United States also highlighted the need for clear, disclosed tariffs for pipeline third-party access with standard terms and conditions that are enforceable as well as the clear separation of accounts. The United States welcomes steps Japan will take to achieve reform in this important sector in a manner that promotes efficiency, reduces energy costs through competition, and encourages market entry.

Medical Devices and Pharmaceuticals

The United States and Japan address regulatory and reimbursement pricing issues in the medical device and pharmaceutical sectors through the Working Group on Medical Devices and Pharmaceuticals. The Working Group meets under the Regulatory Reform Initiative and the 1986 Market-Oriented, Sector-Selective (MOSS) Medical Equipment and Pharmaceutical Agreement. In these bilateral consultations, the United States focuses on ensuring that Japan's regulatory system provides faster approvals and that its reimbursement system appropriately values innovation.

The U.S. Government's top regulatory priority in the medical device and pharmaceutical sectors is faster product approvals. In this regard, the United States has welcomed the establishment of Japan's new regulatory agency, the Pharmaceuticals and Medical Devices Agency (PMDA), which is intended to speed approvals in part by the effective use of expanded resources provided through an increase in user fees paid by product applicants. The U.S. Government therefore urges PMDA to implement measures outlined in the June 2004 Third Report to the Leaders, such as meeting targets for faster product approvals and publishing annual progress reports. For example, Japan established a target of concluding its work on approvals for 90 percent of new medical device applications and 80 percent of new drug applications within one year by 2009 and set similarly specific shorter-term targets for gradual improvements in the intervening years. The United States has been urging Japan to attain those targets.

Since the establishment of PMDA in April 2004, however, the U.S. medical device and pharmaceutical industries have reported that companies have faced significant delays in product reviews and approvals due in part to a backlog of old applications. U.S. companies have reported, for instance, that the time to schedule a meeting with regulators on the design of drug clinical trials has doubled to six months, delaying the introduction of useful new medicines. The U.S. Government has raised concerns with the Japanese government about the backlog's effect on the speed of reviews. The U.S. Government's October 2004 Regulatory Reform submission to the Japanese government urges Japan to develop in consultation with industry measures to evaluate PMDA's performance that enhance the detail and transparency of PMDA's annual report on its compliance with the performance targets. The U.S. submission also encourages Japan to develop a new pharmaceutical performance goal, adopt international standards for medical devices, and make the regulatory process more transparent. In 2005, the United States has been encouraging Japan to speed reviews and approvals.

PMDA's creation was a key part of a major reform of Japan's regulation of medical devices and pharmaceuticals through Pharmaceutical Affairs Law (PAL) amendments that were to be fully implemented by April 1, 2005. One effect of PAL reform will be an increase in PMDA's responsibilities for inspections of medical device and drug factories. The U.S. submission urges Japan to ensure that overseas audits or factory inspections not delay approvals of new products. PAL reform will also alter the licensing requirements for distributors and importers, requiring them to bear greater responsibilities for post-marketing safety. The U.S. submission therefore urges Japan to adopt measures to prevent the withdrawal of manufacturers from Japan's market because of this change.

As for pricing reform, the U.S. Government's top priority is to ensure that Japan's policies reward the development and introduction of innovative medical devices and pharmaceuticals. Japan has recognized that innovation can foster economic growth and improved healthcare, as noted in its "Visions" policy papers, which contain plans to improve the international competitiveness of its medical device and pharmaceutical industries and markets. The United States has urged Japan to implement the Visions quickly. Japan has taken recent steps to foster innovation that were noted in the Third Report to the Leaders, such as deciding more frequently whether to grant reimbursement prices to innovative medical devices and introducing two new premium pricing rules for particularly effective drugs. The U.S. Government has continued to encourage Japan to reform pricing rules to accurately assess the value of innovative products to Japan's healthcare system, and apply pricing premiums more fully to reward and stimulate advances in drug research and medical technology.

Regarding drug pricing, the United States has proposed that in setting reimbursement prices Japan consider manufacturers' suggested prices, which are based on data on factors such as the long-term cost savings for the healthcare system from use of a given drug. The United States also has proposed that when basing prices for new drugs on prices of existing drugs that Japan use the existing drug's original price level (before its price was cut). In addition, the U.S.

Government has requested that Japan expand the data it uses to set prices and award premiums, and adopt a manufacturer's suggested price method for biologics.

Regarding medical device pricing, the U.S. Government has expressed concern about the "Foreign Price Adjustment" rule for devices that caps Japanese prices by linking them to lower prices abroad. The rule fails to consider the higher cost of doing business in Japan. The United States is urging Japan to review the Foreign Price Adjustment rule for devices and also proposing changes in Japan's method of setting prices for innovative devices.

Separately, Japan's 2002 Blood Law established a principle of "self-sufficiency" and included a Supply and Demand Plan that enables the Japanese government to manage supply and demand in the blood market. The United States has been urging Japan to ensure that the Plan does not discriminate against foreign blood plasma products and is consistent with Japan's international trade obligations. The United States has also been encouraging Japan to consult fully with industry on regulatory and reimbursement pricing matters related to blood products, and to apply policies and regulations in a fair and transparent manner.

Financial Services

Japan's financial sector has become increasingly integrated into the global financial system in the past few years. Foreign financial institutions have made important acquisitions in securities brokerage, insurance, and banking. Consolidation among Japanese financial institutions has continued, while traditional segmentation among various types of financial institutions is steadily being phased out. These changes have expanded opportunities for foreign financial firms in Japan to compete on a clear and level playing field. While supervision and disclosure have improved, Japan must continue to move forward in establishing transparency in regulation and supervision of financial institutions in line with international standards and best practices.

The Japanese Diet took further steps to liberalize financial services and make regulation more transparent in 2004. Perhaps most significantly, the United States and Japan in March 2004 ratified a bilateral tax treaty that, among other things, completely eliminates source-country withholding taxes on certain income such as royalty income between the two countries. The key withholding provisions of the treaty went into effect July 1, 2004. Also significantly, the two Governments signed the Social Security Totalization Agreement in February 2004, which will prevent the double payment of social security contributions in the U.S. and Japan.

In addition, Japan revised its Securities and Exchange Law in December 2004 to allow private financial institutions, such as banks and insurance companies, to engage in securities businesses. Other amendments, which will go into effect April 1, 2005, introduce a system of fines to combat unfair trading practices and revise the law governing paperless stock transactions to permit companies to stop issuing physical stock certificates. In December 2004, the Diet passed legislation to allow foreign exchange trading on margin. The legislation, which will take effect in July 2005, is designed to protect investors by setting forth specific criteria for margin forex trading.

Japan also approved public pension reform legislation in 2004. The package calls for incrementally raising mandatory pension premiums and gradually reducing benefit payments, in order to cope with Japan's aging population and declining work force. Additionally, the legislation sets statuary limits on future pension premium rates, intended to wipe out concerns that premiums may go up indefinitely.

In December 2004, Japan enacted legislation to remove a ban on sales of mutual funds at post offices. Japan Post will start selling mutual funds in October 2005 at 550 of its 24,700 post offices. This development may create distribution opportunities for foreign firms operating in Japan.

Agriculture

Agricultural issues were taken up in 2004 for the first time under the Regulatory Reform and Competition Policy Initiative. The main topic being addressed is the adoption by Japan of international plant health standards for the conduct of pest risk assessments and official control policy.

The Japanese government routinely requires that imported produce be fumigated for insect species that are already present in Japan. This practice is inconsistent with international practice and with the International Plant Protection Convention (IPPC). Japan claims these pests are under official control by MAFF in order to limit their spread within Japan. In practice, however, the Ministry of Agriculture, Forestry and Fisheries (MAFF) does not appear to have internationally recognized official control programs for domestically grown produce. The fumigation requirement is particularly detrimental to trade in fresh fruits and vegetables, including lettuce, citrus, and cut flowers. Fumigation adds unnecessary costs and results in produce deterioration, making products unmarketable. The U.S. lettuce industry estimates that exports would increase by at least $100 million if this issue could be resolved.

After repeated requests by foreign governments for reform, MAFF has begun to implement a non-quarantine pest list by partially amending the Plant Quarantine Law to exempt 53 pests and 10 plant diseases from fumigation requirements. While this appears to be an important positive step, the exemption list does not include ten common insect species found on U.S. fresh fruits and vegetables, which are also known to occur in Japan.

This issue was discussed in the first round of the Cross-Sectoral Working Group under the Regulatory Reform Initiative in Tokyo in December. In this meeting, U.S officials stressed the need for Japan to align its pest risk assessment procedures and official control practices with international standards. The United States also stressed the need for improved transparency and market predictability in Japan’s phytosanitary enforcement procedures. The Japanese government acknowledged that it is working on the requests from the United States and other countries to shift some pests from quarantine to non-quarantine status. The United States will continue to urge Japan to adopt international standards, to develop a comprehensive list of non-quarantine pests, and to reduce excessive, unnecessary, trade-distorting fumigation.

A related issue was included in the Regulatory Reform and Competition Policy Initiative under the Special Zones section. *(See Special Zones section under Transparency and Other Government Practices.)* A proposal to import a limited amount of fresh potatoes directly to potato chip manufacturers under a special safety protocol has been submitted under the Special Zones initiative but has been repeatedly rejected on the basis of phytosanitary concerns raised by MAFF. The U.S. Government is working with U.S. industry to address MAFF's concerns and press for progress on the basis of this proposal.

STRUCTURAL REGULATORY REFORM

Antimonopoly Law and Competition Policy

Under the Regulatory Reform Initiative, the United States has been proposing a number of progressive measures to strengthen competition policy and enforcement of Japan's Antimonopoly Act (AMA) that would bolster competition and improve market access. One of the key problems in addressing anticompetitive practices in the Japanese market has been the historically weak status of the Japan Fair Trade Commission (JFTC) and its lack of sufficient enforcement powers and resources to implement the AMA effectively. Significant improvements may result from a bill to amend the AMA, the first significant revision of the AMA in over 25 years, which was submitted to the Diet in October 2004 but held over for consideration during the 2005 regular session.

Strengthening the Effectiveness of Antimonopoly Enforcement. Cartel activity, including widespread bid rigging, continues to be a serious problem in Japan. One important reason is that existing administrative and criminal sanctions do not constitute an adequate deterrent against companies and individuals engaging in unlawful anticompetitive practices. Administrative surcharges (fines) are too low to serve as a meaningful deterrent. The current maximum surcharge is six percent of the sales in question over a maximum of three years, but comparisons of prices before and after the JFTC has broken up cartels suggest that illicit profits from such arrangements in Japan average around 16 percent. Although the AMA provides for criminal sanctions against violators, criminal prosecutions have been sporadic, and prison sentences against corporate officials have been routinely suspended. The JFTC has initiated only seven criminal prosecutions of AMA violators since 1990 and only one since 1999. Where these cases have resulted in convictions, fines have been imposed, but all prison sentences were suspended, even for an individual convicted of a repeat offence in the most recent case.

A number of other factors limit the effectiveness of the JFTC's enforcement against egregious AMA violations. The JFTC does not have the powers enjoyed by other Japanese criminal investigation authorities, including the power to conduct compulsory searches and seizures. Nor does it have the authority to reduce or eliminate criminal sanctions and administrative surcharges for companies that come forward to expose illegal activities through a corporate leniency program for cartel whistleblowers.

The October 2004 legislative proposal to amend the AMA would increase administrative surcharges to a maximum of 10 percent of cartel sales for a first-time offense and 15 percent for a repeat offense, and expand the range of violations subject to surcharges and criminal prosecution. The bill also would introduce a corporate leniency program to eliminate administrative surcharges and criminal penalties for the first company to report to JFTC its participation in an unlawful cartel and cooperate with JFTC's investigation and reduce surcharges for up to two more companies applying for leniency. In addition, the bill provides criminal investigation powers for the JFTC, penalties for interfering with JFTC investigations or for non-compliance with JFTC cease and desist orders, streamlined hearing procedures, and an extension of the statute of limitations for AMA violations to three years after the conduct stopped.

The JFTC's ability to enforce the AMA also is hindered by insufficient personnel. Some progress has been made, as seen by the increase in the JFTC's staff levels from 474 in 1990 to 672 for 2004. More importantly, the number of the JFTC's investigative staff has increased from 154 in 1990 to 331 in 2004. Nonetheless, the JFTC remains understaffed, particularly in the areas of economic analysis and investigations, to adequately enforce the AMA. JFTC inaugurated a Competition Policy Research Center in 2003, staffed in part by visiting academic economists; however the assignment of economists to JFTC investigations still appears to be quite limited.

Increasing the Procedural Fairness of JFTC Enforcement Activities: Segments of Japan's business community have complained that JFTC procedures lack due process. In order to enhance the JFTC's authority and credibility with the business community, the United States is recommending an increase in the number of judges and lawyers acting as hearing examiners and procedural changes to allow companies subject to a proposed public warning by JFTC to make arguments as to why such a warning should not be issued.

Prevention of Bid Rigging: Japan has undertaken important steps in recent years to strengthen sanctions against bid rigging. In January 2003, the Diet enacted a law against bureaucrat-led bid rigging (so-called kansei dango). In September of 2003, the Ministry of Land, Infrastructure and Transport (MLIT) extended the maximum period of suspension of designation for companies engaging in bid rigging to one year. Nevertheless, concerns persist that debarment sanctions often are applied only in slow seasons and that sanctions against government officials complicit in bid rigging activities are weak or ineffective. The United States is recommending that Japan take further measures to address prolific bid rigging, including stronger penalties for government officials involved in bureaucrat-led bid rigging and consideration by MLIT of an administrative leniency program that exempts whistleblowers from administrative sanctions such as suspension of designation. The United States is also recommending the adoption of new measures by the Ministry of Internal Affairs and Communications (MIC) against bid rigging at the local level, improved transparency in sanctions against companies found to have engaged in bid rigging, and consideration of new bidding procedures to make bid rigging more difficult.

Promoting Competition: As the only Japanese agency charged with promoting competition throughout the economy, the JFTC should substantially boost its actions as an advocate of competition policy and regulatory reform, not just through AMA enforcement actions, but also through advocating to other government agencies the adoption of pro-competitive regulations and measures. To this end, the United States has proposed that the JFTC actively participate in developing pro-competitive privatization policies and that JFTC monitor entities in the process of privatization to ensure they do not engage in anti-competitive activities. Furthermore, the United States is recommending that the JFTC actively participate in official study groups considering sectoral reforms.

Transparency and Other Government Practices

Over the years, the United States has taken up a broad range of issues under "Transparency and Other Government Practices" with the aim of recommending ways for Japan to create a more transparent and participatory regulatory system that fosters accountability and ensures fairness and predictability for Japanese consumers as well as domestic and foreign firms. Japan has made some progress in expanding meaningful public participation, but additional measures are needed, and in its October 2004 Regulatory Reform submission, the United States urged Japan to increase transparency in the following areas:

Public Comment Procedures: While Japan's Public Comment Procedures (PCP) have been in place since 1999, implementation of those procedures often fails to support the PCP's central purpose of promoting transparency and a fairer and more open rule-making system. The Ministry of Internal Affairs and Communications (MIC) released another annual survey of PCP implementation in August of 2004, which demonstrated continuing problems with the PCP. That survey showed that in FY 2003, roughly half of the public comment periods for regulatory revisions requiring Cabinet decisions were shorter than 28 days – less than one percent of these comment periods were closer to a more reasonable 60-day period. Additionally, the survey showed that public comments were not incorporated into a vast majority of the final regulations. The United States urges Japan to eliminate inadequacies in PCP implementation so as to make it an effective and meaningful regulatory mechanism, most importantly by standardizing a 60-day comment period (or at minimum requiring the use of a minimum 30-day comment period, except in urgent cases), and incorporating the PCP into the Administrative Procedures Law.

Special Zones for Structural Reform: The U.S. Government continues to support regulatory reform in Japan through the establishment of the Special Zones for Structural Reform. The United States is pleased to note that since the approval of the first zones in April 2003, the total number has grown to almost 400, with 26 deregulation measures approved for application nationwide by the Cabinet in September 2004. To ensure this initiative continues to help revitalize local economies throughout Japan, the United States recommends that: transparency remain a centerpiece of all aspects of the zones initiative; a focus be placed on expanding market-entry opportunities; the Special Zones Headquarters continue to place a priority on expeditious nationwide application of successful measures and continue to work with U.S. and other foreign companies to submit zone ideas, participate in existing zones, and participate in the zones process at every stage; and foreign participation be encouraged by publishing in English on the Internet a comprehensive list of current zones, progress on zone applications, and updated zone information.

No Action Letters: The United States recommends that Japan take further steps to enhance the effectiveness and increase the usage of Japan's no-action letter system, which provides regulated firms with an opportunity to seek clarification of an administrative agency's interpretation of laws and regulations. Measures that would contribute to a more effective no-action letter system include giving Japan's no-action letter system – which was established under a Cabinet Decision – the force of law by incorporating its requirements into the Administrative Procedures Law (APL), and establishing both government-wide and agency-specific fora for seeking private sector input as to how to improve the no-action letter systems of the various government administrative agencies.

Public Participation in the Development of Legislation: The United States encourages Japan's ministries and agencies to accelerate the practice of providing greater opportunities for the public to comment on legislation in the early stages of its formation. Specifically, the United States urges Japan to fully utilize and implement the Public Comment Procedures and ensure that the insurance industry (both domestic and foreign) and all interested parties are provided meaningful opportunities to be informed of, comment on, and exchange views with officials on proposed amendments to the Insurance Business Law, the Life Insurance Policyholder Protection Corporation (Life PPC) reform legislation or other existing laws and regulations related to the Life PPC prior to their implementation and/or submission to the Diet.

APEC Transparency Standards: APEC leaders have agreed to a package of transparency standards for the range of trade and investment areas. The United States and Japan have worked closely to create these standards. Accordingly, the United States and Japan should work jointly to achieve full implementation of the APEC Transparency Standards in the domestic legal regimes of countries in the Asia-Pacific region.

Privatization

Included in this year's October Regulatory Reform recommendations is a new, separate section on privatization, which underscores the importance the United States attaches to this ongoing process in Japan, particularly in regard to the privatization of Japan Post. Over the years, the United States has continued to take interest in Prime Minister Koizumi's efforts to restructure and privatize Japan's public corporations. The United States also recognizes that, if implemented vigorously, this reform initiative can have a major impact on the Japanese economy, stimulating competition and leading to a more productive use of resources. As reform of the public corporations advances, the United States has been urging Japan to: (1) conduct the restructuring and privatization in a transparent manner; and (2) ensure that domestic and foreign private sector entities that will or may be affected by the reform have meaningful opportunities to provide input in the privatization process, such as through use of the Public Comment Procedures.

In its October submission to Japan, the United States specifically recommends that privatization of Japan Post be ambitious and market-oriented to achieve maximum economic benefits for the Japanese economy. A truly market-oriented approach must include the establishment of undistorted competition in Japan's insurance, banking, and express delivery markets through, among other measures, the elimination of all advantages accorded to Japan Post over its private sector competitors. These advantages have long been of concern to U.S. and Japanese companies alike. (*For detailed discussion of Japan Post privatization, please see Insurance under Services Barriers section.*)

Commercial Law

Japan has been making steady progress on its efforts to reform its commercial law, starting with the substantial revisions to its Commercial Code in 2002. Problems, however, still remain that impede foreign investment and corporate restructuring, and that hinder good corporate governance practices. In its October 2004 Regulatory Reform submission, the United States urged Japan to build on past reforms by further improving its commercial law and corporate governance. Specifically, the United States is recommending that Japan introduce modern merger techniques into its commercial law, and to provide appropriate tax treatment for such transactions. Japan is now set to submit to the regular 2005 Diet session legislation to permit certain modern merger techniques, including triangular mergers, cash mergers, and short form (squeeze-out) mergers, as part of its commercial law revision. The United States is also urging Japan to improve corporate governance by requiring pension fund and mutual fund managers to adopt active proxy-voting policies that are aimed at benefiting fund beneficiaries.

Legal System Reform

Reform of the Japanese legal system is essential to the establishment of a legal environment in Japan that is conducive to international business and investment and that supports deregulation and structural reform. After more than 15 years of urging by the United States and the foreign legal community, Japan enacted legislation in 2003 that substantially eliminates restrictions on the freedom of association between foreign and Japanese lawyers, effectively permitting partnership and employment relationships between foreign and Japanese lawyers.

In its October 2004 Regulatory Reform submission, the United States again welcomed passage of the legislation regarding free association between Japanese and foreign lawyers and urged implementation by Nichibenren that upholds the spirit of the new law. The United States also calls on Japan to allow foreign lawyers to form professional corporations and establish branches throughout Japan, and to count all of the time foreign lawyers spend practicing law in Japan toward the three-year experience requirement for licensure as a foreign legal consultant.

In addition, the United States welcomed Japan’s commitment to create a flexible and open legal environment that facilitates the development of Alternative Dispute Resolution (ADR) mechanisms in Japan. Japan enacted legislation in late 2004 creating a government certification system for ADR providers, but the legislation has the potential to impede, rather than facilitate, ADR processes in Japan. The United States is recommending that Japan ensure that its legal regime for ADR is consistent with international norms and practice, that foreign lawyers and non-lawyers will be permitted to act as neutrals in ADR processes without supervision from Japanese lawyers, and that the new law is not construed to cast doubt on the enforceability of ADR decisions and settlements in which non-certified ADR providers participated.

Distribution and Customs Clearance

Japan has taken steps over the past year to improve customs clearance procedures and increase competitiveness at its international ports through the reduction of customs charges nationwide. More needs to be done, however, to facilitate the flow of goods for the benefit of Japanese consumers. In its October 2004 Regulatory Reform submission, the United States urged Japan to: (1) move from the Cost of Insurance and Freight (CIF) to the Free on Board (FOB) method for calculating duty on low-value goods at entry, which would more fairly represent the value of shipped goods and ease the work of Customs by decreasing the number of shipments over the 10,000-yen *de minimis* line; (2) increase the Customs Law *de minimis* limit from its current 10,000 yen in order to reduce the workload for both Customs and express carriers and streamline the customs clearance process; and (3) continue its pro-growth Customs policies by further reducing Customs overtime charges in International Physical Distribution Special Zones to zero.

Widespread use of credit, debit and ATM cards benefits consumers and provides for a more smoothly operating economy. In the United States, Europe, and Canada, 90 percent of all merchants accept credit or debit cards and over one-third of all purchases are made with these cards. Low card acceptance at both traditional merchants and ATMs in Japan, however, inconveniences Japanese residents and is also a common complaint of foreign visitors to Japan. The United States welcomes Japan’s recent moves to boost card acceptance at some public hospitals, and urges Japan to: (1) further promote the use of credit and debit cards by businesses and as payment for government services; (2) mandate compliance with international PIN security and network encryption standards across ATM networks in Japan; and (3) strictly enforce laws and regulations relating to credit card fraud.

Another issue of significant importance to the United States is the high landing and user fees at Japan's Narita and Kansai International Airports. These fees, the highest in the world, increase the costs for cargo, mail delivery, and air travel, and are at odds with the region-wide trend of lowering landing fees. Announced fees for the new Central Japan International Airport in Nagoya are compatible to Narita or Kansai's. In its October 2004 Regulatory Reform submission, the United States is calling on Japan to reduce airport fees to improve the business and tourism climate and help boost the economy. As the Ministry of Land, Infrastructure and Transport (MLIT) sets financial terms for the private company airport, it is in a position to ensure reasonable fees are established in a transparent matter.

IMPORT POLICIES

Rice Import System

Although Japan has generally met import volume commitments made during the Uruguay Round and subsequent negotiations, Japan's highly regulated and non-transparent distribution system for imported rice assures that high quality U.S. rice does not enjoy meaningful access to Japanese consumers. U.S. rice exports to Japan in January-October of 2004 were valued at just over $166 million, representing 361,200 metric tons of rice or over 50 percent of Japan's minimum access requirement. In 1999, Japan established a tariff rate quota (TRQ) that was to assure access to the Japanese market for 682,000 metric tons (milled basis) of imported rice annually. The Japan Food Department (JFD) of the Ministry of Agriculture, Forestry, and Fisheries (MAFF), manages imports within the TRQ through periodic minimum access (MA) tenders for imported rice and by imports through the simultaneous-buy-sell (SBS) system. In both programs, the activities of the JFD lack transparency. Moreover, less than one-half of one percent of rice imported from the United States reaches Japanese consumers as an identifiable product of the United States. Imports of U.S. rice under the periodic MA tenders, for example, are destined almost exclusively for government stocks or re-exported as food aid. A small share of U.S. rice imported under these tenders is released from JFD stocks and permitted to enter the industrial food-processing sector. Since Japan adopted a tariff system in 1999, no rice has been imported outside of the import quota because it would be subject to a duty of 341 yen per kilogram, which is equivalent to a 400-1,000 percent *ad valorem* tariff, depending on the variety of rice. Through the MA tenders, the JFD imports roughly 582,000 metric tons of rice. The U.S. rice industry has been disappointed by the JFD's record of buying medium-quality rice for industrial use, food aid, and blending, rather than top quality rice for table use. The U.S. industry also faces barriers in moving rice imported under the JFD's MA tenders into the market place. The industry believes that medium-grain U.S. rice - the type of rice imported directly by the JFD - can be competitive in the non-table use market. However, lack of information on obtaining U.S. rice held in JFD stocks has made the development of this commercial market difficult.

Under the SBS system, also administered by the JFD, Japan imports the remaining 100,000 metric tons of its total MA commitment. The U.S. rice industry is particularly concerned over the operation of the SBS system, which was designed to allow exporters access to final consumers in Japan in order to engage in consumer market development. The SBS system, which provides a substantial mark-up to the JFD (equal to the difference between the import price of rice and the wholesale price in Japan), has not allowed U.S. exporters to develop markets in Japan for high-quality short grain U.S. rice used for the table market.

In June 2003, the Japanese Diet passed a law that included a comprehensive rice reform plan designed to cut government spending, curb surplus production, and make Japanese rice farmers more efficient. The reforms are scheduled to be fully implemented by 2008. Many areas of the plan, however, remain vague, and there is concern that parts of it may be undone before it is fully implemented. In the long term, the reforms would reduce the need for extremely high levels of protection for Japanese rice farmers.

Despite these reforms, Japan's position on market access for rice in ongoing WTO agricultural negotiations is to decrease Japan's Minimum Access commitment for rice, allegedly because of Japan's changing demographics and declining rice consumption. This proposal is counter to one of the principal aims of the Doha Development Agenda (DDA), which is to open agricultural markets and expand trade. Expanding market access for U.S. rice hinges on increasing Japan's market access commitment, reducing tariffs, changing the import system to make pricing and bidding more transparent, and revising the SBS system so the market can function freely. Currently, Japan's complex import system for rice makes it impossible to ensure price stability and a stable year-round supply of U.S. rice. Since the majority of U.S. rice imports sit in warehouses, importers of U.S. rice are denied the opportunity to establish direct relationships with Japanese consumers. The United States will seek great market access, particularly for direct access to Japanese consumers, for U.S. rice in the Doha Development Agenda.

Wheat Import System

Japan requires that wheat be imported through the Ministry of Agriculture, Forestry and Fisheries' (MAFF's) Food Department, which then releases wheat to Japanese flour millers at prices that are substantially above import prices. These high wheat prices discourage wheat consumption by increasing the cost of wheat-based foods in Japan. The United States is seeking greater discipline on the trade distorting practices of state trading companies in the Doha Development Agenda agriculture negotiations.

Corn for Industrial Use

To support demand for domestically produced potatoes and sugar, the Japanese government requires Japanese corn starch manufacturers to blend potato starch with corn starch in manufacturing corn sweeteners. The tonnage of cornstarch production must be matched by purchases of domestic potato and sweet potato starch in the ratio of one part of potato starch for 12 parts of cornstarch. If corn sweetener producers use potato starch at a lower ratio than 1:12, they cannot import corn at the zero tariff rate accorded to the pooled quota. Instead they must pay a tariff on corn equal to 12,000 yen per metric ton or 50 percent of the value of a shipment, whichever is higher.

The blending requirement discourages consumption of imported corn by raising the cost of corn sweeteners, and directly displaces over 200,000 metric tons of U.S. corn sales annually. The United States is seeking resolution of this issue in the Doha Development Agenda agriculture negotiations. In December 2004, Japan notified industry and the U.S. Government that it is considering abolishing the blending requirement by 2007 and moving to a tariff or levy regime instead. The decision should be made by March 2005.

Pork Import Regime

U.S. pork exports to Japan, valued at approximately $800 million annually, comprise more than 65 percent of the value of global U.S. pork exports. Japan's pork import system, however, is inflexible and fails to meet the needs of either Japan or the United States. The system includes a gate price and a safeguard negotiated during the Uruguay Round, which automatically raises tariffs if imports are 19 percent or more above the average level of imports during the previous three years.

The gate price system distorts pork trade by encouraging Japanese importers to buy mixed shipments of different cuts of pork (rather than the cuts the market would otherwise demand) to minimize tariffs by keeping the average CIF price of their shipments at or below the gate price.

Japan's pork safeguard, which was triggered for the fourth consecutive time in 2004, is also of concern because it results in erratic purchasing patterns. The safeguard system encourages increased imports when the safeguard is not in place, and these high levels of imports then tend to trigger the safeguard. Once the safeguard is triggered, importers tend to buy more expensive cuts of pork in order to raise the cost of their import shipments to the new, higher gate price.

In the Doha Development Agenda negotiations, the United States is seeking substantial reductions in pork tariffs, reform of the gate price system and safeguard, and greater transparency in Japan's import regime.

Beef Safeguard

The United States has worked with like-minded parties to express opposition to Japan imposing a beef safeguard when Japanese consumption of beef fell due to Japan's first case of Bovine Spongiform Encephalopathy (BSE). Japan's beef safeguard was negotiated during the Uruguay Round to afford protection to domestic producers in the event of an import surge. The safeguard is triggered when imports increase by more than 17 percent from the previous Japanese Fiscal Year on a cumulative quarterly basis. Once triggered, the safeguard remains in place for the rest of the fiscal year. If triggered, tariffs on chilled beef increase from 38.5 percent to 50 percent. In 2002 and 2003, the United States pressed at the highest levels of the Japanese government to recognize the non-typical market conditions due to BSE in the application of the beef safeguard. The safeguard was lifted in March 2004 due to reduced imports resulting from Japan's ban on

U.S. beef after the discovery of a single case of BSE. The United States is intent on negotiating a change in the beef safeguard in the Doha Development Agenda.

Fish Products

Japan is the most important export market for U.S. fish and seafood, accounting for over 40 percent of U.S. exports of such products in 2004. Japan maintains several species-specific import quotas on fish products. U.S. fish products subject to import quotas include pollock, surimi, pollock roe, herring, Pacific cod, mackerel, whiting, squid, and sardines. During the Uruguay Round, Japan agreed to cut tariffs by about one-third on a number of fishery items, but avoided commitments to modify or eliminate import quotas.

The United States and Japan hold annual government-to-government consultations on fish to discuss issues related to Japan's import quota system, including its administration, marine science, ecology and other bilateral and international fishery-related issues. The most recent consultations were held in January 2005 in Seattle, following consultations that were held in November 2003. U.S. exporters have been concerned about the quota application process and other administrative procedures. Over the past few years, however, Japan has made substantial improvements in its import quota system for fish products, due in large part to recommendations from the United States and European Union. These changes include greater transparency in disclosing the recipients of quota allocations, changes in the timing of quota allocations, and the breakout of several types of fish (including mackerel, sardines, Pacific cod and others) from the "Fish and Shellfish" category into individual categories with quotas listed by weight rather than value. Although the requests of U.S. exporters for access to the Japanese market have been largely accommodated in recent years, the U.S. Government has urged the Japanese government to disband the import quota system on the grounds that it has outlived its usefulness.

As part of ongoing WTO discussions, a number of countries are working to resolve issues involving fish subsidies under the WTO Rules Committee. Japan provides numerous fishery subsidies but these and those of other countries have yet to be classified and addressed within the WTO context.

High Tariffs on Beef, Citrus, Dairy, and Processed Food Products

Japan maintains high tariffs on a number of food products that are important trading items for the United States, including red meat, citrus, and a variety of processed foods. Examples of double-digit import tariffs include 38 percent on beef, 32 percent on oranges, 40 percent on processed cheese, and 30 percent on natural cheese. These high tariffs generally apply to food products where Japan is protecting domestic producers.

High tariffs discourage the use of imported products, and in some cases keep Japanese prices so high that they reduce total consumption of certain products. Tariff reductions are therefore a high priority in the Doha Development Agenda agriculture negotiations.

Wood Products, Housing, and Building Materials

Japan is the second largest overseas export market for U.S. wood products, with U.S. exports totaling almost $630 million in the first 10 months of 2004. With just under 1.2 million housing starts in 2003, Japan's home building materials market is second in size to only that of the United States. Estimates of the size of the home building and construction materials markets range upward of $62 billion, not including materials going into the repair and remodeling market. Imports of wood and building materials from the United States fell 6.1 percent, to $967 million in 2003, in large part due to the strength of the dollar and the high cost of U.S. wood and building materials, resulting from historic booms in the U.S. domestic housing market. New housing starts in Japan are not expected to strengthen appreciably in the foreseeable future but pent-up demand for wood and various building products from the repair and remodeling sector for the existing and outdated housing stock are expected to remain strong. Starts of North American style wood-frame housing increased by 3.2 percent in 2003 to 81,502 units, and this sector's starts from Jan-Oct of 2004 are up 11 percent from the same period in 2003.

Japan continues to restrict the import and use of U.S. manufactured wood products through tariff escalation (i.e., progressively higher tariffs on more processed wood products). The elimination of tariffs on wood products has been a long-standing U.S. objective, and the United States will continue to urge Japan to eliminate wood product tariffs. In 2001, the United States and Japan agreed that future discussions on wood/building products issues would be pursued under the government auspices of the Wood Products Subcommittee and its two technical committees, the Building Experts Committee (BEC) and JAS Technical Committee (JTC). The Wood Products Subcommittee met in Tokyo in April 2002, and the Building Experts Committee and the JAS Technical Committees last met in Vancouver in September 2004 to discuss a range of issues related to the newly instituted Japanese regulatory constraints on indoor air quality, fire performance requirements for wood products, and acceptance of overseas product testing and performance data and technical calculation methods. The discussions were generally productive but many technical issues remain unresolved. Japan gave information on upcoming changes to the Building Standards Law and agreed to work with the United States and Canada to promote harmonization of fire testing results.

Marine Craft

Japan continues to maintain an inspection system for new boats and marine engines which is unique in the world in its severity and complexity and has the effect of seriously impeding market access for American manufacturers. Japan's regulations – administered by the Ministry of Land, Infrastructure and Transport (MLIT) and the Japan Craft Inspection Organization (JCI) – are vague and subject to arbitrary and inconsistent interpretation. Product testing requirements are expensive and documentation requirements are non-transparent and burdensome, forcing companies to disclose sensitive proprietary information about product design, material specifications, and manufacturing techniques. A fundamental problem with the inspection requirements is that they are applied to boats used for recreational purposes as well as to boats used for commercial fishing and other commercial uses. Fees are extremely high and bear no relationship to the actual costs of conducting the inspections. Moreover, considerable restrictions on the use of boat trailers, a principal means of transporting recreational boats, have significantly limited boating in Japan. In addition, a complicated small craft operator's licensing system accompanied by mandatory expensive and lengthy classes have restricted the ability of Japanese citizens to acquire an operator's license. Over-regulation has not improved boating safety in Japan compared to other major boating nations and has helped to keep the recreational boating industry (marinas, boats, engines, accessories, etc.) unusually small when compared to other developed nations.

The U.S. Government has made some inroads in encouraging Japan to deregulate this market under the Working Group Agreement reached on July 2, 2003. For example, in August 2004, MLIT agreed to further deregulate its license system by eliminating, effective November 1, 2004, the five-ton weight limit on pleasure boat operators' licenses. This limitation had been a major irritant for many years to U.S. industry, which has been a world leader in this segment of the market. In order to realize the full benefit of this deregulatory measure, other burdensome aspects of the Japanese inspection system must be addressed. The United States urges Japanese regulatory authorities to study how recreational boating is regulated in similar markets around the world and make major changes to their small craft inspection system to bring Japan's regulatory practices into line with international standards.

The Working Group, which includes participants from MLIT, JCI, the Japan Marine Importers Committee (JMIC), U.S. industry and the U.S. Department of Commerce, plans to meet for an additional year in order to discuss remaining outstanding issues.

Leather/Footwear

In 1991, Japan liberalized treatment of footwear imports, setting a footwear quota of 2.4 million pairs per year. By JFY 1998 it had raised this quota to roughly 12 million pairs per year. In the Uruguay Round, Japan agreed to reduce tariffs over an eight-year period on under-quota imports of leather footwear, crust leather, and other categories.

The process by which the Japanese government establishes quotas lacks transparency. U.S. industry reports that there is no consultation with leather shoe importers to determine anticipated import levels. Indeed, Japanese authorities make no effort to limit quota allocations to firms that plan to use them. The U.S. Government will continue to seek elimination of these quotas.

Above-quota imports of footwear still face market access barriers, despite the fact that Japan has met its Uruguay Round agreements to lower the *ad valorem* ceiling rate by 50 percent and the alternative "per pair" or specific-rate ceiling by 10 percent. According to the latest Japanese government Customs Tariff Schedule, the above-quota rates have declined to the higher duty of either 21.6 percent *ad valorem* or 4,300 yen per pair. However, because Japan is entitled to apply the higher of the two rates, which is typically the 4,300 yen per pair specific rate, the effect of the larger *ad valorem* rate reduction is negated.

U.S. industry has expressed concern that the quota on leather footwear imports effectively bars U.S. footwear manufacturers and U.S. brands from the Japanese market, one of the largest consumer markets in the world. According to the industry, the only way U.S. footwear companies can penetrate the Japanese market is through licensing arrangements where footwear is produced in Japan under a licensee. Many U.S. companies, however, have avoided this option because of the potential threat to the reputation of their brands by uncontrollable licensees that may not uphold the brand's quality or effectively market the brand's name.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Japan has many standards that limit trade in farm, forest, and industrial products. Japan has always been particularly conservative on questions involving food safety, human health, and the application of sanitary and phytosanitary standards. Recently, however, there appears to have been an increase in Japan's use of standards and other administrative requirements to limit agricultural and wood product imports in particular, and a greater tendency to deviate from scientific principles in setting new import policies and requirements.

Beef

Reopening the Japanese market to U.S. beef is a top priority of the Administration on the bilateral trade front in 2004. Japan imposed a ban on U.S. beef after the December 2003 discovery of a single imported cow with BSE in Washington State. Before the ban, U.S. beef and beef product exports to Japan (the largest market for U.S. beef) totaled roughly $1.7 billion annually. The U.S. Government immediately engaged Japan at a technical level and provided Japan with extensive documentation on the situation on the ground and the numerous additional measures that the United States implemented to further ensure the safety of U.S. beef for both domestic consumption as well as for export.

Since April 2004, while technical meetings continued to be held, the U.S. Government has also engaged the Japanese government in an extensive, high-level effort to reopen the Japanese market to U.S. beef. U.S. Government officials made numerous trips to Japan, organized visits of Japanese officials to Washington, D.C. as well as trips to feedlots, laboratories, and processing plants in the rest of the United States. President Bush and Prime Minister Koizumi also discussed this issue on several occasions.

After prolonged negotiations to determine the conditions under which the trade would be resumed, the two Governments agreed on a framework on October 23, 2004 designed to pave the way for resumption of beef trade between Japan and the United States. More specifically, that agreement was developed to enable U.S. beef trade to resume under a special marketing program pending an additional study on the correlation of the U.S. grading standards and age of cattle.

After six months of operation of partial market opening, that program will then be reviewed, with a view toward returning trade to more normal patterns. The United Stats has addressed all questions related to science and consumer safety raised by Japan about U.S. beef. We are urging Japan promptly to reopen its market to U.S. beef. We will continue to press Japan on this important issue at all levels of the U.S. Government until U.S. beef exports resume.

Building Size, Designs, and Wood Products

Restrictions on building size, designs, and wood products continue to constrain the use of some foreign building products and systems commonly used in the United States and elsewhere, thereby limiting choice for consumers and artificially inflating housing costs. The United States continues to have serious reservations about the transparency and basis of certain testing methodologies for evaluating fire resistance and formaldehyde emissions. The standard for testing fire resistance is inconsistent with international standards, and the testing criteria are such that test results (for the same product) can vary from one testing laboratory to another. As of late 2004, there were no testing bodies recognized outside of Japan to undertake the necessary testing for fire resistance.

The Japanese government has adopted and implemented regulations with respect to indoor air quality and the emission of certain volatile organic compounds, including formaldehyde, which are found in some building materials. Regulations on indoor air quality covering volatile organic compounds appear to be overly restrictive for some products such as wall coverings but are not applied to carpeting and interior furnishings, even though such products emit high levels of formaldehyde. The United States also has concerns about guidelines for other chemicals, especially if those guidelines become mandatory as well.

Fresh Apples Quarantine Requirements for Fireblight

For years, Japan imposed burdensome quarantine restrictions on apples, limiting the ability of U.S. growers to access the Japanese market. Of particular concern are Japan’s requirements that aim to prevent transmission of fireblight. Japan’s quarantine restrictions for fireblight included the prohibition of imports of U.S. apples from any orchard containing fireblight, three inspections of fireblight-free orchards at different times in the growing season, maintenance of a 500-meter fire-blight free buffer zone surrounding export orchards, and post-harvest treatment of apples with chlorine. These requirements were not scientifically based, significantly raised costs, and reduced the competitiveness of U.S. apples in Japan.

In light of Japan’s continued refusal to modify its restrictions on the basis of the scientific evidence, on March 1, 2002, the United States initiated WTO dispute settlement procedures. In its report of July 15, 2003, the dispute settlement panel agreed with the United States that Japan’s inspection and buffer-zone requirements are inconsistent with Japan’s obligations under the WTO *Agreement on the Application of Sanitary and Phytosanitary Measures*.

In June 2004, Japan amended its quarantine restrictions arguing that the changes brought Japan into compliance with the WTO panel decision. In the view of the United States, Japan failed to come into compliance with the WTO rulings. In July 2004, therefore, the United States requested that a WTO compliance panel be convened to determine whether Japan's revised measures are consistent with its WTO obligations. The compliance review panel is scheduled to circulate a final report no earlier than spring of 2005.

Ban on Fresh Potatoes

Japan bans imports of fresh potatoes from the United States, alleging that such a ban is necessary to prevent the introduction of golden nematode and potato wart into Japan. The United States has urged Japan to immediately lift the ban on fresh potatoes for processing from major production areas not infested by the golden nematode, such as the Pacific Northwest, California, and other U.S. potato exporting areas. Potato wart is not found in the United States. Separately, MAFF has raised new concerns regarding a number of viruses that would necessitate post-entry quarantine of imported potatoes even if the ban were lifted. The United States will continue to urge Japan to recognize disease-free areas in the United States for golden nematode. The United States is also urging Japan to permit limited imports of potatoes for use in the potato chip manufacturing industry under a strict safeguarding protocol. These issues were discussed at technical bilateral meetings in November 2004. In these meetings, Japan agreed to consolidate all of its concerns into one list and the United States agreed to respond to these questions, even though many of them may have already been addressed. The next technical bilateral meetings are scheduled to take place around May 2005.

Biotechnology

While Japan has adopted a largely scientific approach in its approval process for agricultural biotechnology products, the United States is concerned with the recent changes in Japan's regulatory system, and seeks assurances that new requirements will be science-based, clearly stated, and will provide sufficient time for compliance as well as a smooth transition in order to reduce risk of trade disruption.

To date, MAFF and the MHLW, which regulate biotechnology products, have approved the importation of 59 biotechnology plant varieties for food, including corn, potatoes, cotton, and soybeans. In July 2003, Japan inaugurated a Food Safety Commission (FSC) with responsibility for performing food related risk evaluations. MAFF is requiring new mandatory environmental safety reviews for all biotech products, including those that have already gained approval, as part of their implementation of the Biosafety Protocol. It is still unclear what will be required for these mandatory environmental reviews.

The United States is also concerned by Japan's efforts to expand mandatory labeling of foods made from the products of biotechnology when no health risks exist, thereby potentially discouraging consumers from purchasing these foods. In 2002, MAFF included potato products, frozen potatoes, dried potato, and potato starch and potato snacks in the mandatory biotechnology-labeling scheme. The United States believes consumers should have information on foods that have been produced through biotechnology, but alternatives to mandatory labeling, such as educational materials, public discussions, and voluntary labeling regimes, can provide more meaningful information to consumers and respond to consumer and market demands. The United States is also concerned by MAFF's possible plans to expand mandatory labeling to feed and seed, which are now being discussed internally in the Ministry.

The United States is urging Japan to continue to participate in discussions on biotechnology advancement and regulation in international fora, such as the WTO, the Codex Alimentarius Commission, the OECD and APEC. Given the continuous development of new biotechnology-produced food products, the United States and Japan share a common interest in working together to promote effective biotechnology approval and regulatory policies.

Restrictive Food Additive List

Japan's overly restrictive list of food additives still limits imports of U.S. food products, especially processed foods. Japanese regulations, which limit the use of specific food additives on a product-by-product basis, are out of step with international practice. Japan refuses, for example, to allow the importation of light mayonnaise, creamy mustard, or figs containing potassium sorbate, a food additive evaluated and accepted by numerous national and international standard-setting organizations, including the Joint FAO/WHO Experts Committee on Food Additives. Japan, however, allows its use in 36 other foods, most of which are traditional Japanese food products not normally produced outside of Japan. In 2002, Japan created a list of 46 food additives for expedited review. Since then, however, the United States and many of Japan’s other trading partners have been very disappointed by the lack of progress to approve these or any other additives. In addition, Japan classifies post harvest fungicides as food additives, even though the international community, including Codex, classifies them as pesticides. The United States urged MHLW to begin regulating post harvest fungicides as pesticides as part of their revised positive list of Maximum Residue Levels (MRLs), but MHLW has indicated it will not consider this request. No post harvest fungicides have been approved since the 1970’s.

Feed Additive Ban

In August 2002, MAFF publicly announced its intent to ban 29 animal feed additives. After gathering additional information, MAFF decided in October 2003 to ban only those additives that could create a resistance problem for humans. Antibiotic animal feed additives have been in use for over 30 years. Many countries, including the United States, are in the process of reviewing regulations regarding the use of these antibiotics. In December 2002, the United States received conflicting reports that Japan had decided to move forward with a ban in advance of a report on the matter from a MAFF scientific committee, and seemingly in the absence of a science-based risk assessment. The Japanese Food Safety Committee set up detailed guidelines for risk assessment in September 2003, and although industry is relatively satisfied with the guidelines, the United States will continue to follow the issue closely to ensure that Japan follows through in a manner consistent with its WTO obligations.

Nutritional Supplements

Although Japan has taken steps toward liberalization of its market for nutritional supplements, there are still restrictions or prohibitions on the use of many food additives and ingredients commonly used in markets outside Japan. Consequently, many U.S. nutritional supplements require a costly reformulation for the Japanese market. The U.S. Government's Regulatory Reform submission in October contained several proposals for liberalization of the market, including allowing educational and informational statements on labels and in advertising, reducing duties for nutritional supplements to the same level as duties for drugs containing the same ingredients, increasing Japan's participation in nutrition-related Codex activities, and basing potency limits on risk assessments. The United States has urged Japan to further liberalize this market.

Poultry

Since 2002, Japan has imposed a number of national and statewide bans on U.S. poultry meat due to the detection of low pathogenic strains of avian influenza (AI) in limited areas in the United States. As a result, U.S. poultry meat exports to Japan have decreased substantially since then, from roughly $81 million in 2001 to $45 million in 2002, $29 million in 2003, and $31.1 million in 2004.

According to standards set by the international animal health organization, the Office of International Epizootics (OIE), quarantine procedures and some restrictions on imports are appropriate for highly pathogenic strains of AI, and not for low pathogenic strains. The OIE standards also provide for regionalization in the case of highly pathogenic AI (i.e., importing countries should limit bans to zones where highly pathogenic AI has occurred, while allowing imports from other regions in the exporting country, when the exporting country has effective control and surveillance measures in place to quarantine the affected region).

Japan again prohibited all imports of U.S. poultry meat for several months in 2004 due to localized outbreaks of low pathogenic AI in some Northeastern and Atlantic states such as Delaware, Pennsylvania, and Maryland and a subsequent high pathogenic avian influenza outbreak in Texas. Despite the fact that the OIE declared the United States free of all types of AI in August 2004, Japan still is imposing bans on the states of Connecticut and New Jersey. The United States has repeatedly raised concerns with the Japanese government on its improper institution of these bans. The two Governments continue to work on revising the existing protocol for poultry meat and are also working towards finalizing new protocols for heat-treated poultry meat and heat-treated egg products.

GOVERNMENT PROCUREMENT

Construction, Architecture and Engineering

Although Japan has the second largest public works market in the world ($190 billion for 2004), U.S. firms annually obtain far less than one percent of projects awarded. Two public works agreements are in effect: the 1988 U.S.-Japan Major Projects Arrangements (MPA) (updated in 1991) and the 1994 U.S.-Japan Public Works Agreement, which includes the "Action Plan on Reform of the Bidding and Contracting Procedures for Public Works" (Action Plan). The MPA included a list of 42 projects in which international participation is encouraged. Under the Action Plan, Japan must use open and competitive procedures for procurements valued at or above the thresholds established in the WTO Agreement on Government Procurement.

Problematic practices continue to inhibit the full involvement of U.S. design/consulting and construction firms in Japan’s public works sector. These practices include failure to address rampant bid rigging, use of arbitrary qualification and evaluation criteria to exclude U.S. firms, unreasonable restrictions on the formation of joint ventures, unclear or conflicting bid/contract procedures, and the structuring of individual procurements so they fall below thresholds established in international agreements. Public works issues are raised in the Trade Forum under the U.S.-Japan Economic Partnership for Growth. During the July 2004 Expert Level Meeting on Public Works under the Trade Forum (Expert Level Meeting), the United States urged Japan to eliminate the obstacles that prevent U.S. companies' full participation in this sector.

During the Expert Level Meeting, the United States also encouraged Japan to strengthen its efforts to eliminate bid-rigging practices (*dango*), under which companies consult and prearrange a bid winner. The United States also expressed concern about the practice of Japanese firms submitting bids on projects that are so low that they raise the question as to whether the work can be performed without a financial loss. This is hampering U.S. firms' abilities to offer quality services while remaining competitive.

The United States urged Japan to increase the number of Construction Management (CM) and Project Management (PM) projects commissioned during this fiscal year and structure procurements in such a way that foreign firms with appropriate expertise are able to compete.

(CM and PM are advanced project delivery and management systems that maximize the efficiency of a project.) The United States also urged Japan not to use ISO 9000 series registration with the effect of creating a barrier to international trade. Japan's Ministry of Land, Infrastructure, and Transport confirmed that it would not use ISO 9000 as a pre-qualification criterion for public projects. The United States urges other Japanese commissioning entities to follow suit.

The United States again urged Japan to abolish its three company joint venture rule (which limits to three the number of members in joint ventures for most construction projects), to increase use of the "mixed-type procurement" (which allows companies to decide whether to bid solo or as a joint venture), and to use Design Architect procurements to increase joint venture opportunities for firms specializing in architectural design. The United States also raised concerns regarding costly and unclear procedures for design proposals, including conflicting documentation requirements, and the lack of information on new bid/contract procedures that were not included in the Action Plan. The United States asked that steps be taken to make these procedures more fair, open, and transparent.

The United States is concerned that developments in Japan's public works market since the Action Plan was implemented have led to conditions that existing agreements do not fully address. The United States is promoting U.S. firms' participation in new types of public works projects in Japan such as Urban Renewal, Private Finance Initiative (PFI), and Local Area Renewal projects. During the Expert Level Meeting, the United States welcomed Japan's confirmation that Action Plan procedures would be used for Urban Renewal and PFI projects commissioned by Action Plan entities and above the specified thresholds. The United States also urged major municipalities in Japan to use Action Plan procedures for Urban Renewal projects. In November 2004, Japanese private sector organizations hosted the sixth U.S.-Japan Construction Cooperation Forum, which focused on facilitating the formation of joint ventures between U.S. and Japanese companies for Urban Renewal projects.

The United States is paying special attention to several major projects covered by the public works agreements of particular interest to U.S. companies. These projects include the New Kitakyushu Airport; Haneda Airport development and expansion; Kansai International Airport; Kobe Airport; Kyushu University Relocation Project; Okinawa Institute of Science and Technology; Okinawa Zukeran General Hospital Project; International Medical Center; laboratory projects commissioned by the Ministry of Education, Culture, Sports, Science and Technology; Japan Railways' procurements; major public buildings; urban development and redevelopment projects, including major PFI projects; and remaining MPA projects.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The United States continues to pursue its intellectual property rights protection agenda with Japan through bilateral consultations and effective coordination in multilateral and regional fora. For its part, Japan continues to make progress in improving the protection of intellectual property rights and, relative to other countries, piracy is not a major problem, though several key issues remain, including the need to improve Japan's legal and administrative intellectual property framework to protect copyrights in the digital age. The United States has identified a number of areas where further action by Japan is needed, including: (1) addressing persistent patent-related problems; (2) improving and expanding protection of copyrighted works, particularly on the Internet; (3) providing effective protection for well-known trademarks; (4) providing protection for geographical indications; (5) affording greater protection of trade secret information; and (6) continuing to improve border enforcement mechanisms.

Patents

The United States has focused particular attention on improving the processing and approval of patent applications, and reforming Japan's practice of affording only narrow patent claim interpretation. The United States remains concerned with several aspects of Japan's patent administration, including the relatively slow process of patent litigation in Japanese courts, the lack of an effective means to compel compliance with discovery procedures, and the lack of adequate protection for confidential information produced relative to discovery.

In recent years, Japan has taken a number of steps to address these issues. A revised patent law took effect on January 1, 2000. This law is designed to make it easier for plaintiffs to prove patent infringement in courts. Key provisions include requiring defendants to justify their actions, obligating defendants to cooperate with calculation experts, giving judges discretion over the amount of damages, increasing the penalty in cases where patents were obtained fraudulently, and allowing courts to seek technical advice from the Japan Patent Office (JPO). The United States will continue to monitor closely whether these revisions reduce the cost of access to Japanese courts that has been particularly onerous to foreign patent owners in the past. The United States welcomes these steps to improve the level of patent protection in Japan and will continue working with Japan to strengthen its patent laws in several fora.

Copyrights

The increasing use of the Internet and explosive growth of high-speed access in Japan has presented new challenges for protecting intellectual property rights, especially for copyrighted materials. The protection of this material is critical for electronic commerce to flourish and for the continued development of content-related industries such as games, music, film, and software. The United States is therefore concerned that Japan's Internet Service Provider (ISP) liability law does not provide adequate protection for the works of right holders on the Internet or the appropriate and necessary balance of interests among telecommunications carriers, service providers, right holders and website owners. The United States urges Japan to use all the opportunities available to improve these shortcomings in the law. *(This issue is also taken up in the Information Technologies section under Sectoral Regulatory Reform.)*

The United States is also urging Japan to reduce the piracy rate, especially in light of the growing threat of online piracy. A notable step toward creating an effective deterrent against piracy would be amending Japan's Civil Procedures Act to award statutory damages rather than actual damages, and to provide for more effective procedures for collecting evidence. In addition, in order to set an example for the private sector, the United States urges Japan to issue a decree forbidding any copyright infringement in its government operations. The United States is also concerned about the personal use exception both as it applies to the Internet and to students and book piracy. Japan should make its law crystal clear that the use of peer-to-peer networks to copyright and distribute copyrighted works without the right holder's authorization is not permitted under the personal use exception. The personal use exception appears to allow students to copy entire textbooks for personal use as long as they do not distribute copies. The United States urges Japan to explicitly incorporate the three-part test from international treaties into the Copyright Law to address both these problems.

In addition, the United States is concerned about the provision on anti-circumvention in the Copyright Law, which states that the penalties for technological protection measures (TPM) circumvention devices will be applied only to devices whose principal function is circumvention.

In a positive vein, Japan put into effect an extension of the term of copyright protection for cinematographic works, animation, and video games to 70 years to bring the term of protection closer to the growing international trend. The United States continues to urge the Japanese government to extend all copyright terms to life plus 70 years, or where the term of protection of a work (including a photographic work), performance or phonogram is to be calculated on a basis other than the life of a natural person, to 95 years.

Trademarks

Trademarks must be registered in Japan to ensure enforcement. Thus, any delays in the registration process make it difficult for foreign parties to enforce their marks. Legislation passed in preparation for Japan's ratification of the Madrid Protocol in March 2000 contains several useful provisions. Effective January 1, 2000, Japan began establishing a system to notify the public of trademark applications received. Effective March 14, 2000, trademark holders are entitled to compensation for damages for the period from application until registration of the trademark.

Regrettably, in spite of the existence of provisions in Japan's Unfair Competition Law designed to afford greater protection to well-known marks, protection of such marks remains weak. Of particular concern is Japan's register of well-known marks, where employees of the Japan Patent Office make *ex officio* determinations whether a mark is well-known or not. One defect of the "list" approach to well-known mark protection is that one can essentially pay one's way onto the list by requesting defensive registrations in many classes. A trademark committee is currently reviewing the scope of protection for well-known marks and the U.S. Government will continue to monitor its progress.

Geographical Indications (GIs)

Articles 22 to 24 of the TRIPS Agreement set forth the obligations of WTO Members with respect to GIs and their relationships to trademarks. It is unclear whether Japan currently provides interested parties with the legal means to prevent misuse of a GI or whether Japan provides trademark owners with the legal means for resolving conflicts between trademarks and asserted GIs, as required by the TRIPS Agreement. The United States understands the Japanese government is currently studying the issue of GI protection and fully supports that effort. Outstanding questions in this area remain of particular concern since it is unclear whether Japan maintains an undisclosed list of protected GIs against which applications for trademark registration are reviewed. The United States also understands the Japanese government is considering the use of GIs to protect the identity of traditional food products from well-known production areas in Japan but it is unclear how Japan would implement such protection. Japan has recently announced that it has three new Japanese terms which have been designated as GIs for wines and spirits by the Commissioner of the National Tax Agency through its Labeling Standard Concerning Geographical Indications, "to be protected in the territories of WTO members." The United States is concerned as to why the Japanese Tax Commissioner is designating GIs under the TRIPS Agreement – an intellectual property agreement, not a tax agreement – and whether foreign GIs are directly registrable under the Japanese GI system without intervention by a foreign government. The United States looks forward to receiving further information on these concerns.

Trade Secrets

Although Japan amended its Civil Procedures Act to improve the protection of trade secrets in Japanese courts by excluding court records containing trade secrets from public access, the law is inadequate. Since Japan’s Constitution prohibits closed trials, the owner of a trade secret seeking redress for misappropriation of that secret in a Japanese court is forced to disclose elements of the trade secret in seeking protection. Because of this, and the fact that court discussions of trade secrets remain open to the public with no attendant confidentiality obligation on either the parties or their attorneys, protection of trade secrets in Japan’s courts will continue to be considerably weaker than in the courts of the United States and other developed countries. The Diet passed a bill to partially amend the Unfair Competition Prevention Law in May 2003. The bill contains a provision that states a person who illegally acquires, uses, and discloses corporate secrets is subject to criminal sanctions. The scope of the amendment, however, is limited. The United States continues to urge Japan to undertake further reform in this area.

Border Enforcement

The United States continues to monitor the Japan Customs and Tariff Bureau’s (JCTB) implementation of the policy to allow parallel imports of patented products based on a 1997 Japan Supreme Court. Further, insofar as Japan provides *ex officio* border enforcement of trademarks and copyrights through the JCTB, efforts should be made to enhance such enforcement through aggressive interdiction of infringing articles. In an effort to bolster Japan's border control measures, the United States has urged Japan to improve its application, inspection, and detention procedures to make it easier for foreign right holders to obtain effective protection against infringed intellectual property rights at the border. Although Japan increased the amount of resources devoted to enforcement during 2004, the United States urges Japan to continue to improve and tighten its border enforcement to ensure effective implementation of TRIPS obligations.

SERVICES BARRIERS

Insurance

Japan's private insurance market is the second largest in the world, after that of the United States, with direct net premiums of an estimated $335 billion in FY 2003. In addition to the offerings of Japanese and foreign private insurers, substantial amounts of insurance are provided to Japanese consumers by the large life insurance unit (Kampo) of government-owned Japan Post, the National Public Health Insurance System, and a web of mutual aid societies (Kyosai).

Given the size and importance of Japan's private insurance market, the United States continues to place a high priority on ensuring that Japan's regulatory framework fosters an open, fair, and competitive insurance market. Two bilateral Insurance Agreements, implemented in 1994 and 1996, are in effect and have contributed significantly to deregulating the Japanese insurance market. Largely as a result of positive changes brought about by these agreements, foreign insurance companies have substantially increased their presence in Japan's private sector insurance market (total market excluding Kampo/Kyosai), now holding an estimated 20 percent of the life insurance market (FY 2003) and a 5.5 percent share of the non-life insurance market (FY 2002). In the third sector, foreign firms have captured approximately 64 percent of the private sector life medical/nursing care insurance market (FY 2003) and about 24 percent of the private sector non-life medical/personal accident market (FY 2002).

Several issues of concern, however, continued throughout 2004, including the lack of a level playing field between private industry and Kampo/Kyosai, the introduction of new product offerings by Kampo and Kyosai, and uncertainty regarding future funding of the life and non-life insurance safety net systems or Policyholder Protection Corporations. The United States consistently raised its concerns and views about these and other key issues, such as plans to privatize the postal insurance system. Fora used to express these views included U.S.-Japan bilateral insurance consultations held in Tokyo on August 20, 2004, regularly scheduled Working Groups under the U.S.-Japan Regulatory Reform Initiative, and other regular contacts between U.S. and Japanese government officials.

Kampo is effectively the world's largest insurer and remains by far the largest player in Japan's insurance market. Kampo is bigger than the four largest private sector Japanese life insurers combined and is estimated to account for nearly 40 percent of all life insurance assets in Japan.

In FY 2003, there were 76 million Kampo issued life insurance policies in force compared to 123 million for all private life insurance companies combined. In addition, according to the Japan Cooperative Insurance Association, Kyosai-issued policies amounted to more than 20 percent of all in-force life policies in the market and 35 percent of all in-force non-life policies in 2002.

Although Kampo and Kyosai compete with the private sector, they enjoy significant legal and regulatory advantages over private sector insurers. For example, both are exempt from Japan's Insurance Business Law and from contributing to Japan's insurance safety net systems. Kampo and Kyosai both possess advantageous tax status, which in Kampo's case exempts it from paying corporate and income taxes. Kampo insurance policies also are guaranteed by the Japanese government.

Postal Insurance: The United States has continuously voiced its Kampo-related concerns to the Japanese government, stressing the need for, *inter alia*, a prohibition on Kampo's ability to underwrite any new or altered insurance products until a level playing field with private companies is established, and for postal financial institutions to be subjected to the same legal, tax, and business requirements and supervision as their private sector counterparts. As any modification to the postal financial system could have significant impact on competition in the Japanese insurance market, the U.S. Government also strongly urged that decisions related to the future of the postal financial institutions, including possible privatization, be made and implemented in an open and transparent manner, in full consultation with domestic and foreign private insurers.

Japan Post introduced a new insurance product in January 2004 in spite of strong concerns voiced by the U.S. Government, Japanese and foreign companies, other foreign governments, industry analysts, and the media. The U.S. Government continues to closely monitor the performance of this product, which includes a rider providing for supplemental health coverage under a hybrid whole life and term life contract. The U.S. Government also continues to convey to the Japanese government its strong view that no additional Kampo products should be permitted until a level playing field is established.

The U.S. Government is also closely following developments related to the Japanese government’s plan to privatize Japan Post, including its Kampo insurance business. The initiative has large potential implications for the conditions of competition in the insurance market between Japan Post and private companies. Prime Minister Koizumi made Japan Post privatization a priority issue during 2004, stating his aim of securing passage of privatization legislation by the Japanese Diet in 2005. To help achieve this goal, the Prime Minister established the Office for Privatization of Japan Post under the Cabinet Secretariat in the spring of 2004 to prepare legislation and also created the new post of Minister of State for Privatization of the Postal Services in September.

In September 2004, the Cabinet endorsed the “Basic Policy on the Privatization of the Japan Post” as a blueprint for privatization. The blueprint stated that “competitive conditions will be equalized with other private companies" and specifically called for the application of the same tax, legal, and safety net obligations for Japan Post that the private sector must meet. The blueprint also called for an end to government guarantees on postal insurance products. These proposed changes, long advocated by the United States, are welcome steps. The U.S. Government also continued to emphasize its long-standing concern about the timing for allowing the introduction of new Japan Post insurance products and raised other issues related to privatization reforms that, if left unaddressed, could undermine the potential for privatization to bring about a truly level playing field in Japan's insurance market.

Dialogue between U.S. and Japanese government representatives on privatization issues remained active throughout 2004 and will continue as the privatization process proceeds. The U.S. Government also welcomed the transparent manner in which the Japanese government has undertaken the privatization process, including the opportunities provided to private sector interested parties to directly share their concerns and views with key Japanese government representatives, and urged that these efforts continue.

Kyosai: Kyosai operations have also received increased attention in 2004. Some Kyosai are regulated by their respective agencies of jurisdiction (Ministry of Agriculture, Forestry and Fisheries, or Ministry of Health, Labor and Welfare, for example), while others operate without any regulatory supervision. These separate regulatory schemes undermine the ability of the Japanese government to provide companies and policyholders a sound, transparent regulatory environment, and afford Kyosai critical business, regulatory, and tax advantages over their private sector competitors. The U.S. Government has stated its position that all Kyosai should be subject to the same regulatory standards and oversight as their private sector counterparts to ensure a level playing field and to protect Japanese consumers.

The U.S. Government welcomed a review of unregulated Kyosai undertaken during 2004 by a working group of the Japanese government's Financial System Council (FSC). A working group report on its discussions was issued in October 2004 and opened to public comment, to which the U.S. Government submitted its views. The working group then issued a formal report with recommendations in December 2004, outlining steps to bring unregulated Kyosai under new government regulation and supervision. The U.S. Government also urged the Japanese government during 2004 to conduct a similar review of regulated Kyosai in the near future. The U.S. Government moreover expressed its concern over the introduction of new products by large regulated Kyosai during 2004, including a new whole life medical product from JA Kyosai and a new whole life medical product from Zenrosai.

Policyholder Protection Corporations: The life and non-life Policyholder Protection Corporations (PPCs) are mandatory policyholder protection systems created in 1998 to provide capital and management support to insolvent insurers. The Life PPC fund, in particular, had been nearly depleted as a result of industry failures. Private sector insurers have contributed considerable sums to the PPC systems, and U.S. industry, particularly life insurers, has expressed serious concern at the prospect of additional contributions. The U.S. Government has stressed the need for a sustainable funding framework that did not unfairly burden the private sector.

Legislation was implemented in 2003 that assessed private sector life insurers an additional 100 billion yen to extend its funding guarantee to the Life PPC. The Japanese government also pledged to thoroughly review the PPC system and consider reforms long recommended by private insurers. U.S. insurers, although displeased with the additional levy, welcomed the review. The U.S. Government urged the Japanese government to ensure that the review is completed and necessary legislation enacted before the current Life PPC structure expires on March 31, 2006. A FSC working group conducted discussions on PPC review through much of 2004, issuing a report in December. The United States emphasized the need for transparency in subsequent government decision-making on the future of PPC funding and reform.

Bank Sales: Since April 2001, banks have been permitted to sell long-term fire insurance, debt repayment support insurance, credit life insurance, and overseas travel accident insurance. In October 2002, the list of permissible products was expanded to include individual annuities, maturity refund personal accident insurance with an annuity payout feature, zaikei (asset formation) insurance, and zaikei personal accident insurance. Although the U.S. Government welcomes these steps, the above list represents only a tiny fraction of the universe of private insurance products that could be made available to Japanese consumers through the bank sales channel.

In 2004, the U.S. Government continued to urge the Japanese government to promptly and completely liberalize the bank sales channel to allow banks to sell all types of insurance offered by any regulated private insurer and not specifically target third sector products by liberalizing only that sector first. In a March 2004 report, the FSC recommended full liberalization be accomplished within three years at the latest, and that partial liberalization within one year be carried out as a means to monitor the implementation and effectiveness of new anti-pressure sales rules. The U.S. Government expressed concern about a possible delay in the first stage of partial liberalization, and conveyed its view of the importance of meeting the FSC recommendation to complete liberalization no later than within three years. In order to promote bank sales of insurance in a manner that effectively serves the financial planning needs of consumers, the U.S. Government believes the Japanese government should promptly abolish or undertake appropriate revision of enforcement regulations that require banks to obtain customer consent in writing prior to the use of non-financial personal information in order to offer insurance products to customers.

The United States will continue to work closely with industry in following these issues and will urge the Japanese government to adequately resolve these concerns in an open and transparent manner.

Professional Services

U.S. and other foreign firms and individuals are hampered in providing professional services in Japan by a complex network of legal, regulatory, and commercial practice barriers. U.S. professional services providers are highly competitive. Their services also help facilitate access for U.S. exporters of other services and goods, and contribute valuable expertise to the economies they serve. The availability of such services can be a key factor in U.S. firms' decisions whether to invest, and thus is central to improving the environment for foreign direct investment in Japan.

Accounting and Auditing Services: U.S. providers of accounting and auditing services face regulatory and market access barriers in Japan that impede their ability to serve this important market. Only Certified Public Accountants (CPAs) or Audit Corporations (made up of five or more Japanese CPAs) can offer accounting services. Foreigners must pass a special examination to qualify, an examination last offered in 1975. The United States will continue to urge Japan to remove restrictions on accounting services.

Legal Services: As noted above in the Legal System Reform portion of the Regulatory Reform Initiative section, 2003 and 2004 brought sweeping reform in the area of association between Japanese and foreign lawyers, and the new system of Joint Law Firms (*kyodo jigyo*) is expected to be implemented by April 1, 2005.

Medical Services: Restrictive regulation limits foreign access to the medical services market. In the U.S.-Japan Investment Initiative, the United States has advocated allowing commercial entities to provide for-profit medical services and allowing more outsourcing of certain medical services, such as diagnostic and chronic care services (advanced imaging, maintenance dialysis, rehabilitation, etc.) to open this sector to foreign capital-affiliated providers.

Educational Services: Over-regulation also has discouraged foreign universities from operating branch campuses in Japan, presenting obstacles in the form of both administrative requirements and restrictions on pedagogical choices. The U.S.-Japan Investment Initiative has taken up these issues, and the Japanese government has announced the establishment of a new category for Foreign Branch Campuses of accredited institutions of higher education in the U.S. and elsewhere. The United States expects this designation will provide these campuses a number of important rights (such as student rail passes and the issuance of student visas) similar to those accorded Japanese educational institutions.

INVESTMENT BARRIERS

Despite being the world's second largest economy, Japan continues to have the lowest inward foreign direct investment (FDI) as a proportion of total output in any major OECD nation. Foreign participation in mergers and acquisitions (M&A) activity, which accounts for some 80 percent of FDI in other OECD countries, also lags in Japan, although it is on an upward trend.

This relative lack of foreign investment can act as a restraint on the expansion of imports. Much of the recent increase in FDI flows represents important opportunities and restructuring in the financial services and telecommunications sectors. The Japanese government has recognized the importance of FDI in revitalizing its economy. Prime Minister Koizumi, for example, vowed in January 2003 to double the stock of FDI in Japan in five years. Japan has since taken several steps to improve the FDI environment, including passage of legislation in 2003 to permit the use of triangular stock swaps for international M&A deals. U.S. businesses have applauded these steps, but continue to urge that tax rules be clarified and amended to facilitate use of modern merger techniques.

Cross-border M&As are more difficult in Japan than in other countries, partly because of conservative attitudes towards outside investors and partly because of the relative lack of financial transparency and disclosure and differing management techniques. The scarcity of qualified lawyers, auditors, and accountants is another impediment. Nevertheless, attitudes throughout Japan towards FDI have become considerably more positive, and some progress has been made through the introduction of consolidated taxation and revised bankruptcy procedures that make it easier for corporations and their assets to be acquired or merged in a "rescue" format.

The U.S.-Japan Investment Initiative co-chaired by the U.S. Department of State and Japan's Ministry of Economy, Trade and Industry (METI) was established in 2001 to focus on needed changes in the basic operating rules of Japanese markets and to encourage policy changes to improve the overall environment for foreign (and domestic) investment. The Investment Initiative has held a series of meetings and seminars. The first Working Group meeting of the Initiative in 2005 was held on January 26 in Tokyo, and Investment Seminars will be held in Nagoya and Chiba in May 2005. The private sector participates actively in this process and has offered detailed suggestions on how to increase transparency, as well as recommending the introduction of new financial instruments for international transactions.

ANTICOMPETITIVE PRACTICES

There are detailed discussions related to anticompetitive practices and Antimonopoly Act (AMA) enforcement in several other parts of this report, particularly under the Regulatory Reform sections.

Law Against Unjustified Premiums and Misleading Representations: The JFTC imposes overly restrictive limits on the use of premium offers (prizes) and other sales promotion techniques, and thereby discourages even legitimate cash lotteries and product giveaways used in such promotions. Foreign newcomers, who depend on innovative sales techniques to market their company names and products, are significantly impaired by the JFTC's restrictions on premiums. In addition, the JFTC allows "fair trade associations" (essentially, private trade associations) to set their own promotion standards through self-imposed "fair competition codes." Trade associations often use the cover of these codes to adopt additional standards that are stricter than required by JFTC regulations under the Premiums Law and have the effect of restraining vigorous competition. As of December 31, 2004, there were still 40 JFTC-authorized premium codes.

ELECTRONIC COMMERCE

The United States made numerous recommendations in its October 2004 Regulatory Reform submission for increasing consumer confidence and promoting electronic commerce in the private sector, including: removing regulatory and non-regulatory barriers, strengthening the protection of intellectual property rights, implementing new privacy legislation in a transparent and consistent manner, promoting alternative dispute resolution (ADR), and ensuring effective network security. The United States is urging Japan to support private sector self-regulatory mechanisms for privacy and ADR, as well as to ensure that laws governing electronic transactions are technology-neutral and that all final guidelines are consistent and complement existing international regulations. The United States will continue to work with Japan on these and other electronic commerce issues through the IT Working Group under the Regulatory Reform Initiative. (*For more details, see the Information Technologies section under Regulatory Reform.*)

OTHER BARRIERS

Aerospace

Japan is the largest foreign market for U.S. aircraft and aerospace products. The commercial aerospace market in Japan is generally open to foreign firms, and many Japanese firms have entered into long-term relationships with American aerospace firms. The U.S. Government continues to monitor METI's funding for the development of an indigenous small aircraft.

Military procurement by the Japan Defense Agency (JDA) accounts for over half of the domestic production for aircraft and aircraft parts, and continues to offer the largest source of demand in the aircraft industry. Japanese defense projects are carried out according to the current Mid-Term Defense Program (JFY 2001 - JFY 2005) with a projected budget of 25.16 trillion yen, or approximately $206 billion, over this five-year period. The current Mid-Term Defense Program (MTDP) will end this JFY 2004 and a recently announced MTDP (JFY 2005-2009) will begin in April 2004. The projected budget is 24.24 trillion yen over this five-year period. Major projects include: ground and maritime ballistic missile defense systems, new maritime patrol aircraft, and new transport and tanker aircraft.

Although U.S. firms have frequently won contracts to supply defense equipment to Japan (over 90 percent of the annual foreign defense procurement is from the United States), the JDA has a general preference for domestic production or the licensing of U.S. technology for production in Japan to support the domestic defense industry. Also, European aviation competitors are starting to make inroads with some limited sales of aviation equipment for defense purposes.

Although Japan has considered its main space launch vehicle programs as indigenous for many years, in fact U.S. firms continue to participate actively in those space systems, including Japan's primary space launch vehicle, the H2-A. The U.S. Government has welcomed Japan's plans to develop a supplementary GPS navigation satellite constellation known as the "quasi-zenith" system, with the first launch scheduled for 2008. The United States is working very closely at the technical level with Japanese counterparts to ensure the Japanese system remains compatible with ours, and anticipates that U.S. companies will have the opportunity to supply major components of this system. The United States will continue to promote expanded access by American firms to commercial opportunities within Japan's domestic space programs as appropriate.

Autos and Auto Parts

Further opening of the Japanese auto and auto parts markets remains an important objective of the United States, but access to Japan’s automotive market continues to be impeded by a variety of overly restrictive regulations, a lack of transparency in rule making, and lackluster enforcement of antitrust laws. While there has been a trend toward closer integration and important technological advancements in the global automotive industry over the past several years, the effect these changes will have on market access and competition in this sector remains unclear.

The U.S. Government remains disappointed with falling sales of North American-made vehicles and parts in Japan. Sales in Japan of motor vehicles produced in the United States declined in the first eleven months (January-November) of 2004, with sales decreasing by 30.5 percent following a decline of 15 percent in CY 2003. U.S. automakers sell less than a quarter as many U.S.-made vehicles in Japan as they did in 1995.

Even as American automakers have invested in Japanese auto manufacturers, foreign access to Japan’s automotive distribution network remains troubling to U.S. auto companies. The U.S. automotive trade imbalance with Japan, $44 billion in 2003 ($32 billion deficit in autos and $12 billion deficit in auto parts), is the equivalent of more than 66 percent of the overall U.S. trade deficit with Japan and made up eight percent of the 2003 worldwide U.S. trade deficit.

Auto and auto parts issues are addressed under our bilateral Automotive Consultative Group, which is co-chaired by USTR and the Department of Commerce on the U.S. side and METI and the Ministry of Land, Infrastructure, and Transport (MLIT) on the Japanese side. At its last meeting held in 2003, the group discussed industry trends based on a series of trade and economic data on autos and automotive parts provided by both countries and identified areas in which specific action can be taken by Japan to address U.S. concerns. This would include further deregulation (particularly in the automotive parts aftermarket), increased transparency in rules and regulations governing this sector, and more rigorous application of Japanese competition laws. The United States also continues to address crosscutting issues affecting the automotive sector, such as expanding opportunities for foreign investment, increasing transparency in rule making, and promoting corporate restructuring in the Japanese economy under the Economic Partnership for Growth.

Civil Aviation

Although market access for U.S. air carriers in Japan was improved significantly by an agreement reached in 1998, U.S. carriers remain constrained by extremely high airport costs in Japan and by enduring restrictions on traffic rights, operational flexibility, and pricing.

Several rounds of formal and informal talks aimed at further liberalization have taken place between the two sides since the 1998 agreement was signed, but without any success. As of the end of 2004, no further talks were scheduled. The U.S. Government continues to urge the Ministry of Land, Infrastructure and Transport (MLIT) to advance liberalization. Key U.S. concerns include passenger code carrier sharing limitations that further distort market inequities brought about by slot, designation and frequency restrictions; increased access to the Japanese market and additional “beyond Japan” service rights for non-incumbent cargo carriers; pricing liberalizations; and improvements in the regime for service between U.S. Pacific Islands and Japan.

In comparison to similar international airports in other countries, movements at Narita fall well below potential airport capacity, unnecessarily limiting slot availability. In periods of high demand, U.S. non-incumbent combination carriers have been unable to operate routes made available under the 1998 Memorandum of Understanding (MOU). A second runway opened in April 2002 provides additional slots, but at less than 2500 meters, the runway cannot accommodate most long-haul operations. The issue of excessively high landing fees at Narita and Kansai and the new Central Japan International Airport (Centrair) airports continues to be raised in the U.S.-Japan Regulatory Reform talks and in bilateral aviation discussions. (*See Regulatory Reform Initiative, Distribution Section.*)

The United States will continue to press hard for further liberalization consistent with its global policy to promote competition and market access in civil aviation.

Business Aviation

Japan's over-regulated aviation system impedes the development of business aviation. Japanese firms cannot use business aircraft in an economical manner, and foreign users also find landing business planes difficult in Japan due to limited slots and commercial airline regulations that apply to charters and business aircraft. These regulations, which are administered by MLIT and the Japan Civil Aviation Bureau (JCAB), make costs prohibitive and are restrictive in particular for landing near Tokyo.

In Japan, the result of such regulatory burdens is that business aviation has yet to be used effectively as a tool for its global companies. Further, these burdens are a barrier to foreign direct investment since the investors cannot easily land; "Japan passing" is forced on CEOs even if they are inclined to stop due to "vampire hours" for late-night landings at Haneda as well as high fees for landing and other ground services. As a result, Japan has few landings and only about 25 dedicated commercial-use business aircraft, or less than a tenth of the 283 in Britain and an unusually small number when compared to other developed nations.

The Japanese government promises to improve the situation for landing slots at regional airports and, in the long run, in Tokyo. In central and western Japan, the Chubu and Kansai regions now have multiple airports that welcome such landings. By April 2005, regional airports (other than Type I) may accept landings of international charter and business aviation flights with only three days notice, a reduction from 10 days notice (provided that customs, immigration and quarantine or "CIQ" will be available). In the future, additional slots at Narita and Haneda may be available to ease access to Tokyo and to support both domestic and international business aircraft. Further, the additional runway at Haneda planned for 2009 should be a long-term target for significant improvement in the frequency and convenience of landing slots near Tokyo.

Growing needs among users (not to mention the renewed demands from U.S. firms and the U.S. Government) should force reexamination of these MLIT and JCAB regulations for business aviation. U.S. aircraft manufacturers believe that the regulatory situation has limited sales of their planes, and the U.S. Government has urged improvement. Bilateral initiatives for foreign investment, increased access and tourism, and long-term economic cooperation may also include means to ease use of business aircraft in Japan.

Electric Utilities

The United States continues to stress that by introducing genuine competition into non-fuel procurement (valued at approximately $10 billion annually), Japan can effectively reduce the costs of its electric power, which remain among the highest in the industrialized world. U.S. exports should rise significantly if barriers are lifted. U.S. exports currently account for approximately 3.5 percent of Japanese electric utility procurements, or around $350 million per year.

Japan's utilities actively participate in the New Orleans Association (NOA), a U.S. Embassy-sponsored forum that enhances communication between Japanese electric power utilities and U.S. suppliers of non-fuel materials, equipment, and services. The United States continues to urge Japanese utilities to further increase procurement of foreign products and services (which often prove more economical) to seek greater transparency and fairness in the procurement process.

Nevertheless, foreign firms face barriers due to standards and specifications used by Japanese utilities that often discriminate against or disproportionately burden foreign suppliers. Problems remain in the use of narrow, dimension-based technical standards rather than performance-based technical standards, and requirements that suppliers provide detailed information for spare parts originating from outside sources. In addition, because each utility uses its own specifications (in some cases, different departments of a utility use their own specifications), suppliers must prepare more than ten production lines in order to sell to Japan's ten electric power companies. Some Japanese utilities also require that foreign and domestic suppliers register with the utility, a process that can involve submission of product and test data and can be extraordinarily time consuming. In addition, there have been allegations that Japanese utilities rejected registration applications by foreign suppliers because the foreign companies are not consumers of electricity generated by Japanese utilities. Finally, good access to procurement information is difficult to obtain.

Motorcycles

In 2004, the Diet finally eliminated Japan's ban on tandem riding of motorcycles (carrying a passenger) on Japanese motorways. This was followed by the Cabinet issuing a Cabinet Ordinance to allow motorcyclists aged 20 or higher with more than three years experience to tandem ride starting April 1, 2005. The previous prohibition of tandem riding ban artificially limited Japan's market for large motorcycles, adversely affecting U.S. exports. More importantly, by forcing riders to use less-safe ordinary roads, the ban significantly reduces the safety of motorcycling in Japan. The U.S. Government strongly supports this reform and will monitor its implementation.

Sea Transport/Ports

U.S. carriers serving Japanese ports have long encountered a restrictive, inefficient, and discriminatory system of port transportation services. In October 1997, after repeated diplomatic efforts to remove these restrictions, the U.S. Federal Maritime Commission (FMC) assessed a $100,000 fee on each ocean voyage to the United States by Japanese shipping lines. This prompted Japan to agree in October 1997 to substantial regulatory reform of its ports sector and the fees were suspended in November 1997. The U.S.-Japan understanding also noted side agreements designed to reduce the power of the Japan Harbor Transport Association (JHTA) from deterring competition in the sector. Japan amended its Port Transportation Business Law (effective November 2000) to eliminate the need for new entrants to prove there is surplus demand. Charges for harbor services in nine large ports are subject to a prior notification requirement and there is an approval requirement for other ports by the Ministry of Land, Infrastructure and Transport (MLIT). The nine large ports are Keihin (Tokyo, Yokohama and Kawasaki), Chilba, Shimizu, Nagoya, Yokkaichi, Osaka, Kobe, Kanmon (Shimonoseki and Kitakyushu), and Hakata. In May 1999, the FMC removed its rule imposing the fees, and imposed a semi-annual reporting requirement on two U.S. and three Japanese shipping lines.

Since 1999, the United States has expressed its concern that reforms have not lessened JHTA's ability to deter new entry and restructuring in the ports sector. The United States has noted that the revised Port Transportation Business Law did eliminate the economic needs test and licensing requirement at the nine large ports, although the amended law still maintains a permission system for new entrants to port services operations in those ports. The Port Transportation Business Law introduces new requirements that run counter to the need of efficient port operations and discriminate against new entrants wishing to offer port services. For example, minimum manning levels for new entrants was set at 150 percent; new terminal operators are required to conduct all terminal operations as a joint venture or under a close ties relationship with established Japanese operators; a new licensing rule was introduced, requiring excessive and unnecessary information such as business plans; and the Japanese government now has the authority to disallow rates for port services found to be anticompetitive. In addition, MLIT has not addressed concerns about the prior consultation process conducted by the JHTA nor about the apparent threat of illegal strikes against foreign carriers who obtain permission to operate their own container terminals.

In August 2001, citing its continuing concern that these issues had not been resolved, the FMC ordered the five U.S. and Japanese carriers and several other major shipping lines serving the U.S.-Japan trade to report detailed information on the effects of recent changes in Japanese port laws and ordinances; the ongoing semi-annual reporting requirements continue only for the two U.S. carriers and the three Japanese lines named in the original proceeding. The United States will continue to closely monitor how these changes affect port operations and to urge faster regulatory reform in the port sector. Both the Japanese and U.S. positions, however, have solidified over the years. At the March 2004 High Level Regulatory Reform meeting, the U.S. Government reiterated its position that the Japanese government has failed to implement important aspects of the wide-ranging port deregulation promised in 1997.

Steel

U.S. steel producers have previously expressed concerns that Japanese steel companies may be engaging in anticompetitive practices. With respect to Japan's domestic market, it has been alleged that Japan's integrated producers have coordinated output, pricing, and market allocation goals. In addition, it has been alleged that Japanese mills have entered into arrangements with foreign counterparts to regulate bilateral steel trade.

Japan participated constructively in bilateral consultations and in OECD High-Level Meetings on Steel during 2004 aimed at eliminating subsidies in the steel sector. In June 2004, the OECD High Level Group on Steel reaffirmed their commitment to the ultimate goal of stronger subsidy disciplines in the global steel sector, and decided to shift the focus of the talks to bilateral and plurilateral consultations to explore bridging the differences on the key issues. The High Level Group also agreed to reconvene in 2005 to evaluate prospects for a steel subsidies agreement.

KAZAKHSTAN

TRADE SUMMARY

The U.S. trade deficit with Kazakhstan was $219 million in 2004, a decrease of $5 million from $224 million in 2003. U.S. goods exports in 2004 were $319 million, up 89.6 percent from the previous year. Corresponding U.S. imports from Kazakhstan were $538 million, up 37.1 percent. Kazakhstan is currently the 85th largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Kazakhstan in 2003 was $5.4 billion, up from $5.3 billion in 2002. The National Bank of Kazakhstan (NBK) calculated new U.S. FDI for the first half of 2004 to be $700 million. Most investment in Kazakhstan to date has been in the oil and gas sectors. Kazakhstan's external position is at its strongest since independence, due to growing oil export prices. The petroleum sector accounts for almost one third of gross domestic product (GDP) and well over one-half of all export earnings.

The U.S.-Kazakhstan Bilateral Trade Agreement, which came into force in 1993, provides for normal trade relations (NTR) between the United States and Kazakhstan and governs other aspects of the bilateral trade relationship. A bilateral investment treaty (BIT) between the United States and Kazakhstan came into force in January 1994.

Kazakhstan submitted its application for World Trade Organization (WTO) membership on January 29, 1996, and the fact-finding phase of the accession process was completed in 2003. Kazakhstan's Working Party met in March and November of 2004, and the next meeting is expected to take place in the first half of 2005. While Kazakhstan hopes to enter the WTO in 2005, it has been slow to enact key reforms to make its trade regime WTO-compliant. Kazakhstan also lacks key enforcement mechanisms, even in areas where appropriate laws have been passed.

IMPORT POLICIES

Kazakhstan is a member of the Eurasian Economic Community (EAEC) along with Russia, Kyrgyzstan, Belarus and Tajikistan - Moldova and Ukraine currently have observer status. Trade among the five EAEC countries is generally duty-free, but protective measures may be applied. These countries have not yet established a common external tariff. The EAEC is currently developing coordinated customs procedures that would reduce the cost of transshipping U.S. goods destined for Kazakhstan through the EAEC member states. Kazakhstan is also part of the Single Economic Space (SES) with Russia, Ukraine and Belarus, a nascent customs union. Although the four partners, with varying degrees of intensity, have made the political commitment to move forward with SES integration, the required implementing agreements and legal harmonization will likely not be completed until at least 2007.

Tariffs

The simple weighted import tariff in Kazakhstan in 2004 was approximately 7.9 percent. In January 2004, the Value-Added Tax (VAT) was reduced from 16 percent to 15 percent. Imported goods are subject to the VAT on the value of the goods at the time of importation (VAT destination principle), except for oil and oil products imported from Russia, where the VAT is applied before export. Kazakhstan plans to adopt the destination principle for the VAT application for all imports in the context of WTO accession. In the interim, it has negotiated agreements to this effect with individual members of the Commonwealth of Independent States (CIS), e.g., Kyrgyzstan, Moldova, and Azerbaijan. Most recently, Kazakhstan's Parliament voted to ratify an additional protocol to Kazakhstan's agreement with Russia regulating collection of indirect taxes on bilateral trade that would apply the destination principle to all goods. The protocol will go into effect with the President's signature.

Goods imported for short-term use in Kazakhstan under the temporary import regime can be fully or partially exempt from duties, taxes and non-tariff regulations. The government has the right to issue a list of goods that cannot be temporarily imported into Kazakhstan. Goods not eligible for duty exemptions have traditionally included food products, industrial wastes and consumables.

Similar to the 1994 Foreign Investment Law, the Law on Investments, enacted in January 2003, provides customs duty exemptions for imported equipment and spare parts if Kazakhstan-produced stocks are unavailable or not of international standards.

Customs Procedures

Kazakhstan's new Customs Code became effective May 1, 2003, superseding the law of 1995. There are positive changes in the Code, such as a provision intended to provide WTO-compliant customs valuation methodologies. However, as of January 2004, importers continued to report that customs officials were failing to comply with these methodologies. In addition, key provisions for such practices as voluntary disclosure are not included in the Code. In September 2004, the Customs Control Agency was subordinated to the Ministry of Finance; customs authorities previously reported directly to the Presidential Administration.

The Customs Control Agency continues to discuss the automation of customs procedures, but little progress has been made. Since October 2002, Kazakhstan has maintained a "customs audit" procedure administered by a private contractor. The private contractor determines customs value based on a database of world prices, in contravention of international standards. Under this system, approximately 20 percent of all goods crossing Kazakhstan's borders are subject to valuation uplifts. While the government pays for inspections, the declaring party pays penalties in the event of discrepancies. There are concerns that this process is used to generate extra-legal revenues beyond existing duties and taxes. Courts have decided over 85 percent of all appeals under this system against the Customs Agency. In addition, Ministry of State

Revenues Order 402 sets conditional prices for certain imports, a practice inconsistent with international norms.

U.S. companies have consistently identified Kazakhstan's requirement that they obtain a "transaction passport" to clear imported goods through customs as a significant barrier to trade. This regulation is designed to stem capital outflows and money laundering by requiring importers to show copies of contracts and other documentation to legitimize and verify the pricing of import/export transactions. The practice retards the growth of trade, as the regulations place relatively tight restrictions on transaction parameters. For example, the regulations allow a maximum financing term for imports of 120 days, after which time the transaction passport must be closed out. This limits the range of business activity and creates a potential bias towards short-term financing in the economy.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The present system of Metrology, Accreditation, Standards and Quality (MAS-Q) in Kazakhstan is weak and fragmented. Many businesses complain of mandatory certification requirements that have no purpose or technical basis. The Committee on Standards, Metrology and Certification, Gosstandart (the national governing body operating under the Ministry of Industry and Trade), undergoes frequent management changes that make stable, long-term progress difficult. Government enforcement of compliance with existing standards, testing, labeling and certification requirements continues to be uneven.

In 1999, two laws – "On Standardization" and "On Certification" – were enacted to bring these areas into compliance with international standards and practices. In 2000, the law "On Ensuring Uniformity of Measurement" was passed. In 2001, the Government adopted Resolution No. 590, which outlines a national Program for Quality for 2001-2005. These laws and the quality program are intended to bring Kazakhstan's MAS-Q system into general conformity with WTO requirements under the Technical Barriers to Trade and Sanitary and Phytosanitary Agreements. However, there has been little progress in the implementation of this program.

The Law on Certification requires that all imported products subject to mandatory certification requirements be accompanied by documents identifying the producer, the date of production, the expiration date, storage requirements and the code of use in both the Kazakh (state) and Russian languages. The government has accepted placement of Kazakh language stickers on products as compliance with the law, instead of requiring entirely new labels. The government has also issued a wide-ranging regulation exempting pharmaceutical products and several other categories of goods from the Kazakh labeling requirement.

GOVERNMENT PROCUREMENT

Kazakhstan is not yet a member of the WTO Agreement on Government Procurement. With the support of the World Bank, Kazakhstan is reforming and harmonizing its system of state procurement. Some potential U.S. investors have raised concerns about the transparency and efficiency of the government tender process. In October 2002, Kazakhstan adopted "Rules for the Organization and Holding of State Procurement." These rules established a standardized format for publicizing tenders and specified in which newspapers the offers should appear, based on the newspaper's circulation and the tender's value. However, Article 26 of this law gives broad and seemingly unrestricted preferences to domestic suppliers in all sectors.

The State Procurement Agency was established by Presidential decree in December 1998, and the Regulation on the State Procurement Agency was approved in March 1999. This legal structure strengthened the monitoring functions of the Agency, improved control systems, and provided independence in the selection of methods for high value procurements. The Rules on Oil and Gas Procurement, which went into effect in 2003, also give significant preferences to local suppliers, and establish what many firms consider unwarranted state interference in even small tenders. Despite governmental promises to amend the Rules, they stand as originally written. However, there are have been no reports yet of attempts to enforce the Rules.

U.S.-funded assistance projects are helping Kazakhstan establish a database to assist in procurement. The database was launched by the State Procurement Agency in 2003 but remains a work in progress. Not all tenders are listed, and some Government offices contacted in January 2004 stated that they do not rely on the database but instead continue to use their own contact lists to publicize tenders.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Significant deficiencies remain in Kazakhstan’s regime for the protection of intellectual property. Due to these deficiencies, a case remains pending to review Kazakhstan’s status as a beneficiary country under the U.S. Generalized System of Preferences (GSP) Program. Kazakhstan has been on the Special 301 Watch List since 2000.

The 1992 U.S.-Kazakhstan Agreement on Trade Relations incorporates provisions on the protection of intellectual property rights (IPR). Kazakhstan has fulfilled a number of the agreement’s obligations regarding intellectual property under the agreement, but several bilateral commitments remain yet unfulfilled. As a part of its effort to accede to the WTO, Kazakhstan took steps in 2004 to bring its IPR laws into compliance with the WTO's Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS Agreement).

In 2004 Kazakhstan ratified the World Intellectual Property Organization (WIPO) Copyright and Performances and Phonograms Treaties. The Kazakh Law on Copyrights was also amended to guarantee protection for pre-existing copyrighted works. In addition to legislative initiatives, Kazakhstan has worked cooperatively with law enforcement agencies, public organizations and international organizations to fight piracy.

In October 2003, the Kazakhstan Ministry of Justice held a national campaign for IPR in accordance with the Justice Minister's decree of September 30, 2003, aimed at studying the cause of Kazakhstan's high incidence of piracy and developing an appropriate strategy for protecting IPR in Kazakhstan. The campaign was held to raise public awareness about IPR issues, including piracy and other illegal activities, develop methods of strengthening the working relationships between various state authorities concerned with IPR, improve law enforcement practices, and solicit suggestions from the public for improving IPR legislation. The campaign continued in 2004, when the IPR Committee of the Justice Ministry, among other activities, began publishing a quarterly journal on IPR issues.

Criminal penalties for IPR violations were adopted in 2001, but the United States remains concerned about the effectiveness of these Criminal Code provisions in deterring piracy and counterfeiting due to the high burden of proof required of prosecutors. It remains unclear whether new criminal penalties for IPR violations will be effectively enforced and will deter piracy. U.S. industry reports that it is difficult to obtain judgments in infringement cases and that this serves as *de facto* encouragement for future trademark piracy. In 1999, Kazakhstan also amended its Customs Code to provide for the seizure at the border of items that violate IPR laws. However, illegal material, including illegal sound recordings, continues to be imported, particularly from Russia and China.

SERVICES BARRIERS

Oil and Gas Procurement Regulations, enacted in June 2002 (see Investment Barriers, below) stipulate that oil companies purchase services only from Kazakhstan-based companies unless the required service is unavailable in Kazakhstan.

INVESTMENT BARRIERS

Kazakhstan's new Investment Law, passed in January 2003, supersedes and consolidates past legislation, but according to major investors and law firms, represents no marked improvement over previous laws. There is concern about the Law's narrow definition of investment disputes, lack of clear provisions for access to international investment arbitration, and little stability protection for contracts signed after the law went into effect. More positively, however, the Investment Law eliminates time limits for stability clauses for existing contracts, and in some cases, most notably oil and gas, gives precedence to sector-specific legislation.

For several years, there has been a growing trend to favor domestic over foreign investors in most state contracts. The 1999 amendments to the Oil and Gas Law required mining and oil companies to favor local goods and services. The rules implementing these legal provisions were enacted in June 2002 (Decree 612), but were not being enforced as of December 2003. The decree creates onerous requirements for government involvement in, and approval at, each stage of private companies' procurement processes.

Kazakhstan recently added a controversial ‘pre-emption’ amendment to its Law on Subsurface Use. The amendment guarantees the state a right of first refusal when a party seeks to sell any part of its stake in a mineral resource extraction project. The state claims this preeminent right even in cases where the controlling agreement assigns preemptive rights elsewhere (e.g., to other investors in a consortium). The amendment specifically applies the preeminent right retroactively as well. This new amendment calls into question Kazakhstan's commitment to contract sanctity.

The Law on Subsurface Use allows both citizens of Kazakhstan and foreigners to own land under commercial and non-commercial buildings, including dwellings and associated land. Such land may be leased for up to 49 years. In June 2003, a new Land Code came into effect, which, for the first time, allows Kazakh citizens to privately own agricultural, industrial, commercial and residential land. However, foreign individuals and companies may still only lease agricultural land for up to 10 years, although the wording of the law is unclear with regard to purchase of such land by local legal entities, either wholly-owned or joint ventures. Kazakh authorities often require, as part of a foreign firm's contract with the Government, that the firm contribute to social programs for local communities.

Foreign insurance companies are limited to operating in Kazakhstan through joint ventures with Kazakhstani companies. Overall capital of all foreign insurance companies should not exceed 25 percent of the non-life insurance market and 50 percent of the life insurance market. The total registered capital of banks with foreign participation is less than 25 percent of the total registered capital of all banks in Kazakhstan. Foreign ownership of individual mass media companies is limited to 20 percent.

Difficulty in obtaining work permits for foreign investors' employees in Kazakhstan continues to be a problem. In 2001, a quota system was established that limited the number of work permits to 10,500, with exceptions for investors' lead representatives. The quota is set each year, based on a percentage of the total national workforce. Many companies report that permits for key managers and technicians are routinely rejected or granted for unreasonably short periods, or are conditioned upon demands for additional local hires. Companies also note that the regulations are confusing and interpreted differently by various local officials and the Ministry of Labor and Social Protection.

Although Kazakhstan is a signatory to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, there is one arbitral award (arbitrated through the World Bank’s International Centre for Settlement of Investment Disputes, as provided for under the U.S.-Kazakhstan Bilateral Investment Treaty), which the Kazakh government has neither paid nor attempted to have annulled.

OTHER BARRIERS

There are other structural barriers to investment in Kazakhstan, including a weak system of business law, a lack of effective judicial process for breach-of-contract resolution, and an unwieldy government bureaucracy. Many companies report significant logistical difficulties serving the Kazakhstani market. In addition, there is a burdensome tax monitoring system for all companies operating in Kazakhstan. Many companies report that they need to maintain atypically large back-office operations in Kazakhstan to deal with the tax system and frequent inspections.

In 2001, Kazakhstan adopted transfer-pricing legislation that gave tax and customs officials the authority to monitor export and import transactions in order to stop distortion of earnings through manipulation of export prices. Foreign investors are concerned because the government rejected the use of OECD standards to determine proper market prices, creating instead a methodology that fails to account for all cost and quality differences. The government also holds that transfer pricing can take place even in transactions between unaffiliated parties.

KENYA

TRADE SUMMARY

The U.S. trade balance with Kenya went from a trade deficit in 2003 of $53 million to a trade surplus of $42 million in 2004. U.S. goods exports in 2004 were $398 million, up 100.5 percent from the previous year. Corresponding U.S. imports from Kenya were $352 million, up 41.2 percent. Kenya is the 80th largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Kenya in 2003 was $92 million, up from $73 million in 2002

IMPORT POLICIES

Kenya's trade regime has been liberalized, apart from a small list of import licensing controls based on health, environmental, and security concerns. However, imports are still subject to some barriers to access. All imports with f.o.b. value of more than $5,000 are subject to pre-shipment inspection (PSI) for quality, quantity, and price, and require a Clean Report of Findings by a government-appointed inspection agency. In June 2003, the Finance Minister specified that the Import Declaration fee, which includes a PSI fee, would be 5,000 Kenya shillings (about $64). Importers who fail to obtain inspection in advance pay a 15 percent penalty for local inspection (25 percent for motor vehicles).

High import duties and value-added tax (VAT) pose trade barriers, especially in the agricultural sector. Kenya's import regulations on agricultural products are sometimes altered to reflect fluctuations in domestic supply and demand as well as political factors. Effective January 1, 2005, the government eliminated the import duty for inputs and raw materials used in the manufacturing sector. Duties on a number of raw materials and capital goods previously taxed at 5 percent were reduced to zero in the 2002-03 budget. Current rates are 10 percent for intermediate goods and 25 percent for finished goods. Import duties for fabrics are set between 25 percent and 35 percent, while duties on basic inputs such as yarn are zero. The current import duty on foodstuffs that compete with Kenyan products -- including meat and meat products, poultry and poultry products, and dairy products -- is 35 percent. In its 2004-05 budget statement, the government introduced an export tax on hides, skins, and scrap metal to encourage local processing rather than the export of these items. There is now a flat tax of Ksh 10 and Ksh 3 (approximately $0.12 and $0.04) per kilogram for hides/skins and scrap metal, respectively. Effective January 1, 2005, Kenya significantly raised duties on worn clothing to $0.75/kilo or 50 percent *ad valorem*, whichever is higher, reportedly as part of its implementation of the East African Customs Union. U.S. industry claims that this tariff hike constitutes a *de facto* ban on the entry into Kenya of used clothing.

The Kenyan government continues to carefully control imports of seed corn by subjecting hybrid varieties to a certification process that effectively restricts trade. Until a seed variety is fully registered (a process that can take 3-4 years), the Ministry of Agriculture restricts cereal seed imports by setting quantitative ceilings. However, once a variety is certified, the quantitative restrictions are lifted.

The government sometimes manipulates the application of the VAT to support policy priorities, both to protect "strategic" sectors, such as transportation and agriculture, and to address short-term needs. In 2004, Kenya eliminated the VAT and duty on a limited quantity of imported maize to address severe food shortages.

Customs Procedures

In 2000, Kenya started implementing the WTO Customs Valuation Agreement. Under the agreement, Kenya uses the transaction value for valuation of goods imported from other WTO signatories. Kenya's customs procedures are detailed and rigidly implemented, often leading to delays in clearance of both imports and exports. The delays negatively impact Kenya's business climate by reducing the private sector's legal options in trade disputes. The two private sector firms that administer Kenya's pre-shipment inspection regime are charged with ensuring that up-to-date customs valuation and risk assessment methods are applied.

Regional Trade Agreements

Kenya is a member of several regional trade arrangements, including the East African Community (EAC), the Intergovernmental Authority on Development (IGAD), and the Common Market for Eastern and Southern Africa (COMESA). Kenya is one of 11 members of COMESA's Free Trade Area. The EAC's Customs Union, which entered into force on January 1, 2005, will phase in duty-free transit of most goods between Kenya, Tanzania, and Uganda over a five-year period.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Commercial and research applications of agricultural biotechnology in Kenya are currently regulated through guidelines, which are neither formal regulations nor enacted law. The guidelines, published in 1998, describe a committee-based approach for review and approval of agricultural biotechnology imports, including specific review of end uses (e.g., planting seeds for trials). Substantial quantities of agricultural biotechnology products have been imported into Kenya for food aid purposes since the establishment of the Biosafety Committee, and significant volumes of food products derived from agricultural biotechnology crops are available commercially. Kenya has received food aid containing biotechnology components. These shipments do not appear to have been tested for biotechnology content. Kenya also imports maize from South Africa, where biotechnology varieties are commercially available. Kenya is a party to the Cartagena Protocol on Biosafety.

Certain Kenyan standards do not conform to international standards, and this has adversely affected foreign investment in the country. The Kenya Plant Health Inspectorate Service (KEPHIS) subjects certain imported agricultural goods to further inspection. The Inspectorate also regulates the import and export of plant materials and trade in biosafety control organisms (organisms that require special handling to ensure they are not accidentally released into the environment). KEPHIS evaluates commercial hybrid grain seeds for a period of three years before the seeds can be released to market. Industry has found this certification process to be tedious and restrictive.

GOVERNMENT PROCUREMENT

The Public Procurement Directorate in the Finance Ministry is the central organ for policy formulation, implementation, and oversight of the public procurement process in Kenya. The Directorate monitors the overall functioning of the public procurement process in Kenya and submits proposals for action to the Minister. Regulations require establishment of Ministerial or District Tender Committees (MTCs or DTCs). The Accounting Officer (the permanent secretary for ministries and the chief executive for corporations) chairs and directs the procurement process for goods worth less than Ksh 500,000 (about $6,400), according to the Exchequer and Audit (Public Procurement) Regulations of 2001. Tenders for goods and services exceeding that amount are supposed to go through the MTC or DTC. The MTC and DTC review tender documents and requests for proposals where the estimated value exceeds Ksh 1 million (approximately $12,800). The chairman can veto any committee decision. Any veto is supposed to be reported to the Public Procurement Complaints, Review and Appeals Board. The Minister of Finance appoints a chair of the Board from the private sector. Board decisions are final unless judicial review action is commenced within thirty days under any existing written law concerning judicial review of administrative decisions.

Any member of a procuring entity, the Public Procurement Directorate, or the Appeals Board who breaches regulations, is subject to a fine not to exceed Ksh 2 million (about $25,600). A corporation that violates the regulations is subject to a fine not to exceed Ksh 5 million (approximately $64,000). In 2003 the government proposed the Public Procurement and Disposal Bill to establish the Public Procurement Oversight Authority. The bill aims to make procurement more transparent and accountable and would require procurement agencies to carry out an annual update of pre-qualified firms, especially when dealing with restricted tenders such as military tenders. The bill as drafted does not address one common area of potential abuse by which government property is significantly undervalued for disposal to private entities. To date, Parliament has not voted on this important legislation.

Despite continuing concerns about transparency in public procurement, there has been some improvement in this area in recent years. For example, the government increased transparency in bidding by removing from its tenders the clause that read, “the government reserves the right to accept or reject any bid and is not obliged to give any reasons for its decisions.” The Central

Tender Board (CTB) now publishes its decisions and, if the bidder asks, provides reasons for rejecting certain bids.

Nonetheless, the public procurement system remains an area of considerable controversy. The World Bank, IMF, European Union, and other donors have conditioned some of their official assistance programs, including direct budget support, to reform of public procurement and privatization. Tenders are frequently manipulated and awarded to noncompetitive firms in which government officials have a significant interest, and conflict-of-interest regulations are rarely enforced. Cases have been reported in which tender specifications are tailored to favor one firm. In November 2003, a tender worth over $190 million involving procurement of Kenya Ports Authority cranes was cancelled after it was established that three Kenyan cabinet ministers had, by seeking postponement of the tender, interfered in the tender process. In early 2004, press reports exposed two procurement scandals involving government officials and a previously unknown international financing company, Anglo Leasing and Finance, Ltd., involving over $90 million in secret, single-source contracts for security-related items. Although two permanent secretaries were sacked following the scandals, Cabinet Ministers and other senior government officials alleged to have been involved in the deals have not been indicted. Similar cases involving corruption and tendering for insurance of public property have been reported.

In May 2003, the government suspended more than 1,000 procurement officers after an internal audit found massive and widespread irregularities in government tendering and procurement. Since that time, many of the same officers were brought back to work so that the government could function and there have been no more significant changes in government procurement procedures. Kenya is not a signatory to the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

In 2001, Kenya established the Manufacturing Under Bond (MUB) program to encourage manufacturing for export. The program is open to both local and foreign investors. Enterprises operating under the program are exempted from duty and VAT on imported raw materials and other imported inputs and have 100 percent investment allowance on plant, machinery, equipment, and building. Firms operating in Export-Processing Zones (EPZs) are exempted from all withholding taxes on dividends and other payments to non-residents during the first 10 years. They are also exempted from import duties on machinery, raw materials, and intermediate inputs. There are no restrictions on management or technical arrangements, and EPZ companies are allowed expedited licensing procedures.

EPZ firms are allowed to sell up to 20 percent of their output on the domestic market. However, EPZ firms are liable for all taxes on products sold domestically plus a 2.5 percent penalty. There is no general system of preferential financing, although sectoral government development agencies in areas such as tourism and tea are supposed to provide funds at below-market rates to promote investment and exports.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Kenya is a member of most major international and regional intellectual property conventions – the World Intellectual Property Organization (WIPO), the African Regional Industrial Property Organization, the Paris Convention for the Protection of Industrial Property, and the Berne Convention on the Protection of Literary and Artistic Works.

The Kenyan Parliament passed an amended version of the Kenya Industrial Property Act, which came into force in June 2002, in an effort to make the Act compliant with Kenya's obligations under the WTO Trade-Related Aspects of Intellectual Property Rights (TRIPS) Agreement.

An amended Trademarks Bill was passed in August 2002. The bill provides that goods and services for which application is made for registration of a mark shall be classified in accordance with the Nice Classification System for Goods and Services. The amended bill is designed to be in conformity with the Madrid Agreement and Protocol as well as the TRIPS Agreement. The government has drafted a "Layout Designs of Integrated Circuit Bill" and circulated copies to stakeholders and the WIPO for comments.

An amended Copyright Bill came into force on February 1, 2003. Computer programs, sound recordings, broadcasts, and literary, musical, artistic, and audiovisual works are protected under the Act. The Act created the Kenya Copyright Board, which was established in July 2003 with a broad mandate for assuring that Kenya is in compliance with TRIPS. The Board also coordinates all licensing and treaty activity and has the authority to inspect, seize, and detain suspect articles and to prosecute offenses. Violation of copyrights, especially on music and films, is pervasive, and enforcement remains sporadic at best. Kenyan artists have formed organizations to raise awareness of intellectual property rights and to lobby the government for better enforcement, but merchants are still free to peddle pirated versions of Kenyan and international works without fear of arrest or prosecution. Pirated materials and counterfeit goods produced in other countries are readily available in all major towns in the country. These materials include pre-recorded audiocassette tapes, videocassettes, CDs, and consumer products. Although the exact amount is not available, in June 2004 the Kenya Revenue Authority, through a newly created Counterfeit Department, said the illegal trade costs the Kenyan economy an estimated Ksh 20 billion (about $256 million) in unpaid taxes. Imported drugs, shoes and textiles, office supplies, tubes and tires, batteries, shoe polish, soaps and detergents are the most commonly counterfeited items. Historically, however, penalties and enforcement for copyright infringement have been low. General understanding of the importance of intellectual property is very limited.

SERVICES BARRIERS

In general, individuals and companies supplying services, whether local or foreign, are accorded the same treatment. However, foreign companies offering services in construction, engineering, and architecture may face discrimination on tenders for public projects. New foreign investors with expatriate staff are required to submit plans for the gradual phasing out of non-Kenyan employees. In 1999, the government of Kenya increased fees and security bonds under the Immigration Act by 50 percent to 100 percent in an attempt to discourage the employment of foreign labor. The Kenyan bar admits foreign lawyers for a maximum duration of 12 years. Medical doctors must serve a one-year "induction" in the public hospitals and sit for exams before they are considered for registration in the country.

Since 1995, the government has privatized some government assets through the sale of state-owned tourist facilities, the flotation of shares of state-owned financial institutions on the Nairobi Stock Exchange, and the off-loading of government shares in the Mumias Sugar Company. After awarding a tender for the sale of Kenya Reinsurance Corporation (Kenya-Re) in October 2002, the government suspended the sale. The government has indicated its intention to offload 10 percent of its 35 percent stake in Kenya Commercial Bank although there is no deadline set for this.

The government of Kenya has been hesitant to open public infrastructure to competition because the state-owned companies that control infrastructure are considered "strategic" enterprises. As a result, the reform and partial privatization of telecommunications, power, and rail has fallen behind schedule.

Telecommunications

In July 1999, the government dissolved the Kenya Posts and Telecommunications Corporation, under the Kenya Communications Act of 1998. Three separate entities were then formed: Telkom Kenya (telecommunications); the Communications Commission of Kenya (CCK), the regulatory body; and the Postal Corporation of Kenya (postal services). In January 2005 the Government ended Telekom Kenya's monopoly on Very Small Aperture Terminals (VSATs), Internet bandwidth, and most landlines and has licensed a number of competing firms. In July 2004 the Minister for Information and Communications halted the awarding of a second national operator (SNO) for fixed-line telephone service, citing irregularities in the tendering process. The government announced at the time that a new bidding process for the SNO would be announced later, but this had not yet occurred by year's end. In August 2001, the government announced that three Kenyan firms had succeeded in acquiring the rights to operate eight regional licenses in competition with Telkom Kenya. Telair Communications landed five of the eight licenses for a reported $23 million. Safitel netted two regional licenses for $9 million, and Bell-Western acquired the remaining regional license for $25,000. However, these regional entities have not begun operations. As a result, the government has said it will cancel their licenses while the firms argue that changes in circumstances merit renegotiated contracts.

The CCK has licensed two firms, Safaricom (a joint venture of Telkom and Vodafone) and Kencell (a joint venture of Vivendi and Sameer Investments), to provide mobile cellular telecommunications. These two companies have well over 2.8 million subscribers (as of September 2004), almost twelve times the 240,000 landlines provided by Telkom. In fall 2003, the government awarded a tender to a third mobile operator, Econet Wireless, but the award has been challenged in court.

After more than one year of negotiations to sell its 49-percent stake in Telkom Kenya, the government cancelled the sale in late 2001. In an October 2004 draft National Information and Communication Technology Policy, the government proposed major changes in the sector, including further restructuring Telkom Kenya prior to its privatization in 2005. The government's failure to privatize Telkom Kenya and sell Kenya-Reinsurance (Kenya-Re) has cast doubts on the willingness of the government to privatize other parastatals, such as the Kenya Ports Authority and the Kenya Railways Corporation. The government says its draft Privatization Bill, published in November 2003, will lay the framework for privatization. Although the government has often indicated that the Privatization Bill is an economic policy priority, the bill is unlikely to be passed before mid-2005 at the earliest.

The Communication Commission of Kenya (CCK) regulates telecommunications and radio communications in the country. As of April 2004 there were 73 registered ISPs, but only 16 were actively providing commercial service. Foreign ownership of an ISP is restricted to 40 percent. June 30, 2004 marked the end of exclusivity granted to Telkom Kenya in the provision of certain segments of telecommunication services. The Commission developed a new licensing approach to address challenges and create opportunity for additional players to provide various communication services under a competitive environment. The new approach provides equal licensing opportunities to all players on a first-come-first served basis subject to the potential licensees demonstrating adequate capacity to provide the services for which they are seeking licenses. The new regulatory strategy:

- allows cellular mobile operators (GSM) to construct and operate their own international gateways if they choose, a move necessitated by the need for diversity in international links, high traffic volumes, the need to expand and better manage roaming services including General Packet Radio Service (GPRS) roaming;

- provides for the licensing of additional Internet Backbone and Gateway Operators, Broadcast Signal Distributors, and Commercial VSAT Operators on a first-come, first-served basis;

- allows Public Data Network Operators (PDNOs) to establish International Gateways for data communication services; and

- allows Internet Backbone and Gateway Operators, Broadcast Signal Distributors, Commercial VSAT Operators, and Public Data Network Operators to carry any form of multimedia traffic such as Voice Over Internet Protocol (VOIP.).

Power Generation and Distribution

The Kenyan government split the Kenya Power and Lighting Company (KPLC) into three entities in 1997: a power generator (KenGen); a distributor (KPLC); and a regulator, the Electricity Regulatory Board (ERB), to regulate retail tariffs and to approve power purchase contracts between KPLC and producers. The government also licensed Independent Power Producers to sell electricity to the grid. In late 2001 the ERB commissioned a study to review electricity tariff policy. The draft report was presented to key stakeholders in January 2002 recommending an upward adjustment of electricity tariffs to make the struggling KPLC profitable. The study recommendations are yet to be implemented. In June 2004, the ERB released new rules to govern future operations as part of the ongoing reforms in the sector. The first set, Electricity (Licensing) Rules, 2004 governs power production, local generating, transmission, distribution and supply licensing. The second is the Electric Power (Metering and Consumer Installations) Rules 2004 that covers rights of both customers and electricity supplier. Electric Power (Electric Supply Lines) Rules 2004 allows the public utility to install and access power lines on any property upon appropriate agreement. The rules are enforced alongside the Kenya Electricity Industry Safety Code that spells out obligations of the industry players in ensuring safety. In May 2004, the ERB proposed a new code seeking to end the distribution monopoly of KPLC, although transmission is to remain the preserve of KPLC. The draft Kenya Electricity Grid Code says among its key principles is "to promote competition wherever practicable and facilitate a commercial environment" leading to competition among distributors for contracts with the transmission entity.

Railways

The Kenya Railways Corporation has contracted for the maintenance of all of its locomotives to General Electric. The corporation has restructured its operations and recruited senior management from the private sector in the hope of turning the loss-making company into a profitable entity. The government has indicated it would like to contract with a private company to operate the railway, but plans for privatization seem to have stalled. However, a joint concessioning of the Kenya-Uganda Railways is moving forward. By the end of October 2004, five companies that had presented bids for the undertaking had been cleared. Among the firms bidding to run the two railways for the next 25 years include the U.S.-based Railway Development Corporation.

INVESTMENT BARRIERS

The Kenyan government maintains some restrictions on foreign ownership of publicly traded companies and companies in the financial services and telecommunications sectors. In June 2002, the rules were amended to allow up to 75 percent foreign ownership (personal or corporate) of firms listed on the Nairobi Stock Exchange (NSE). If foreign ownership in a company is 75 percent at the time of listing on the NSE, the foreign owner is allowed to maintain (or reduce) but not to increase its share. Foreign investors may be allowed to increase their investment with prior written approval from the Capital Market Authority if the shares reserved for local investors are not fully subscribed. Foreign brokerage companies and fund management firms must be locally registered companies, with Kenyan ownership of at least 30 percent and 51 percent, respectively.

The legal system protects and facilitates acquisition and disposition of all property rights, including land, buildings, and mortgages. Foreigners are not allowed to have a freehold title anywhere in the country. However, leasehold titles -- normally 99 years for land in towns and coastal beachfronts and 999 years elsewhere -- are allowed. The cumbersome and opaque process required to purchase land, and concerns about security of title because of past abuses relating to distribution of public land, constitute serious impediments to new investment. Lack of confidence in the speedy and fair resolution of disputes, and requests from officials for illicit payments, continue to dampen the country's ability to attract more foreign investment.

The Kenyan government says it would like to attract foreign investment, and has taken some steps to improve the investment climate. Private investment, however, has responded slowly to the reform measures. The share of investors who perceive the investment climate to be deteriorating outnumbers the share who perceive it to be improving, according to a recent World Bank study. If Kenya is to attract meaningful foreign investment it will need to address rampant corruption; degraded road, rail, and telecommunications infrastructure; relatively high energy costs; and inefficient government expenditures. In December 2004, the government enacted the Investment Promotion Act, which is expected to streamline administrative and legal procedures.

The government has begun to restructure the financial system and taken measures to increase the role of the private sector and to establish greater accountability and transparency. A managed, floating exchange rate regime has been adopted, and companies may retain foreign exchange earnings and repatriate capital and profits without certification. Technology transfer requirements have been abolished. Local partners are encouraged but not required. Kenyan partners are no longer required for small-scale commercial enterprises.

OTHER BARRIERS

Although the new Kenyan government undertook some noteworthy anti-corruption measures in the first half of 2003 -- including enactment of two key anti-corruption bills and a much-lauded purge of corrupt judges and magistrates -- there are concerns among donors and others that progress in this area has stalled. In September 2004, the government finalized the long-awaited establishment of the Kenya Anti-Corruption Commission when President Kibaki approved the appointment of the director and three assistant directors. On December 20, 2004, the IMF, based on its first review of Kenya's economic performance under a three-year Poverty Reduction and Growth Facility arrangement, which was originally approved on November 21, 2003, approved a $76.9 million disbursement for Kenya based on the Board's assessment that Kenya is making adequate progress on its economic reform agenda. At the same time, the IMF noted that corruption in Kenya remains a concern for business, potential investors, and donors, and that Kenya needs to make more progress in this area to restore donor and investor confidence.

KOREA

TRADE SUMMARY

The U.S. trade deficit with Korea was $19.8 billion in 2004, an increase of $6.7 billion from $13.2 billion in 2003. U.S. goods exports in 2004 were $26.3 billion, up 9.4 percent from the previous year. Corresponding U.S. imports from Korea were $47.2 billion, up 24.0 percent. Korea is currently the 7th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Korea were $8.4 billion in 2003 (latest data available), and U.S. imports were $4.4 billion. Sales of services in Korea by majority U.S.-owned affiliates were $3.2 billion in 2002 (latest data available), while sales of services in the United States by majority Korea-owned firms were $217 million.

The stock of U.S. foreign direct investment (FDI) in Korea in 2003 was $13.3 billion, up from $12.2 billion in 2002. U.S. FDI in Korea is concentrated largely in the manufacturing, banking, and finance sectors.

IMPORT POLICIES

Tariffs and Taxes

While Korea has a relatively low average weighted tariff rate of 4.5 percent for industrial products, the weighted average of Korea's bound tariffs on all agricultural products is 64.1 percent, which poses a significant barrier to the trade of agricultural goods. Although Korea bound 91.7 percent of its tariff line items in the WTO Uruguay Round negotiations, tariffs on most forestry and fishery products are not bound. The United States continues to press Korea to reduce its applied tariffs on agricultural and food products.

As part of Uruguay Round WTO Agreement on Agriculture, Korea agreed to lower duties on more than 30 agricultural products including mixed feeds, feed corn, wheat, vegetable oils and meals, and fruits and nuts between 1995 and 2004, and has fully phased in those tariff reductions. However, duties remain very high on many high-value agricultural and fishery products. Korea imposes tariff rates of 30 percent or higher on most fruits and nuts, many fresh vegetables, starches, peanuts, peanut butter, various vegetable oils, juices, jams, beer, and some dairy products. Many products of interest to U.S. suppliers, including table grapes, beef, canned peaches, canned fruit cocktail, apples, pears, and a variety of citrus fruits are subject to tariff rates of 40 percent or higher. In many instances Korea applies prohibitively high tariffs despite the absence of domestic production.

As part of its Uruguay Round commitments, Korea also established tariff-rate quotas (TRQs) that were intended to provide minimum access to previously closed markets or to maintain pre-Uruguay Round access. (*See also "Quantitative Restrictions, TRQs and Import Licensing."*) In-quota tariff rates are zero or very low, but the over-quota tariff rates for some products are prohibitive. For example, natural and artificial honey are subject to an over-quota tariff rate of 243 percent; skim and whole milk powder, 176 percent; barley, 324 percent; malting barley, 513 percent; potatoes and potato preparations, more than 304 percent; and popcorn, 630 percent.

In order to protect domestic agricultural, fishery and plywood producers, Korea also uses "adjustment tariffs" and compounded taxes to boost applied tariff rates. Most of the adjustment tariffs are imposed on agricultural and seafood products, including frozen croaker and skate, which are products of interest to U.S. exporters.The U.S. Government has expressed concerns regarding these practices to the Korean government. In 2004, Korea eliminated adjustment tariffs on three textile products (silk yarn, woven silk fabrics, and woven cotton gauze fabrics other than narrow fabrics), renewed adjustment tariffs on 19 items, and reduced the tariff rates for 7 of these 19 items. In 2005, Korea eliminated the adjustment tariff on frozen poulp squid, renewed adjustment tariffs on 10 products, and lowered adjustment tariffs on 8 products.

Through its Uruguay Round commitments, Korea has also reduced bound tariffs to zero on most or all products in the following sectors: paper, toys, steel, furniture, semiconductors, and farm equipment. Korea has harmonized its chemical tariffs to final rates of 0 percent, 5.5 percent, or 6.5 percent, depending on the product. In addition, tariffs on scientific equipment have been reduced 65 percent from pre-Uruguay Round levels. On textile and apparel products, Korea has harmonized and bound most of its tariffs at the following levels: 13 percent to 16 percent for man-made fibers and yarns, 30 percent for fabrics and made-up goods, and 35 percent for apparel.

(For discussion of the impact of auto tariffs on market access, see "Motor Vehicles" section.)

NON-TARIFF MEASURES

Internal Supports

As part of its commitments under the WTO Agreement on Agriculture, Korea agreed to reduce its domestic support (Aggregate Measurement of Support, or AMS) for agricultural products by 13 percent by 2004. However, the Korean government substantially increased the level of domestic support it provided to its cattle industry during 1997 and 1998, thereby raising the overall level of support for agriculture. The issue of whether Korea's domestic support is in line with its WTO commitments on domestic subsidies was raised by the United States and Australia, along with other related issues, in WTO dispute settlement proceedings in 1999. While the panel ruled against Korea, the outcome of the dispute was inconclusive because the WTO Appellate Body was unable to make a specific finding on the consistency of Korea's subsidy level with the applicable obligations under the WTO Agreement on Agriculture. Nonetheless, the Appellate

Body did conclude that Korea had not been computing the current level of domestic support in a manner compatible with the requirements of the Agreement. The United States will continue to monitor Korea's notification of its AMS to the Committee on Agriculture to ensure that the calculation is in conformity with its commitments.

Quantitative Restrictions - Tariff-Rate Quotas (TRQs)

Most imported non-food goods no longer require prior government import approval, but some products, mostly agricultural and fishery items, face import restrictions such as quotas or tariff rate quotas (TRQs) with prohibitive out-of-quota tariffs. Korea implements quantitative restrictions through its import licensing system, which is administered by domestic producer groups or government buying agencies such as the Agricultural Fishery Marketing Corporation (AFMC) and the Public Procurement Services (PPS). A government export-import notice lists restricted products.

Korea also continues to restrict imports of value-added soybean and corn products. By aggregating raw and value-added products under the same quota, Korea restricts market access for value-added products such as corn grits, popcorn, and soy flakes. Domestic producer groups, which administer the quotas, invariably allocate the more favorable in-quota rate to their larger members, who use it to import raw ingredients.

Rice

In the Uruguay Round, Korea received a ten-year exception to tariffication of rice imports, and instead negotiated a Minimum Market Access (MMA) quota. Under the MMA quota, Korea’s rice imports grew over ten years from zero to four percent of domestic consumption. The Korean government, through state trading enterprises, exercised full control over the purchase, distribution, and end-use of imported rice. While Korea did not purchase any U.S. rice in the early years of the MMA program, in recent years the U.S. share of Korea’s total MMA rice imports increased to roughly one-fourth, and the United States became Korea’s second largest supplier of imported rice (after China).

That MMA arrangement was set to expire at the end of 2004, but under WTO rules, Korea exercised its right to negotiate with WTO rice exporting countries, including the United States and eight other interested parties, to seek an additional ten-year extension. Korea’s stated goal was to extend the MMA arrangement to coincide with a new ten-year agricultural adjustment program introduced in 2004 by the Roh Administration. The United States made clear it would only agree to extension of the MMA program if the program were amended to significantly expand commercial opportunities for U.S. rice exporters and offer them a genuine opportunity to develop meaningful relationships with Korean rice retailers.

Agreement on a ten-year MMA extension was reached in December 2004. For U.S. rice exporters, there are three major benefits to this agreement: Korea will double its total rice imports over the next ten years (from four to roughly eight percent of domestic consumption); Korea has guaranteed at the WTO that it will purchase at least 50,076 metric tons of rice from the United States in each of the next ten years; and for the first time, imported rice will be made available to Korean consumers at the retail level. This new MMA arrangement was notified to the WTO in late December 2004 and will be implemented in 2005 once it is approved by the Korean National Assembly and by a consensus of WTO Members.

Import Clearance Procedures

Despite the steps taken by the Korean government in the past few years, import clearance of agricultural products at Korean ports remains generally slow and procedures continue to be somewhat arbitrary. Surveys indicate that for most U.S. trading partners in Asia, import clearance for most agricultural products requires three to four days; in Korea, however, import clearance for new products still typically takes from 10 to 18 days, and six months to a year if a food additive is not specifically recognized in Korea's Food Additive Code for use in the imported product. (Food additives must go through a formal approval process before they can be approved for use in a particular food.) The United States will continue to urge the Korean government to improve its import clearance procedures until clearance times at Korean ports are comparable to those in other Asian ports, and until Korean procedures are based on science and are consistent with international trade rules and norms.

After WTO dispute settlement consultations initiated by the United States between 1995 and 1999, the Korean government revised its import clearance procedures by: (1) expediting clearance for fresh fruits and vegetables; (2) instituting a new sampling, testing, and inspection regime; (3) eliminating some non-science-based phytosanitary requirements; (4) revising the Korean Food and Food Additives Codes to bring, for example, Korean pesticide residue level standards for citrus into conformity with CODEX Alimentarius standards; and (5) requiring food ingredient listings by percentage for major, rather than for all, ingredients.

The Ministry of Agriculture and Forestry (MAF) and its agencies responsible for administering plant, animal, and animal product inspection, including the National Plant Quarantine Service and the National Veterinary Research and Quarantine Service, account for the greatest delays in import clearance. MAF imposes numerous requirements that restrict access or delay import clearance, such as incubation testing for non-quarantine pests and product detention if there are clerical errors on export certificates (e.g. incorrect zip codes for meat establishments). These practices add costs for importers and, ultimately, for consumers. Past improvements in expedited clearance of fruits and vegetables are slowly being eroded through various new testing and documentation requirements, extension of detention periods for pest identification, and an unreasonably high number of insects registered as potential pests subject to quarantine measures. (*See also "Standards and Conformity Assessment Procedures" section*.)

Customs Procedures

The Korea Customs Service (KCS) frequently classifies "blended products" under the Harmonized System (HS) heading for the major ingredient of that product, rather than under the HS heading for the blended product, which usually has a lower tariff rate. Changes in classification are often based on arbitrary standards and are at odds with practices observed by other OECD members. (For example, for dehydrated potato flakes to be classified as a blended product, they must include at least 10 percent non-potato ingredients.) "Blended products" disadvantaged by this practice include potato flakes, soybean flakes, flavored popcorn, and peanut butter chips. KCS also classifies beef bones with meat attached as pure muscle meat, subject to a tariff of 40 percent, rather than as offal, which would be subject to an 18 percent tariff.

KCS's misclassification of potato preparations under HS heading 1105 restricts U.S. exports of these products to Korea. U.S. exports of dehydrated potato products to Korea should be allowed under the unrestricted HS 2005 heading, with an applied tariff rate of 20 percent and a bound rate of no more than 31.5 percent. KCS has issued tariff code classifications for commodities that diverge from classifications observed in other markets, such as the United States and the European Union. For example, the United States and the European Union classify “Citrus Pulp Pellets” under HS 2308. Due to the percentage of molasses content, however, Korea has classified them under HS 2309, and therefore they are subject to an import quota. In addition, KCS routinely rejects customs clearance applications on administrative grounds (wrong font size, erasure marks on application, etc.), thereby delaying the customs clearance process. Finally, Korean regulations often require local trade associations to certify or approve import documentation. In addition to requiring the importer to pay a processing fee, which is used to help fund the association, this rule requires importers to submit proprietary business information.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Standards and Conformity Assessment Procedures (Sampling, Inspection, Testing and Certification)

Korea maintains standards and conformity assessment procedures, such as sampling, inspection, testing and certification, which are overly burdensome and have a disproportionate impact on imports. Each year, in an attempt to harmonize its regulations with international standards, Korea makes revisions to its food-related standards and specifications. More work is needed, however, to bring Korea's food codes, food additive codes, and labeling standards up to international standards. For example, Korea has not effectively adopted the "generally recognized as safe" standard. Instead, Korea's standards are more restrictive than internationally recognized standards; consequently, imports of "generally recognized as safe" food are frequently detained. The Korean Food and Drug Administration (KFDA) defines product categories eligible to use specific food additives too narrowly; if a particular product does not fit in the defined product category, it is then classified within the "other products" category, making it considerably more difficult to obtain approval for microbial standards and food additives. Additionally, KFDA's extensive documentation requirements for functional foods and for food additives, and its determination that a product is new if formula ratios are changed or if substitute ingredients are used, set its procedures apart from other OECD countries.

A number of Korea's sanitary and phytosanitary requirements and certification procedures continue to limit market access for a variety of products. However, progress has been made in several areas. In April 2003, after lengthy consultations, MAF issued a final rule allowing access for all cherry varieties. (Prior to this ruling, only certain cherry varieties could be imported.) In November 2004, the Korean government indicated it would be prepared to accept imports of U.S. codheads that met U.S. sanitary standards, rather than significantly more stringent Korean standards which significantly exceeded international norms, thus opening the Korean market to U.S. codhead exports. The Korean government also noted it was prepared to change construction standards to allow houses of wood frame construction to be built to five stories rather than the previous height limit of three stories; this should expand the market for U.S. timber exports.

For non-agricultural products, Korean government agencies require prior approval to import pharmaceuticals, chemicals, computers, telecommunications equipment, and other products (including all food additives). While many other countries require prior approval for some products, the range of affected products is exceptionally broad in Korea, and companies must submit documentation that is extraordinarily detailed. Moreover, in the past, proprietary information provided by importers as part of the prior approval/certification processes often was not adequately protected.

Beef

The U.S. has made the re-opening of the Korean beef market a top priority. Korea banned imports of U.S. beef in December 2003, after the detection of one positive case of an imported cow with Bovine Spongiform Encephalopathy (BSE) in the State of Washington. Prior to the ban, Korea was the third largest export market for U.S. beef and beef products and other ruminants, with annual exports valued at $1.3 billion in 2003. The U.S. Government has repeatedly explained, including at the most senior levels, that U.S. beef is safe, emphasized that any decisions about beef trade should be based on science, and expressed concern at the slow pace and the lack of transparency of Korean steps to re-open the beef market. At the time of publication of this report, the U.S. and Korean Governments are engaged in discussions designed to lead to the re-opening of the Korean beef market as soon as possible. The United States has also expressed concern that Korea’s ban includes products that are recognized in international standards as not carrying the BSE prion, such as muscle meat, milk, tallow and genetics products.

Korea’s ban also includes other ruminant products in addition to beef and beef products such as sheep and goats, which international standards indicate can also be safely imported from countries with cases of BSE with appropriate risk mitigating measures. Korea's import ban on non-ruminant products such as poultry meal from countries where there have been BSE cases is also overly restrictive.

Korea has continued to permit the imports of certain products containing ruminant ingredients, such as pharmaceuticals and cosmetics, in view of the scientific data disproving any risk of BSE contamination from them. However, U.S. exporters of those products have noted that since the Korean ban on U.S. beef was imposed, Korea's document requirements for BSE-free certification have become increasingly burdensome, and have begun to impede the flow of U.S. exports to Korea.

Oranges

In April 2004, Korea suspended navel orange imports from California's Tulare and Fresno counties (which together account for 80 percent of U.S. navel orange shipments to Korea). Korea alleged to have detected the presence of the fungal infection *septoria citri* in shipments of navel oranges from those two counties. The U.S. Government performed its own tests on the shipments of oranges rejected by Korea and did not detect the fungus in either California orchards or in laboratory tests of samples taken from infected shipments identified by the Korean government officials. This made the identification of appropriate mitigation measures difficult. However, the U.S. Government worked extensively with the California citrus industry to develop proposed mitigation measures for *septoria citri* to present to Korean officials. The U.S. Government submitted this new protocol to Korea in August 2004, to serve as the basis for Korea's resumption of navel orange imports, and the U.S. officials then participated in a series of bilateral technical discussions that followed to ensure the new protocol reflected only necessary and operationally feasible measures. In November 2004, the United States and Korea agreed to the new protocol, and California navel orange exports resumed in December 2004. The agreement is to remain in place for two years with a provision that refinement of mitigation measures may take place after the first year.

Poultry

In 2004, Korea, in response to detection of low pathogenic avian influenza (LPAI) in Delaware and a subsequent case of highly pathogenic avian influenza (HPAI) in Texas, banned imports of raw poultry meat from the United States (although Korea continued to permit the import of live poultry and cooked eggs and cooked poultry meat from the United States). In 2003, U.S. exports of poultry meat to Korea totaled $53 million. Throughout 2004 and in early 2005, U.S. officials met with Korean counterparts to explain the measures the United States had implemented to contain and erdicatge H5 and H7 avian influenze incidents in Texas and the Middle Atlantic. In response, Korea's Ministry of Agriculture and Forestry announced, in February 2005, it was prepared to lift the ban on U.S. poultry, and later that month solicited public comment on a set of draft rules for the resumption of U.S. poultry imports.

Biotechnology

Since 1999, the Korea Food and Drug Administration (KFDA) has had in place a voluntary safety assessment program for biotechnology crops for human consumption. In August 2002, as part of revisions to Korea's Food Sanitation Act, safety assessments of biotechnology crops were scheduled to become mandatory on February 26, 2004. The U.S. Government and U.S. industry expressed concerns that the requirement to complete mandatory safety assessments prior to February 26, 2004, could result in trade disruptions if resource constraints made it impossible for KFDA to process all applications prior to the deadline. In response to these concerns, KFDA revised the implementation timetable for its assessment guidelines: safety assessments for soybeans, corn, and potatoes still had to be completed by February 26, 2004; but the deadline for safety assessments for all other biotech crops was extended to February 26, 2005. To date, 26 biotech crops and 11 biotech additives have undergone KFDA safety assessments and have received KFDA approval.

Korea's approach to implementation of the Cartagena Protocol on Biosafety to the Convention on Biological Diversity (the Biosafety Protocol) and plans to introduce mandatory environmental risk assessments are of concern to the United States. A lack of clarity and transparency in the proposed regulations related to the Biosafety Protocol, and a lack of coordination among ministries involved in enforcement of the Biosafety Protocol, are expected to cause confusion, trade disruptions, and the duplication of requirements for imports at ports of entry. Environmental risk assessments for biotechnology crops will become mandatory when the Ministry of Commerce, Industry, and Energy's Live Modified Organism Act goes into effect in the second half of 2005 after Korea ratifies the Biosafety Protocol. So far, 17 applications have been submitted for voluntary environmental assessments (nine for corn, one for soybean, four for cotton, and three for canola) and seven assessments have been completed to date. The U.S. Government continues to urge Korea to notify the appropriate WTO Committee of revised requirements resulting from the implementation of the Biosafety Protocol; to provide an adequate grace period that will allow the completion of environmental risk assessments prior to the implementation of the Biosafety Protocol; and to implement minimally restrictive requirements, which avoid major disruptions of trade.

Maximum Residue Level (MRL) Testing

In 2003, a new import inspection program was introduced by the Ministry of Health and Welfare (MHW) and the Korea Food and Drug Administration (KFDA), which has undermined Korea's earlier efforts to harmonize its import clearance programs with international norms. In January 2003, a draft version of Korea's revised Ministerial Ordinance of the Food Sanitation Act was notified to the WTO in G/SPS/N/KOR/123. The United States and other countries raised elements of the new import inspection regime in subsequent meetings of the WTO Sanitary and Phytosanitary Committee (in October 2003 and in March, June, and October 2004), questioning their consistency with Korea's national treatment obligations. Of particular concern, the new import inspection program mandates annual maximum residue limit (MRL) testing of agricultural products on a packinghouse basis. The fee for the inspection of approximately $1,960 is to be borne by the importer. Domestic agricultural products, however, are subject only to random tests, which are paid for by the Korean government. In October 2003, KFDA, the agency charged with implementing the new import inspection program, initially indicated a readiness to lower the MRL testing fees to about $242; however, the new requirements went into effect on August 18, 2003, unchanged.

In 2004, in response to concerns voiced by the U.S. Government and other Korean trading partners, KFDA reduced the number of chemicals subject to testing from 196 to 47, and cut the fee for MRL testing from $1960 to approximately $500 (although this revised testing fee is still twice as large as the fee proposed by KFDA in October 2003). KFDA has also stated that it will revise its current import inspection program to allow an exemption from mandatory laboratory inspection for food imports from foreign food processors with a clean record. Even if the exemption for products with a clean record is implemented, the fee associated with mandatory laboratory inspection will remain as a barrier to new-to-market products. The United States will continue to urge Korea to resolve this issue.

Functional Foods

On June 28, 2003, KFDA announced new "Proposed Standards and Specifications for Health Functional Foods." The objective of the so-called "Functional Food Code" is to regulate health foods and nutritional supplements by listing products that can be classified as functional foods (i.e., foods that may provide health benefits beyond basic nutrition) and setting standards and specifications for them. Only products classified as functional foods can carry "efficacy claims" on their labels. In the proposed Functional Food Code, however, the limited number of functional food categories, as well as non-science-based upper limits on vitamin and mineral content, restricted entry of U.S. health foods and supplements into the Korean market. The U.S. Government and U.S. industry submitted comments detailing concerns about the potential for these proposals to restrict trade in health foods and nutritional supplements that are exported without similar complications to other markets. The KFDA amended the final version of its functional food regulations, which were implemented January 31, 2004, to address U.S. concerns regarding its proposed upper limits on vitamins and minerals. However, KFDA has not addressed U.S. concerns regarding the limited number of functional food categories, which currently do not provide for sport nutrition products or herbal products, categories that are widely accepted in other countries.

Regarding inspection of imported functional food, Korea has required mandatory laboratory testing for every shipment of functional food weighing less than 100 kilograms. In 2004, the U.S. Government repeatedly expressed concerns that this unusual weight-based testing requirement represented a barrier to trade. In response to U.S. Government concerns, Korea revised the current testing requirements to eliminate mandatory laboratory testing of subsequent shipments of functional food shipments weighing less than 100 kilograms, if the first shipment of the same product passes laboratory tests.

Organic Foods

In 2002, KFDA port inspectors detained many shipments of U.S. processed organic foods because the inspectors lacked clear guidelines from KFDA headquarters regarding the required documentation for clearance of imported processed organic food. After intervention by the U.S. Government, KFDA headquarters agreed to recognize an original transaction certificate issued by U.S. Government-accredited organic certifying agents for U.S. processed organic food. However, detention of U.S. processed organic food accompanied by the original transaction certificate issued by U.S. Government certifying agents continued because some regional KFDA inspectors still demanded unnecessary documentation.

In 2004, KFDA again changed its enforcement of regulations regarding imported organic foods. KFDA now requires that either governments or exporters provide copies of their country's organic certification regulations; after a review of the submitted regulations, KFDA decides whether that country's organic certification regulations meet Korean standards. After reviewing the National Organic Program (NOP) of the United States in 2004, KFDA decided to accept copies of NOP organic certificates issued by USDA-accredited certification agents located in the United States for import clearance of U.S. processed organic food. A list of USDA-accredited certifying agents that can issue organic certificates for products to be exported to Korea is posted on the KFDA website. However, KFDA only accepts certificates issued to producers, manufacturers, or processors. An original ingredient statement issued by the manufacturer must also be presented for import clearance. Insufficient communication between KFDA headquarters and regional KFDA offices about the changes in required import clearance documents, and the arbitrary interpretation of regulations by KFDA field inspectors, continue to cause delayed import clearance for imported organic products. The U.S. Government has noted its concern about these unnecessary delays and urged the KFDA to take steps to eliminate them.

Pharmaceuticals

In June 2002, the KFDA implemented Drug Master File (DMF) requirements that oblige manufacturers to submit significant quantities of proprietary manufacturing data to the KFDA as part of the drug approval process. The Korean government says the requirements are designed to assure product quality. U.S. industry representatives, however, have expressed concern that because the requirements apply only to new drugs, they apply almost exclusively to foreign manufacturers of innovative pharmaceuticals, and not to local generic companies. U.S. companies fear that the requirements may delay market access and could jeopardize intellectual property protection. A KFDA task force is studying the concerns expressed by U.S. industry and other stakeholders.

In addition, KFDA approval for the sale of drugs developed outside Korea remains slow. The frequent need for companies to duplicate clinical trials in Korea that have already been completed elsewhere is of particular concern because such trials are costly and delay market access for U.S. products. Duplicate trials were expected to decrease following Korea's 1999 announcement that it would implement International Conference on Harmonization (ICH) guidelines. While the KFDA has made progress in accepting the concepts in the ICH E5 guidelines, the KFDA typically does not consider Koreans to be members of the general Asian population for drug testing purposes and presumes that the effect of drugs on Koreans is unique unless proven otherwise. The U.S. Government will continue to press Korea to adopt more streamlined clinical trial application processes.

Finally, the Korean government continues to require that each shipment of a drug imported into Korea for commercial purposes be tested once registered. This is expensive, inefficient, and scientifically unsound. The United States will continue to urge the Korean government to implement appropriate international guidelines, to accept foreign clinical test data, to make the approval process for new drugs more science-based, and to shorten the overall drug approval process in Korea.
(*See also "Intellectual Property Rights Protection" and "Pharmaceuticals."*)

Telecommunications Standards

The U.S. Government is concerned about a pattern of exclusionary practices in the setting of standards for new technologies in the field of next generation communications. The Korean government appears to be continuing to encourage the development and selection of homegrown "Korea-only" technology standards. In addition, the government has, in some important areas, decided to mandate a single standard for emerging technologies, rather than allowing companies and consumers to freely choose the technology that best suits their needs. Such an approach can sharply limit opportunities for providers of proven foreign technologies. (*See also Telecommunications section.*)

Automotive Standards

(See "Automotive Standards Experts Working Group" in Motor Vehicles section.)

Labeling Requirements

U.S. exporters cite Korea's non-transparent and burdensome labeling requirements as barriers to entry for a variety of goods, despite various recent changes by the Korea government to these requirements. The U.S. Government will continue to address these issues with the Korean government.

On January 1, 2001, new Ministry of Environment (MOE) packaging and labeling standards for food went into effect. Aimed at protecting the environment by minimizing landfill material, the standards prohibited the use of PVC-shrink-wraps and promotional packaging that included more than 20 percent "dead space" in the container. MOE addressed U.S. Government concerns about the restricted use of PVC-shrink-wrap on some products, including frozen products. However, the U.S. Government continues to question Korea's rationale for restricting package size based on gross “dead space.” The United States has argued that net space displaced by such containers, once collapsed and measured (MOE does not allow this), is minimal and well within the objective of the standard.

Biotechnology: Korea implemented mandatory biotechnology labeling requirements for corn, soybeans, and soybean sprouts in March 2001, and for processed foods containing biotechnology enhanced corn and soybeans in July 2001. In March 2002, MAF extended biotechnology-labeling requirements further to include fresh potatoes. MAF officials have indicated to the U.S. Government that U.S. fresh potatoes are exempt from biotechnology labeling requirements with no requirement for extra documentation as long as no biotechnology potatoes are produced in the United States. The United States expressed concern to Korea that new labeling requirements appear far more burdensome than necessary to achieve their stated goal of providing Korean consumers clear information, and appear to raise national treatment concerns as well. In September 2002, after lengthy consultations, Korea agreed to accept notarized self-declaration as certification that products meet the criteria for exemption from biotechnology labeling.

Functional Foods: New Korean-language labeling requirements for functional foods are also of concern to the United States. The labeling guidelines for functional foods indicate that labels must be printed on packages. Under the new labeling requirements for functional foods, no provision is made to affix labels by means of a sticker. Stickers, however, are allowed for over-the-counter pharmaceutical products. The U.S. Government has expressed concern that the requirement for Korean language packaging rather than a Korean language sticker on functional foods can serve as a deterrent to trade, and will continue to press the Korean government to simplify labeling requirements.

Beef Labeling: In 2004, some National Assembly members filed a draft bill that would require mandatory “country of origin” labeling for beef dishes served in restaurants. Similar efforts by the Korean government and the Korea Consumer Protection Board that took place prior to this legislative effort were not implemented. The U.S. Government expressed concerns to the Korean government that requiring “country of origin” labeling on menus would limit the flexibility of restaurant owners to choose the origin of beef that they wish to purchase based on market principles. The bill is still pending. The United States has also noted that the meat packaging requirements of the Korean Ministry of Environment (MOE) Extended Producer Responsibility (EPR) system, introduced in January 2004, could potentially serve as an impediment to trade, and is monitoring the implementation of the new system.

GOVERNMENT PROCUREMENT

Korea joined the WTO Agreement on Government Procurement (GPA) on January 1, 1997, and agreed to cover procurement of goods and services over specific thresholds by numerous Korean central government agencies, provincial and municipal governments, and some two dozen government-invested companies. In accordance with its commitments under the GPA, procurement of satellites was included in Korea's coverage as of January 1, 2002. Over the past year, the U.S. Government has assented to the de-listing of some formerly state-run companies from which the Korean government has divested.

EXPORT SUBSIDIES

Korea committed several years ago to phase out export subsidy programs that are not permitted under the WTO Agreement on Subsidies and Countervailing Measures. However, Korea continues to promote its economic development based on undue reliance on exports, particularly from its traditional export-oriented industries such as automobiles, semiconductors, shipbuilding, and steel. In addition, Korea is encouraging the development of export-oriented “next generation” industries, such as semiconductors and telecommunications. The U.S. Government continues to strongly urge Korea to ensure that its government support programs fully comply with its WTO obligations.

In February 2002, the Korean government revised the "Act for the Export-Import Bank of Korea"to enable the Export-Import Bank of Korea (KEXIM) to become more active in undertaking risks and extending credit lines to exporters. Under the new regulations, KEXIM is able to undertake risks that commercial banks are reluctant to assume. In addition, KEXIM's financing sources were expanded to include non-bank guarantee fees, thereby boosting exports from Korean companies. The U.S. Government will continue to monitor modifications made to the Act to ensure that they are consistent with Korea's WTO obligations, including that financing provided under this Act does not take the form of a prohibited subsidy. In addition, the United States will also work to ensure that Korea is respecting its obligations as a participant in the OECD Export Credit Arrangement. KEXIM financing has been an issue in the ongoing trade dispute between Korea and the EU on alleged government subsidies to the Korean shipbuilding industry.

Government Support for Certain Industrial Sectors

The U.S. Government continues to be concerned with support extended to Hynix Semiconductor, Inc. (Hynix), Korea's second largest semiconductor manufacturer, by Korean government-owned financial institutions. Because the Korean government continued to provide financial assistance to Hynix, a formal countervailing duty (CVD) investigation was conducted and completed by the U.S. Commerce Department and the International Trade Commission in 2003. As a result of this investigation, Hynix's exports to the United States have subsequently been subject to countervailing duties of 44.29 percent. In June 2003, Korea initiated dispute settlement proceedings in the WTO. In January 2004, a panel was established to review Commerce’s subsidy determination. The EU has also conducted a CVD investigation and found injurious subsidization – which is being challenged in the WTO by Korea – and a Japanese CVD investigation is pending as well.

The U.S. Government also continues to focus on concerns raised by the U.S. paper industry about targeted Korean government aid to its coated paper sector, including low-cost facility investment loans and loan guarantees, tax benefits for facility expansion, government-sponsored creation of a paper manufacturing complex and government sale of debt obligations. Since the United States and other trading partners constitute a significant export market for Korean coated paper, U.S. industry remains concerned that such support may be distorting international markets for certain paper goods. The U.S. Government has raised the issue repeatedly with Korean government officials over the past two years, including in an experts meeting on paper in Seoul in February 2004. However, the Korean government has not yet taken concrete steps to adequately address this issue. The U.S. Government will continue to consult closely with U.S. industry to determine the best course of action to address concerns in this sector.

With regard to government support across all sectors, the U.S. Government also has concerns about the role played by the government-owned Korea Development Bank (KDB). Traditionally, the KDB has been one of the government's main sources for policy-directed lending to favored industries. Lending and equity investments by the KDB appear to have contributed to current overcapacity of certain Korean industries, an overcapacity that causes distortion in trade. The U.S. Government will continue to monitor the lending policies of the KDB and other government-owned or affiliated financial institutions.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

While important steps have been taken to improve the protection of intellectual property rights in Korea, there remain areas of concern to the United States. This has become of increasing importance in recent years, as the digitization of Korea's economy, including the highest broadband penetration rate in the world, has significantly increased the opportunity for unauthorized copying of copyrighted material. The U.S. has also noted that with Korean films and music increasing their popularity throughout the Asia-Pacific region, and Korea's industrial products and trademarks enjoying global success, Korean creators of intellectual property would benefit from the sort of improvements the U.S. has advocated, both to Korea's own intellectual property regime and internationally.

Korea was elevated from the Special 301 Watch List to the Priority Watch List in January 2004 as the result of an Out-of-Cycle Review (OCR), and then maintained on the "Priority Watch List" in the annual Special 301 determination in April 2004. During the OCR, Korea's progress was assessed based on the following criteria, which were set out in the Special 301 report, including: (1) granting police authority to the Special Inspection Team (SIT) of the Ministry of Information and Communication (MIC) to conduct raids for software piracy; (2) submitting legislation to the National Assembly giving the exclusive right of transmission for sound recordings, including both the right of making available and the full right of communication to the public, seeking its enactment by the end of 2003; (3) providing additional data on the Korean government's enforcement efforts in order to evaluate more fully the range of enforcement activities, including the imposition of deterrent penalties, and to allow right holders to have the opportunity to take action against infringers who are not convicted; (4) submitting legislation to the National Assembly to grant the Korea Media Rating Board (KMRB) all authority necessary to stop film piracy; and (5) implementing fully and faithfully its agreement on the Wireless Internet Platform for Interoperability (WIPI) intellectual property issue.

Throughout 2004, the U.S. continued to urge the Korean Government to address these issues. By early 2005, the Korean Government had taken steps to address each of these concerns (although amendment of Korea's Copyright Act to provide comprehensive transmission rights legislation will require legislative action in Korea's National Assembly, which as of this writing has not been scheduled but is expected in the first half of 2005).

The U.S. Government also continues to urge Korea to strengthen its legal regime for the protection of temporary copies, technological protection measures, Internet Service Providers (ISP) liability, reciprocity provisions regarding database protection, *ex parte* relief, the lack of full retroactive protection for pre-existing copyrighted works and copyright term extension. In addition, concerns remain on book piracy in universities, street vendor sales of illegally copied DVDs, counterfeiting of consumer products, protection of pharmaceutical data, and lack of coordination between Korean health and IPR authorities on drug product approvals for marketing. These issues will be revisited during the next Special 301 Review, which will be completed in April 2005.

Transmission Rights for Sound Recordings

Important aspects of Korea's copyright regime have failed to keep pace with the market transformation resulting from digitization and high-speed access to the Internet. Because Korea has one of the highest levels of broadband Internet penetration in the world, the Korean government should show an effective response to the challenges posed by the changing nature of digital copyright piracy. The U.S. Government has expressed concern that on-line piracy rates will likely continue to grow and damage the revenues of both domestic and foreign recording industries, and has urged Korea to introduce legislation that provides a full set of transmission rights for sound recording producers. New legal tools need to be adopted and to continue to improve.

The Copyright Act was amended on October 16, 2004 (effective January 2005), to provide transmission rights for sound recording producers and performers; this legislation provides phonogram producers "interactive transmission rights" to control the making available of recordings through means such as posting copies on websites for downloading on demand. Further Copyright Act amendments were introduced in the National Assembly in early 2005 which would, inter alia, provide transmission rights for non-interactive transmissions -- other methods by which sound recordings may be digitally disseminated to the public such as webcasting, streaming and digital broadcasting. The legislation is expected to be considered by the National Assembly within the first half of 2005.

Korea Media Rating Board

Ratings by the Korea Media Rating Board (KMRB) are required for a motion picture to be distributed in Korea; in recent years, KMRB ratings granted to entities that were not legally authorized right holders (who submitted fraudulent applications for ratings) have facilitated the distribution of pirated copies. In December 2003, the Korean National Assembly passed legislation that the Korean government has stated grants the Korea Media Rating Board (KMRB) the authority to identify and stop the fraudulent rating of motion pictures. The KMRB announced implementing regulations which became effective from May 30, 2004. The U.S. Government worked with Korea to ensure the regulations would not place any undue burdens on legitimate rights holders to prove their rightful ownership. In addition, the Korean government clarified in October 2004 that KMRB itself has the authority to revoke ratings of titles which were fraudulently registered before the effective date of the new regulations, upon the evidence-supported request of a legitimate right holder.

In 2004, the KMRB unexpectedly applied the new regulations to other media, namely, music videos. Because the new regulatory scheme is specifically geared towards motion pictures, this has caused unnecessary complications and is a serious barrier to the importation of music videos from the U.S. into Korea. The U.S. has urged Korea to resume its previous and satisfactory process with regard to music videos; in early 2005, the KMRB agreed to introduce a streamlined application system for music video ratings.

IPR Enforcement

Korea passed legislation in July 2003 to give police powers to the Standing Inspection Team (SIT) of the Ministry of Information and Communication. From October 18, 2003, the SIT inspectors have been authorized to conduct raids on commercial firms and other institutions suspected of using illegal software. In June 2003, the Ministry of Justice sent a directive to all regional prosecutor offices to work proactively in pursuing IPR infringement violations. As a result, the Korean police and prosecutors' raids against software end-users have become more consistent with higher damages discovered than in previous years. Raids are more frequently initiated based on leads provided by the software industry. The United States remains concerned, however, about the transparency of the Standing Inspection Team's enforcement process, including whether the SIT acts on tips provided by industry, and whether right holders will be able to participate in raids to the maximum extent possible and be notified about all SIT raids, even when discovered infringements are minor.

The United States continues to urge Korea to further strengthen the penalties for IPR violations to increase their deterrent effect against piracy. In January 2001, the Korean government enacted amendments to the patent, trademark and utility model laws that increased both fines and terms of imprisonment for IPR violators. In response to requests by the U.S. Government in April 2002 that the Korean government provide detailed information on the results of IPR enforcement efforts, Korea has provided regular quarterly reports during 2003 and 2004 on the inspections of the SIT, the disposition of cases by prosecutors and on court verdicts (i.e. acquittals, convictions, punishments). In 2004, Korea began to provide data on the level of fine and jail times to which infringers were sentenced.

Temporary Copies

The United States believes that both the Copyright Act and Computer Program Protection Act, Korea's two principal copyright laws, should be strengthened by revising the law to clarify that the copyright owner has the exclusive right to make copies, temporary or permanent, of a work or phonogram. Current Korean law does not extend the reproduction right to cover copies made in the temporary memory of a computer, an enormous and still growing manner for use of copyrighted works.

Copyright Act

In April 2003, the Korean National Assembly passed revisions to the Copyright Act, with implementing regulations announced in July 2003. That package of revisions strengthened the Copyright Act in two important ways. First, the amendments improved the effectiveness of technological protection measures (TPMs) by prohibiting the production and trafficking of devices aimed at circumventing TPMs. Secondly, the framework for a "notice and take-down system" was introduced under which an Internet Service Provider (ISP) would be given a legal incentive to respond promptly to requests from rights holders to take down sites where pirated activities are taking place. Korea subsequently ratified the WIPO Copyright Treaty in June 2004. However, Korea still needs to take further steps in order to meet its treaty obligations and fully protect content in the digital age.

The Copyright Act revisions do not clearly protect those technical protection measures that manage who can access a work, nor does it prohibit the act of circumvention of TPMs, but only the creation or distribution of circumvention tools. A party who strips off protection and leaves the work "in the clear" for others to copy without authorization may escape liability. These changes need to be enacted for Korea to bring the TPM provisions into compliance with the global minimum standards embodied in the WIPO treaties.

While certain provisions of the Copyright Act defining Internet Service Provider liability were harmonized with the Computer Program Protection Act (CPPA) in 2003, further clarification is required. The Copyright Act amendments still leave unclear the scope of the underlying liability of service providers and the limitations on and exceptions from liability. In addition, there are concerns that the documentation requirements for the rights holders in a takedown request are too burdensome.

Concerning library exceptions under Korea's Copyright Act, the U.S. Government believes that a notice period of at least 30 days should be given to the right holders prior to the unauthorized digitization of their works to minimize any negative effects. Under the current law, library exceptions still apply only to literary works and not to broadcasts, performances and sound recordings.

The U.S. Government has also urged Korea to delete the reciprocity limitations relating to database protection in the Copyright Act, as it discourages the introduction of databases from countries without such legislation, including the United States.

The United States has also recommended that the Korean government clarify the availability of injunctive and *ex parte* relief in civil enforcement actions under the Copyright Act, as required under the TRIPS Agreement.

In line with international trends, the United States is urging Korea to extend the term of copyright protection for works and sound recordings to the life of the author plus 70 years or 95 years from date of first publication where the author is a legal entity. Korea currently provides copyright protection for the life of the author plus 50 years. Korea also remains in violation of its obligations under Berne Article 18 and TRIPS Article 14.6 to provide full retroactive protection for pre-existing works and sound recordings.

The U.S. Government has told the Korean government that the private copy exceptions in Articles 27 and 71 of the Copyright Act should be re-examined in light of the growth of digital technologies. These exceptions generally should not be applicable to the Internet environment, which by its very nature extends far beyond private home use. In the digital environment, the market harm threatened by the unauthorized creation of easily transmittable perfect digital copies far exceeds the harm threatened by analog personal copying. Legislation on this issue was introduced in early 2005. It is unclear what next steps may be taken.

Computer Program Protection Act (CPPA)

The modernization of Korea's Computer Program Protection Act (CPPA) to meet current challenges as well as to comply with new global norms continues incrementally. In late

December 2002, the National Assembly passed revisions to the CPPA that provided for transmission rights, a critical element of an effective copyright regime in the digital age. The CPPA amendments were signed into law on December 30, 2002, and took effect on July 1, 2003, with the implementing regulations becoming effective in August 2003.

The United States believes that the CPPA needs to be strengthened further and has urged Korea to revise the law to clarify that the copyright owner has the exclusive right to make copies, temporary or permanent, of a work or phonogram. Unlike the Copyright Act, the CPPA does have provisions on protection of TPMs used in connection with computer programs. However, these provisions need to be strengthened, including the narrowing of several broadly worded exceptions.

The United States has also recommended that the Korean government clarify the availability of injunctive and *ex parte* relief in civil enforcement actions under the CPPA, as required under the TRIPS Agreement.

Data Protection

In October 2004, a new high priority issue of concern to U.S. industry emerged in the area of intellectual property protection for pharmaceutical firms. In response to pressure from Korea's domestic generic drug industry, the Korean Food and Drug Administration (KFDA) proposed eliminating Korea's current rules which protect proprietary data submitted by a company for marketing approval from unfair commercial use for a set period of time. In doing so, KFDA would allow generic companies to rely on such proprietary data for marketing approval without permission of the originator or owner of that data. The United States raised serious concerns regarding this proposal, noting that such an action would bring into question Korea's adherence to its bilateral and multilateral commitments. Under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), Korea is required to protect undisclosed test data related to pharmaceutical products submitted for marketing approval against disclosure and unfair commercial use. While at the end of 2004 during bilateral consultations the Korean government affirmed it would not change the current system, in early 2005, the United States learned that such a change continued to be under active consideration. The U.S. Government has repeatedly made clear to Korea we expect that the Korean government will fully live up to its international obligations to protect undisclosed data from unfair commercial use. This issue will continue to be a high priority on the U.S. Government's agenda in 2005.

Book and Video-DVD Piracy

In August 2002, the National Assembly enacted the "Publication and Printing Business Promotion Act", which became effective February 2003 and allows private sector involvement in enforcement measures against book piracy. The Act gives the Ministry of Culture and Tourism (MOCT) the administrative authority to inspect and dispose of illegal copies of copyrighted books, but to date this law has provided minimal practical benefit to U.S. publishers. In 2003, the Korean authorities carried out few effective enforcement efforts against ongoing book piracy, which remains a common practice on and near Korea's university campuses. In February 2004, the Ministry of Education wrote a letter to all Korean university presidents, requesting them not to tolerate copyright infringement on their campuses; in February 2005, the Minister of Education sent a follow-up letter to Korean university presidents, reminding them of their responsibilities to combat piracy and asking for an update on their efforts. The U.S. Government has urged Korean authorities to coordinate with foreign book publishers and right holders in order to provide effective enforcement, and will continue to monitor implementation of this law.

Pirated audio-visual materials in DVD format, sold on the street by illegal vendors, continue to be a serious problem in Korea. The Korean government needs to meet this digital piracy challenge with stronger enforcement efforts and deterrent penalties. Despite active enforcement efforts in 2004, video-DVD piracy in Korea is increasing due to the growing sophistication of pirate production facilities and advanced distribution technologies. Intensified and consistent enforcement activities on the part of Korea's law enforcement agencies is needed to cope with this problem.

Patent and Trademark Acts, and Trade Secrets

Korean patent law is fairly comprehensive, offering protection to most products and technologies. In 2003, changes to the Patent Act strengthened and streamlined the application process. In 2002 the law was amended to streamline the procedures for foreign Patent Cooperation Treaty (PCT) members. From March 2003, the time limit for entering into the national phase of PCT international applications in Korea was extended for 30 months after the priority date. The revision also gave the Korean Intellectual Property Office (KIPO) more authority to protect technologies exchanged through the Internet. In December 2003, KIPO prepared an amendment to the law to improve collection regulations concerning patent fees, registration fees and commissions imposed in accordance with patent, utility model, design and trademark laws in order to improve the convenience for petitioners.

Despite the progress, U.S. industry still believes that some deficiencies remain in the interpretation of claims and in the treatment of dominant and subservient patents. While KIPO has amended relevant laws to address U.S. concerns regarding restrictions on patent term extension for certain pharmaceutical, agrochemical and animal health products (which are subject to lengthy clinical trials and domestic testing requirements), problems still remain. Of top priority has been the lack of coordination between Korean health and safety and intellectual property officials, which results in the granting of marketing approval for products that may infringe on existing patents.

Korea's Trademark Act has been amended over the years to strengthen provisions that prohibit the registration of trademarks without the authorization of foreign trademark holders, by allowing examiners to reject any registrations made in "bad faith." Despite this change, the complex legal procedures that U.S. companies must follow to seek cancellation proceedings acts as a barrier to effective enforcement by discouraging U.S. companies from pursuing legal remedies. In particular these problems still arise with respect to "sleeper" trademark registrations. ("Sleepers" are trademarks filed and registered by Koreans without authorization in the late 1980s and early 1990s, when KIPO was still developing a more effective and accurate trademark examination and screening process.) These registrations - although a clear infringement of the rights of legitimate trademark owners - are not challenged and removed. The Madrid Protocol, an international trademark application system, entered into force in Korea on April 10, 2003.

The U.S. Government continues to urge Korean authorities to increase efforts to halt trade in counterfeit goods. The Korean government agreed to cooperate with the USG "Strategy Targeting Organized Piracy (STOP!) initiative in October 2004. Also, in an effort to enhance border enforcement against the exports of counterfeit products, the Korean Customs Service has significantly upgraded its computer system. The United States has noted particular concern that while textile designs were afforded copyright protection (in addition to protection under Korean design law) through the 2000 Copyright Act revisions, enforcement over the last four years has not been consistent, and the protection of textile designs remains problematic. Some Korean companies allegedly pirate U.S.-copyrighted textile designs and export them to third countries where they compete with genuine U.S.-produced goods.

Korean laws on unfair competition and trade secrets provide a level of trade secret protection in Korea, but are insufficient in some instances. For example, some U.S. firms, particularly certain manufacturers of chemicals, pet food, and chocolate, face continuing problems with government regulations requiring submission of very detailed product information, such as formulae or blueprints, as part of registration or certification procedures. U.S. firms report that, although the release of business confidential information is forbidden by Korean law, in some instances, government officials do not sufficiently protect this proprietary information and the trade secrets were made available to Korean competitors or to their trade associations. In response to these concerns, the Korean Food and Drug Administration (KFDA) revised the Pharmaceutical Affairs Act implementing regulations to stipulate that submitted data must be protected from unauthorized disclosure when the submitting party requests protection.

SERVICES BARRIERS

Korea continues to maintain restrictions on some service sectors through a "negative list." In these sectors, foreign investment is prohibited or severely circumscribed through equity or other restrictions. (*See also "Investment Barriers".*)

Construction

The construction, architectural design, and engineering markets in Korea were first opened to foreign competition in 1996. Foreign companies may bid on public projects, including the massive capital projects designed to improve basic infrastructure in Korea. Foreign firms still report problems with attempts to renegotiate accepted bid prices, non-recognition of overseas performances, and excessively burdensome registration and bonding procedures.

Advertising

Korea is among the world's top twelve largest advertising markets; however, the market remains highly restricted. Since broadcast advertising time is still sold exclusively through the state-sponsored Korea Broadcast Advertising Corporation (KOBACO), advertisers and their agencies must work through KOBACO to advertise on broadcast television. Legislation was passed in 1999 to end KOBACO's monopoly, but implementation of these laws has been delayed.

Screen Quotas

Korea maintains stringent screen quotas on imported motion pictures, requiring that domestic films be shown in each cinema a minimum number of days per year (currently 146 days with reductions to 106 days possible if certain criteria are met). The quota discourages trade and hurts the competitiveness of the Korean film industry – a criticism that has been made by the Korean Fair Trade Commission as well. In January 1999 and in December 2000 the National Assembly passed resolutions stating that a relaxation of the screen quota should only be considered if and when Korean films achieve a 40 percent market share. Since 2001, Korean films have far exceeded that goal, maintaining a market share of 53 percent in 2003 and 57 percent in 2004. In 1999, the U.S. and Korean governments suspended negotiations of a Bilateral Investment Treaty pending resolution of the screen quota issue. The Roh Moo-hyun Administration has indicated renewed interest in resolving this issue. In 2004, the Minister for Culture and Tourism opened a dialogue with the local film industry to amend the screen quota system but real, positive movement by Korea on this issue has yet to occur.

Foreign Content Quota for Free Terrestrial TV

Korea restricts foreign activities in the free television sector by limiting the percentage of monthly broadcasting time (not to exceed 20 percent) that may be devoted to imported programs. Annual quotas also limit broadcasts of foreign programming to a maximum of 75 percent for motion pictures, 55 percent for animation, and 40 percent for popular music. Foreign investment is not permitted for terrestrial television operations.

Foreign Content Quota for Cable TV

Korea restricts foreign participation in the cable television sector by limiting per channel airtime for most foreign programming to 50 percent. Annual quotas for broadcast motion pictures are set at 70 percent and for animation at 60 percent. These restrictions limit foreign access and the development of Korea's film and animation industries. The Korean government also restricts foreign ownership of cable television-related system operators, network operators, and program providers to 49 percent. For satellite broadcasts, foreign participation is limited to 33 percent.

Satellite Re-Transmission

The Integrated Broadcast Law mandates that Korean firms that wish to re-broadcast satellite transmissions of foreign programmers must have a contract with the foreign program provider in order to obtain approval from the Korean Broadcasting Commission (KBC). Foreign re-transmission channels are limited to 10 percent of the total number of operating channels. This artificial restriction limits the amount of international broadcasting which could otherwise be made available to Korean consumers and limits foreign investment in Korea in the broadcasting sector.

Restrictions on Voice-overs and Local Advertisements

Presently, there are restrictions on voice-overs (dubbing) and local advertising for foreign re-transmission channels. These restrictions are written into the Korean Broadcasting Commission's guidelines for implementation of the Broadcasting Act, and as such, could easily be revised. Allowing voice-overs in the Korean language would make the broadcasts truly accessible to Korean consumers (especially for breaking news and children's cartoons, where the time-consuming requirement to create subtitles is particularly ill-suited to the target audience); it would also benefit the Korean economy by creating more studio-production jobs and foreign investment. The prohibition on local advertising for foreign re-transmission channels restricts the long-term viability of foreign re-transmission channels in the Korean market. Foreign re-transmission channels should be allowed to broadcast their content and add local advertising in order to ensure their financial stability as well as to show relevant advertising to their Korean viewers.

Accounting

Korea restricts the establishment of foreign accounting firms by requiring that companies must employ at least 10 Koreans, at least three of whom must be partners and seven of whom must be certified accountants. Foreign Certified Public Accountants (CPAs) are required to fulfill the same requirements as Korean CPAs, including: (1) obtaining Korean certification; (2) completing a two-year internship; and (3) registering with the public accountants association. Accounting firms in Korea are prohibited from making an investment in, or providing a debt guarantee to, any other firm in excess of 10 percent of the accounting firm's paid-in-capital.

Engineering

Although there are no restrictions on foreign engineering services specified in Korean law or regulation, procuring agencies (national, local, and private) can specify particular conditions and/or requirements for engineers and engineering services depending on the nature of the project. Such specifications can be written to favor domestic engineering services firms.

Legal Services

At the time of Korea's accession to the OECD in 1996, the Korean government amended the "Lawyers Act" to permit non-Koreans to be licensed to practice law in Korea, provided that they meet the same criteria that are applied to Korean nationals. The Korean government also amended regulations on foreign investment in 1997 to allow for foreign investment in the legal sector. Any individual not qualified as a lawyer under Korean law is prohibited from providing legal services to Korean and foreign clients in Korea and from establishing a law firm or office in Korea. There is no provision for "foreign legal consultants" in Korean law, although in practice many foreign attorneys in Korea perform legal advisory functions. The U.S. Government continues to urge the Korean government to allow foreign law firms to practice law in Korea.

Financial Services

As a condition of its post-Asian financial crisis IMF economic stabilization package, Korea agreed to bind its OECD commitments on financial services market access in the WTO. Korea's revised schedule of WTO financial services commitments entered into force in September 1999. After most foreign exchange transactions were liberalized in 2001, Korea's financial authority lifted almost all restrictions on the foreign exchange market, and foreign bank and financial subsidiaries do not have to receive Bank of Korea (BOK) permission on their financial transactions, even capital account transactions. The U.S. Government will continue to work with Korea to ensure that it meets its WTO and OECD financial services commitments and to establish more liberal treatment of foreign financial services providers.

Insurance

Korea is the second largest insurance market in Asia after Japan, with $51 billion in premiums paid in the fiscal year ending March 31, 2004. The environment for foreign insurance companies has improved considerably since Korea implemented a series of regulatory changes following its 1996 OECD accession.

The 1997-1998 financial crisis led to an ambitious restructuring of the Korean insurance industry. In 1998, the newly established Financial Supervisory Commission (FSC), the Korean government's financial watchdog and center for financial reform, revoked the licenses of some insurance companies, forced the merger of others on the grounds of insolvency, and assisted 16 insurance companies through FSC–supervised workout programs.

The Korean government is gradually liberalizing foreign entry into the life and non-life insurance markets and has lifted some restrictions on partnering with Korean financial companies and on hiring Korean insurance professionals. In April 1998, Korea liberalized insurance appraisals and activities ancillary to the management of insurance and pension funds. Korea's brokerage market was opened to foreign firms in April 1998. Several foreign reinsurance firms have since entered the market. In April 2003, the National Assembly passed a new insurance act that effectively reduced regulations and requirements for foreign insurance companies. The act reduces the minimum working capital requirement for on-line insurance companies, changes from a permission system to a notification system for offering new insurance products and entry into side businesses, and softens regulations related to asset management by insurance companies. Despite these improvements, a considerable gap remains between Korea's practices and those found in more developed insurance markets.

Banking

In the aftermath of the Asian financial crisis, the Korean government injected over 86.7 trillion won ($72.3 billion) in public funds into the commercial banking system, effectively nationalizing it. The IMF and the U.S. Government have repeatedly urged Korea to privatize state owned banks to allow market forces to more efficiently allocate financial resources and increase investor confidence in the Korean economy. Responding to IMF recommendations, Korea has begun to privatize state-owned banks to allow market forces to more efficiently allocate financial resources and increase investor confidence in the Korean economy. In 2004, the Korean government sold its share (21 percent) of Hana Bank. As a result, at the end of September 2004, foreign investors' stake in Hana had risen to 68.3 percent as compared to 37.9 percent at the end of 2003.

At the beginning of 2002, Korea modified its regulations to allow foreign bank branches to borrow from their head offices and to include the net borrowing as Class B capital. However, the Korean government did not allow the foreign branches to use head office capital to meet regulatory lending limit requirements and continues to restrict the operations of foreign bank branches based on branch capital requirements.

These restrictions limit: (1) loans to individual customers; (2) foreign exchange trading; and (3) foreign-bank capital adequacy and liquidity requirements. Foreign banks are subject to the same lending ratios as Korean banks, which require them to allocate a certain share of their loan portfolios to Korean companies other than to the top four chaebol conglomerates and to small and medium enterprises.

Foreign banks are permitted to establish subsidiaries or direct branches. Since 1998, the Korean government opened capital markets to foreigners, permitting foreign financial institutions to engage in non-hostile mergers and acquisitions of domestic financial institutions.

All banks in Korea continue to suffer from a non-transparent regulatory system and must seek approval before introducing new products and services - an area where foreign banks are most competitive. The April 1999 Foreign Exchange law introduced the first phase of foreign exchange and import-export transaction liberalization. The second phase of foreign exchange liberalization became effective on January 1, 2001, and deregulated foreign exchange and capital account transactions for individuals, but a few restrictions on foreign exchange transactions and derivatives trading by corporations and financial institutions still remain, which are applied to domestic and foreign institutions.

In 2005, members of Korea's National Assembly introduced draft legislation that would impose nationality and residency requirements for members of the boards of directors of Korea's banks. The United States has noted that the adoption of these or similar measures would send a negative signal to foreign investors in Korea's financial sector.

Securities

On June 24, 2000, the Korean government removed limits on local currency issues of stocks and bonds by foreign firms. The Korean government places no limits on foreign ownership of listed bonds or commercial paper, no longer restricts foreign ownership of securities traded in local markets, and has removed almost entirely foreign investment ceilings on Korean stocks. By the end of October 2004, foreigners owned more than 43.8 percent of the shares on Korean stock exchanges, according to Korean government statistics. Despite this liberalization, foreign securities firms in Korea continue to face some non-prudential barriers to their operations.

INVESTMENT BARRIERS

The Roh Moo-hyun government has continued to voice a commitment, shared by the previous administration, to create a more favorable investment climate and to facilitate foreign investment in Korea. In 2004, FDI increased to $12.8 billion, much of it mergers and acquisitions in the financial sector. The Citigroup purchase of KorAm Bank and Shanghai Motor's acquisition of Ssangyong Motor in December 2004, contributed significantly to FDI, which had decreased in 2003. There were also some announcements by U.S. companies regarding plans for investment in Korea, including: GE Capital's plans to buy a 38 percent share of Hyundai Capital for 1 trillion won (about $900 million) in 2006; and Phillips's plans to invest 25 trillion won (about $23 billion) by 2014 in LG-Phillips. The more positive attitude toward foreign investment on the part of the Korean government, many in private industry, and by a growing number of Koreans, is helping to open the Korean economy. However, while progress has been made in recent years, additional steps are needed to more fully improve the environment for foreign investment, including the removal of remaining structural barriers such as labor market inflexibility (e.g., better pension mobility, more flexibility in hiring and firing workers, expanded unemployment compensation, less rigid worker visa rules, and better job training and placement services), labor-management disputes, and insufficient regulatory transparency.

The 1998 Foreign Investment Promotion Act, in addition to simplifying investment procedures, providing more tax incentives, and establishing Foreign Investment Zones, increased the number of business sectors open to foreign investment. Nonetheless, two sectors – television and radio stations – remain fully closed to FDI, and 27 remain partially closed. Capital market reforms have eliminated or raised ceilings on aggregate foreign equity ownership, individual foreign ownership, and foreign investment in the government, corporate, and special bond markets. These reforms have also liberalized foreign purchases of short-term financial instruments issued by corporate and financial institutions. However, the Korean government still maintains foreign equity restrictions with respect to investments in various state-owned firms and many types of media, including basic telecommunication service providers, cable and satellite television services and channel operators, as well as schools and beef wholesalers.

The Korean government has taken several important steps to privatize state-owned corporations, although there were no new privatizations in 2004. The Korean government has also removed restrictions on the direct purchase of land by foreigners through the 1998 revision of the Alien Land Registration Acquisition Act. Foreigners, however, still cannot produce certain agricultural products for commercial purposes nor remove agriculturally zoned land from agricultural production.

As an additional liberalizing measure, the Korean government has opened Free Economic Zones (FEZs) with an extensive range of incentives including tax breaks, tariff-free importation, relaxed labor rules, and improved living conditions for expatriates in areas such as housing, education, and medical services. While establishing these zones is an important step in making Korea's business environment more open, liberal, and responsive to economic needs, the FEZ's will likely not address many of the key factors inhibiting additional foreign investment in Korea.

ANTICOMPETITIVE PRACTICES

Competition Policy

The Korean government's enforcement of its competition policy, although historically weak, has been strengthening. The Korea Fair Trade Commission (KFTC) has been playing an increasingly active role both in enforcement of Korea's competition law and in advocating for regulatory reform and corporate restructuring. KFTC's powers to conduct investigations and to impose tougher penalties were enhanced in January 1999, with the revision of the Monopoly Regulation and Fair Trade Act. The Act was subsequently revised in December 2000, to broaden KFTC's authority in corporate and financial restructuring and to raise substantially the administrative fines for violations or for failure to cooperate with KFTC investigations. In support of the KFTC's more aggressive stance, in October 2003, the Roh Administration submitted legislation to the National Assembly that would extend the KFTC's monopoly regulation authority under that act to allow it to trace the bank accounts of domestic companies through 2007. The National Assembly approved that bill on December 9, 2004. This legislation also increases the maximum surcharge against cartels to 10 percent (from the previous 5 percent maximum), facilitates private damage actions, authorizes payment for information from informants, exempts certain transactions from pre-merger reporting requirements, limits large conglomerates' (chaebol) voting rights in their affiliates to 15 percent from the current 30 percent starting in 2008, and reintroduces the KFTC's authority to monitor chaebol bank accounts for evidence of illegal inter-subsidiary dealings.

ELECTRONIC COMMERCE

Korea is considered to be a global leader in technology trends and was among the first countries to see widespread use of wireless phones. Korea has more high-speed Internet connections per household than any other country, and the government has actively pursued legislation to encourage electronic commerce.

The Korean government has been working to address data privacy issues by drafting a Basic Privacy Act and revising or adding sector-specific laws. Korea's Presidential Committee on Government Innovation and Decentralization and National Assembly are drafting the Basic Privacy Act, which is expected to pass in early 2005 following a one-time public hearing to gather input from industry experts. Industry-specific issues will be addressed separately by regulations to be put in place over a period of six months to two years following the passage of the Basic Privacy Act. As much of the draft Act addresses information held by the government, not the private sector, each relevant ministry will be responsible for devising associated regulations. The United States will work with Korea to try to ensure that is concerned that Korea does not develop a labyrinth of overly-burdensome regulations that inhibit the cross-border flow of information, which would negatively impact Korean and American companies and would limit consumer choice.

Numerous privacy issues have been discussed on the margins of the APEC Privacy Framework, to which Korea has contributed. NGOs in Korea are asking for stricter requirements in a number of areas which may impact cross-border data flows, thus hindering e-commerce. Korea is also considering establishment of a central office responsible for data privacy, similar to the data protection authorities that exist in other countries.

These efforts build upon actions the Korean government has already taken to encourage electronic commerce. For example, in December 2003, the Korean government teamed up with the private computer security industry to cope with the emergence of digital threats. The Ministry of Information and Communication launched a national cybersecurity agency under its roof, aimed at protecting critical infrastructure and enhancing Internet security. The new organization, the Korea Internet Security Center (KISC) is similar to the Computer Emergency Response Team in the United States, which provides timely alerts, coordinates information among private companies and government agencies, and monitors backbone Internet networks. The Basic Law on Electronic Commerce establishes the validity and enforceability of digital signatures as well as the admissibility of electronic messages.

Korea has also strengthened its regulation of spam. New laws, enacted in July 2003, require online marketers in Korea to flag their e-mails as advertisements and to set up a free telephone hot line so people can opt out of future e-mails. The laws also forbid marketers from scanning web sites for e-mail addresses. The Ministry of Information and Communication can impose a fine of up to 10 million Korean Won (USD 9400) on spam violators. The law also provides criminal penalties for the use of illegal technology or the distribution of maleficent advertisements to minors.

OTHER BARRIERS

Regulatory Reform and Transparency

The lack of transparency in Korea's rule making and regulatory system is a cross-cutting issue affecting U.S. firms in many different sectors, including the automotive, pharmaceutical, agricultural and telecommunications sectors, and continues to be one of the principal problems cited by U.S. traders and investors seeking to compete in the Korean market. In an effort to address these systemic issues, beginning in 2004, the United States and Korea deepened their focus on regulatory reform and transparency issues.

Korean laws, regulations, and rules often lack specificity, and implementing regulations frequently diverge from the stated objectives of the law. Korean officials exercise a great deal of discretion in applying broadly drafted laws and regulations, resulting in inconsistency in their application and uncertainty about how to comply with them within businesses. Compounding this problem is the frequent failure by various Korean ministries to provide to all stakeholders specific and timely notification of planned or actual changes to laws and regulations. When public comments are solicited, the timeframe for their submission is frequently unreasonably short. In addition, in many instances, final legislation and regulations do not reflect the extensive comments provided by stakeholders. Moreover, vague laws or regulations are sometimes reinterpreted and then applied retroactively, penalizing companies that have sought to fully follow Korean government guidance.

As more U.S. companies increase their presence in Korea, these administrative practices, which frequently involve "domestic" Korean regulations rather than traditional trade measures like tariffs or quotas, will have a greater impact on U.S. firms' access to the Korean market. During bilateral trade consultations in 2004, the United States outlined for Korean officials how Korea's administrative practices have affected U.S. companies operating in Korea, and pressed for improvements in the Administrative Procedures Act (APA) particularly related to: more explicit government-wide guidance on how the APA should be adhered to and enforced by various ministries; expanded use of notice-and-comment procedures, including for subordinate statues; and the publication of administrative actions.

Related to the pharmaceutical sector specifically, the United States also provided Korea with a list of concrete suggestions on how Korea's system for pricing and reimbursing innovative medicines could be made more transparent. Among other things, the U. S. Government urged Korea to establish an independent appeals process, thereby providing companies with an avenue to appeal questionable regulatory and pricing decisions to an authority other than the original decision-making body.

These bilateral efforts on regulatory transparency coincide with a Korean government focus on regulatory reform. The Roh Government has charged the Deregulation Taskforce Team, the Corporate Difficulties Resolution Center, and the standing Regulatory Reform Committee all to focus on different aspects of regulatory reform, both systemic and sector-specific. During trade consultations in 2004, the United States sought to identify how regulatory issues of concern to the United States might be brought to the attention of these three organizations. In 2005, the U.S. Government, in coordination with the U.S. business community, will continue to press Korea to adopt forward-leaning changes and to create a more transparent rule-making system that fully involves all stakeholders throughout the process.

Motor Vehicles

While the Korean auto industry has developed into the fifth largest auto industry in the world, access to the Korean market for foreign motor vehicles remains limited. While Korean auto sales in the U.S. market in 2004 were a record-high 688,670 vehicles, or 4.1 percent of the U.S. market, U.S. manufacturers sold only 5,415 vehicles in Korea. Furthermore, while sales of imported cars in Korea also hit a record in 2004, total auto imports into Korea represented only 2.1 percent of the market, or 23,345 vehicles. The U.S.-Korea auto deficit of $10 billion represented roughly half of the overall U.S.-Korea trade deficit in 2004.

The United States and Korea concluded a Memorandum of Understanding (MOU) in October 1998, designed to improve market access for foreign motor vehicles. Although the Korean government has implemented many of its commitments under the 1998 MOU, the United States continues to have serious concerns about the lack of progress toward the fundamental goals of the agreement, including substantially increasing market access for foreign motor vehicles and establishing the conditions to allow Korea's motor vehicle sector to operate by market principles. The United States has urged the Korean government to take additional meaningful actions to open the automotive sector, including eliminating or at least reducing Korea's eight percent tariff on imported automobiles, which is more than three times the U.S. tariff. The effect of the tariff is compounded by the cascading effect of multiple automotive taxes calculated on top of the tariff, which raise the effective rate to above 12 percent. The combination of relatively high tariff and taxes renders imported automobiles significantly less price competitive in Korea. A Korean study showed that if the auto tariff were reduced to 2.5 percent, foreign auto imports could increase to 12 percent of the Korean market within five years – an import level much closer to that of Korea's main auto trading partners. The Korean government has responded that it will likely defer any tariff reductions until the completion of the WTO Doha Development Agenda negotiations.

The United States has also expressed concern that Korea's current system of auto taxes discriminates against the larger vehicles that exporters tend to sell in the Korean market. Noting the MOU commitment to restructure and simplify the automotive tax regime in a manner that enhances market access for imported vehicles, the U.S. Government has urged the Korean government to lower the overall tax burden, reduce the number of taxes assessed on vehicles, and move away from engine-displacement taxes towards a value-based system. The U.S. Government has stressed that these commitments should be met through the development of a transparent and comprehensive plan, which would allow manufacturers and consumers adequate time to make adjustments. While the Korean government has taken some specific actions on automotive taxes over the last several years, to date, it has produced a transparent plan to meet the long-term MOU goals. In 2003, the U.S. Government presented a proposal requesting the Korean government to consider basing the calculation of Korea's multiple cascading automobile taxes on the actual value of imported vehicles at port of entry (CIF) rather than on the CIF value plus the tariff, as under the current system; however, the Korean government replied it has no current plans to modify the cascading auto tax system. The U.S. Government will continue to press for Korea to lower automotive tariffs and to undertake reforms of its overall automotive tax system in an open and transparent manner that fully involves all stakeholders throughout the process and enhances market access for U.S.-made vehicles.

The United States and Korea have also worked together in the bilateral "Automotive Standards Experts Working Group" (created in 2001) to address a range of motor vehicle standards issues, consistent with Korea's commitment in the 1998 MOU to simplify and streamline its safety and environmental standards and certification procedures. The meetings of this group have been productive, and the United States believes this forum offers the potential to build a stronger cooperative relationship on standards and certification issues. During 2004, the auto standards working group made progress in resolving concerns including: the implementation of self-certification procedures for vehicles imported into Korea; environmental testing of 4x4 vehicles within Korea; and the implementation of Korea's new Average Fuel Economy (AFE) system. U.S. auto exporters had expressed concern about a lack of transparency in the development of the Korean AFE regulations and the speed with which the requirements were to be implemented. Discussions in the standards experts group regarding AFE laid the foundation for a successful compromise on a mutually acceptable timeframe for implementation, and for ensuring that Korea's proposal to introduce a new style and shape of license plate would not disfavor U.S.-made autos or require costly modifications.

The U.S. Government also looks forward to continued efforts by the Korean government to address any anti-import sentiments and negative perceptions that could serve as barriers to the purchase of an imported automobile.

In 2001, General Motors of the United States bought a controlling share in Daewoo Motors, Korea's third largest auto manufacturer. In 2004, Daewoo Motors accounted for roughly 16 percent of Korea's vehicle production (for domestic and export markets combined).

Motorcycles

Although progress was made over the past several years to resolve U.S. concerns over Korea's pass-by-noise standard, several market access issues remain including a highway ban, tariff and tax levels, and standards and certification procedures. Korea's highway ban is the most serious of these barriers because it prohibits the use of motorcycles on expressways and on designated bridges and severely restricts the market penetration potential for heavyweight motorcycles, safely designed for highway use. Korea is the only major world market in which heavy motorcycles are denied access to major highways and designated overpasses in cities. Traffic safety statistics from other developed countries and research organizations demonstrate that highways are actually safer for motorcycles than are other types of roads with numerous intersections and hazards. The U.S. and Korean governments continue consultations on lifting the ban.

Pharmaceuticals

The U.S. remains seriously concerned about Korean government measures that result in unnecessary delays in market access for innovative medicines, do not appropriately value innovation, and diminish the contribution of Korea to research and development of innovative pharmaceutical products. The Korean government often develops its policies in this sector in a non-transparent manner without adequate input from domestic or foreign stakeholders. The resulting policies often harm U.S. companies, discourage investment in Korea, and impede the development of advanced biomedical research in Korea thereby hindering Korea's ability to achieve its goal of becoming a "biotechnology hub" for Asia.

The U.S. and Korean governments worked extensively in 1999 through a consultative process to address a number of priority issues in this sector. One result of this process was that U.S. and other international pharmaceutical companies were for the first time allowed to have their products listed under the Bureau of National Health Insurance's reimbursement guidelines. However, while some progress has been made in this sector in recent years, several important concerns remain.

Transparency: The lack of transparency in Korea's procedures for pricing and reimbursing innovative medicines under its national healthcare system was a key focal point of bilateral discussions in 2004. While the Korean government has agreed to consider new ways to increase the transparency of the drug pricing and reimbursement system, there are signs – including in the recommendations of a Korean government-commissioned health insurance reform study released in September – that progress could be reversed. The U.S. Government believes that developing policies that improve health care for all Koreans is best pursued by consulting with all domestic and foreign stakeholders, including foreign industry and governments. The U.S. Government will continue to urge the Korean government to consult regularly with foreign industry, ensure the use of public comment procedures, allow for appeal of MHW decisions on drug pricing, and combat corruption.

In addition to U.S. Government efforts in this important area, a bilateral Pharmaceuticals Working Group was formed in 2002, with the goal of increasing transparency in drug policy. The group is composed of Korean and U.S. pharmaceutical companies and Korean government officials, with U.S. Embassy staff serving as observers. While the Working Group's meetings have helped set a more positive tone for dialogue between the Korean government and the research-based pharmaceutical industry, there was no significant progress on any of the substantive issues U.S. industry raised during the two meetings that were held in 2004. The U.S. Government continues to work with Korea to ensure that the Working Group is useful in facilitating discussion and formulating possible solutions to bilateral issues.

Pricing: Other major obstacles to U.S. companies in the Korean pharmaceuticals market remain the absence of a fair and transparent pricing regime and the lack of transparent reimbursement guidelines. In 1999, Korea agreed to price innovative drugs at the average ex-factory price of A-7 countries (United States, United Kingdom, Germany, France, Italy, Switzerland, and Japan). All other drug prices would be determined using the Actual Transaction Price ("ATP"). While there was initially good progress in implementing the new system, problems have surfaced. Korea has not adequately implemented or enforced the A-7 or ATP systems. This has led to market distortions and corrupt prescribing practices, which have kept prices of generics artificially high and created incentives for doctors to prescribe for profit. Further, Korea has implemented a problematic "triennial repricing system" without adequate consultation with stakeholders.

A-7 Pricing: Despite Korea's 1999 agreement to use A-7 pricing, Korean authorities have been restrictive in granting new pharmaceuticals A-7 status and have used non-transparent criteria for determining whether a new pharmaceutical qualifies as "innovative." Korea's Health Insurance Review Agency (HIRA) has rejected – with no explanation – nearly two-thirds of the medicines that U.S. pharmaceutical companies have submitted since 2000 for A-7 pricing. The Korean government has not provided applicants for A-7 pricing an explanation as to why their products were determined to be ineligible. In December 2004, reinforcing a proposal that U.S. industry put forward earlier to achieve greater transparency and accountability, the U.S. Government proposed that the Korean government issue a one-page justification for its decisions not to provide A-7 pricing. The Korean government agreed to do so in January 2005. The U.S. Government welcomed this step and will continue to monitor the situation relating to A-7 pricing policies.

Actual Transaction Price: The United States was pleased when Korea reinstituted ATP in 2004 after a brief period of using a "Lowest Transaction Price" system. ATP, which bases reimbursement prices on a sales weighted average from the previous quarter, was intended to end hospital practices of demanding a discount from pharmaceutical manufacturers when purchasing drugs and then receiving a full reimbursement from the national health insurance system. However, Korea's poor enforcement of ATP has meant that reimbursement prices have not fallen. Further, Korea currently allows wholesalers to bundle their sales of drugs to hospitals and doctors. As a result, it is difficult to accurately determine the individual transaction cost of pharmaceutical sales. Bundled products that are sold include both low-margin and high-margin products in one package. The U.S. Government will continue to press Korea to better enforce the ATP system.

Triennial Repricing: The Triennial Repricing system, which took effect on January 1, 2003, affects all drugs registered on the national reimbursement list as of the end of 1999. All registered drugs will be subject to repricing every three years under this system. In 2003, out of 344 items subject to triennial re-evaluation, prices were reduced for 82 items by an average 7.5 percent. The repricing system does not allow for price increases when data supports such action. The repricing system was implemented without meaningful consultation, and the lack of transparency in the selection and pricing of drugs continues to be a concern.

Reimbursement Guidelines: As part of its efforts to trim health-care costs, the Health Insurance Reimbursement Agency (HIRA) has imposed restrictive reimbursement guidelines on the innovative drugs of foreign pharmaceutical companies without a rigorous transparent scientific review. These guidelines are initially set by the Korea Food and Drug Administration, but can later be modified by guidelines established by HIRA. The process by which HIRA establishes these modified guidelines is non-transparent. Although an appeals process exists, it is not codified by law and appeals are not made to an independent appeals panel but to the same office that made the initial ruling. The U.S. Government has raised concerns regarding the guidelines with the Ministry of Health and Welfare (MHW) and HIRA, and continues to urge the Korean government to develop a transparent process for revising reimbursement guidelines. In addition, the Pharmaceuticals Working Group initiated a task force to look at improving transparency in the reimbursement guideline-setting process. The Working Group has also submitted a list of recommendations for amending the reimbursement guideline-setting system, and U.S. members have reported some progress to date; however, more needs to be done.

Corruption

Corruption continues to be a widespread problem in the Korean healthcare system. As noted above, the complex distribution system and lack of transparency in government decision-making are large contributors to this problem. In 2005, the U.S. Government will continue to work with the Korean government to bring about a more transparent, fair science-based health care system that provides predictability for our companies in pharmaceutical pricing, reimbursement guideline setting, and regulatory affairs.

Medical Devices

The United States continues to be concerned about reimbursement pricing practices (particularly related to orthopedic devices and cardiovascular/endovascular devices), hospitals' buying practices, problematic provisions of the Medical Devices Act, and a proposal for third party review of product approvals. There is a need for a more transparent and streamlined regulatory approval process. In late 2002, the Ministry of Health and Welfare (MHW) approved proposed price reductions on medical products from between 2 to 75 percent, depending on the product and category. These reductions, effective January 1, 2003, are especially burdensome for all categories of orthopedic devices, for which reimbursement prices have been reduced between 14 percent and 60 percent.

In October 2003, the Korea Health Industry Development Institute (KHIDI) completed a study containing various recommendations for pricing, re-pricing, and disposable medical device management (including re-use and processing of human organs for surgical treatment). On pricing, KHIDI recommended setting price ceilings for new medical products at 90 percent or below the prices of similar products; using cost data (manufacturing costs for local manufactured products and import Free On Board prices for imported products) for calculations; setting a ceiling of 10 percent above the current market price for new medical technology; using prices in other countries (including Japan, France and Taiwan) as pricing benchmarks; and conducting re-pricing every two years. U.S. industry has expressed concern about these study results.

The Medical Device Act (MDA) was passed by the National Assembly in May 2003, and took effect on May 29, 2004. The MDA establishes a new legal framework for the regulation of medical devices, separate from the Pharmaceutical Affairs Act. The new legislation established a new four-class system which is consistent with global trends and will allow U.S. device firms to use global data for registration approvals with less need for data specific to Korea. In compliance with WTO obligations to eliminate tariffs on medical products, the Korean government eliminated tariffs on orthopedic devices in 2000 and eliminated tariffs on other medical products in 2004.

Telecommunications

As one of the world's most advanced telecommunications markets, Korea is actively commercializing a variety of cutting-edge wireless technologies, such as cdma2000, 1x EV-DO, W-CDMA, and portable wireless broadband Internet, as well as introducing terrestrial and satellite-based digital TV broadcasting. Given the tremendous commercial opportunities provided by this market, ensuring that Korea maintains fair and open competition in its telecommunications market is of paramount importance.

Despite rapid growth in the sector, U.S. suppliers have been negatively affected by excessive governmental influence over private operators' selection of technologies and interference in issues such as foreign licensing, royalty payment arrangements, and technology transfers. This governmental influence on the equipment and technology choices of private companies also often manifests itself in the licensing process for operators and in localization policies for procurement. The Korean government's control over tariff rate approvals, equipment certification, and other regulatory authority provide additional means by which it can exert strong influence over industries' selection of specific standards or technologies.

The Korean government has sometimes discouraged use of foreign-sourced goods and services for certain telecommunications applications, while simultaneously supporting development of applications based upon a domestic technology. In 2004, for example, the Korean government initially backed domestic technologies at the expense of proven foreign technologies in the development of standards for mobile phone applications and portable broadband wireless Internet. The Ministry of Information and Communications funds the development of domestic telecommunications technologies primarily through its research and development arm, the Electronics and Telecommunications Research Institute (ETRI), and through grants to universities and other research institutes. The U.S. Government has recently stepped up efforts to urge Korea to allow fair and open competition in this sector. In particular, the U.S. Government has urged the Korean government not to mandate specific technologies or intervene in private sector negotiations. A continuation of such practices runs counter to the Roh Administration's policies and its goal of encouraging foreign direct investment in Korea.

An important issue for U.S. industry and the U.S. Government in 2004 was Korea's plans to mandate the domestic Wireless Internet Platform for Interoperability (WIPI) standard for mobile phone applications. As originally envisioned, WIPI would have been the exclusive technology for downloading content from the Internet onto cell phones, thereby shutting out competing systems, including a U.S. system that already had over 7 million Korean subscribers. The U.S. Government, which opposes mandating exclusive standards such as WIPI, strongly objected to Korea's plans. As a result of extensive negotiations in 2003-2004, the Korean government agreed to allow other applications platforms to coexist in with WIPI in the market. The U.S. Government will continue to monitor implementation of the agreement.

The Korean government also recently announced that it plans to reallocate the 2.3-gigahertz spectrum to a new portable broadband Internet system and that it will only permit one technology standard to be used for this service. Licenses for the system were allocated in January 2005. At the insistence of the United States, the Korean government provided a written justification for its one-technology preference in January 2004. The U.S. Government and private sector found serious flaws in Korea's justification, some of which called into question Korea's adherence to its bilateral and WTO commitments. In June 2004, the Korean government modified its position and officially announced that all license holders will have to use a technology compatible with the International Institute of Electrical and Electronics Engineers

(IEEE) 802.16(e) Rev. D (or any subsequent version) air interface standard, as well as to satisfy some minimum performance requirements. Although less trade restrictive than mandating a "home grown" Korean standard – as the Korean government originally planned – this decision nevertheless remains overly trade restrictive, as it closes the market to several firms trying to market commercially-ready proprietary systems and inappropriately restrains operators' technology choices in a way not necessary for realizing the government's ostensible policy goals. The U.S. Government will continue to urge Korea to ensure that competition in services and technologies is allowed to thrive in its telecommunications market.

More generally, the U.S. Government is concerned that the Korean government's ambitious plans for promoting the information and communications technology sector, described in the Ministry of Information and Communication's "IT 839 Strategy" (8 services, 3 infrastructures, 9 new growth engines) could put a strain on U.S.-Korea trade relations if they are implemented in a discriminatory fashion. Responding to political pressure from the National Assembly, the Korean government recently publicly espoused a policy of reducing royalty payments made to foreign firms and encouraging the development of domestic standards and core technologies. While the government has since seemed to discontinue rhetoric calling for reducing royalty payments to foreign firms, it continues to actively promote the domestic development of technology, leading to concerns that it will seek to facilitate the commercialization of such technologies by protecting its home market. The U.S. Government views this development as discriminatory against foreign technology producers. The U.S. Government has expressed repeatedly its concerns that decisions to limit permissible services to a single technology are overly trade restrictive.

The Korean government divested the government's final holdings in Korea Telecom (KT) in May 2002. The United States believes that full privatization should inject much-needed competition into the market and allow more U.S. suppliers to qualify for KT procurement through locally qualified agents and distributors. In the telecommunications services sector more generally, foreign ownership restrictions, including a ceiling of 49 percent foreign ownership for facilities-based (Type 1) carriers, also impede the access of foreign firms to the Korean market.

KUWAIT

TRADE SUMMARY

The U.S. trade deficit with Kuwait was $1.7 billion in 2004, an increase of $941 million from $770 million in 2003. U.S. goods exports in 2004 were $1.5 billion, up 0.8 percent from the previous year. Corresponding U.S. imports from Kuwait were $3.2 billion, up 41.9 percent. Kuwait is currently the 53rd largest export market for U.S. goods.

The United States and Kuwait signed a Trade and Investment Framework Agreement (TIFA) in February 2004, providing a forum to address U.S. concerns.

IMPORT POLICIES

Tariffs

As a member of the Gulf Cooperation Council (GCC), Kuwait applies the GCC common external tariff of five percent for most products, with a limited number of country-specific exceptions. Kuwait's exceptions include 417 food and agriculture items, which will remain duty-free, as well as tobacco products, on which tariffs remain at 100 percent.

Import Licensing

Kuwait prohibits the importation of alcohol and pork products, and requires a special import license for firearms.

Documentation Requirements

In Kuwait, the import clearing process is time-consuming, requiring numerous transfers, large quantities of paperwork, and numerous redundancies. This process is prone to errors and fraud, since human judgment plays a major role in processing the transactions, especially auditing, valuation, and inspection. In most instances, the same task is repeated two or more times at different stages of the process in order to gather customs-related data or to validate documentation. However, the Customs Department is currently undergoing a major privatization effort. Customs has contracted with a private company to manage customs services, including customs clearing. The implementation of a state-of-the-art computer system should also make the import process less complicated.

Customs Valuation

Kuwait began implementation of the WTO Customs Valuation Agreement in September 2003.

Textiles

Textiles accounted for approximately seven percent of Kuwait's imports in 2003, and tariffs are five percent.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Kuwait maintains restrictive standards that impede the marketing of some exports. Kuwait strictly enforces government-mandated shelf life standards on 44 of 75 food products listed in Gulf Standard 150/1993, but recognizes the shelf-life established by manufacturers on all other food products. Shelf-life requirements for processed foods are far shorter than necessary to preserve freshness and result in processed U.S. goods being non-competitive with products shipped from countries geographically closer to Kuwait. Standards for medical, telecommunications, and computer equipment tend to lag behind technological developments, with the result that government tenders frequently specify the purchase of obsolete, often more costly items.

In late December 2004, Kuwait removed its December 2003 ban on imports of U.S. beef and beef products, originally imposed due to concerns of Bovine Spongiform Encephalopathy (BSE), but kept in place a ban on imports of beef originating in the state of Washington. Such a regional ban has caused concern in U.S. industry.

In December 2002, Kuwait notified WTO members of its proposal for an International Conformity Certification Program (ICCP). Kuwait's proposal was similar to a program maintained by Saudi Arabia. According to Kuwait, the program was necessary because it lacked laboratory facilities to properly conduct its own inspections of product conformity to specified standards. On March 17, 2003, Kuwait implemented the ICCP, which applies to five import groups: (1) household appliances and electronics; (2) new and used cars and vehicles; (3) chemicals, including motor oil and paint; (4) building materials, including cement, gypsum, and bricks; and (5) paper and plastic items. Covered products must be tested and certified by a single private company before being exported to Kuwait.

In July 2004, the regulatory authority responsible for the ICCP, the Public Authority for Industry (PAI), held a one-year review of the program. At that time, the PAI said that over 30,000 individual products had been issued ICCP certificates, and that it was considering expanding the types of products requiring certification. Importers and representatives of foreign businesses all voiced serious concerns with the program. The United States and other WTO members have raised concerns about the ICCP bilaterally and during WTO meetings of the WTO Technical Barriers to Trade Committee.

In November 2004 the PAI indicated that it would introduce changes to the ICCP and transition, over a period of 18 months, to a new Kuwait Conformity Assessment Scheme (KCAS.) The United States is evaluating the potential impact of Kuwait's proposed changes and their conformity with WTO requirements.

GOVERNMENT PROCUREMENT

Kuwait's government procurement policies specify the purchase of local products when available and prescribe a 10 percent price advantage for local firms in government tenders. In 2004, the Council of Ministers agreed to increase this price advantage to 15 percent; implementation of this increase, however, would require amending the GCC countries' unified agreement.

In January 2002, the Kuwaiti government transformed its offset program into the major mechanism for inducing foreign investment in Kuwait. The offset requirements imposed an offset obligation on civilian contracts with the Kuwaiti Government of 10 million Kuwaiti dinar (approximately $33 million) or more and on defense contracts of KD 1 million (approximately $3.3 million) or more. The obligation amounted to 35 percent of the contract value, which had to be invested in an approved offset business venture. A supplier had to sign a memorandum of agreement with the Offset Program Division at the Ministry of Finance before the contract was signed. The supplier also had to present a bank guarantee totaling 6 percent of the value of the offset obligation.

In September 2004, the Council of Ministers decided to suspend implementation of the offset program for all new government contracts in the military and civilian sectors pending further review by the Finance Ministry. A six-month review of the program was to take place, at the end of which the offset program would either be modified, reinstated or discontinued. No contracts awarded during the review period will carry an offset requirement.

Kuwait is not a signatory to the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

The Industrial Bank of Kuwait offers below market rate loans to local industry. Land is also provided at low cost.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Kuwait's copyright law must be amended to make it consistent with its obligations under the TRIPS Agreement. The government is currently in the process of drafting these amendments, but has not yet set a date by which these will be submitted to the National Assembly. Kuwait's revised patent and trademark legislation took effect on January 14, 2001. Enforcement of these laws remains inadequate to prevent widespread marketing of pirated products. Moreover, it appears that Kuwait does not provide for the protection of geographical indications.

Following Kuwait's elevation to the Special 301 Priority Watchlist in 2004, the Ministry of Commerce and the General Administration of Customs have increased their efforts to protect intellectual property rights. However, the Ministry of Information (which is statutorily responsible for ensuring intellectual property rights) does not place a high priority on IPR protection and the Ministry of Interior has declined to use its police resources for enforcement efforts. Consequently, sales of pirated goods remain high in Kuwait, and the use of unauthorized computer software continues in private enterprise. Uncertain and slow judicial action remains a hurdle, and penalties, when imposed, generally are inadequate to deter future crimes. In August 2004, the government submitted a draft law to the National Assembly that would increase penalties for those convicted of violating intellectual property rights.

SERVICES BARRIERS

Insurance

Pursuant to a November 2003 Council of Ministers resolution, foreign investors may establish insurance companies in Kuwait with the Ministry of Commerce and Industry's approval.

Banking

Under Kuwait's 2001 Foreign Direct Investment law, foreigners could own up to 49 percent of existing or newly formed Kuwaiti banks, subject to approval by the Central Bank. In January 2004, the National Assembly gave final approval to a bill permitting 100 percent foreign ownership of banks. In August 2004, BNP Paribas was the first foreign bank granted a license to operate in Kuwait; other foreign banks have also submitted applications.

Agent and Distributor Rules

According to Kuwait's Commercial Agencies Law of 1964, only Kuwaiti nationals and corporations may act as agents and distributors for foreign companies and exporters.

INVESTMENT BARRIERS

Kuwait currently maintains restrictions on direct foreign investment and applies discriminatory taxation policies. In May 2000, Kuwait's National Assembly approved legislation that allows foreign nationals to own up to 100 percent of all listed companies on Kuwait's stock exchange, except banks. Foreign-ownership in banks was limited to 49 percent with the additional restriction that any foreign-ownership above 5 percent must be approved by Kuwait's Central Bank. In 2004, this restriction was eliminated and foreign ownership may now be 100 percent.

In March 2001, the National Assembly passed a direct foreign investment bill that authorizes majority foreign-ownership in new investment projects (and 100 percent foreign-ownership in the following sectors: infrastructure projects such as water, power, waste water treatment or communications; investment and exchange companies; insurance companies; information technology and software development; hospitals and pharmaceuticals; air, land and sea freight; tourism, hotels, and entertainment; housing projects and urban development). The law also authorizes up to 10-year tax-holidays for new investors. The law went into effect on February 23, 2003. Despite this legislation, foreign companies still report numerous delays in getting approval to operate in Kuwait and the law does not appear to have significantly changed Kuwait's investment climate. Foreign firms still may not invest in the upstream petroleum sector, although they are permitted to invest in petrochemical joint ventures. Implementing legislation brought before Parliament in January 2004 would allow for limited, controlled investment in the petroleum sector. This law was submitted specifically to allow for investment in and development of Kuwait's northern oilfields, but may be used to allow for other investment in the petroleum sector in the future.

ELECTRONIC COMMERCE

Kuwait and the other GCC member states are currently negotiating a unified electronic commerce law.

OTHER BARRIERS

Corporate Tax Policies

Foreign firms are currently subject to a maximum income tax rate of 55 percent, although the government is currently drafting a new law that would reduce the tax rate. Kuwaiti-listed companies are not subject to income tax, but are required to make an annual zakat (charitable) contribution of 2.5 percent of their net profits to the Kuwait Foundation for the Advancement of Sciences (KFAS). They must also contribute 2.5 percent of their net profits toward a National Labor Force Fund.

MALAYSIA

TRADE SUMMARY

The U.S. trade deficit with Malaysia was $17.3 billion in 2004, an increase of $2.8 billion from $14.5 billion in 2003. U.S. goods exports in 2004 were $10.9 billion, down 0.2 percent from the previous year. Corresponding U.S. imports from Malaysia were $28.2 billion, up 10.8 percent. Malaysia is currently the 16th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Malaysia were $1.2 billion in 2003 (latest data available), and U.S. imports were $494 million. Sales of services in Malaysia by majority U.S.-owned affiliates were $1.4 billion in 2002 (latest data available), while sales of services in the United States by majority Malaysia-owned firms were $232 million.

The stock of U.S. foreign direct investment (FDI) in Malaysia in 2003 was $7.6 billion, up from $7.0 billion in 2002. U.S. FDI in Malaysia is concentrated largely in the manufacturing, mining, and wholesale sectors.

IMPORT POLICIES

Tariffs

Tariffs are the main instrument used to regulate the importation of goods in Malaysia. The simple average applied normal trade relations (NTR)/most-favored nation (MFN) tariff rate is approximately 8.56 percent, but duties for tariff lines where there is significant local production are often higher.

The level of tariff protection is generally lower on raw materials and increases for those goods that have value-added content. In addition to import duties, a sales tax of 10 percent is levied on most goods. Neither import duties nor this sales tax is applied to raw materials or machinery used in export production.

Seventeen percent of Malaysia's tariff lines (principally in the construction equipment, agricultural, mineral, and motor vehicle sectors) are also subject to non-automatic import licensing designed to protect import-sensitive or strategic industries.

Import Restrictions on Motor Vehicles

Malaysia has long protected its automobile manufacturing industry from foreign competition using high tariffs and non-tariff trade barriers. The government has slowly begun to dismantle some of its protections in order to meet its commitments to the WTO and the ASEAN Free Trade

Agreement (AFTA Agreement). For instance, in January 2004, the government completely eliminated local content requirements that were inconsistent with its obligations under the WTO TRIMS Agreement. Government policies, however, continue to block open trade in the automotive sector.

The Ministry of International Trade and Industry oversees a system of approved permits (APs) that allows the holder to import cars and distribute them locally. The AP system was designed to provide bumiputera (ethnic Malay) companies easy entry into the automobile distribution and service sector. The AP system acts as quota by restricting the total number of automobiles that can be imported in a given year relative to the size of the domestic market. In addition to restricting market access for imports, many of the permits are sold for profit, with the associated costs passed on to consumers further raising the costs of imported vehicles.

The government amended the automotive tax regime in 2004 and again in 2005 to meet its commitments under the AFTA Agreement. The import duty rate for vehicles with at least 40 percent ASEAN content fell to 20 percent in 2005, and will be lowered to 5 percent in 2008. However, the government imposed automobile excise taxes for the first time in 2004 and increased them in 2005 to make up for the revenue it lost by cutting import tariffs, so the tax burden for automakers remains high. The tax regime continues to protect domestic producers: Malaysia's automobile manufacturers Proton and Perodua, plus two locally incorporated joint ventures assembling imported kits, receive a 50 percent rebate on excise taxes . The excise tax rebate was extended to certain other local producers, but the exact criteria for the exemption remain unclear at this point. The government is expected to announce other incentives for domestic car makers by mid-2005.

The import duty/excise tax schedule is complex. In general, the current applied import tariffs and excise tax rates for completely built-up (CBU) and completely knocked-down (CKD) vehicles are as follows:

	ASEAN Tariff (%)	**Non-ASEAN Tariff**	**Excise (%)**
Automobiles (CBU)	20	50	90-250
Automobile (CKD)	0	10	90-250
Multipurpose Vehicles (CBU)	20	50	40-170
Multipurpose Vehicles (CKD)	0	10	40-150
4WD (CBU)	20	50	80-170
4WD (CKD)	0	10	80-150
Motorcycles (CBU)	20	40	20-60
Motorcycles (CKD)	0	0-10	20-60

Textiles

Import duties on textiles and apparel range between 0 percent and 30 percent. Malaysia does not require import licenses or impose burdensome labeling requirements on the import of textiles.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Nutritional labeling

Malaysia requires that certain processed, packaged food products sold in Malaysia be labeled with nutritional information. These items include cereals, breads, milk, canned meat, canned fish, canned fruits and canned vegetables, fruit juices, soft drinks and salad dressings. Nutrition Labeling Regulations issued in March 2003 outline what type of nutritional information is required and the format in which the information is to appear on the package. The regulations limit the kinds of nutritional claims, such as “reduced sodium,” “low cholesterol,” or “high fiber,” that can appear on food packaging. Enforcement of the regulation began on March 1, 2004.

Halal Certification

All meat, processed meat products, poultry, eggs, and egg products must receive *halal* (produced in accordance with Islamic practices) certification from Pusat Islam (the Islamic Center). U.S. producers have expressed concern that the *halal* certification process is confusing and non-transparent. Each individual product, rather than the plant, must receive *halal* certification. This certificate is issued on the joint recommendation of Malaysia’s Department of Veterinary Services in the Ministry of Agriculture and Pusat Islam following an on-site inspection. The government of Malaysia has the right to re-inspect approved plants after one year. In practice, up to three years may elapse before a Malaysian inspection team visits the United States, which limits the opportunities for new products to obtain certification.

Although the government of Malaysia applies no import duty on poultry parts, imports are regulated through licensing and sanitary controls. Import levels appear to be below the minimum access commitments established during the Uruguay Round.

GOVERNMENT PROCUREMENT

Malaysia is not party to the plurilateral WTO Government Procurement Agreement (GPA). Malaysia’s government policy calls for procurement to be used to support national public policy objectives, such as encouraging greater participation of *Bumiputera* (ethnic Malays) in the economy, transferring technology to local industries, reducing the outflow of foreign exchange, creating opportunities for local companies in the services sector, and enhancing Malaysia’s export capabilities. As a result, foreign companies do not have the same opportunity as some local companies to compete for contracts and, in most cases, foreign companies are required to take on a local partner before their bids will be considered. Some U.S. companies have voiced concerns about the non-transparent nature of Malaysia's government's procurement decision-making process.

U.S. firms have also expressed concern about anticompetitive bias in the Malaysian government's software procurement policy. The policy, announced on July 16, 2004, is not technology neutral, but instead gives preference to Open Source Software (OSS) for government procurement, "in situations where the advantages and disadvantages of Open Source Software (OSS) and proprietary software are equal." Malaysia's government has announced specific targets for the share of OSS in specific sectors.

EXPORT SUBSIDIES

Malaysia offers several export allowances. Under the export credit-refinancing scheme operated by the Central Bank, commercial banks and other lenders provide financing to exporters at a preferential rate for both post-shipment and pre-shipment credit. Malaysia also provides tax incentives to exporters, including double deduction of expenses for overseas advertising and travel, supply of free samples abroad, promotion of exports, maintaining sales offices overseas, and research on export markets.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Malaysia is a member of WIPO and is a party to the Berne Convention for the Protection of Literary and Artistic Works and the Paris Convention for the Protection of Industrial Property. Malaysia has not ratified the WIPO Copyright Treaty or the WIPO Performance and Phonograms Treaty, which extend traditional copyright principles to the digital environment.

In 2000, Malaysia's parliament amended the Copyright Act, the Patents Act, and the Trademarks Act, as well as legislation on layout designs of integrated circuits and geographical indications, in order to bring Malaysia into compliance with its TRIPS obligations. In 2004, Malaysia passed the "Protection of New Plant Varieties Act 2004" in line with the requirements of Article 27.3 (b) of the TRIPS Agreement. Enabling regulations for this law are expected in 2005. Malaysia does not prohibit other companies from relying on test and other undisclosed information submitted by another company to the government to obtain marketing approval of pharmaceuticals and agricultural chemicals, as called for under TRIPS Article 39.3.

Optical Media Piracy

Malaysia has a significant problem with piracy of copyrighted materials, particularly those embodied on optical media. Malaysia's production capacity for CDs and DVDs far exceeds local demand plus legitimate exports. U.S. industry estimates Malaysia's excess capacity is between ten to twenty times that needed for the legitimate market. The resulting surplus is exported globally - pirated products believed to have originated in Malaysia have been identified throughout the Asia-Pacific region, North America, South America, Europe, and Africa. U.S. industry reports that Malaysia is the largest exporter of pirated entertainment software in the world. Better enforcement of licensed and unlicensed production facilities is needed, as is a concerted effort to reduce the outflow of pirate goods from the country.

Malaysia has tightened its laws on the protection of intellectual property. The Optical Disc Act 2000 established a licensing and regulatory framework to control the manufacture of optical discs and to fight piracy. Under the Act, manufacturers are required to obtain licenses from both the Ministry of International Trade and Industry and the Ministry of Domestic Trade and Consumer Affairs, to place identification codes (SID codes) on each disk, and to allow regular inspections of their operations. This law should be modernized to ensure inspection authority covers all locations where optical media production may occur and also include as offenses such acts as 'gouging' or tampering with the SID codes and 'burning' of recordable discs. Enforcement and prosecution remain an ongoing challenge.

The government is making further efforts to reduce trade in pirated goods. A special task force, chaired by the Minister of Domestic Trade and Consumer Affairs and including representatives from all ministries and agencies with responsibility for IPR, has overseen the expansion of enforcement staff and a more vigorous program of raids on sellers of pirated products. A prolonged crackdown in the summer of 2003 had some success in curbing open market sales of pirated goods and drove much of the sales force underground.

The International Intellectual Property Association (IIPA) estimates 2004 industry losses in Malaysia due to piracy at $188 million. IIPA estimates 2004 piracy rates at 63 percent for business software, 52 percent for music, and 50 percent for movies. Malaysia has remained on the Special 301 Watch List since October 2001, in particular due to its failure to substantially reduce pirated optical disc production and export.

In 2004, Malaysia's government made further progress in prosecuting manufacturers and vendors of pirated goods. The government arrested the owners of four factories licensed under the Optical Disc Act suspected of producing pirated VCDs. Six illegal factories running eight production lines were shut down in 2004. The government also made some headway in tackling the judicial backlog for infringement cases. Through the first 10 months of 2004, 160 cases went to trial, with 51 cases recording guilty pleas. Malaysia's courts have imposed deterrent sentences imprisonment and/or fines for the offenders.

Government and industry cooperation has expanded in the past several years. For example, the Malaysian government and the Business Software Alliance (BSA) have coordinated several "crackdowns" targeting corporate use of unlicensed software. Police and legal authorities are generally responsive to requests from U.S. firms for investigation of copyright infringement cases. But much work remains in educating the general public about the value of intellectual property rights to the businesses that own them.

Malaysia continues to impose a hologram labeling requirement for optical discs containing copyrighted material.

Pharmaceuticals

Sales of counterfeit pharmaceuticals are a growing problem in Malaysia. Industry groups currently do not have a firm measure of problem, but expect to complete a market survey in the first half of 2005 that will provide an estimate. Counterfeit medicines that have been identified include "drugs" with the wrong ingredients, insufficient active ingredients, and those with fake packaging. The copied drugs are believed to originate in China. Unregistered generic copies of patented products, primarily imported from India, are also available in Malaysia. Both street vendors and health professionals sell the counterfeit products. The counterfeit medicines siphon off profits of legitimate manufacturers, and leave companies vulnerable to lawsuits from patients who may have adverse reactions to the counterfeit products.

In 2003, Malaysia's Ministry of Health announced to local industry groups its intention to require all medicines and health care products to be affixed with a hologram label as part of the government's effort to combat rising counterfeiting in these goods. The proposed labeling policy would apply to pharmaceuticals, over-the-counter medicines, and traditional medicines. U.S. pharmaceutical companies oppose the mandatory requirement scheme because of concerns about cost and efficacy of this “one-size-fits-all" approach. The Ministry of Health has deferred implementation of the policy until May 2005.

Trademarked Consumer Products

A number of U.S. consumer product companies have also suffered significant losses due to the manufacture and sale of counterfeit products. The volume is difficult to determine because of the broad scope of products involved. Counterfeiting in Malaysia goes beyond the counterfeiting of luxury branded products to include printer cartridges, plastic container systems, motor oil, household cleaning agents, shampoo and skin care items, herbicides, and penlight batteries. Counterfeiters have improved the quality of packaging and marketing so that consumers are misled into purchasing the products. The products have caused harm to individuals, and damage to automobiles and household goods. Some of the pirated goods are produced in Malaysia, while many are brought into the country from China, Thailand, and India.

Enforcement by the local government is hampered by the lack of training and scarcity of information about ongoing counterfeiting activities. Complicating enforcement of trademark-related violations is a Malaysian Court of Appeals interpretation of the trademark law that requires enforcement officials have a “Trade Description Order” to conduct criminal raids when the counterfeit product seized is not identical to the trademarked original. igh specificity requirements necessary to seize a shipment suspected of containing pirated or counterfeit products also represent an enforcement obstacle to U.S. industry.

SERVICES BARRIERS

Malaysia's services sector constitutes about 56 percent of the national economy and remains highly protected.

Basic Telecommunications

Under the WTO Basic Telecommunications Agreement, Malaysia made limited commitments on most basic telecommunications services and partially adopted the reference paper on regulatory commitments. Malaysia guarantees market access and national treatment for these services only through acquisition of up to 30 percent of the shares of existing licensed public telecommunications operators, and limits market access commitments to facilities-based providers. These restrictions constitute one of the most restrictive regimes for an economy of Malaysia's level of development. Value-added service suppliers are similarly limited to 30 percent foreign equity. Restrictions on these activities tend to benefit the dominant provider, government-controlled Telekom Malaysia, and hamper the development of a more efficient information infrastructure.

Direct Selling

Malaysia's requirements for the licensing and operation of direct selling companies include a provision that no more than 30 percent of a locally incorporated direct selling company may be foreign-owned. The Ministry also "recommends" local content targets. Local companies that seek multi-level direct selling licenses require paid-up capital of RM 2.5 million ($657,000), while companies with foreign shareholders must have paid-up capital of twice that amount, or RM 5 million ($1.3 million).

The Malaysian Government also included local content requirements in new "Guidelines on Foreign Participation in the Distributive Trade Services" issued in October 2004. Among other provisions, department stores, supermarkets and hypermarkets must provide 30 percent of shelf space in their premises for goods and products manufactured by bumiputera-owned small and medium industries. The guidelines also require that the stores "sell at least 30 percent" of these bumiputera products, a rule which does not take into account discretionary behavior on the part of consumers.

Legal Services

Foreign lawyers may not practice Malaysian law or operate as foreign legal consultants, nor may they affiliate with local firms or use their international firm's name. Foreign law firms may not operate in Malaysia except as minority partners with local law firms, and their stake in any partnership is limited to 30 percent. Under the Legal Profession Act of 1976, the practice of Malaysian law is normally restricted to Malaysian citizens or permanent residents who have apprenticed with a Malaysian lawyer, are competent in Bahasa Malaysia (the official language), and have a local law degree or are accredited British Barristers at Law. The Attorney General has authority to grant limited exceptions on a case-by-case basis, provided the applicant has seven years of legal experience. Malaysia limits foreign attorneys' scope of services to advice concerning home country and international law. Malaysian law does not allow for foreign legal consultancy except on a limited basis in the Labuan International Offshore Financial Center (see "Banking" below). Persons not licensed as lawyers are subject to criminal penalties if they directly or indirectly undertake activities relating to the Malaysian legal system, including drafting documents.

Architectural Services

A foreign architectural firm may operate in Malaysia only as a joint-venture participant in a specific project with the approval of the Board of Architects. Malaysian architectural firms may not have foreign architectural firms as registered partners. Foreign architects may not be licensed in Malaysia but are allowed to be managers, shareholders, or employees of Malaysian firms. Only licensed architects may submit architectural plans.

Engineering Services

Foreign engineers may be licensed by the Board of Engineers only for specific projects, and must be sponsored by the Malaysian company carrying out the project. The license is only valid for the duration of a specific project. In general, a foreign engineer must be registered as a professional engineer in his or her home country, have a minimum of 10 years experience, and have a physical presence in Malaysia of at least 180 days in one calendar year. To obtain temporary licensing for a foreign engineer, the Malaysian company often must demonstrate to the Board that they cannot find a Malaysian engineer for the job. Foreign engineers are not allowed to operate independently of Malaysian partners, or serve as directors or shareholders of a engineering consulting company. A foreign engineering firm may establish a non-temporary commercial presence if all directors and shareholders are Malaysian. Foreign engineering companies may collaborate with a Malaysian firm, but the Malaysian company is expected to design and is required to submit the plans for domestic approval.

Accounting and Taxation Services

Foreign accounting firms may provide accounting and taxation services in Malaysia only through affiliates. All accountants who wish to provide auditing and taxation services in Malaysia must register with the Malaysian Institute of Accountants (MIA) before they may apply for a license from the Ministry of Finance. Citizenship or permanent residency is required for registration with MIA. Malaysian citizens or permanent residents who received degrees from local universities or are members of at least one of the 11 recognized overseas professional bodies recognized by Commonwealth countries may apply for registration. Members of the American

Institute of Certified Public Accountants (AICPA) are not eligible to become members of the MIA.

Banking

The Malaysian government limits foreign participation in financial services in an effort to encourage the development of domestic financial services providers. The government's policies are guided by the Banking and Financial Institutions Act of 1989 (BAFA) and the ten-year Financial Sector Masterplan unveiled in 2001. The plan is focused on building competitive domestic banks, in large part through banking consolidation, and defers the introduction of new foreign competition until after 2007. Foreign banks currently operate in Malaysia under a grandfathering provision. No new licenses are being granted to either local or foreign banks; foreign banks must operate as locally controlled subsidiaries. In 2004, Bank Negara pressed existing foreign banks, including U.S. banks, to expand back office operations or establish significant computing operations in Malaysia.

In September 2003, Bank Negara announced plans to issue three Islamic banking licenses to foreign banks active in the Islamic banking sector. Bank Negara similarly implied in a December 2004 announcement that it would give licenses to three foreign commercial banks in 2005. On April 1, 2003, the government removed the restriction that foreign-controlled companies were required to obtain 50 percent of their local credit from Malaysian banks. However, sourcing of funds of more than RM 50 million ($13.2 million) from local banks requires approval from Bank Negara.

The Federal Territory of Labuan was established as an International Offshore Financial Center in October 1990. Foreign investors receive preferential tax treatment for offshore banking activities, trust and fund management, offshore insurance and offshore insurance-related businesses, and offshore investment holding business.

Insurance

The insurance industry remains dominated by foreign providers, including several U.S. firms. The Financial Sector Masterplan recommends phased liberalization of the insurance industry, including increasing caps on foreign equity, fully opening the reinsurance industry to foreign competition, and lifting existing restrictions on employment of expatriate specialists. Branches of foreign insurance companies were required to incorporate locally under Malaysian law by June 30, 1998, although Malaysia's government has granted individual extensions. Foreign shareholding exceeding 49 percent is permitted only with Malaysian government approval. As part of the 1997 WTO Financial Services Agreement, Malaysia agreed to allow existing foreign shareholders of locally incorporated insurance companies to increase their shareholding to 51 percent. New entry by foreign insurance companies is limited to equity participation in locally incorporated insurance companies and aggregate foreign shareholding in such companies may not exceed 30 percent. However, this limit has been subject to negotiation.

Securities

Malaysia currently allows 49 percent foreign ownership in stock-broking companies and a 30 percent foreign stake in unit trusts. The Securities Commission's ten-year Capital Market Masterplan, released in February 2001, proposed liberalizing foreign participation limits by 2003, at which time foreigners would be permitted to purchase a limited number of existing stock-broking licenses and to take a majority stake in unit trust management companies. As of mid-December 2004, foreign participation limits remained unchanged, in part because the consolidation of stock-broking firms globally has reduced companies' interest in having a presence in Malaysia. In September 2004, Malaysia announced that up to five foreign stock brokerage firms and five global fund management firms could obtain licenses to operate in Malaysia. Application approvals are set for early 2005. Fund management companies may be 100 percent foreign-owned if they provide services only to foreigners, but they are limited to 70 percent foreign ownership if they provide services to both foreign and local investors. In September 2003, the Securities Commission began allowing foreign firms operating in Malaysia to seek listing on the Kuala Lumpur Stock Exchange. Futures brokerage firms may now be 100 percent foreign-owned.

Advertising

Commercials are restricted to a maximum of 20 percent foreign film content. The government recently relaxed enforcement of regulations governing the appearance of foreign actors in commercials shown in Malaysia. The government of Malaysia has an informal and vague guideline that commercials cannot "promote a foreign lifestyle."

Audio-Visual and Broadcasting

Malaysia's government maintains broadcast content quotas on both radio and television programming. Eighty percent of television programming is required to originate from local production companies owned by ethnic Malays (an increase from the previous limit of 60 percent). However, in practice, local stations have been granted substantial latitude in programming due to a lack of local programming. Sixty percent of radio programming must be of local origin. Foreign investments in terrestrial broadcast networks are prohibited. As a condition for obtaining a license to operate, video rental establishments are required to have 30 percent local content in their inventories. Malaysia regularly censors movies and television shows deemed offensive on religious or sexual grounds.

INVESTMENT BARRIERS

Malaysia encourages foreign direct investment, particularly in export-oriented manufacturing and high-technology industries, but retains considerable discretionary authority over individual investments. Especially in the case of investments focused toward the domestic market, it has used this authority to restrict foreign equity (normally to 30 percent) and to require foreign firms to enter into joint ventures with local partners. To alleviate the effects of the regional economic crisis, in 1998 Malaysia temporarily relaxed foreign-ownership and export requirements in the manufacturing sector for those companies that do not directly compete with local producers. In June 2003, the government extended indefinitely the policy, permitting 100 percent foreign ownership in new investment and the expansion of existing investments in manufacturing concerns, and in September 2004 the government announced that venture capital firms could be 100 percent foreign-owned. Malaysia continues to suffer shortages of skilled and technical employees, particularly in the electronics sector. Most foreign firms face restrictions in the number of expatriate workers they are allowed to employ. In June 2003, the government released new guidelines liberalizing the policy on employment of expatriates in the manufacturing sector. Manufacturing companies with foreign paid-up capital of at least $2 million receive automatic approval for up to 10 expatriate posts.

ELECTRONIC COMMERCE

Malaysia currently applies no special restrictions on products or services traded via electronic commerce. Products that are ordered via the Internet and physically delivered are subject to applicable import duties. Engineering services may not be provided via the Internet unless the engineer is properly licensed.

OTHER BARRIERS

Transparency

U.S. companies have indicated that they would welcome improvements in the transparency of government decision-making and procedures, and limits on anticompetitive practices. A considerable proportion of government projects and procurement is awarded without transparent, competitive bidding. After taking office in October 2003, Prime Minister Abdullah Badawi announced that the government would introduce open tenders for government procurements and major projects, with direct negotiations limited to special cases. Malaysia's government has declared that it is committed to fighting corruption. To promote that objective, Malaysia maintains an Anti-Corruption Agency (ACA) that is part of the Office of the Prime Minister. The ACA has the independent power to conduct investigations and is able to prosecute cases with the approval of the Attorney General.

MEXICO

TRADE SUMMARY

The U.S. trade deficit with Mexico was $45.1 billion in 2004, an increase of $4.4 billion from $40.6 billion in 2003. U.S. goods exports in 2004 were $110.8 billion, up 13.7 percent from the previous year. Corresponding U.S. imports from Mexico were $155.8 billion, up 12.9 percent. Mexico is currently the 2nd largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Mexico were $15.9 billion in 2003 (latest data available), and U.S. imports were $11.7 billion. Sales of services in Mexico by majority U.S.-owned affiliates were $8.1 billion in 2002 (latest data available), while sales of services in the United States by majority Mexico-owned firms were $900 million.

Mexico has signed a total of 11 free trade agreements with 43 countries, including the European Union, Chile, the five economies of the Central American Common Market, Israel, and Uruguay. Mexico also signed an Economic Partnership Agreement with Japan in November 2004.

The stock of U.S. foreign direct investment (FDI) in Mexico in 2003 was $61.5 billion, up from $55.7 billion in 2002. U.S. FDI in Mexico is concentrated largely in the manufacturing and banking sectors.

North American Free Trade Agreement

The North American Free Trade Agreement (NAFTA), signed by the United States, Canada, and Mexico, entered into force on January 1, 1994. The NAFTA progressively eliminates tariffs and non-tariff barriers to trade in goods; improves access for services trade; establishes rules regarding investment in the territory of a Party by an investor of another Party; strengthens protection of intellectual property rights; and creates an effective dispute settlement mechanism. The NAFTA is accompanied by supplemental agreements that provide for cooperation to enhance and enforce labor standards and to encourage environmentally friendly practices and bolster environmental protection in North America.

IMPORT POLICIES

Tariffs and Market Access

Under the terms of the NAFTA, Mexico eliminated tariffs on all remaining industrial and most agricultural products imported from the United States on January 1, 2003. Remaining tariffs and non-tariff restrictions on corn, sugar, milk powder, orange juice, and dried beans will be phased out by January 1, 2008. The safeguard action for U.S. chicken leg quarters expires at the end of

2007 (see section on agriculture, below).

Trade growth in agricultural products has in fact been fairly balanced since the NAFTA was implemented, with U.S. exports to Mexico increasing by 135 percent from 1993 to 2004, and U.S. imports from Mexico increasing by 167 percent. The numbers are less balanced, however, when considering nonagricultural trade. U.S. imports from Mexico grew 299 percent, compared with U.S. export growth of 169 percent from 1993 to 2004.

A number of U.S. exports, both agricultural and non-agricultural, are subject to antidumping duties that limit access to the Mexican market. Products subject to these duties currently include beef, rice, liquid caustic soda, ammonium sulfate, and polyvinyl chloride, bond paper, and corrugated rods. Mexico also initiated antidumping investigations of crystal polystyrene, epoxidized soy oil, and pork legs (hams), industrial fatty acids, stearic acid, and welded carbon steel pipe and tube in 2004.

On January 1, 2002, Mexico published amendments to its Income Tax Law that treat small retailers selling mostly imported goods differently than other small companies by taking away from them the option of using an alternative tax reporting and payment system. The alternative system, available to other "small contributors", is administratively simpler and potentially results in a lower tax burden, depending on the specific financial circumstances of the company.

Agricultural Products

The United States exported $8.5 billion in agricultural products to Mexico in 2004, a new record. Mexico is the United States' third largest agricultural market. Under NAFTA, Mexico has eliminated nearly all import tariffs and tariff-rate quotas on agricultural products from the United States. As of January 1, 2004, the only U.S. agricultural exports subject to tariffs or tariff-rate quotas are corn, sugar, dry beans, orange juice, chicken leg quarters, and milk powder.

During the past year, Mexico's Secretariat of Economy (SECON) continued antidumping duties on beef, rice, and apples and modified existing duties on beef, while eliminating antidumping duties on live hogs. SECON terminated its antidumping investigation of U.S. pork, finding no cause for continuing the investigation, yet subsequently self-initiated an antidumping investigation of U.S. hams. Concerns about Mexico's methodology for determining injury to the Mexican domestic industry and for calculating dumping margins in the rice case led the United States to challenge the antidumping measure at the WTO. The panel report in that case is expected in early 2005. With respect to the antidumping investigation on beef, a NAFTA Chapter 19 panel ruled that SECON did not sufficiently demonstrate that U.S. beef imports had damaged Mexico's beef industry. In response, SECON eliminated the seven cent per kilo antidumping duty on U.S. beef carcasses and lifted the requirement that all beef must be aged less than 30 days and graded Choice or Select to qualify for the lower company specific rates. The NAFTA panel must now approve the changes or recommend additional changes. Mexican policies in this area have reduced the number of U.S. suppliers and altered product trading patterns. Industry believes that $100 million to $500 million in revenue is lost each year due to antidumping duties in the beef sector.

On December 29, 2004, the Ministry of Economy announced it would suspend the 46.58 percent antidumping duty on red and golden delicious apples from the United States and implement a new reference price agreement with U.S. exporters in the Northwest, effective February 28, 2005. However, implementation did not occur and the duties remain in place. The United States takes very seriously the commitment the Mexican Government made after two years of intense consultations and expects the unjustified duties to be removed or replace with the reference price agreement very soon.

In July 2003, Mexico imposed a NAFTA safeguard on U.S. chicken leg quarters that will remain in effect until December 31, 2007. The safeguard takes the form of a tariff-rate quota (TRQ) on chicken leg quarters. The TRQ preserves market access for U.S. exporters at levels achieved in recent years. Pursuant to the NAFTA, Mexico agreed to provide compensation to the United States, including a commitment not to impose any additional import restrictions on U.S. poultry products and to eliminate certain sanitary restrictions on U.S. poultry products.

On December 31, 2001, the Mexican Congress approved a 20 percent tax on certain beverages sweetened with ingredients other than cane sugar, including high-fructose corn syrup (HFCS). Industry estimates that the cost of this trade barrier to the United States is roughly $200 million in U.S. corn and HFCS exports and $800 million in U.S. investment in Mexico since NAFTA's implementation in 1994. HFCS sales fell dramatically below prior volumes, as bottling companies in Mexico switched to cane sugar. Although temporarily suspended by the Fox Administration, the Mexican Supreme Court ruled this action unconstitutional and reinstated the tax on July 12, 2002. The tax has been renewed each year by the Mexican Congress, including for 2005. On March 16, 2004, the United States requested consultations under the dispute settlement procedures of the WTO, and on July 6, 2004 a WTO panel was established to review the dispute. The panel's final decision is expected by the end of May 2005.

For 2004 and 2005, the Mexican Congress approved a measure stating that SECON could not lower the NAFTA out-of-quota tariff rate in order to facilitate the importation of white corn beyond the volumes provided for within the tariff-rate quota.

Sanitary and Phytosanitary Issues

In recent years, Mexican sanitary and phytosanitary standards have created barriers to exports of certain U.S. agricultural goods, including grains, seed products, apples, stone fruit, pork, beef, poultry, citrus, wood and wood products, dry beans, avocados, and eggs. In addition, procedural requirements regarding sanitary and phytosanitary inspections at the port-of-entry do not always reflect agreements reached between U.S. Department of Agriculture officials and the Mexican Secretariat of Agriculture, resulting in unnecessary delays at the border points of entry, seaports, and airports. In 2004, significant quantities of imports were rejected or delayed at the border.

Disagreements over the prevalence and nature of certain pests and certain administrative requirements led to a delay in the implementation of the stone fruit protocol in 2003 and 2004, which provides for a systems approach to prevent transmission of quarantinable pests. Because of this delay in implementing the systems approach protocol, the U.S. industry has had to revert to more costly fumigation procedures. While the protocol for 2005 has been concluded well in advance of the shipping season, U.S. industry maintains that Mexico is using unscientific phytosanitary concerns that are making it increasingly difficult to arrive at a system that is cost effective for U.S. stone fruit exporters. While originally scheduled for termination in 2001, tThe last Mexican inspector was finally withdrawn from the State of Washington apple inspection program in 2004. Mexican plant quarantine authorities have notified APHIS of their intent to add new pests to their lists of quarantine concerns, even though no quarantine pests have been detected in over 52 million boxes of apples the United States has shipped to Mexico since 1993. USTR and USDA have raised these issues several times over the last year.

Despite the lack of a protocol for returning live animals and adequate inspection facilities in Mexico, in June 2004, the Mexican Congress approved a measure requiring that the inspection of imported live animals take place in Mexico. The lack of adequate inspection facilities has hampered the importation of live animals. Similarly, the Mexican Congress approved a measure for 2005 that would charge an inspection fee of approximately $26 per ton for the inspection of all imported animal products. SECON is reviewing the legality of this provision. Industry estimates that these fees would add $40 million annually to the cost of U.S. meat and animal product sold in Mexico. The Fox Administration subsequently determined the tax was illegal and is not collectingd such fees.

Mexico banned imports of U.S. beef in December 2003 following the detection of one positive case of Bovine Spongiform Encephalopathy (BSE) in the State of Washington. In March 2004, Mexico announced that it would accept U.S. boneless beef from cattle under 30 months of age, and it subsequently lifted restrictions on a number of offals and processed boneless beef products. Currently, bans or restrictions remain on bone-in beef, live cattle, certain offals and processed products, and pet food. As of the publication of this report, the United States is taking aggressive action and working intensively to fully re-open the market as quickly as possible. In addition, the United States is working in the International Organization for Epizootics to revise international standards on BSE to reflect current scientific knowledge.

Despite the eradication of Low Pathogenic Avian Influenza in nine U.S. states, Mexico continues to restrict imports of certain poultry products from these states, chiefly raw poultry for direct consumption.

Administrative Procedures and Customs Practices

U.S. exporters continue to be concerned about Mexican customs administration procedures, including insufficient prior notification of procedural changes; inconsistent interpretation of regulatory requirements at different border posts; and uneven enforcement of Mexican standards and labeling rules. There have been relatively few specific complaints, however, and Mexican Customs has been putting procedures in place to address issues of non-uniformity at border ports of entry. Agricultural exporters note that Mexican inspection and clearance procedures for some agricultural goods are long, burdensome, non-transparent and unreliable. Customs procedures for express packages continue to be burdensome, though Mexico has raised the *de minimis* level from $1 to $50. However, Mexican regulations still hold the courier 100 percent liable for the contents of shipments.

To be eligible to import well over 400 different items, including agricultural products, textiles, chemicals, electronics and auto parts, Mexican importers must apply to the Secretariat of Finance and Public Credit (SHCP) and be listed on a special industry sector registry. U.S. exporters complain that the registry requirement sometimes causes costly customs clearance delays when new products are added to the list of subject items with immediate effect, thereby denying importers sufficient notice to apply. They also report that certain importers have been summarily dropped from the registry without prior notice or subsequent explanation, effectively preventing U.S. exporters from shipping goods to Mexico.

Mexico requires import licenses for a number of commercially sensitive products. It also uses estimated prices for customs valuation of a wide range of products imported from the United States and other countries, including apples, milled rice, beer, distilled spirits, chemicals, wood, paper and paperboard products, textiles, apparel, toys, tools, and appliances.

Since October 2000, the Mexican government has imposed a burdensome guarantee system for goods subject to estimated prices. Importers cannot post bonds to guarantee the difference in duties and taxes if the declared value of an entering good is less than the official estimated price. Instead they must deposit the difference in cash at a designated Mexican financial institution or arrange one of two alternative sureties (a trust or line of credit). The cash deposit is not returned for six months, and then only if the Mexican government has not initiated an investigation and if the supplier in the country of exportation has provided an invoice certified by its local chamber of commerce. Mexican banks charge as much as $1,500 to open an account for this purpose and $250 for each transaction, making this a burdensome and costly regulation for businesses on both sides of the border. The governments of the United States and Mexico are discussing an exchange of customs data that would result in the elimination of the estimated pricing regime.

In addition, U.S. exporters have expressed concerns regarding post-importation verification practices implemented by Mexican Customs and administered by private entities. Mexico has indicated that all information will remain confidential and that verifications are intended to validate the accuracy of all information presented to Mexican Customs. However, U.S. firms remain apprehensive about sharing business confidential information with a third-party. The U.S. Government continues to monitor the situation.

U.S. firms also have raised concerns with a Mexican regulation that requires certain textile products to include detailed information regarding their specifications on customs documentation. In particular, the regulation asks for proprietary information and results in increased paperwork for the importer. Moreover, it also appears that the requirements for the regulation can change suddenly and are not applied uniformly throughout Mexican ports of entry.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Under NAFTA, Mexico was required, starting January 1, 1998, to recognize conformity assessment bodies in the United States and Canada on terms no less favorable than those applied in Mexico. To date, no U.S. certification bodies have been recognized by Mexico. The United States is still awaiting action on a 2003 request by a U.S. certification body to be recognized in Mexico. On January 21, 2005, Mexico published the *convocatoria* (formal announcement) in the *Diario Oficial* stating that one or more government agencies are requesting certification organizations for the standards involved. While the publication of the convocatoria is positive, no U.S. certification bodies have yet been recognized by Mexico.

U.S. exporters have alleged that certain regulations are enforced more strictly for imports than for domestically-produced products, and that there has been inconsistent treatment for the same goods at various ports of entry. Mexico has over 700 mandatory technical regulations called *normas oficiales mexicanas* (NOMs) issued by a number of different agencies, each with its own compliance procedures. Only the Secretariat of Economy and the Secretariat of Agriculture (for a limited sub-set of its NOMs) have published their procedures. After discussions with the U.S. government, the Secretariat of Economy implemented procedures in 2000 designed to reduce the cost of exports to Mexico by allowing U.S. manufacturers and exporters to hold title to a NOM certificate of compliance (an official document certifying that a particular good complies with applicable standards) and assign it to as many distributors in Mexico as needed to cover the market. Previously, only Mexican producers or importers were allowed to obtain a NOM certificate, which posed a problem for U.S. firms using multiple importers, because each importer was required to pay a substantial fee to have the exact same product tested at a Mexican laboratory every year. Moreover, while the new procedures were implemented with the alleged goal of addressing redundant testing requirements, U.S. firms contend that the certification bodies have increased the cost of certification by, among other things, charging for certificates to be assigned to other regulatory entities. In addition, key Mexican ministries such as Health, Energy and Labor have yet to publish their respective product testing procedures.

The United States is Mexico’s largest export market for tequila, accounting for 50 percent of Mexican production. In 2003, the United States imported over $402 million of tequila. Approximately 77 percent of the total volume was tequila in bulk form. In August 2003, the Mexican government, citing the need to ensure the quality of Mexican tequila, had considered amending the official standard for tequila to require that tequila be “bottled at the source” in Mexico. Currently, the Mexican standard requires that only 100 percent agave tequila be bottled at the source. Tequila that is made from less than 100 agave tequila can be sold and exported in bulk form under the current official standard. On November 15, 2004, Mexico published a new draft standard that did not include a requirement that all tequila be bottled in Mexico, but which did propose an onerous registration and inspection system for all bottlers. Government officials from the NAFTA partners have been engaged in discussions regarding aspects of trade in tequila and hope to reach an agreement in the near future.

U.S. exporters of vitamins, nutritional supplements, and herbal remedies have reported that Mexico's revised health law regulations are discriminatory and arbitrarily impede access to the Mexican market. While Mexico has stated that it is looking at ways to address these concerns consistent with its WTO and NAFTA obligations, the U.S. Government has thus far seen no progress. According to industry's estimates, the cost of this alleged trade barrier to the United States is over $500 million annually.

GOVERNMENT PROCUREMENT

Mexico's efforts to make its government procurement regime more transparent through policies and technologies have resulted in increased competition as well as savings for the government. The Mexican government has established several "e-government" Internet sites to increase transparency of government processes and establish guidelines for the conduct of government officials. "Compranet" allows on-line processing of government procurement and contracting. According to the Mexican Secretariat of Public Administration, 321 government offices processed 3,800 electronic transactions for procurement through Compranet in 2002.

The NAFTA Government Procurement Chapter allowed Mexico to cover only a temporary, narrow list of services, based on the requirement that it would develop a permanent list of excluded services by July 1, 1995. After several years of discussion, the United States, Canada and Mexico reached agreement on a list of excluded services in December 2004. Mexico must now take the necessary steps to implement its negative list of services.

NAFTA provides for the gradual increase of U.S. suppliers' access to purchases by the two largest Mexican procuring authorities, Mexico's parastatal petroleum and electricity monopolies, PEMEX and the Federal Electricity Commission (CFE), respectively. As of January 1, 2003, NAFTA limits the total value of contracts that PEMEX and CFE may remove from coverage under NAFTA to $352 million per year.The United States has not been able to confirm whether this commitment has been properly implemented, as Mexico has not provided the statistics called for under NAFTA. Starting in December 2005, Starting in December 2005, Mexico will send to the United States and Canada notice of the set-aside calculation, along with the methodology used in the calculation.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Under NAFTA and the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), Mexico is obligated to implement certain standards for the protection of intellectual property and procedures to address infringement, including copyright piracy and trademark counterfeiting. Despite a fairly comprehensive set of IPR laws and an increase in the number of seizures and arrests in 2003, the extent of IPR violations in Mexico remains dramatic. Monetary sanctions and other penalties, when imposed, are minimal and therefore generally ineffective in deterring these illegal activities. Increasing organized crime and violence impair enforcement actions and deter rightholders from attempting to enforce their rights under Mexican law. The United States remains concerned about the continuing high levels of piracy and counterfeiting in Mexico and closely monitors how the Mexican Government is addressing these problems. Mexico was taken off the Special 301 Watch List in 2000, but put back on in 2003 and remained on the Watch List in 2004 due to enforcement deficiencies.

Copyright Protection

Copyright piracy remains a major problem in Mexico, with U.S. industry loss estimates growing each year. Although enforcement efforts by the Mexican Government seem to be improving, piracy levels continue to rise, resulting in closures of legitimate copyright-related businesses, according to industry sources. Pirated and counterfeit sound and motion picture recordings are widely available throughout Mexico, where piracy has shifted from traditional formats to optical discs (CD, DVD, CD-ROM). The International Intellectual Property Alliance (IIPA) estimates that trade losses due to copyright piracy in Mexico totaled $870.2 million in 2004. That year, music piracy represented 60 percent of the total market. Industry estimates that the business software piracy level was 65 percent in 2004.

In July 2003, the Mexican Congress amended the Mexican copyright law. These amendments fail to address the comprehensive reforms needed by Mexico to: (1) effectively implement the obligations of the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty (Mexico is a party to both agreements); and (2) correct existing incompatibilities in the law with Mexico's obligations under the NAFTA IPR Chapter and the WTO TRIPS Agreement. Implementing regulations that Mexico has indicated would address these concerns were to have been published by the end of October 2003 but as of March 2005 have not yet been made available. The United States has been urging Mexico to meet its various obligations by issuing satisfactory implementing regulations.

Mexican law enforcement agencies have conducted thousands of piracy raids. In 2003, the Attorney General's Office created an IPR enforcement unit, which combines federal prosecutors and police to make the enforcement regime more effective and efficient. Industry representatives report that raids against pirate and counterfeit operations have improved from 2003 and that there has been improved access to prosecutors. Despite increased raids and seizures of pirated and counterfeit material, only 24 of the 1087 pirates and counterfeiters who were arrested in 2003 and 2004 received sentences greater than one year, thus undercutting the deterrent effect of the raids and arrests. Very few IPR violations result in prison terms. As a result, pirates and counterfeiters are often released and return to their illegal activities. Well-known markets selling pirated and counterfeit goods, such as Tepito in Mexico City, remain ubiquitous.

Patent, Trademark, Pharmaceutical and Agricultural Chemical Protection

Patents and trademarks are under the jurisdiction of the Mexican Institute of Industrial Property (IMPI), an independent agency that operates under the auspices of the Secretariat of Economy. Some U.S. trademark holders have encountered difficulties in enjoining former subsidiaries and franchisees from continued but unauthorized use of their trademarks.

U.S. companies holding trademarks in Mexico have cited problems with trademark enforcement and administration. When counterfeit items are discovered, injunctions against trademark violators are often unenforceable and are consistently challenged before the courts. Although federal administrative actions are supposed to be completed within four months, actions related to trademark enforcement often take as long as 18 months. The time can be lengthened by jurisdictional and procedural disputes within the Mexican government, as well as by internal coordination problems within IMPI. Trademark applications in Mexico are not subject to opposition. Registrations are issued and can only be canceled after registration. On average, it takes two and a half years to cancel a trademark registration, and the registrant is allowed to continue using the mark for one year following cancellation.

U.S. pharmaceutical and agricultural/chemical companies are concerned about the lack of coordination between IMPI and other Mexican agencies with regard to government procurement of copies of patented pharmaceuticals. In 2003, the Mexican Ministry of Health agreed that starting with purchases scheduled for delivery on January 1, 2003, IMSS (Mexican Social Security Institute) and possibly ISSTE (Social Security Institute for Government Workers) would purchase only patented products where a patent already exists in Mexico.

In September 2003, the Ministries of Health and Economy implemented a Presidential decree that requires applicants for safety and health registrations to show proof of patent and proof that test data was obtained in a legitimate matter. According to the regulation, failure to present proof of patent and test data will result in denial of the registration. Also, if a company is caught providing false information, it can now be subject to both civil and criminal proceedings. It is hoped that compliance with this decree will help to eliminate copies of patented pharmaceuticals from the supply chain for IMSS and ISSTE.

While this measure is a positive development, the regulation limits linkage to product patents only. Furthermore, U.S. industry reports that the Ministry of Health continues to provide local companies authorization to market unauthorized copies of patented pharmaceutical products.

Border Enforcement of IPR

NAFTA Article 1718 and Article 51 of the TRIPS Agreement obligate Mexico to allow U.S. intellectual property rights holders to apply to Mexican authorities for suspension of release of goods with counterfeit trademarks or pirated copyright goods. Intellectual property rights owners seeking to use the procedure must obtain an order from IMPI that directs customs officials to detain the merchandise. Companies requesting such actions generally report positive outcomes. However, U.S. industry has sought increased cooperation and communication between IMPI and Mexican Customs in order to prevent the release of counterfeit goods into the Mexican market.

SERVICES BARRIERS

Telecommunications

The recent conclusion of a WTO dispute settlement proceeding brought by the United States has prompted much-needed reform to Mexico's international telecommunications rules. This is expected to bring benefits worth tens of millions of dollars to U.S. consumers and telecommunications companies, including families keeping touch across the border. Pursuant to an agreement reached with the United States regarding implementation of the recommendations included in the WTO panel report adopted on June 1, 2004, Mexico agreed to remove the provisions of Mexican Law which had created the uniform tariff and proportional return systems and the requirement that the carrier with the greatest proportion of outgoing traffic to a country negotiate the settlement rate on behalf of all Mexican carriers. Mexico also committed to allow the introduction of resale-based international telecommunications services in Mexico by July 2005. Mexico, however, continues to prevent foreign carriers from using leased lines to bring calls directly into the domestic network.

More broadly, Mexico's former state-owned telecommunications monopoly (Telmex) continues to dominate Mexico's telecom sector. Competition in the sector has been hampered by the inability of Mexico's telecommunications regulator, the Federal Telecommunications Commission (COFETEL) to enforce its own regulatory findings. Enforcement authority resides with the Secretariat of Communications and Transportation (SCT), which has been slow to act against Telmex. Telmex competitors complain of inaction by both COFETEL and SCT in resolving disputes, resulting in many cases lingering for months or years without resolution. Failure to ensure non-discriminatory quality of service for interconnection, highlighted by a COFETEL report documenting the inferior quality Telmex provided to competitors, is particularly troubling. In most cases where the government has taken action, Telmex has successfully used court-ordered injunctions to prevent enforcement against it. In addition, lawmakers have shelved a telecommunications reform bill proposed by President Vicente Fox to increase COFETEL''s independence and regulatory powers.

COFETEL recently proposed a rule that would switch mobile phone payment systems to a "calling party pays" system, thereby requiring those placing international and domestic long-distance calls to mobile phones in Mexico to pay for the interconnection and termination of those calls. Although the proposed rule encourages long-distance and local companies to negotiate prices, industry sources expect that COFETEL will ultimately establish the new rates. The proposed rule could result in significant additional costs for U.S. companies and consumers.

Uncertainty regarding the treatment of Voice over Internet Protocol (VOIP) services in Mexico is also cause for concern. Telmex has reportedly advocated prohibiting cable TV providers from providing VOIP until Telmex is permitted to participate in the video market. Irrespective of the merits of Telmex's ambitions in the video market, restrictions on the ability of any entity, foreign or domestic, to supply VOIP appears inappropriate and would only serve to limit competition in voice services.

In the satellite sector, preferences accorded to Mexican satellite service suppliers remain a significant barrier and thwart access by Mexican consumers and businesses to cost-effective technology U.S. providers could supply. In particular, the United States has urged Mexico to eliminate the unreasonable requirement that a concession be required to supply cross-border satellite services, particularly since only Mexican entities are eligible for such concessions.

INVESTMENT BARRIERS

Ownership Reservations

Mexico's Constitution and Foreign Investment Law of 1992 reserve ownership of certain sectors, such as oil and gas extraction, to the state; other laws limit activities (e.g., forestry exploitation) to Mexican nationals. In addition, only Mexican nationals may own gasoline stations. Investment restrictions prohibit foreign ownership of residential real property within 50 kilometers of the nation's coasts and 100 kilometers of its borders. However, foreigners may acquire the effective use of residential property in the restricted zones through trusts administered by Mexican banks. A national foreign investment commission reviews foreign investment in Mexico's restricted sectors, as well as investments of above 49 percent in non-restricted sectors with a threshold value of above $150 million, as adjusted each year for growth in Mexico's nominal GDP. These restrictions are incorporated into the NAFTA.

MOROCCO

TRADE SUMMARY

The U.S trade surplus with Morocco was $8 million in 2004, a decrease of $75 million from $83 million in 2003. U.S. goods exports in 2004 were $524 million, up 11.9 percent from the previous year. Corresponding U.S. imports from Morocco were $515 million, up 33.7 percent. Morocco is currently the 71st largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Morocco in 2003 was $309 million, up from $280 million in 2002.

IMPORT POLICIES

The United States – Morocco Free Trade Agreement (FTA) will improve U.S. exporters' goods and services competitiveness in this market. The FTA was ratified by the United States Congress in August 2004 and by the Moroccan Parliament in January 2005. The Agreement is expected to enter into force in the latter half of 2005. In addition to the high-standard obligations that Morocco is adopting in the FTA, the United States will be providing targeted technical assistance to help the Moroccan side implement the agreement.

Morocco also has an Association Agreement with the European Union (EU) that provides preferential tariff treatment for most EU industrial and some agriculture exports to Morocco, and which puts American producers at a comparative disadvantage. Morocco has also concluded an FTA with Turkey, and has a regional FTA with Jordan, Egypt and Tunisia.

Tariffs

Currently, U.S. goods entering Morocco face an average tariff of over 20 percent. Under the FTA, more than 95 percent of bilateral trade in consumer and industrial products will become duty-free immediately upon entry into force of the FTA, with all remaining tariffs to be eliminated within nine years – the best market access package of any U.S. free trade agreement with a developing country. Key U.S. export sectors such as information technologies, machinery, construction equipment and chemicals will gain immediately duty-free access to Morocco,

U.S. textile products will also gain enhanced access to the Moroccan market. For certain sensitive products, imports to Morocco will be subject to TRQs that will grow in the future.

Agriculture

The Moroccan agriculture sector is dominated by traditional small-scale farmers, particularly grain farmers. The Moroccan trade regime is designed to maintain this status quo, particularly through the imposition of high, prohibitive tariffs. These tariffs have created significant barriers to trade for U.S. exporters. For example, tariffs on poultry and beef products range up to 124 and 275 percent, respectively, on an applied basis.

Tariffs on virtually all U.S. farm exports to Morocco will be phased out within 15 years, while the FTA also takes into the unique circumstances facing Morocco's agriculture sector. U.S. farmers and ranchers of poultry and beef (products that have been kept out of the market due to high tariffs) will benefit from new tariff rate quotas that grow over time. U.S. wheat producers will benefit from new tariff rate quotas on durum and common wheat that have the potential to lead to significant increases in exports over recent levels.

Tariffs on goods such as corn and corn products, sorghum, soybeans and soybean meal will be eliminated immediately or in a short amount of time.

Customs

The FTA requires improvement in the transparency, efficiency and administration of the Moroccan customs regime, effectively improving access to the Moroccan market for U.S. exports. The FTA requires rapid customs clearance of express delivery shipments. The FTA's rules of origin are designed both to ensure that only U.S. and Moroccan goods benefit from the increased access under the FTA, and to be easy to administer. These rules are consistent with those in other U.S. free trade agreements in the region.

STANDARDS, TESTING, LICENSING, LABELING

Morocco generally has not provided adequate notice of new proposals or changes to existing standards, technical regulations and conformity assessment procedures, thereby denying interested U.S. parties the opportunity to comment on them before they are finalized. The FTA recently concluded with Morocco requires Morocco to make its system more transparent and open. In particular, the Agreement provides for more open participation in the development of standards, technical regulations and conformity assessment procedures; creates opportunities for interested U.S. persons to provide comments on draft measures; and requires Morocco to explain how comments have been taken into account in the final drafting of its measures.

EXPORT SUBSIDIES

Morocco has provided export subsidies to reduce transportation costs for tomatoes. The FTA requires the Moroccans to end this practice and otherwise not to provide export subsidies.

SERVICES BARRIERS

Morocco effectively prevents U.S. service firms from competing in large segments of Morocco's service economy. The government has either stipulated outright bans on foreign participation in the domestic market and/or included onerous ownership requirements or business operating practices.

The FTA accords U.S. firms substantial market access across Morocco's entire service regime, subject to very few exceptions. Key service sectors covered by the agreement include audiovisual, express delivery, telecommunications, computer and related services, distribution, and construction and engineering.

The FTA provides benefits for businesses wishing to supply services cross-border as well as businesses wishing to establish a presence locally in the other country.

Under the agreement, Morocco will also be required to permit U.S. financial service firms to establish subsidiaries and joint ventures in Morocco. In addition, banks and insurance companies will be permitted to establish branches, subject to a four-year phase-in for most insurance services.

The United States also gained enhanced access to the telecommunications market, including the right to interconnect with a dominant carrier in Morocco at non-discriminatory, cost-based rates. U.S. firms seeking to build a physical network in Morocco will have non-discriminatory access to key telecommunications facilities, and will be able to lease lines from Morocco's dominant carrier and re-sell telecom services to build a customer base.

INVESTMENT BARRIERS

The United States and Morocco have a Bilateral Investment Treaty (BIT), which entered into force in 1991. The FTA updates the legal framework for U.S. investors operating in Morocco. All forms of investment will be protected under the FTA, such as enterprises, debt, concessions, contracts, and intellectual property. The FTA removes certain restrictions and prohibits the imposition of other restrictions on U.S. investors, such as requirements to buy Moroccan rather than U.S. inputs for goods manufactured in Morocco.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Moroccan intellectual property rights (IPR) laws and enforcement of these laws have been insufficient to combat intellectual property theft. Enforcement resources have been inadequate, and civil and criminal penalties have not been stiff enough to provide sufficient deterrence.

The FTA addresses many of the U.S. IPR concerns. The agreement's strong anti-piracy provisions mandate both statutory and actual damages under Moroccan law for IPR violations.

Under these anti-piracy provisions, monetary damages can be awarded even when it is difficult to determine the amount of actual economic harm (retail value, profits made by violators). Each government also commits to granting and maintaining the right for authorities to seize, forfeit, and destroy counterfeit and pirated goods and the equipment used to make them. The agreement also requires each government to provide criminal liability for internet piracy, even if there is no motivation of financial gain.

The FTA further expands the protection of trademarks, copyrights, patents and trade secrets. Protection extends to cover state-of-the-art elements such as trademark disputes used in Internet domain names and strong anti-circumvention provisions to prohibit the tampering of technologies designed to prevent piracy and unauthorized distribution over the Internet.

OTHER BARRRIERS

Lack of transparency and regulatory predictability have inhibited U.S. access to the Moroccan market.

Under the FTA, each government must publish its laws and regulations governing trade and investment, and, beginning within one year, publish proposed regulations in advance and provide an opportunity for public comment on them. The Moroccan government will commit to apply fair procedures in administrative proceedings covering trade and investment matters directly affecting companies from the other country.

NEW ZEALAND

TRADE SUMMARY

The U.S. trade deficit with New Zealand was $892 million in 2004, an increase of $336 million from $555 million in 2003. U.S. goods exports in 2004 were $2.1 billion, up 12.3 percent from the previous year. Corresponding U.S. imports from New Zealand were $3.0 billion, up 23.5 percent. New Zealand is currently the 43rd largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to New Zealand were $973 million in 2003 (latest data available), and U.S. imports were $1.1 billion.

The stock of U.S. foreign direct investment (FDI) in New Zealand in 2003 was $3.8 billion, down from $4.0 billion in 2002. U.S. FDI in New Zealand is concentrated largely in the finance, wholesale, and manufacturing sectors.

IMPORT POLICIES

In general, tariff rates in New Zealand are low as a result of several rounds of unilateral tariff cuts that began in the mid-1980s and continued until the current Labor government, elected in 1999, decided to freeze further reductions until at least July 2005. The New Zealand government announced in September 2003 that it would resume unilateral tariff reductions. On July 1, 2006, New Zealand plans to begin gradually reducing its highest tariff rates of between 17 percent and 19 percent to 10 percent by July 1, 2009. The top rates apply mostly to clothing, footwear, carpets, and certain automobiles and auto parts. *Ad valorem* tariffs on other goods also will gradually be reduced to 5 percent by July 1, 2008. The New Zealand government will conduct a review in 2006 to determine rates for the period after July 1, 2009.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Biotechnology Commercial Release Moratorium

New Zealand's Parliament passed the New Organisms and Other Matters (NOOM) Bill 2003 on October 14, 2003, ending New Zealand’s moratorium on acceptance of applications for the commercial release into the environment of products produced through modern agricultural biotechnology. The new law put in place a revised regulatory framework by amending the Hazardous Substances and New Organisms (HSNO) Act 1996, under which the moratorium was scheduled to sunset on October 29, 2003. New Zealand's commercial release moratorium had precluded applications for the commercial planting of biotechnology crops, the commercial importation of biotechnology seeds, and the release into the environment of biotechnology animals. It did not, however, affect the use and sale of processed biotechnology foods and ingredients or veterinary medicines.

The NOOM Bill 2003 provides for a new conditional release category of approval for new organisms, including biotechnology products. This will permit New Zealand's Environmental Risk Management Authority (ERMA) to accept for review and its approval applications for release of biotechnology products with controls applied on a case-by-case basis. Under the provisions of the NOOM Bill, ERMA now will be able to approve a conditional release for biotechnology products that will allow field trial activity to expand from the limited scope of a fully contained trial to larger farm scale, encouraging ongoing research activity in New Zealand. Products from large-scale conditional field trials that ERMA may now approve could be sold domestically if the terms of project approval do not explicitly preclude such sales.

A Member of Parliament representing New Zealand's Green Party is sponsoring an amendment to the HSNO Act, which would reinstate the ban on the commercial release of genetically modified organisms into the environment until 2008. The bill is not likely to receive its first reading in Parliament before early 2005. After the first reading, Members of Parliament will vote on whether the bill should move forward to a select committee or be removed.

Biotechnology Food Approval

Imported biotechnology foods can be offered for sale and consumption in New Zealand after being assessed and approved by Food Standards Australia New Zealand (FSANZ) under delegated authority of the New Zealand Food Safety Authority (NZFSA). In mid-1999, a mandatory standard for foods produced using modern biotechnology came into effect. The standard established under the Food Act 1981 prohibits the sale of food produced using gene technology, unless the food has been assessed by FSANZ and listed in the food code standard. FSANZ had received 28 applications for safety assessments of bioengineered foods as of March 2004. Of these, 23 had been approved, four applications were being processed, and one approval request was withdrawn.

Biotechnology Food Labeling

Mandatory labeling requirements for foods produced using gene technology became effective in December 2001. Biotechnology labeling is required if a food in its final form contains detectable DNA or protein resulting from the application of biotechnology, with a few exceptions. Meeting New Zealand's biotechnology food labeling regulations places a burden on manufacturers, packers, importers, and retailers. They are especially relevant for U.S. agricultural exports, which consist primarily of processed food. Wholesalers and retailers frequently demand biotechnology-free declarations from their supplier/importer, which passes liability in the event of biotechnology labeling non-compliance back to the importer. New Zealand food legislation requires businesses to exercise due diligence in complying with food standards, which usually is defined as maintaining a paper or audit trail similar to a quality assurance system.

The NZFSA conducts periodic compliance audits. Individuals and companies found to be in non-compliance with biotechnology food labeling requirements may be assessed penalties under the Food Act 1981. The New Zealand government is reviewing authorized penalties stipulated under the act to make sure that they represent an adequate economic deterrent. New Zealand food retailers are discouraged from sourcing biotechnology food products, in part because of these regulations.

A retail food audit conducted by NZFSA in September 2004 reportedly found 17 of the 117 processed products evaluated to have genetically modified (GM) content that exceeded a 1 percent threshold. These included two products that had been labeled as GM-free, which were referred to the New Zealand Commerce Commission for action under the Fair Trading Act 1986. Additional NZFSA measures were taken to ensure that companies involved with those products whose labels failed to provide information on their GM content, but did not have false GM-free declarations, meet future labeling compliance standards.

Sanitary and Phytosanitary (SPS) Measures

New Zealand maintains a strict regime of SPS control for virtually all imports of agricultural products. The United States and New Zealand have held discussions on New Zealand's highly conservative regulatory approach as well as on specific SPS issues. The two sides continue to make progress in addressing specific issues that negatively impact trade in products supplied by the United States.

Beef. U.S. beef and beef variety meats were restricted from entering New Zealand following the December 2003 announcement of bovine spongiform encephalopathy (BSE) in the United States. Import restrictions also have been imposed on live cattle, certain pet food, non-protein free edible tallow, and U.S. processed food products containing beef such as soups or those containing gelatin made from bovine bone material. New Zealand imports of U.S. bovine products for human consumption now require assessment and approval by NZFSA on a case-by-case basis before importation. This can be time-consuming, results in additional costs to importers and exporters, and deters sales. As of mid-February 2005, the NZFSA continues to assess a U.S. Department of Agriculture (USDA) request for New Zealand to accept U.S. BSE control measures as equivalent to that of New Zealand. If agreed to, this would eliminate individual product approval procedures initiated following the BSE detection in the United States. A country assessment review by the Ministry of Agriculture (MAF) is under way that would permit a reinstatement of New Zealand's Import Health Standard (IHS) for U.S. live cattle and a resumption of trade.

Table Grapes. The New Zealand Ministry of Agriculture (MAF) in September 2002 issued a new IHS for the import of table grapes from California that effectively reopened trade to U.S. exporters. The IHS contained specific mitigation measures to address the detection of post-border, black widow and other exotic spiders. As of December 2004, no significant biosecurity breaches were reported to the New Zealand government following the resumption of trade. The

United States requested a modification of these mitigation measures to reduce costs to U.S. exporters and New Zealand importers without compromising New Zealand's biosecurity standards. MAF responded in December 2004 by agreeing to reduce table grape inspection levels for Californian shipments. It further modified import requirements for California table grapes by eliminating mandatory cold treatment, effective January 2005.

Pork Meat. In June 2002, New Zealand modified its regulations imposed a year earlier requiring pork meat products imported from countries with porcine reproductive and respiratory syndrome (PRRS), including the United States, to be cooked to a certain temperature, either before export or after import in special facilities in New Zealand. The cooking requirement results in a darker meat color, which tends to be negatively received by consumers. New Zealand revised its import regulations in 2003, allowing pig meat products from the United States to be microwave treated. MAF again modified its import regulations for U.S. pork meat in November 2004, this time allowing entry of pork meat products derived from pigs imported live into the United States from Canada for immediate slaughter. Prior to this, New Zealand's IHS had allowed entry only of U.S. pork meat derived from U.S. resident animals or from pigs resident and slaughtered in Canada and further processed in the United States. The Ministry of Agriculture remains willing to consider scientific evidence related to the PRRS issue that would justify a review of its import health standard for pork meat.

Poultry Meat. New Zealand implemented measures that suspended the importation of poultry meat from various nations, including the United States, in late 2001 because of the risk of introducing infectious bursal disease (IBD). U.S. exporters are unable to sell uncooked poultry meat to New Zealand, while cooked poultry meat is restricted to canned products. Discussions between the United States and New Zealand on this issue continue.

Soybean meal. New Zealand's import regulations for oilseed meals were modified in May 2004, requiring an official phytosanitary certification to address certain manufacturing practices. USDA does not monitor or inspect U.S. production facilities for soybean meal and was unable to meet New Zealand's new certification requirements. Following consultations with USDA, MAF again amended its IHS for oilseed meals in August 2004 and November 2004. These revisions allow an independent verification authority in conjunction with a manufacturer's certificate to address the production process issue and, taken together with USDA documentation, meet New Zealand's import requirements. The new import regulations establish clarity and certainty regarding certification of U.S. soybean meal and allowed normal sales and supplies to resume.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

In October 2003, the New Zealand Parliament enacted a ban on the parallel importation of films, videos and DVDs for the initial nine months after a film's international release. The ban applies only to film media, not to parallel importation of music, software and books. It is scheduled to sunset in 2008, unless extended.

The new legislation, which amended the Copyright Act 1994, also makes it easier to challenge copyright violations in court by shifting the burden of proof in certain copyright infringement cases to the defendant, who must prove that an imported film, sound recording or computer software is not a pirated copy.

By omitting a ban on parallel imports of music, software and books, however, the legislation failed to roll back all the provisions of the New Zealand government's 1998 amendment to the Copyright Act. While the legislation addressed many of the U.S. film industry's concerns about parallel importing, other U.S. industries, particularly producers and distributors of music and software, have voiced concerns that allowing parallel imports makes it more difficult to detect and combat piracy and erodes the value of their products in New Zealand and in third-country markets.

The music industry also is concerned about a proposed amendment to the Copyright Act that would legalize the duplication of sound recordings in other formats for a purchaser's private use. The government says this would enable consumers to employ new digital technologies and would legalize what already is common practice. The music industry warns that such an exception to copyright protection would make copyright infringement difficult to police, send the wrong message to consumers and cost the industry an estimated $13.7 million in sales revenue and $1.97 million in profits per year.

The music industry also has expressed concern over another proposed exception to the Copyright Act, which would allow the unauthorized time-shifting of virtually all works communicated to the public. The industry warns that the exception could eliminate the ability of right holders to develop new approaches to meeting consumer demand for electronically delivered materials and reduce access and choice for New Zealand consumers to these materials.

U.S. Industry has expressed concern over another proposed exception to the Copyright Act, which would allow the unauthorized time-shifting of virtually all works communicated to the public. The industry warns that the exception could eliminate the ability of rights holders to develop new approaches to meeting consumer demand for electronically delivered materials and reduce access and choice for New Zealand consumers to these materials.

With amendments proposed in June 2003 to the Copyright Act 1994, the government aims to bring New Zealand law into closer conformity with the WIPO Copyright Treaty (WCT) and the WIPO Performances and Phonograms Treaty (WPPT). The amendments are intended to reflect developments in digital technologies and international developments in copyright law and are expected to be introduced in 2005. If this legislation is enacted, the New Zealand government will determine whether to accede to the WCT and WPPT treaties.

New Zealand also took a number of actions to strengthen its IPR enforcement regime. To deter counterfeiting and copyright piracy, the Trade Marks Act 2002, which entered into force in August 2003, creates new criminal offenses for counterfeiting trademarks and increases the penalties for pirating copyright goods. For those offenses, the act provides for penalties of up to NZ $150,000 (US $97,065) in fines or up to five years' imprisonment.

Following a government review of the Patents Act 1953 that began in August 2000, the Ministry of Economic Development has drafted legislation intended to bring the act into closer conformity with international standards. The draft would keep the maximum patent term at 20 years, but would tighten the criteria for granting a patent, from a patentable invention being new in New Zealand, to being new anywhere in the world and involving an inventive step.

The draft's prohibition of patents for methods of medical treatment concerns some pharmaceutical companies. The industry also is concerned by the Cabinet's decision in mid-2004 to halt a study on the economic impact of extending patent terms for pharmaceuticals. In a submission to the New Zealand government, the pharmaceutical industry group, Researched Medicines Industry Association of New Zealand, had contended that New Zealand's effective patent life for pharmaceuticals had been substantially eroded. It recommended adoption of a supplementary protection certificate arrangement, similar to those used in a number of OECD and European Union countries. This would effectively extend patent protection. However, the draft legislation fails to address this issue.

The pharmaceutical industry also is concerned by an amendment, enacted in December 2002, to the Patents Act 1953. This amendment provided that it is not a patent infringement for a person to make, use, exercise or vend an invention for purposes related to gaining regulatory approval in New Zealand or other countries. It effectively expedites the approval process for generic competition to products going off patent. The amendment was passed quickly and not as part of the ongoing and thorough review of the Patents Act. The pharmaceutical industry is strongly opposed to this "springboarding" legislation.

The United States continues to monitor developments in IPR issues closely.

SERVICES BARRIERS

Local Content Quotas

Radio and television broadcasters have adopted voluntary local content targets, but only after the New Zealand government made it clear that it would otherwise pursue mandatory quotas. While New Zealand government officials have said they are sensitive to the implications of quotas under the WTO General Agreement on Trade in Services (GATS), they reserve the right to impose them.

Telecommunications

U.S. industry has expressed concern about the cost of completing calls onto mobile networks in New Zealand, which is among the highest in the world. The New Zealand regulating authority began an investigation in May 2004 into mobile termination rates and in an October 2004 draft decision said that mobile network operators had been able to set unreasonably high rates because of limited competition in the market. The authority called for such charges to be regulated. It is unclear whether the final recommendation, expected in early 2005, will retain the draft decision's recommendations. The final decision rests with the Communications Minister, who can accept the regulating authority's recommendation, reject it or refer it back for further consideration. The final decision is expected in late 2005.

Competitors of the formerly state-owned monopoly Telecom were disappointed by the New Zealand government's decision in May 2004 against unbundling the local loop. Although under competitive pressure, Telecom still dominates the market. The Communications Minister accepted the regulator's recommendation against ordering Telecom to open its national fixed-line network to competitors. Saying he aimed to increase competition in broadband services, the Minister also agreed with the regulator's recommendation to require bitstream unbundling, or access to Telecom's equipment by service providers in order to sell their own broadband services, and to accept Telecom's offer to provide within six months unbundled partial private circuits, primarily used for business data services. As of the end of 2004, however, Telecom and regulators had yet to agree on commercial terms and conditions for the unbundled bitstream service.

INVESTMENT BARRIERS

Investment Screening

New Zealand screens certain types of foreign investment through the Overseas Investment Commission (OIC). Amid growing public concern about foreigners buying coastal properties, the New Zealand government in November 2003 launched a review of OIC's powers. That review led to proposed legislation, introduced in November 2004, that would raise the minimum threshold for scrutiny of proposed business purchases, but toughen the screening and monitoring of land purchases. Under the legislation, the threshold for screening non-land business assets would be increased from NZ $50 million (US $35.7 million) to NZ $100 million (US $71.3 million), where a foreigner proposes to take control of 25 percent or more of a business. Government approval still would be required for purchases of land over 5 hectares (12.35 acres) and land in certain sensitive or protected areas. For land purchases, foreigners who do not intend to live in New Zealand would have to provide a management proposal covering any historic, heritage, conservation or public access matters and any economic development planned. That proposal would have to be approved and generally made a condition of consent. In addition, investors would be required to report regularly on their compliance with the terms of the consent. Overseas persons would continue to have to demonstrate the necessary experience to manage the investment. Any application involving land in any form still would have to meet a national interest test. The United States has raised concerns about the continued use of this screening mechanism. New Zealand's commitments under the GATS Agreement of the WTO are limited as a result of New Zealand's screening program.

OTHER BARRIERS

Pharmaceuticals

The U.S. government continued to raise concerns about New Zealand's pharmaceutical sector policies, which do not appropriately value innovation and diminish the contribution of New Zealand to research and development of innovative pharmaceutical products. New Zealand's Pharmaceutical Management Agency (PHARMAC) administers a Pharmaceutical Schedule that lists medicines subsidized by the New Zealand government and the reimbursement paid for each pharmaceutical under the national health care system. The schedule also specifies conditions for prescribing a product listed for reimbursement. PHARMAC, a stand-alone Crown entity structured as a statutory corporation, accounts for 73 percent of expenditures on prescription drugs in New Zealand.

New Zealand does not directly restrict the sale of non-subsidized pharmaceuticals in the country. However, private medical insurance companies will not cover non-subsidized medicines, and doctors are often reluctant to prescribe non-subsidized medicines for their patients, who would have to pay out-of-pocket costs. Thus, PHARMAC's Pharmaceutical Schedule decisions determine the selection and pricing of the bulk of pharmaceutical drugs sold in New Zealand. Its decisions have a major impact on the availability and price of non-subsidized medicines and the ability of pharmaceutical companies to sell their products in the New Zealand market.

The United States has serious concerns relating to the transparency, predictability and accountability of PHARMAC's operations. U.S. pharmaceutical suppliers report that the methodology used to determine Pharmaceutical Schedule decisions lacks transparency. The Boards of PHARMAC and the Researched Medicines Industry Association of New Zealand have been meeting to discuss these concerns. The U.S. government will continue to closely monitor developments in this sector.

On December 10, 2003, the New Zealand and Australian governments signed a treaty to create a joint agency to regulate medical devices, prescription and over-the-counter medicines, dietary and nutritional supplements, and cosmetics such as sun creams. Aside from prescription pharmaceuticals, New Zealand does not currently regulate market entry of these products. The new agency is scheduled to begin operations July 1, 2006. Each country's government will continue to determine funding of prescription medicines. The new agency may charge full cost-recovery fees to register products and require additional documentation and assessments for certain products, even if they already have U.S. Food and Drug Administration approval. U.S. manufacturers and distributors of non-pharmaceutical therapeutic products have expressed concerns that those requirements would be overly burdensome and costly, and could serve to discourage exports of their products from the United States to New Zealand.

NICARAGUA

TRADE SUMMARY

The U.S. trade deficit with Nicaragua was $399 million in 2004, an increase of $131 million from $268 million in 2003. U.S. goods exports in 2004 were $592 million, up 18.0 percent from the previous year. Corresponding U.S. imports from Nicaragua were $990 million, up 28.7 percent. Nicaragua is currently the 69th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Nicaragua in 2003 was $261 million, up from $250 million in 2002.

IMPORT POLICIES

Free Trade Agreement

The United States engaged in free trade agreement negotiations with five Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) in 2003. The United States concluded negotiations with El Salvador, Guatemala, Honduras, and Nicaragua in December 2003 and with Costa Rica in January 2004. In May 2004, the six countries signed the United States – Central America Free Trade Agreement. During 2004, the United States and the Central American countries engaged in negotiations with the Dominican Republic to integrate that country into the free trade agreement. On August 5, 2004, the seven countries signed the Dominican Republic – Central America – United States Free Trade Agreement (CAFTA-DR). El Salvador ratified the Agreement in December 2004 and Honduras ratified in March 2005. Legislative approval is pending in the United States and the other signatories to the Agreement.

The CAFTA-DR will remove barriers to trade with and investment in the region and will further regional economic integration. The CAFTA-DR will also require the Central American countries and the Dominican Republic to undertake needed reforms to confront many of the problems noted below in areas including: customs administration; protection of intellectual property rights; services, investment, and financial services market access and protection; government procurement; sanitary and phytosanitary (SPS) barriers; and other non-tariff barriers.

Tariffs

In 2002 and 2003, Nicaragua completed implementation of most of a broad package of tariff reductions that had been approved in 1997. In those same years, two tax reform bills introduced additional tariff changes. The overall thrust of the changes in both legislation and practice over the last several years has been to reduce tariffs (though there have been a few increases), reduce non-tariff barriers, and greatly reduce the discretion of government officials to waive the application of tariffs. The reform process is in accordance with the reduction and harmonization of a common external tariff among members of the Central American Common Market (CACM) to between zero percent and 15 percent on most items.

Nicaragua imposes regular import duties of 10 percent or 15 percent on many final consumer goods and a duty of 5 percent on certain primary or intermediate goods from outside Central America that compete with products produced in CACM countries. The tariff is assessed on a good's CIF value. Once the CAFTA-DR goes into effect, about 80 percent of U.S. industrial and commercial goods will enter the region duty-free, with the remaining tariffs on such goods phased out over 10 years. Nearly all textile and apparel goods that meet the Agreement's rules of origin will be duty-free and quota-free immediately, promoting new opportunities for U.S. and regional fiber, yarn, fabric and apparel manufacturing. (The Agreement's tariff treatment for textile and apparel goods may be made retroactive to January 1, 2004.)

A small number of protected agricultural commodities, notably rice and chicken parts, have particularly high tariff rates. Processed rice faces tariffs as high as 61 percent, down from a maximum of 103.5 percent in 2002. Certain chicken parts face a tariff of 170 percent. Tariffs on corn, previously higher, now range from 10 percent to 15 percent. In May 2003, Nicaragua raised tariffs on cheese and certain other dairy products from countries outside the CACM region to a common external tariff rate of 40 percent, from a prior rate of 15 percent, an increase that was consistent with Nicaragua's WTO rights.

Under the CAFTA-DR, Nicaragua will eliminate its tariffs on nearly all agricultural products within 15 years, including its tariffs on rice and yellow corn. Nicaragua will eliminate its tariffs on chicken leg quarters within 18 years and on dairy products within 20 years. For the most sensitive products, tariff rate quotas will permit some immediate zero-duty access for specified quantities during the tariff phase-out period, which will expand over time. Nicaragua will liberalize trade in white corn through expansion of a TRQ.

Non-Tariff Measures

A "consumption tax" on luxury items is levied on a limited number of items. The tax is generally lower than 15 percent, with a few exceptions noted below. Although the ISC is not applied exclusively to imports, the value on which it is based varies depending on whether the product is produced domestically or abroad. While the ISC on domestic goods is based on a manufacturer's price, the ISC on imported goods is based on the CIF value. Alcoholic beverages and tobacco products are exceptions; for these products, the ISC is based on the price charged to the retailer.

In accordance with April 2000 amendments to Nicaragua's tax laws, the ISC on soft drinks was lowered from a level of 18 percent in 1999 to 15 percent in 2000 and 12 percent in 2001. A further reduction to the target rate of 9 percent became effective in 2004.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Products that meet domestic U.S. standards are generally accepted in the Nicaraguan market with little need for further certification. U.S. exporters of food products must meet minimal phytosanitary and labeling requirements. In Nicaragua, all brands of alcoholic beverages must be registered annually with the Ministry of Public Health, and import licenses are required to import beverage alcohol. Under CAFTA-DR, Nicaragua commits to abide by the terms of the WTO's Import Licensing Agreement.

U.S. industry has expressed concern with Nicaragua's proposed standards for rum and aguardiente. However, the five Central American countries, including Nicaragua, are in the process of developing common standards for several products, including distilled spirits, which could serve to increase market access and facilitate trade. Nicaragua committed under the CAFTA-DR to explicitly recognize Bourbon and Tennessee whiskey as distinctive products of the United States, an objective of our distilled spirits industry.

There is currently no regulatory process for approving agricultural biotechnology products for import or sale. Imported agricultural products derived from biotechnology are supposed to be identified as such, but there is no law in place governing the use of labels on biotechnology products. In August 2003 an executive decree called for the establishment of an interagency commission to develop procedures for risk analysis of agricultural biotechnology products, norms for their use, and regulations for their production and importation.

When the United States and Central America launched the free trade agreement negotiations, they initiated an active working group dialogue on SPS barriers to agricultural trade that met alongside the negotiations to facilitate market access. The objective was to leverage the impetus of active trade negotiations to seek difficult changes to the Central American countries' SPS regimes. Through the work of this group, Nicaragua has committed to resolve specific measures affecting U.S. exports to Nicaragua. In particular, for meat, dairy and poultry, Nicaragua is moving toward recognizing import eligibility for all plants inspected under the U.S. food safety and inspection system.

GOVERNMENT PROCUREMENT

Nicaragua's law on government procurement, which went into effect in January 2000, provides for nondiscrimination among suppliers and requires that most government procurement contracts be advertised in national newspapers and the Internet. However, some contractors have complained of inadequate notification of pending procurements. Nicaragua is not a party to the WTO Agreement on Government Procurement.

The CAFTA-DR requires fair and transparent procurement procedures, including advance notice of purchases and timely and effective bid review procedures. Under the CAFTA-DR, U.S. suppliers will be permitted to bid on procurements covered by the Agreement for most

Nicaraguan government entities, including key ministries and state-owned enterprises on the same basis as Nicaraguan suppliers. The anti-corruption provisions in the Agreement require each government to ensure that bribery in matters affecting trade and investment, including in government procurement, is treated as a criminal offense, or is subject to comparable penalties, under its law.

EXPORT SUBSIDIES

Nicaragua does not provide export financing. However, all exporters receive tax benefit certificates equivalent to 1.5 percent of the FOB port of exit value of the exported goods. Foreign inputs for Nicaraguan export goods from the country's free trade zones enter duty-free and are exempt from value-added tax. Under the CAFTA-DR, Nicaragua may not adopt new duty waivers or expand existing duty waivers conditioned on the fulfillment of a performance requirement (e.g., the exportation of a given level or percentage of goods). Nicaragua may maintain existing duty waiver measures provided such measures are consistent with its WTO obligations.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Nicaragua has strengthened its legal framework for protection of intellectual property rights over recent years. Nonetheless, although the Nicaraguan government has dedicated three public prosecutors solely to IPR issues, enforcement remains weak. Protection of well-known trademarks is poorly enforced. According to industry sources, the government made two attempts to crack down on music recording piracy in 2001 but has made no significant raids or arrests since then, and anecdotal evidence suggests an increase in the reproduction of pirated music and videos. The U.S. Government and industry are working with the Nicaraguan government to provide training for effective enforcement. Lack of protection for pharmaceutical and agricultural product test data against unfair commercial use also remains a serious concern. Implementation of the CAFTA-DR obligations will require Nicaragua to protect undisclosed test data submitted for the purpose of product marketing approval of pharmaceutical and agricultural chemical products against disclosure and unfair commercial use

CAFTA-DR obligations will also strengthen Nicaragua's IPR protection regime to conform with, and in many areas exceed, WTO norms. CAFTA-DR obligations will also provide stronger deterrence against piracy and counterfeiting by criminalizing end user piracy and requiring Nicaragua to authorize the seizure, forfeiture, and destruction of counterfeit and pirated goods and the equipment used to produce them. The CAFTA-DR text also mandates both statutory and actual damages for copyright and trademark infringement, which would ensure that monetary damages can be awarded even when it is difficult to assign a monetary value to the violation.

SERVICES BARRIERS

Financial Services

Nicaragua has ratified its commitments under the 1997 WTO Financial Services Agreement. Nicaragua's WTO commitments cover most banking services, including acceptance of deposits, lending, leasing, guarantees, and foreign exchange. However, its WTO commitments do not cover security or asset management. Nicaragua allows foreign banks to operate either as 100 percent-owned subsidiaries or as branches, but no U.S. bank has yet re-entered the Nicaraguan financial market since several major U.S. banks withdrew in the 1970s. The CAFTA-DR will make it easier for U.S. banks to enter the Nicaraguan market. U.S. financial service suppliers will have full rights to establish subsidiaries, joint ventures or branches for banks.

Legislation passed in 1996 opened the insurance industry to private sector participation. Private insurance companies now compete with the government-owned firm INISER. However, no U.S. or other foreign insurance company has entered the Nicaraguan market. Under the CAFTA-DR, U.S. insurance suppliers will have full rights to establish subsidiaries, joint ventures or branches. Nicaragua will allow U.S.-based firms to supply insurance on a cross-border basis, including reinsurance; reinsurance brokerage; marine, aviation and transport (MAT) insurance; and other insurance services. Further, Nicaragua will accord substantial market access in services across their entire services regime, subject to very few exceptions.

The telecommunications sector is in transition from state ownership to private ownership. Fifty-one percent of Enitel, the former state telephone monopoly, has been sold and a process to sell the remaining 49 percent is nearly complete. Private mobile telephone companies, and international operators, have at times complained that the regulatory agency TELCOR exhibits favoritism toward Enitel. For example, at the end of 2004, Enitel unilaterally raised termination rates for calls sent to wireless networks and blocked traffic to such networks when carriers refused to pay the 100% increase in those rates. This action by Enitel was met with little or no intervention by TELCOR to require Enitel to justify such rate increases. In general, however, TELCOR has encouraged competition in its licensing and regulatory practices, and under the CAFTA-DR, Nicaragua has committed to open its telecommunications sector to service and investment by U.S. providers.

The Law on Promotion of National Artistic Expression and on Protection of Nicaraguan Artists (Law no. 215, National Gazette 134, July 17, 1996) requires that foreign production companies contribute 5 percent of total production costs to a local cultural fund. In addition, the law requires that 10 percent of the technical, creative or artistic staff must be hired locally. Under the CAFTA-DR, Nicaragua would no longer require these contributions or local hiring for film production.

INVESTMENT BARRIERS

Poorly enforced property rights and the resulting proliferation of property disputes are among the most serious barriers to investment in Nicaragua. The Sandinista government confiscated nearly 30,000 properties during the 1980s. Many thousands of individuals -- including over 1,000 U.S. citizens -- have filed claims since 1992 for compensation or return of properties. While there has been progress in resolving claims, many valuable properties remain in the hands of the government or private parties, including former Sandinista government officials and military officers. Property claimants can sue for return of their properties, but the legal system favors the current occupants. The Nicaraguan government offers low-interest bonds as a means of compensation in most instances. The United States continues to urge the Nicaraguan government to resolve claims.

Nicaragua and the United States concluded a Bilateral Investment Treaty (BIT) in July 1995. Nicaragua's National Assembly ratified the BIT in June 1996, but the U.S. Senate has not ratified it. However, the investment chapter of the CAFTA-DR includes provisions for the protection of U.S. investors similar to those in the 1995 BIT by establishing a secure, predictable legal investment framework. Under the CAFTA-DR, all forms of investment will be protected, including enterprises, debt, concessions, contracts and intellectual property. U.S. investors will enjoy in almost all circumstances the right to establish, acquire and operate investments in Nicaragua on an equal footing with local investors. Among the rights afforded to U.S. investors are due process protections and the right to receive a fair market value for property in the event of an expropriation. Investor rights will be backed by an effective, impartial procedure for dispute settlement that is fully transparent. Submissions to dispute panels and panel hearings will be open to the public, and interested parties will have the opportunity to submit their views.

ELECTRONIC COMMERCE

Electronic commerce is not well developed in Nicaragua. Currently, there are no laws or regulations restricting its use or regulating the treatment of electronic transactions. The CAFTA-DR includes provisions on electronic commerce that reflect the issue's importance in global trade and the importance of supplying services by electronic means as a key part of a vibrant electronic commerce environment. Under the Agreement, Nicaragua committed to provide non-discriminatory treatment of digital products and not to impose customs duties on such products, and to cooperate in numerous policy areas related to electronic commerce.

OTHER BARRIERS

Voices within and outside of Nicaragua have raised concerns that Nicaragua's legal system is weak and cumbersome. Many members of the judiciary, including those at high levels, are widely believed to be corrupt or subject to outside political pressures. Enforcement of court orders is uncertain and frequently subject to non-judicial considerations. Foreign investors are not specifically targeted but are often at a disadvantage in disputes against nationals with political connections. Recognizing Nicaragua’s reputation for problems with corruption, President Bolaños has made anti-corruption a centerpiece of his administration’s domestic policy. This contributed to Nicaragua’s selection, during 2004, as a country eligible to apply for Millennium Challenge Account (MCA) assistance. MCA countries are deemed to have shown a commitment to rule justly (including by tackling corruption), investing in their people, and encouraging economic freedom. The anti-corruption provisions in the CAFTA-DR require each government to ensure that bribery in matters affecting trade and investment is treated as a criminal offense, or is subject to comparable penalties, under its law.

Law 364

U.S. multinational firms and the U.S. Chamber of Commerce have expressed concern regarding Nicaraguan Law 364, enacted in October 2000 and published in January 2001. Law 364, which some U.S. multinationals believe targets them, retroactively imposes liabilities on foreign companies that manufactured or used in Nicaragua the chemical pesticide DBCP, which was banned in the United Sates in 1979, when the Environmental Protection Agency cancelled its certificate for use (with exceptions). U.S. multinationals express concern that the law and its application under Nicaragua’s judicial system lack due process, transparency and fundamental fairness, and that the Nicaraguan Government has not taken sufficient ameliorative action to date.

Concerns with Law 364 include onerous procedures and requirements such as: retroactive application of no-fault liability related to a specific product; waiver of the statute of limitations; irrefutable presumption of causality; truncated judicial proceedings; imposition of a $100,000 non-refundable bond per defendant as a condition for firms to put up a defense in court; escrow requirements of approximately $20 million earmarked for payment of awards; and minimum liabilities as liquidated damages (ranging from $25,000 to $100,000.)

In December 2002, the first judgment under this law was rendered in a consolidated lawsuit in the amount of $489 million. A U.S. district court ruled in October 2003 that the judgment could not be enforced against the companies in the United States. Several hundred lawsuits claiming damages of over $11 billion are pending.

NIGERIA

TRADE SUMMARY

The U.S. trade deficit with Nigeria was $14.7 billion in 2004, an increase of $5.3 billion from $9.4 billion in 2003. U.S. goods exports in 2004 were $1.6 billion, up 52.6 percent from the previous year. Corresponding U.S. imports from Nigeria were $16.2 billion, up 56.3 percent. Nigeria is currently the 52nd largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Nigeria in 2003 was $2.1 billion, up from $1.8 billion in 2002. U.S. FDI in Nigeria is concentrated largely in the petroleum sector.

IMPORT POLICIES

Tariffs

Tariffs provide the Nigerian government with its second-largest source of revenue after oil exports. In its last major tariff revision in March 2003, the Nigerian government cut duties on 230 tariff line items (mostly raw materials, base metals, and capital equipment) to as low as 2.5 percent, while raising them on 30 line items (largely plastic, rubber, and aluminum articles) to as high as 65 percent. Tariffs on agricultural products such as corn and rice were raised to 70 percent and 100 percent, respectively. President Obasanjo announced in October 2004 that Nigeria will begin harmonizing its tariff structure with that of the Economic Community of West African States in January 2005, for implementation in July 2005. Items banned would remain so until sometime in 2007, when the bans would be replaced by tariffs.

Frequent import regime changes and uneven duty collection make importing difficult and expensive, and occasionally create severe commercial bottlenecks. This problem is aggravated by Nigeria's dependence on imported raw materials and finished goods, which affects both foreign and domestic manufacturers. Many importers resort to under-invoicing and smuggling to avoid tariffs or bans.

Non-Tariff Trade Barriers

The United States continues to have concerns about the Nigerian government's use of non-tariff trade barriers. Bans on a variety of items – sorghum, millet, wheat flour, cassava, frozen meat and poultry products, vegetable oil (in bulk), biscuits, pasta, bottled water, fruit juice in retail packs, cookies, confectionery and chocolate products, beer, kaolin, gypsum, mosquito repellent coils, printed fabrics, used clothing, cars more than eight years old, and bagged cement – continued into 2004. Products added to the list of banned items in 2004 included men's footwear, leather bags and plastic bags (excluding ladies purses), all textiles and yarn, furniture, toothpaste, household plastic ware, soap and detergents, fresh and plastic flowers, and fresh fruits. In November 2004, the Nigerian government agreed to exempt from the import ban certain U.S. textile and yarn products entering under a special "Manufacturers In Bond" scheme

Customs Barriers

Nigerian port practices continue to present major obstacles to trade. Importers face long clearance procedures, high berthing and unloading costs, erratic application of customs regulations, and corruption. The Nigeria Customs Service (NCS) stepped up its enforcement of a 100 percent physical inspection program in an attempt to reduce smuggling and under-valuation of imports, but officials admit they do not have the resources to inspect every incoming container. The NCS operates a preshipment inspection regime under which contracted inspection companies at ports of origin issue inspection reports (sampling inspections) that Nigerian customs officials use to determine the value of items shipped and applicable customs duties.

The NCS had planned to replace its preshipment inspection regime with physical inspection at the port of importation in 2002 and 2003, but the change was deferred after importers protested that NCS officials might use their positions as sole-valuation authorities to extract unauthorized fees. The NCS hopes to introduce a physical inspection regime in early 2005; however, NCS risk assessment and other databases were not yet fully operational at the end of 2004. Therefore, it is unlikely the NCS will begin its physical inspection regime as expected, in early 2005.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

Rules concerning sanitary and phytosanitary standards, testing, and labeling are well defined, but bureaucratic hurdles slow the import-approval process. Regardless of origin, all food, drug, cosmetic, and pesticide imports must be accompanied by certificates of analysis from manufacturers and appropriate national authorities, and specified animal products, plants, seeds, and soils must be accompanied by proper inspection certificates. U.S. exporters may obtain these certificates from the U.S. Department of Agriculture. By law, items entering Nigeria must be labeled exclusively in the metric system. The NCS is charged with preventing the entry of products with dual or multiple markings, but such items are often found in Nigerian markets.

High tariffs and uneven application of import and labeling regulations make importing high-value perishable products into Nigeria difficult. Disputes between Nigerian agencies over the interpretation of regulations often cause delays, and frequent changes in customs guidelines slow the movement of goods through Nigerian ports. These factors can contribute to product deterioration and may translate into significant losses for perishable-goods importers.

The National Agency for Food and Drug Administration and Control (NAFDAC) is charged with protecting Nigerian consumers from fraudulent or unhealthful products. The agency recently targeted the illicit importation of counterfeit and expired pharmaceuticals for special attention, particularly imports from the Far East and South Asia. NAFDAC's severely limited capacity for carrying out inspections and testing contributes to what some have characterized as an occasionally heavy-handed or arbitrary approach to regulatory enforcement, and the agency has occasionally challenged legitimate food imports.

U.S. products do not appear to be subject to extraordinary or discriminatory restrictions or regulations, but the alleged widespread use of fraudulent documentation by non-U.S. exporters may put U.S. exporters at a competitive disadvantage.

GOVERNMENT PROCUREMENT

The Obasanjo administration has made modest progress on its pledge to practice open and competitive bidding and contracting for government procurement and privatization. The initial stages of the tendering process tend to be transparent and even-handed, but as tenders move through the decision-making process, the process often becomes less transparent. Allegations by unsuccessful bidders of corrupt behavior by senior government officials and foreign companies are common, but they rarely provoke substantive reactions.

New procurement and contracting guidelines were issued in January 2001, and a due-process office, the Budget Monitoring and Price Intelligence Unit, was also established. The unit acts as a clearing house for government contracts and procurement and monitors the implementation of projects to ensure compliance with contract terms and budgetary restrictions. Procurement above 50 million naira (about $385,000) is subject to "due process" review. (Due process certification aims at ensuring that the procurement process for public projects adheres to international standards for competitive bidding.) In December 2004, the Government submitted a bill to establish a Bureau of Public Procurement to the National Assembly.

Foreign companies incorporated in Nigeria receive national treatment, and government tenders are published in local newspapers. U.S. companies have won government contracts in several sectors. Unfortunately, many companies that have won contracts have subsequently had difficulty getting them funded, and some companies that won contracts for which funds were allocated have had trouble getting paid.

EXPORT SUBSIDIES

The Nigerian Export Promotion Council and the Nigerian Export-Import Bank administer export incentive programs that include tax concessions, export development funds, capital assets depreciation allowances, and foreign currency retention programs. Funding constraints limit the effectiveness of these programs. Since many businessmen alleged that only favored individuals and businesses benefit, the government suspended indefinitely the export-expansion grant program in 2004 until government investigations into corrupt practices associated with its implementation are concluded. Aside from these incentive programs, Nigeria's non-oil export sector does not benefit from subsidies or other significant support from the government.

To attract investment in export-oriented industries, the government established the Nigerian Export Processing Zone Authority (NEPZA) in 1992. Of five zones established under NEPZA, only the Calabar and Bonny Island (Onne) export-processing zones function. NEPZA rules dictate that at least 75 percent of production in the zones be exported, but lower export levels are tolerated. The Nigerian Government converted the Calabar export-processing zone into a free-trade zone in 2001. It is unclear whether the new designation has improved its export performance.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Nigeria is a member of the World Intellectual Property Organization (WIPO) and a signatory to the Universal Copyright Convention (UCC), the Berne Convention, and the Paris Convention for the Protection of Industrial Property. Legislation pending in the National Assembly may establish a legal framework for an IPR system compliant with WTO rules. Nigeria's current IPR laws afford protection that is intended to comply with WTO provisions.

The government's lack of institutional capacity to address IPR issues is a major constraint to enforcement. Relevant Nigerian institutions suffer from low morale, poor training, and limited resources. Fraudulent alteration of IPR documentation is common. Despite Nigeria's active participation in the conventions cited above, its reasonably comprehensive IPR laws, and growing interest among Nigerians in seeing their intellectual property protected, piracy is rampant in Nigeria. Counterfeit auto parts, pharmaceuticals, business and entertainment software, music and video recordings, and other consumer goods are sold openly throughout the country. In 2004, U.S. industry reported a growth of optical disk manufacturing plants, some of which may be contributing to the production of pirated optical disk products. Additionally, book piracy remains a problem and its eradication is frustrated by rights holder difficulties in getting legitimate books to market.

Patent and trademark enforcement remains weak, and judicial procedures are slow and subject to corruption. Nonetheless, recent government efforts to curtail IPR abuse have yielded results. The Federal High Court of Enugu, Nigeria, issued an interim injunction on November 23, 2004 against several firms infringing a Honeywell International trademark for spark plugs. The court warned all distributors, dealers, and retailers in Nigeria that the unauthorized use of Honeywell's "Autolite" trademark is illegal and constitutes an offense punishable by fine or imprisonment.

Nigeria's broadcast regulations do not permit rebroadcast or excerpting of foreign programs unless the station has an affiliate relationship with a foreign broadcaster. This regulation is generally respected, but some cable providers illegally transmit foreign programs. The National Broadcasting Commission monitors the industry and is responsible for punishing infractions.

IPR problems in Nigeria's film industry worsened following the government's 1981 nationalization of the country's filmmaking and distribution enterprises as part of its campaign to "indigenize" the economy. The legitimate film distribution market has yet to recover. Almost no foreign feature films have been distributed in the country in the last two decades, and only one multiplex movie theater operates in Nigeria. Widespread pirating of foreign and domestic videotapes discourages the entry of licensed distributors.

The Nigerian police force, working closely with the Nigerian Copyright Commission, has raided enterprises producing and selling pirated software and videos, and a number of high-profile charges have been filed against IPR violators. Unfortunately, most raids appear to target small rather than large and well-connected pirates, and very few cases involving copyright, patent, or trademark infringement have been successfully prosecuted.

SERVICES BARRIERS

Foreign participation in the services sector is generally not restricted. Regulations provide 100-percent foreign access to service sectors, including banking, insurance, telecommunications, and securities. Central Bank of Nigeria directives stipulate minimum levels of paid-up capital. At least three foreign banks operate in Nigeria, and several Nigerian banks have foreign shareholders.

Professional societies in engineering, accounting, medicine, and law define minimum professional requirements. Nigeria imposes quotas on expatriate employment based on the issued capital of firms. Quotas are especially strict in the oil and gas sector. Oil companies must hire Nigerian workers unless they can demonstrate that particular positions require expertise not found in the local workforce. Positions in finance and human relations are almost exclusively reserved for Nigerians; certain geoscience and management positions may be filled by expatriates with the approval of the National Petroleum Investment and Management Services (NAPIMS) agency. Each oil company must negotiate its expatriate worker allotment with NAPIMS.

INVESTMENT BARRIERS

Under the Nigerian Investment Promotion Commission (NIPC) Decree of 1995, Nigeria allows 100-percent foreign ownership of firms outside the petroleum sector. Investment in the petroleum sector is limited to existing joint ventures or production-sharing agreements. Foreign investors may buy shares of any Nigerian firm except firms on a “negative list” (such as manufacturers of firearms, ammunition, and military and paramilitary apparel). Foreign investors must register with the NIPC after incorporation under the Companies and Allied Matters Decree of 1990. The decree prohibits nationalization or expropriation of a foreign enterprise except when necessary to protect the national interest.

Despite efforts to improve the country’s investment climate, disincentives to investing in Nigeria continue to plague foreign entrepreneurs. Potential investors must contend with poor infrastructure, complex tax administration procedures, confusing land ownership laws, arbitrary application of regulations, corruption, and extensive crime. The sanctity of contracts is often violated, and Nigeria's court system for settling commercial disputes is weak and sometimes biased. Foreign oil companies are under significant pressure to increase procurement from indigenous firms. NAPIMS has set a target of 40 percent local content for oil-related projects by 2005 and 60 percent by 2010. It is not clear whether this local content target will be based on the value of a contract or the nature of the goods and services used, or whether partnering with a Nigerian firm will be sufficient, regardless of the origin of equipment or raw materials.

The government has increased its efforts to eliminate financial crimes such as money laundering and advance-fee fraud (or "419 fraud," named after the relevant section of the Nigerian Criminal Code). With the encouragement and cooperation of U.S. law enforcement agencies, the Nigerian government is now prosecuting more "419" perpetrators. But fraud, theft, and extortion remain rampant.

International monitoring groups routinely rank Nigeria among the most corrupt countries in the world. While sales of U.S. goods and services to public-and private-sector enterprises are not restricted, some U.S. suppliers believe they lose sales when they refuse to engage in illicit or corrupt behavior. Other U.S. exporters say Nigerian businessmen and officials understand that U.S. firms must adhere to the U.S. Foreign Corrupt Practices Act, and believe that the law's restrictions help minimize their exposure to corruption.

ELECTRONIC COMMERCE

The growth of electronic commerce and telecommunications in Nigeria, albeit from a low base, offers opportunities for the provision of U.S. products and services. While there are no trade restrictions against such U.S. services, the high technology industry suffers from the same constraints affecting other industries.

NORWAY

TRADE SUMMARY

The U.S. trade deficit with Norway was $4.9 billion in 2004, an increase of $1.2 billion from $3.8 billion in 2003. U.S. goods exports in 2004 were $1.6 billion, up 9.4 percent from the previous year. Corresponding U.S. imports from Norway were $6.5 billion, up 24.9 percent. Norway is currently the 51st largest export market for U.S. goods. U.S. exports of private commercial services (i.e., excluding military and government) to Norway were $1.6 billion in 2003 (latest data available), and U.S. imports were $1.4 billion. The stock of U.S. foreign direct investment (FDI) in Norway in 2003 was $8.3 billion, up from $6.3 billion in 2002. U.S. FDI in Norway is concentrated largely in the mining and manufacturing sectors.

INDUSTRIAL TRADE POLICIES AND PRACTICES

Norway, with Switzerland, Iceland and Liechtenstein, is a member of the European Free Trade Association (EFTA). EFTA members, except Switzerland, participate in the European Union (EU) single market through the European Economic Area (EEA) accord. Norway grants preferential tariff rates to EEA members. As an EEA signatory, Norway assumes most of the rights and obligations of EU member states. The principal exception is in the agricultural sector, which the EEA accord does not cover.

Norway maintains a liberal and open trade and investment regime with respect to industrial products, but its agricultural sector remains highly protected. Some of Norway's trade restrictions are more severe than those of the EU, such as non-tariff barriers related to labeling and approval for agricultural goods produced through bioengineering. As a general matter, Norway has implemented or is in the process of implementing most EU trade policies and regulations. U.S. exports to Norway therefore face many of the same trade and investment barriers that limit U.S. access to the EU, such as the ban on hormone-treated meat products. As a non-EU member, Norway's ability to influence EU decisions is limited.

Norway's market, except for agricultural products and processed foods, is generally transparent and open. Norway has continued, on a unilateral basis, to dismantle import tariffs on industrial products. The average most-favored-nation (MFN) tariff on non-agricultural products has fallen from 2.3 percent in 2000 to 0.7 percent in 2003. About 94 percent of industrial tariff lines are currently duty free.

Many of Norway's standards are harmonized with the EU. Few technical standards exist except in telecommunications equipment, although there are stringent regulations for chemicals and foodstuffs. No country of origin labeling is required.

AGRICULTURE TRADE POLICIES AND PRACTICES

Though it accounts only for about one percent of Gross Domestic Product (GDP), Norway maintains strict protections for agriculture that shelters the sector from global competition. As justification for these protective policies, Norway emphasizes the importance of "non-trade concerns" – food security, environmental protection, rural employment and the maintenance of human settlement in sparsely populated areas.

Agricultural Tariffs

Norway bound its tariffs for agricultural commodities in 1995 as part of its commitments in the World Trade Organization (WTO). Tariffication of agricultural non-tariff barriers as a result of the Uruguay Round led to the replacement of quotas with higher product tariffs. Although Norway is only 50 percent self-sufficient in agricultural production, it maintains a protective system that assures domestic producers – farmers and the food processing industry – have little competition until domestic production is consumed. Domestic agricultural markets are protected by high tariffs on products grown in-country. Tariff rates on agricultural products currently average about 38 percent – in comparison to less than one percent for non-agricultural products – and can range up to several hundred percent.

Domestic agricultural shortages and price surges have been countered by temporary tariff reductions. Lack of predictability of tariff adjustments and insufficient advance notifications – generally only 2-5 days before implementation – favor nearby European suppliers and make imports from the United States, especially of fruits, vegetables, and other perishable horticultural products, very difficult. For a number of processed food products, tariffs are applied based on their recipes, requiring the Norwegian importer to provide a detailed disclosure of product contents. Many exporters to the Norwegian market refuse to give all requested details and their products are, as a result, subjected to maximum tariffs.

Tariff-Rate Quotas

Norwegian tariff-rate quotas are divided into two categories – minimum access quotas and Generalized System of Preferences (GSP) quotas. Tariff-rate quotas exist for grains and a number of horticultural products. In July 2001, Norway also implemented auction quotas for grain and other carbohydrate feed. All quotas are traded at auctions held by the Norwegian Agricultural Authority, a Ministry of Agriculture agency that controls all agricultural imports.

Interest in the quotas among Norwegian importers is limited, except for grain, despite the substantial reductions in duties for some products. Compared with domestic consumption and production, the quotas are very small. Most of the interest in Norway's quota auction comes from smaller importers who use their quotas for niche products or from large farmer-owned companies working to inhibit competition to their own domestically produced products.

Auction participation costs little and those who secure a quota do not have to import. Although about 98 percent of the quotas each year are sold on these auctions, only 30-40 percent of the quotas auctioned are usually filled through imports. There is no system to reallocate unused import quotas, hindering foreign exporters seeking access to the Norwegian market for these products. In 2002, actual within-quota imports averaged only 33 percent of the quotas sold in the auction, despite the fact that within-quota duties were only one-third of the ordinary tariff. The figure for 2003 is higher – 57 percent – but was skewed by an unusually high requirement for pork imports.

On July 1, 2003, Norway committed to reduce the minimum access quota duty by as much as 25 percent for bovine, swine, chicken, turkey and fowl meat, butter, and eggs. This means that the in-quota duty for these products will only be about 28 percent of ordinary duty. The reductions are pursuant to an agreement between Norway and the EU under the EEA agreement.

Raw Material Price Compensation

Though Norway uses high import tariffs to protect domestic commodities from foreign competition, the situation is more complex for certain processed goods. Although the EEA does not generally apply to agricultural products, it includes provisions on raw material price compensation that are meant to increase trade in processed food. Norway has a special agreement with the EU within the EEA that grants some EU processed food products a preferential duty. In 2003, the agreement extended coverage to bread and baked goods, breakfast cereals, chocolate and sweets, ice cream, pasta, pizza, soups, and sauces. The annual turnover in this sector in Norway is $ 3.36 billion, including the beverage industry. In 2003, the import of these products totaled $61 million. This scheme disadvantages U.S. exporters in the Norwegian market for the covered processed foods.

Norway also maintains a price reduction scheme that includes subsidies for using certain domestically produced raw materials in processed foods. Products for which such subsidies are paid include chocolate, sweets and ice cream (for milk and glucose), and pizza (for cheese and meat). The purpose of the system is to help compensate domestic food processing industry for high domestic raw material costs.

EU-Based Regulations

In addition to its own requirements related to the import of food products, Norway has generally implemented EU regulations since 1999. Some EU regulations that Norway has adopted inhibit trade, e.g., EU regulations on veterinary control of animals and animal products requiring that meat products entering the country come from an EU-approved plant and be accompanied by the necessary certificates. The importer in Norway must be registered and notify authorities twenty-four hours in advance for plants and thirty days in advance for animals of the arrival of any shipment. Except for fish products, shipments must enter through either Oslo harbor or Oslo airport. Twenty entrance locations exist for fish products. Norway also implements EU regulations that bar imports of meat from animals treated with growth hormones.

Agricultural Biotechnology Products

Norway's strict limitations on imports of agricultural biotechnology products have hit U.S. producers particularly hard. Before 1996, when the limitations took effect, U.S. exporters usually supplied 60 percent to 80 percent of the Norwegian soybean market. As a result of the limitations, the entire market has been lost. Norwegian soybean imports in 2003 were 465,000 tons, valued at $111 million, all of which was sourced from Brazil.

Norway's restrictions on agricultural biotechnology products are more severe than the EU's with respect to allowable content and labeling, though Norway is evolving toward adopting EU standards. Norway has implemented EU Directive 90/220 on deliberate release into the environment of agricultural biotechnology products, but also maintains more stringent regulations that require approval for marketing products already approved in other EEA countries.

Under the authority of Norway's 1993 Gene Technology Act, the government may ban the import of agricultural biotechnology products based on several criteria, including ethical issues, sustainable development, and social justification. To date, Norway has only approved four agricultural biotechnology products for import: one type of tobacco plant – grown only in France – and three types of dried, cut carnations grown in greenhouses. Norway has rejected fourteen biotech products approved for use in the EU.

Before approval of an agricultural biotechnology product – even if the product does not require labeling – a health risk assessment must be conducted according to Norwegian guidelines for assessments of novel foods. Norway's guidelines are based on EU standards, but Norway generally interprets and applies the guidelines more broadly (e.g., by liberal interpretation of the possible "unintended effects" of bioengineering) than does the EU.

In October 2004, Norway slightly relaxed its "zero tolerance" policies on agricultural biotechnology products. Norwegian environmental and food safety authorities raised the limit for the "unintentional" presence of material derived from biotechnology in foodstuffs from zero to 0.9 percent. The change paves the way for U.S. "identity preserved" agricultural products, with inadvertent content of 0.9 percent or less, to return to the Norwegian market. However, food products that contain intentional content are still banned.

The Norwegian Food Law of 1997 governs the labeling of agricultural products derived from biotechnology. Norway's new Food Safety Authority (NFSA) currently exercises responsibility for product labeling. Norwegian law requires that all agricultural biotechnology products be labeled, whether or not their properties or characteristics differ from those of comparable conventional food products. Current regulations require that products must be labeled whenever more than 2 percent of any *ingredient* is derived from biotechnology. These labeling standards are stricter than the EU's, which require labeling when more than one percent of the *entire product* contains material derived from biotechnology. However, the NFSA announced in October 2004 that it proposes to conform Norway's labeling regulations to the EU's scheme. The NFSA is conducting a series of hearings on the proposal that should lead to a final decision in 2005.

Taxes and Fees

Norway's internal tax system on agricultural products – various inspection and control levies and taxes – is complex and difficult for potential exporters to navigate. An example is the special inspection fee imposed on U.S. wheat from autumn 2000 until February 2004, rendering U.S. wheat noncompetitive in the Norwegian market. The special fee was directed at wheat and rye imports from countries affected by fungal diseases. The 1.8 percent control fee translated into approximately $3.00 per ton, or U.S. $ 75,000 for a shipment of 25,000 metric tons of wheat. The U.S. had supplied food wheat to Norway for years, but imports from the U.S. practically disappeared when the fee was imposed. The NFSA lifted the fee in February 2004, but did not bring the repeal of the fee to the attention of Norwegian grain importers or American wheat exporters. The manner in which the fee was lifted – an obscure reference in a long list of NFSA actions – also raises transparency issues.

Limited Competition

The spirits and wine retail market in Norway is controlled by a government monopoly, Vinmonopolet. There are 188 Vinmonopolet stores throughout Norway. Spirits and wine sales through ordinary retail stores are not allowed. Gaining approvals to include wines and other alcoholic beverages on Vinmonopolet's retail list is cumbersome, limiting the variety of U.S. wines available to Norwegian consumers. An approved importer/agent and distributor are necessary to enter the market.

Subsidies

Norwegian farming has been highly subsidized and protected for years. This has occasionally contributed to surplus production in excess of domestic demand. However, Norwegian farm production policy has focused on national food self-sufficiency and providing incentives for farmers to remain in sparsely-populated areas of the country, rather than exports. Surpluses, at prices much higher than international price levels, have been disposed of via official government subsidies or producer-financed subsidies. Of the total export subsidies in 2001, only 13 percent were direct support and 87 percent were producer-financed. Outlays for agricultural export subsidies have decreased significantly over the last several years but remain substantial for dairy products.

GOVERNMENT PROCUREMENT

Norway is a signatory to the WTO Government Procurement Agreement (GPA). In addition, under the EEA, Norway implemented EU legislation on government procurement on January 1, 1994. Norway's procurement procedures are non-discriminatory and based on open, competitive bidding for government procurement above certain threshold values. A similar set of national rules applies to public contract tenders below these thresholds. Exceptions for defense procurement leave "gray area" for items such as rescue helicopters that can also be used in military operations. Although disputes may be settled by the European Surveillance Authority (ESA) or by the courts, the process can be unduly lengthy.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Norway is party to key international agreements for the protection of property rights, such as the Paris Convention for the Protection of Industrial Property, the Berne Copyright Convention, the Universal Copyright Convention of 1952, and the Rome Convention. It has notified its main intellectual property laws to the WTO. Norway's intellectual property statutes cover the major areas referred to in the TRIPS Agreement.

The chief domestic statutes governing intellectual property rights include: the Patents Act of December 15, 1967, as amended; the Designs Act of March 14, 2003; the Copyrights Act of May 12, 1961, as amended; the Layout-design Act of June 15, 1990, as amended; the Marketing Act of June 16, 1972; and the Trademarks Act of March 3, 1961, as amended. The above legislation also protects trade secrets and industrial designs, including semiconductor chip layout design. As an EEA member, Norway has implemented the 2002 EU Copyright Directive.

The patent office (Styret for det Industriale Rettsvern) grants patents for a period of 20 years (Acts of June 8, 1979, and May 4, 1985). However, Norway adopted a product patent protection system for pharmaceuticals in 1992, much later than most other European nations. Pre-1992 pharmaceuticals are covered only by process patents. Over 80 percent of prescription drugs currently sold in Norway are covered by the old process patent system.

As in other European countries, internet piracy and cable/satellite decoder and smart card piracy have risen in Norway. Broadband internet is used widely, making peer-to-peer downloads of music and video easy and common. Encoding groups that release early copies of new motion pictures on the internet are problematic. "Fee for download" systems are not generally available in Norway, limiting opportunities for consumers who wish to pay honestly to download copyrighted material.

Legislation is scheduled to be introduced in 2005 to combat internet piracy, which has prompted a significant upsurge in Internet downloads of copyrighted music and video in advance of the anticipated ban. Television and cable companies are active in combating decoder and smart card piracy. Norwegian authorities and private organizations are attempting to raise public awareness of Internet and video piracy, for example running anti-pirating advertisements in movie theaters prior to screening.

Counterfeit and pirated goods are not commonly available in Norway, but there is technically no ban on the importation of pirated goods per se. The trademark or copyright holder must obtain a court order and have the case referred to the police before customs authorities will take action to stop entries of illegal pirated goods. This significant gap in the intellectual property legal regime allows counterfeiters and IPR pirates to use Norway as a "gateway" to third countries, importing illicit goods, paying applicable import duties, and reshipping the goods to EU nations. For example, significant numbers of pirated DVDs from Russia and the Far East are believed to have transited Norway to the EU.

Law enforcement is reasonably effective, helping limit the extent of piracy and counterfeiting. Norwegian police and judicial authorities are generally committed to taking action against piracy and intellectual property right infringement, to the extent authorized by Norwegian law. Police authorities are aware of such problems as the "gateway" gap and are actively working to address them.

SERVICES BARRIERS

Financial Sector

In 2003, Norway repealed a requirement that an investor – foreign or domestic – obtain permission from the Ministry of Finance before purchasing more than 10 percent of the equity of a Norwegian financial institution. Current regulations require that the Norwegian Financial Supervisory Authority grant permission for ownership levels that exceed certain thresholds. The Authority assesses the acquisitions to ensure that prospective buyers are financially stable and the acquisition does not unduly limit competition. The Authority applies national treatment to non-bank foreign financial groups and institutions, but applies nationality restrictions to bank ownership. At least half the members of the board and half the members of the corporate assembly of a financial institution must be nationals and permanent residents of Norway or another EEA nation. Effective January 1, 2005, there will be no ceiling on foreign equity in a Norwegian financial institution, provided the Authority has granted a concession.

The Finance Ministry has abolished restrictions on the establishment of foreign financial institutions, including banks, mutual funds, and others. Norway grants branches of U.S. and other foreign financial institutions the same treatment as domestic institutions.

Telecommunications Sector

In 1998, Norway began to liberalize the former monopoly of the main provider of telecommunications services – Telenor – on fixed line voice services, infrastructure, and telex services. Telenor was partially privatized in December 2000, leaving the government with a stake of 78 percent. In July 2003, the state sold an additional 270 million shares of Telenor to private and institutional investors, reducing the state's share to 62.6 percent. Though its monopoly over telecommunications services has ended, Telenor still maintains exclusive control over fixed line infrastructure and charges consumers a monthly usage fee even if they choose an alternative phone service provider.

Equipment that has not been tested and certified under the EEA's common technical regulations must be type-approved by the Norwegian telecommunications authority. The Norwegian government has said that this takes about six weeks under normal procedures. In the past, U.S. companies have reported that such approval is slow and costly for companies offering new products.

INVESTMENT BARRIERS

Norway welcomes foreign investment as a matter of policy and grants national treatment to foreign investors. There are no general restrictions on foreign investment in the manufacturing sector, though foreign ownership continues to be restricted or prohibited in some other sectors, including financial services, mining, hydropower, property acquisition, and areas considered politically sensitive.

Foreign investors are not required to obtain government authorization before buying shares of Norwegian corporations. Legislation that formerly required both foreign and Norwegian investors to notify the Ministry of Industry and Trade if their holdings of a company's equity capital exceeded certain threshold levels was repealed in 2002. In October 2002, the government also abolished a seven percent tax on investments that applied to purchases of business assets. Norwegian and foreign firms alike complained that the investment tax and its complex accompanying regulations impeded asset acquisitions.

Foreign companies are required to obtain concessions for the acquisition of rights to own or use various kinds of real property, including forests, mines, tilled land, and waterfalls. However, foreign companies need not seek concessions to rent real estate, provided that the rental contract is made for a period not exceeding ten years.

In the offshore petroleum sector, Norwegian authorities encourage the use of Norwegian goods and services. The Norwegian share of the total supply of goods and services has remained approximately fifty percent over the last decade. Though the Norwegian government had in the past shown a strong preference for Norwegian oil companies in awarding the most promising oil and gas exploration and development blocks, foreign oil companies report no discrimination in recent licensing rounds. Norway has implemented EU directives requiring equal treatment of EEA oil and gas companies. However, Norway's concession process still operates on a discretionary basis with the government awarding licenses based on subjective factors rather than strictly according to competitive bidding.

Foreign and domestic investors are barred by law from investing in industries monopolized by the government – postal services, railways, and the domestic production and retail sale of alcohol. The government rarely allows foreign investment in hydropower production, and such investments – if approved – are limited to 20 percent of equity. However, Norway has fully opened the electricity distribution system to foreign participation.

State Ownership and Control of Commercial Enterprises

The government continues to play a strong role in the Norwegian economy through its ownership or control of many of the country's leading commercial firms. The public sector accounts for nearly sixty percent of GDP (compared to about thirty-four percent in the United States). Around 100 enterprises are either fully or partly owned by the central government. Central or local authorities own about 35 percent of the companies listed on the Oslo Stock Exchange, and approximately forty percent of the stock exchange's capitalization at the end of 2003 was in government hands.

The government's April 2002 "White Paper" called for reducing and improving State ownership in the economy. Norway has taken steps over the last several years to implement the policy, partially privatizing some of the country's leading firms. The state oil firm – Statoil – was partially privatized in June 2001, when 19.8 percent of the firm was sold in an initial stock offering. The state's share of Statoil has since fallen to 76.3 percent. A majority share (56.2 percent) of Norway's second largest petroleum firm and largest aluminum producer – Norsk Hydro – is now in private hands, though the government retains "negative control" as the company's largest single shareholder. Prompted by EU calls for liberalization, Norway's Petroleum and Energy Ministry dismantled its gas sales monopoly – Gassforhandlingsutvalget (GFU) – in 2002. All gas producers and operators on the Norwegian continental shelf are now free to negotiate gas sales contracts on an individual basis.

OTHER SECTORAL POLICIES

Competition, Acquisition, and Takeovers

New and tougher legislation governing competition went into effect in Norway on May 1, 2004, replacing the 1993 competition law. The previous law only provided for "intervention" against abuse of dominance – a method appropriate for minor offences, but does not provide sufficient deterrence to serious violations. The new legislation introduces competition infringement fees. The Norwegian Competition Authority (NCA) is now authorized to impose fees through a non-criminal procedure. These fees – the size of which would depend on a variety of factors including company turnover and severity of offense – will be much higher than current Norwegian anti-competition fines and comparable to those charged in the EU. Companies planning mergers are now obliged by law to report to the NCA, and the NCA is empowered to halt merger plans should their implementation significantly weaken competition. The NCA has moved quickly to assert its new authority, finding in December 2004 that the SAS air carrier group abused its dominant market position and engaged in predatory behavior on a particular domestic air route. NCA has warned that it may fine SAS up to 20 million Norwegian kroner (about $3.5 million).

Pharmaceuticals

Foreign pharmaceutical firms continue to experience difficulties in the Norwegian market. Transparency on pricing and reimbursement decisions and recommendations is lacking. U.S. pharmaceutical products often face lengthy delays in securing approval for their products' inclusion in the state health care reimbursement scheme. Reimbursement and approval decisions are complex and political, with Parliament making final decisions as part of its budget process.

The Norwegian Association of Pharmaceutical Manufacturers, which includes U.S. pharmaceutical firms, has complained about Norway's inadequate implementation of EU directives on transparency of measures regulating medicinal products for human use. Although Norway complies with the letter of EU requirements that reimbursement applications be acted on within 180 days, Norwegian authorities often reject applications as the period expires, giving them an unlimited amount of time to consider applications once appealed.

U.S. pharmaceutical manufacturers cite Norway's total prohibition of supplying product information – ranging from advertising to scientific data – to consumers as a barrier to market entry and expansion. Consumers are not fully informed about pharmaceutical innovations, dampening demand for new products and sometimes delaying consumer access to the latest medicines. Drug prices and consumption of medicines in Norway are below European averages.

OMAN

TRADE SUMMARY

The U.S. trade deficit with Oman was $88 million in 2004, a decrease of $284 million from $372 million in 2003. U.S. goods exports in 2004 were $330 million, up 2.3 percent from the previous year. Corresponding U.S. imports from Oman were $418 million, down 39.8 percent. Oman is currently the 83rd largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Oman in 2003 was $358 million, up from $193 million in 2002.

After consultations with Congress, the United States began Free Trade Agreement (FTA) negotiations with Oman in March 2005. An important objective of these negotiations is the removal of trade barriers for U.S. goods and services providers. The FTA with Oman is the next stage in achieving President Bush's vision for a Middle East Free Trade Area by 2013.

IMPORT POLICIES

Tariffs

As a member of the Gulf Cooperation Council (GCC), Oman applies the GCC common external tariff of five percent for most products, with a limited number of GCC-approved country-specific exceptions. Oman's exceptions to the common external tariff include 100 percent tariff rates on pork and alcohol products, 100 percent on cigarettes above the 820 count, a 25 percent duty on edible oils sold in retail pack, plus a few protective duties on a limited number of products such as dried lemon-bananas, dates and ghee.

Import Licensing

In Oman, companies that import goods must be registered with the Ministry of Commerce and Industry, but are no longer required to be 51 percent Omani-owned. Importation of certain classes of goods, such as alcohol, livestock, poultry and their respective products, firearms, narcotics and explosives, requires a special license, and media imports are subject to censorship.

Documentation Requirements

Except for food products, an authentication procedure is not required if the importing company has an existing agency agreement with a U.S. exporter. In 1996, Oman began the process of simplifying customs clearance documentation to expedite the flow of goods and promote its ports and airports. However, only Omani nationals are permitted to submit documents to clear shipments through customs.

Customs Valuation

Oman implemented the Customs Valuation Agreement when it joined the WTO in 2000, and is still working on further enhancing its customs valuation system.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Oman has not yet revised its shelf-life requirements to meet its World Trade Organization (WTO) commitments. In its accession to the WTO, Oman committed to eliminate mandatory shelf-life standards for shelf-stable foods, establish regulations and procedures in line with international norms for highly perishable refrigerated food products, and replace remaining shelf-life requirements with a science-based regulatory framework, but it has not yet done so. In 2000, Oman announced by Royal Decree its intention to adopt internationally recognized Codex standards for the labeling of prepackaged food. Oman still maintains a ban on imports of U.S. beef and beef products that is not in accordance with international guidelines, but did remove its temporary ban on imports of U.S. poultry and poultry products in 2004.

GOVERNMENT PROCUREMENT

Oman provides a 10 percent price preference to tenders that contain a high content of local goods or services, including direct employment of Omanis. The government considers the quality of a product or service and support, as well as cost, in evaluating bids. For most major tenders, Oman typically invites firms either already registered in Oman or preselected by project consultants. To increase transparency in the tendering process, Oman advertises tenders in the local press, international periodicals, and on the tender board's website. Also, bidders are now requested to be present at the opening of bids, and interested parties may view the process on the tender board website. In the past, bidders' costs have sometimes increased dramatically when award decisions were delayed, sometimes for years, or when bidding was reopened with modified specifications and, typically, short deadlines. Oman is known to have an offset program only with the United Kingdom. Offsets are not standard adjuncts to government contracts and have not been associated with any U.S. defense transactions, whether commercial or foreign military sales. As part of its WTO accession, Oman has also committed to begin negotiations to join the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

An independent government-owned company – Export Credit Guarantee Agency – provides export payment guarantees and insurance below local-market interest rates, protecting Oman's few non-petroleum exporters from payment problems on transactions. These guarantees are subject to approval of buyer and country risk. The Omani Ministry of Commerce and Industry also offers soft loans to projects in the industrial, tourism, health, education, and other service-related sectors. Formerly interest-free, these loans now bear about a four percent interest rate.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

As part of its WTO accession, Oman adopted derogations to the GCC patent law to comply with its obligations under the TRIPS Agreement. In 2000, Oman amended its copyright protection law, and in 1999 enacted decrees banning the local sale of pirated videocassettes, sound recordings, and computer software. Enforcement of the copyright protection decree by the Ministry of Heritage and Culture, the Ministry of Commerce and Industry, and the Royal Oman Police has been largely effective, as once plentiful pirated video and audiotapes and computer software have largely disappeared from local vendors' shelves. Nonetheless, under-the-counter sales of unauthorized software and DVDs persist in various locations, and authorities continue to grapple with effective enforcement measures against such sales. In late October 2003, 16 Omani companies signed the Business Software Alliance (BSA) Code of Ethics. The Code of Ethics declares that the signatories would neither commit nor tolerate the manufacture or use or distribution of unlicensed software and would only supply licensed software to customers. According to local satellite television representatives, the Ministry of Commerce is staging sporadic raids on unlicensed distributors of pirated satellite signals in response to industry complaints. In 2000, Oman updated its trademark law as well as issued a new law on geographical indications. However, as the implementing regulations to these new and updated laws have yet to be promulgated, it is unclear if they comply with Oman's with obligations under the TRIPS Agreement.

SERVICES BARRIERS

Insurance

As part of its WTO commitments, Oman is allowing foreign-ownership of up to 100 percent in most insurance sectors, except for brokerage companies that are restricted to a 70 percent limit.

Banking

Omani laws permit the operation of foreign banks. Although Oman barred entry of new non-GCC banks in the past on the grounds of excess capacity in the sector, it has recently licensed the State Bank of India to commence operations. Oman does not permit representative offices or offshore banking.

Agent and Distributor Rules

Since 1993, Oman has permitted an importer to bring in goods without paying a commission to a registered agent, if the goods are imported through an Omani port or airport. However, in practice, it is difficult for a foreign firm to sell directly to the government without an Omani agent identifying and bidding on tender opportunities. In addition, termination of an agency agreement can be difficult, as a supplier may not unilaterally terminate an agency agreement without justifiable cause. Since September 1996, Oman has registered nonexclusive agency agreements. Most recently, Oman has attempted to address unemployment through mandating local hire quotas, limiting distribution from food wholesale centers to Omani nationals, and restricting small grocery food retail sales to businesses owned and operated by Omani nationals.

INVESTMENT BARRIERS

In September 2003, Oman amended its tax law and extended the national tax treatment (i.e., a corporate tax rate of 12 percent) to all Omani and GCC companies regardless of the percentage of foreign ownership. Taxes on branches of foreign-owned companies remained at 30 percent. In addition, Oman exempted companies in the education, health, and aquaculture sectors from taxes. Foreign airlines are now tax-exempt subject to reciprocal agreement. The new tax exclusion also extends to capital gains on disposal of securities listed on the local stock market as well as joint investment funds. Oman frequently reviews and modifies its laws and procedures to attract increased foreign investment. Majority foreign-owned investments are eligible for tax-holidays of up to ten years, a benefit also enjoyed by Omani firms. The tax-holiday waives corporate income tax, as well as customs taxes on goods imported for business purposes under certain categories of projects. Oman now permits 100 percent foreign-ownership on a case-by-case basis with the approval of the Minister of Commerce and Industry, although only a handful of companies have taken advantage of this opportunity. None of the companies listed on the Omani stock exchange is 100 percent foreign-owned.

In Oman, foreigners are permitted to purchase shares on the Muscat Securities Market (MSM). As of midyear 2004, approximately 17.9 percent of the MSM's total market capitalization was foreign-owned.

PAKISTAN

TRADE SUMMARY

The U.S. trade deficit with Pakistan was $1.1 billion in 2004, a decrease of $624 million from $1.7 billion in 2003. U.S. goods exports in 2004 were $1.8 billion, up 114.7 percent from the previous year. Corresponding U.S. imports from Pakistan were $2.9 billion, up 13.6 percent. Pakistan is currently the 49th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Pakistan in 2003 was $1.1 billion, up from $849 million inn 2002.

IMPORT POLICIES

Since 1998, Pakistan has progressively and substantially reduced tariffs. This effort culminated in June 2002 with the establishment of four maximum import tariff bands of 25 percent, 20 percent, 10 percent, and 5 percent. Generally, Pakistan's applied tariffs are below WTO-bound commitments, and the weighted average applied tariff is currently 16.0 percent, down from 56 percent in 1994. The tariff on most consumer goods was reduced to 25 percent, for most intermediate goods to 10 percent, and for most raw materials to 5 percent. In November 2000, Pakistan reached an agreement with the WTO Balance of Payments Committee to phase out quantitative restrictions on textile imports. The government removed all textile products from its "negative list," including woven cotton fabrics, woven synthetic fabrics, bed linens, curtains, certain knitted fabrics and apparel items, tents, carpets, and textile floor coverings. Many of these items are key Pakistani export products. All textile products can now be imported into Pakistan, although the tariff on certain synthetic fibers (scheduled to expire in 2008) remains relatively high.

Pakistan's trade policy in 2004 continued to ban the import of 30 items, mostly on religious, environmental, security, and health grounds. Effective July 1, 2004, Pakistan reduced duties on imported automobiles to between 50 percent and 100 percent from the previous range of 75 percent to 150 percent. The government exempted all domestically produced pharmaceutical-related inputs from its General Sales Tax (GST), a value-added tax, through a Statutory Regulatory Order issued in April 2002. Imported pharmaceutical inputs subject to a 10 percent customs duty rate are also exempt from payment of GST. This includes most, but not all, imported pharmaceutical inputs. In FY 2002, the government reduced duties on instant print film and instant print cameras to 10 percent from the 30 percent to 200 percent range in order to eliminate the incentive to smuggle subject to the higher rates.

The government reserves the power to grant sector-specific duty exemptions, concessions, and protections under Statutory Regulatory Orders (SROs). In recent years, the use of SROs has decreased. SROs and other trade policy and regulatory documents are published on the Central Board of Revenue’s website, www.cbr.gov.pk.

In January 2000, the government began implementing a transactional valuation system pursuant to which 99 percent of import valuation is based on invoice value, in accordance with the WTO's Customs Valuation Agreement. Currently, about 90 percent of imports are assessed duties pursuant to the transactional valuation system. However, a number of traders in food and non-food consumer products report experiencing irregularities and deviations in the application of that system.

STANDARDS TESTING, LABELING, AND CERTIFICATION

The Pakistan Standards and Quality Control Authority (PSQCA) is the national standards body. As of June 30, 2003, PSQCA had established over 21,000 standards for agriculture, food, chemicals, civil and mechanical engineering, electronics, weights and measures, and textile products, including 15,500 ISO standards, an increase of 1,000 new ISO standards since 2003. However, no other new standards were approved in 2004. Testing facilities for agricultural goods are inadequate and standards are inconsistently applied, which industry contends has resulted in occasional discrimination against U.S. farm products. Generally, however, U.S exporters have not reported problems due to the restrictive application of sanitary, phytosanitary or environmental standards. Pakistan accepts most U.S standards.

Pakistan lacks biosafety guidelines for certain bioengineered agricultural goods, a policy gap that appears to have impeded introduction of U.S. bioengineered products that could significantly boost Pakistan’s agricultural productivity, rural incomes, and overall GDP. Pakistan’s Biosafety Commission has compiled draft biosafety guidelines, but Pakistan’s Ministry of Environment has delayed approval of the guidelines for four years.

GOVERNMENT PROCUREMENT

Pakistan is not a member of the WTO Agreement on Government Procurement and has not made a commitment to begin accession negotiations. Work performed for government agencies, including the purchase of imported equipment and services, is often awarded through tenders that are publicly announced or issued to registered suppliers. The government established the Public Procurement Regulatory Authority in May 2002 to strengthen procurement practices. International tenders now are publicly advertised and sole source contracting using company-specific specifications has been eliminated. There are no “buy national” policies.

Political influence on procurement decisions, charges of official corruption, and long delays in bureaucratic decision-making have been common in the past. Investors have reported instances when the government used the lowest bid as a basis for further negotiations, rather than accepting the lowest bid under its tender rules. Occasionally, the government reportedly has "disqualified" experienced and technically proficient bidders otherwise qualified under tender specifications. The government does not invite private tenders for the transportation of crude oil and requires all transport of crude oil to be conducted by the state-owned Pakistan National Shipping Corporation.

EXPORT SUBSIDIES

Pakistan actively promotes the export of Pakistani goods with measures such as tariff concessions on imported inputs and income and sales tax concessions. Subsidies in FY2004 were confined mostly to wheat and totaled roughly $76 million, according to the government sources. The government also provides freight subsidies to some products and these subsidies totaled close to $17 million in FY2004. On January 5, 2005, the government announced that its Export Development Fund would provide a 25 percent air and sea freight subsidy for leather garment exports for calendar year 2005. Pakistan established its first Export Processing Zone (EPZ) in Karachi in 1989, with special fiscal and institutional incentives available to encourage the establishment of exclusively export-oriented industries. The government subsequently established additional EPZs in Risalpur, Gujranwala, and Sialkot in Punjab Province and Saindak and Duddar in Balochistan Province. Principal government incentives for EPZ investors include an exemption from all federal, provincial, and municipal taxes for production dedicated to exports, exemption from all taxes and duties on equipment, machinery, and materials (including components, spare parts and packing material), indefinite loss carryforward, and access to Export Processing Zone Authority "One Window" services, including facilitated issuance of import permits and export authorizations.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Pakistan’s failure to adequately protect intellectual property constitutes one of its most severe barriers to trade and investment. The U.S. government had placed Pakistan on the "Special 301" Watch List every year from 1989 to 2003 due to widespread piracy, especially of copyrighted materials. Continuing IPR violations caused the U.S. Government in 2004 to move Pakistan from the Special 301 Watch List to the Special 301 Priority Watch List. In 2004, Pakistan was among the world’s leading exporters of pirated optical discs and apparel. Pakistan does not adequately enforce patents, copyrights, and trademarks due the lack of a functioning central IPR regulatory and enforcement body, an underdeveloped judicial system, and corruption.

In response to longstanding local and international criticism and the need to implement its WTO TRIPS obligations, the Pakistani Cabinet in 2004 approved legislation creating the Pakistan Intellectual Property Rights Organization (PIPRO) to consolidate authority over trademarks, patents, and copyrights in one government body. However, the legislation has not yet been approved by the parliament, and it has effectively been mothballed for many months. In addition, the Ministry of Commerce established an IPR Advisory Committee (IPRAC) with private sector and non-government organization participation. Unfortunately, IPRAC met once in January 2004 and has been dormant since that time. Although Pakistan has enacted five major new laws relating to patents, copyrights, trademarks, industrial designs and layout designs for integrated circuits in the past few years, the legislation and/or enforcement mechanisms remain lacking in several areas further described below. Pakistan is a party to the Berne Convention for the Protection of Literary and Artistic Works, and is a member of the World Intellectual Property Organization (WIPO). On July 22, 2004, Pakistan acceded to the Paris Convention for the protection of industrial property. Pakistan has not yet ratified the WIPO Copyright Treaty nor the WIPO Performance and Phonograms Treaty. A draft law concerning plant breeders' rights has not progressed because of a dispute over federal and provincial jurisdiction for the past two years.

Patents

Pakistan enacted a patent law in 2000 that protects both process patents and product patents in accordance with its WTO obligations. Under this law, both the patent-owner and licensees can file suit against those who infringe. Unfortunately, the 2002 Patent Ordinance weakened the 2000 Patent Law by eliminating use patents, restricting patent filings to single chemical entities, limiting protection for derivatives, introducing barriers to patenting biotechnology-based inventions. This generated great concern among pharmaceutical firms seeking to sell patented drugs in Pakistan. Pakistan fails to protect against unfair commercial use of test or other data. In addition, the government has authorized the sale of pharmaceuticals without requiring checks confirming that another firm does not hold an active patent on the compound. Although courts have issued injunction orders against firms licensed by the Ministry of Health, that sell drugs in violation of patent holder rights, such orders are not consistently enforced. Patent theft is exacerbated by the fact that it often takes one or two years to register drugs in Pakistan. During this registration process, the government also sets prices - often at a level that does not reflect the cost of developing the product.

Trademarks

Pakistan developed its Trademarks Ordinance in 2000, which provides for the registration and better protection of trademarks and for the prevention of the use of fraudulent marks. The ordinance has been enforced since April 2004 with the enactment of implementing rules. The government has eliminated the requirement that pharmaceutical firms label the generic name on all products with at least equal prominence as that of the brand name. Trademark infringement remains widespread.

Copyrights

According to the International Intellectual Property Association, calendar year 2003 copyright piracy rates in Pakistan stood at 95 percent for motion pictures, 100 percent for records and music, and 83 percent for business software (no figures were available for entertainment software). CD and DVD losses were estimated at $82 million. Pakistan has become a major exporter of pirated optical discs. Industry groups estimate that in 2004 there were ten firms which produced roughly 230 million illegal discs in 2004, up nearly 30 percent over 2003 levels. Industry analysts estimate that almost 90 percent of this production is exported.

This level of piracy occurs despite the current ban on the import and export of pirated materials. Pakistani law includes a maximum punishment of three years imprisonment and a fine of 100,000 rupees ($1,750). Enforcement, however, remains weak, characterized by sporadic raids at the retail level, few prosecutions, and inadequate penalties. In addition, no separate IPR enforcement bodies or IPR courts exist in Pakistan. For example, authorities have not inspected optical disk factories operating in Pakistan.

SERVICES BARRIERS

Pakistan generally permits foreign investment in services, subject to provisions including a minimum initial capital investment of $150,000. Recent changes in the Investment Policy permit foreign investors to hold up to a 100 percent equity stake and allow 100 percent repatriation of profits. This 2004 change eliminates the $300,000 minimum initial capital investment requirement in the services sector with foreign investors required to accumulate 40 percent local equity within 5 years of initial investment. In addition, the repatriation of profits is no longer restricted to a maximum of 60 percent of total equity or profits.

Investment policy also allows foreign investors in services and other non-manufacturing sectors (including international food franchises) to remit technical fees and royalties, although conditions apply. In information technology services, including software development, foreign investors may hold a 100 percent equity stake. Investors in this field are not subject to the requirements for minimum initial investment.

Telecommunications

In the telecommunications sector the government of Pakistan permits 100 percent foreign equity with a minimum foreign equity investment of $150,000 in specific services, including electronic information services, card-pay telephone services, paging services, and voice mail services. This 2004 change eliminates the previous $300,000 minimum initial capital investment requirement in the services sector with foreign investors required to accumulate 40 percent local equity within 5 years of initial investment. In addition, the repatriation of profits is no longer restricted to a maximum of 60 percent of total equity or profits. Competition among service providers is already allowed in cellular telephony. In July 2003, the government announced a telecommunications sector deregulation policy in order to comply with its WTO commitments. Implementation of this policy has ended the exclusive right of the majority state-owned Pakistan Telecommunication Company Limited (PTCL) to provide basic telephone services, and the government has issued 12 licenses to long distance telephone companies, 90 licenses to local loop regional telephone companies, and 70 licenses to wireless local loop companies. Some of these companies will commence operations in early 2005. Pakistan currently allows the cross-border provision of packet-switched data and Internet services. Roughly 70 private firms, including foreign invested companies, provide Internet services on competitive networks, and the government has issued licenses to 55 more companies. At present, the government does not issue exclusive licenses for voice-over-internet providers (VOIP). Long distance telephone license holders can also provide VOIP services.

Limitation on Foreign Films

The Government of Pakistan prohibits the importation of films that are deemed inconsistent with local religious and cultural standards. Films from neighboring India are routinely denied entry via cable transmission or video/digital media, but are widely available in pirated form.

Banking and Insurance

Pakistan improved its financial services commitments in the WTO Financial Services Agreement in December 1997. These commitments grant the right to establish new banks, as well as grandfathering acquired rights of established foreign banks and foreign securities firms. The State Bank of Pakistan (SBP, Pakistan's central bank) has changed its branch licensing policy and has eliminated restrictions on the number of branches for foreign banks. Currently, foreign banks, like local banks, have to submit an annual branch expansion plan to the SBP for approval. The SBP approves new branch openings based on the bank's net worth, adequacy of its capital structure, future earning prospects, credit disciplines, and the needs of the local population. Foreign brokers, like their Pakistani counterparts, must register with the Securities and Exchange Commission of Pakistan.

The government has opened the insurance market as one of its financial sector reforms. Government officials recently clarified that foreign investors are allowed to hold a 51 percent equity share of companies operating in the life and general insurance sectors. Foreign investors are also required to bring in a minimum of $2 million in foreign capital and raise an equal amount of equity in the local market. There are no restrictions on the repatriation of profits, and capital investment made in this sector can be repatriated with the permission of the SBP. Pakistan does not regulate insurance premiums. The government issued a new insurance law in 2000, raising capital adequacy standards and enhancing policyholder protections.

The government permits only the parastatal National Insurance Company to underwrite and insure public sector firms. Private sector firms must use the state-owned Pakistan Reinsurance Company for a minimum of 10 percent of their reinsurance requirements. Market domination in this sector may pose a substantial barrier to entry. The state-owned State Life Insurance Company holds over 80 percent of the life insurance market, while five major companies account for 78 percent of the general insurance market share.

Other Services

Foreign professionals can provide legal and engineering consultancy services with 100 percent equity participation. This 2004 change eliminates the prior requirement that Pakistanis hold 40 percent local equity for 5 years. The minimal capital requirement for these services was also reduced from $300,000 to $150,000 in 2004. A legal consultant need not be licensed to practice law in Pakistan. However, foreign lawyers may not appear in court or otherwise formally litigate cases, even if they work with local lawyers, unless licensed. The Islamabad-based Pakistan Bar Council licenses attorneys in Pakistan, and no *de jure* prohibition exists against the admission of foreign lawyers into the bar. Similarly, foreign doctors must register with the Pakistan Medical and Dental Council, and foreign engineers are required to register with the Pakistan Engineering Council in order to practice their respective professions in Pakistan.

INVESTMENT BARRIERS

Foreign investors are free to establish and own business enterprises in all sectors of the economy with the exception of five restricted areas: arms and munitions, high explosives, currency/mint operations, radioactive substances, and new nonindustrial alcohol plants. There is a minimum initial investment requirement of $300,000 in agriculture and in infrastructure and social services and a $150,000 minimum foreign equity investment requirement in certain services but no minimum investment requirement for manufacturing. Foreign ownership in agricultural investments cannot exceed 60 percent. The government's investment policy promises full repatriation of capital, capital gains, dividends, and profits with the approval of the State Bank of Pakistan. No requirements exist for technology transfer. The law provides for expropriations only upon adequate compensation, and it prohibits changes in benefits and incentives for the purpose of disadvantaging foreign investors.

The government of Pakistan has eliminated most but not all of the local content requirements that it reported to the WTO in 1995 under the Agreement on Trade Related Investment Measures (TRIMS). In 1999, Pakistan's "deletion" program (mandating the use of domestic inputs) encompassed 106 items. As of December 2004, 16 items in the auto and motorcycle industries remain. For these 16 items, Pakistan has petitioned for a three-year extension on its original December 31, 2003, deadline to eliminate all deletions. At the start of 2005, the United States and other WTO Members were still considering this request.

Although Pakistan has enacted a Monopolies and Restrictive Trade Practices Ordinance, and established a Monopoly Control Authority, parastatal firms are exempt from the provisions of this law, and regulatory oversight suffers from resource constraints. Thus, in the Pakistani market, where state-owned firms dominate several sectors, competition policy remains incomplete. The state-owned Water and Power Development Agency (WAPDA) and Karachi Electric Supply Corporation (KESC) retain control of power transmission and distribution and continue to be highly subsidized. Privatization of KESC and Pakistan Telecommunications Company, Limited (PTCL) are scheduled to begin in early 2005. Bidding for PTCL will be held in the first quarter of FY2005-2006. The government plans to transfer management control of PTCL through the strategic sale of 26 percent of its shares, and it has already issued licenses to long distance and local telephone operators, as well as to cellular and wireless local loop operators, ending PTCL's monopolies. Two private airlines compete with state-owned Pakistan International Airlines and the government permits them to fly on the most desirable routes and to undercut PIA on fares. In retail food sales, the government has used pricing in its several hundred-unit Utility Stores Corporation chain to influence prices of essential foodstuffs. Market leaders in the cement and sugar industries are alleged to have formed cartels.

The United States and Pakistan recently initiated negotiations toward a Bilateral Investment Treaty (BIT), which would provide significant protections for U.S. investors in Pakistan. An informal discussion of BIT principles was held in preparation for the first negotiating session.

ELECTRONIC COMMERCE

Although there are no trade restrictions on electronic commerce, the government blocks certain websites that it deems as conflicting with Pakistani religious and cultural norms. Electronic commerce is, however, not well developed in Pakistan. In 2002, the government enacted an Electronic Transactions Ordinance that adopted international standards and provided for the establishment of a certification authority. The Certification Authority has not yet started functioning to implement the ordinance, so companies seeking certification have had to rely on foreign certification services. There are no duties and taxes on electronic commerce in Pakistan.

OTHER BARRIERS

Businesses operating in Pakistan have repeatedly called for strengthening law and order.
Corruption and a weak judicial system remain recurrent and substantial disincentives to investment. Pakistani laws targeting corruption include the 1947 Prevention of Corruption Act, the 1973 Efficiency and Discipline Rules and, most recently, the 1999 National Accountability (NAB) Ordinance. Previously, the NAB, the Federal Investigation Agency (FIA), and Provincial Anti-Corruption Departments shared official responsibility for combating corruption. In October 2002, Pakistan's cabinet approved a National Anti-Corruption Strategy (NACS) that identified areas of pervasive corruption and recommended time-bound measures and reforms to combat corruption. The NACS also named the NAB as the sole anticorruption agency at the federal level.

Contract enforcement is difficult in Pakistan. A long-standing investment dispute between a major U.S. multinational company and a local partner has raised concerns about the sanctity of international arbitration awards under contracts between private parties. In 2004, Pakistan's

Cabinet approved Pakistan's joining the 1958 New York Convention on Recognition and Enforcement of Arbitral Awards; however, its parliament has not yet enacted enabling legislation putting it into force. Pakistan's ranking in Transparency International's Corruption Perceptions Index dropped from 92 out of 133 countries in 2003 to 129 out of 145 countries listed in 2004.

PANAMA

TRADE SUMMARY

The U.S. trade surplus with Panama was $1.50 billion in 2004, a decrease of $43 million from $1.55 billion in 2003. U.S. goods exports in 2004 were $1.8 billion, up 1.6 percent from the previous year. Corresponding U.S. imports from Panama were $316 million, up 4.8 percent. Panama is currently the 48th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Panama in 2003 was $6.5 billion, up from $5.8 billion in 2002. U.S. FDI in Panama is concentrated largely in the financial sector.

FREE TRADE NEGOTIATIONS

In April 2004, the United States and Panama began free trade negotiations, which are ongoing. A Free Trade Agreement (FTA) with Panama will be a natural extension of an already largely open trade and investment relationship. Panama is unique in Latin America, but like the United States, in that it is predominantly a services-based economy. The Panama Canal, the focal point of Panama's economy represents an important opportunity for mutual economic opportunities and growth. An FTA with Panama will also complement the goal of completing a Free Trade Area of the Americas (FTAA), increasing momentum for lowering trade and investment barriers throughout the region.

IMPORT POLICIES

Tariffs

Following its accession to the World Trade Organization (WTO) in 1997, Panama opened its markets considerably and its tariffs ranked among the lowest in Latin America, averaging just 8 percent. However, in September 1999, Panama raised selected agricultural tariffs, some of which reached the maximum amount allowed under Panama's WTO commitments. For example, Panama increased the tariff on frozen french fries from 15 percent to 20 percent. In addition, U.S. exports of fresh potatoes to Panama face an 83 percent over-quota tariff. Panama also retains a 20 percent tariff on sparkling wine and other fermented beverages, and a 40 percent tariff on still wines. In addition, Panama charges a 10 percent tax on wine products.

Non-Tariff Measures

In addition to tariffs, all imports into Panama are subject to a 5 percent transfer (or ITBM) tax levied on the CIF value, and other handling charges. Pharmaceuticals, foods, and school supplies are exempt from the transfer tax. Currently, Panama does not require import licenses on manufactured goods in the country, provided the importing entity holds a commercial or industrial license to operate in Panama.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

With certain exceptions, Panama's application of standards and certification requirements generally conforms to WTO standards. However, restrictions have been applied at times in order to protect local producers. Of particular concern has been the lack of procedural transparency by relevant Panamanian authorities in deciding whether to issue phytosanitary permits.

Panama requires that Panamanian health and agriculture officials certify individual U.S. processing plants as a precondition for the import of poultry, pork, dairy, and beef products. U.S. exporters have assisted Panamanian officials in inspecting U.S. plants, and there have been no instances of a failed inspection by a U.S. plant. However, inspections are often delayed due to budgetary constraints and the lack of personnel in the responsible Panamanian ministries. As such, it is the United States' priority to obtain Panamanian recognition of the U.S. meat inspection system in place of the current plant-by-plant approach. This effort is a primary focus of the ongoing FTA negotiations.

Panama's import licensing process is often arbitrary and non-transparent, constituting a major impediment for U.S. exporters. For example, Panamanian importers of U.S. processed potatoes have had difficulties obtaining import permits in 2003 and 2004. In one instance, arguing that U.S. processed potatoes compete directly with domestic fresh potatoes, the Panamanian government refused to issue import permits for frozen french fries, disrupting the extensive quick service restaurant industry within the country.

While importers of non-agricultural products must register them with the Ministry of Commerce and Industry before distribution or sale in Panama, procedures for registration are usually straightforward and evenly applied. There are no comprehensive labeling or testing requirements for imports, except for food and pharmaceutical products. U.S. industry is seeking a commitment from the Panamanian government to provide explicit recognition of Bourbon and Tennessee Whiskey as a trademark.

When the United States launched FTA negotiations in 2004, it simultaneously initiated a working group on SPS barriers to agricultural trade to meet in parallel with the negotiations and to work on resolution of SPS issues even after the negotiations conclude.

GOVERNMENT PROCUREMENT

Panama's government procurement regime is governed by Law 56 and managed by the Ministry of Economy and Finance (MEF). The law provides for a transparent bidding process for government contracts, but allows for exceptions, such as procurements for national defense. The Panamanian Government has generally handled bids in a transparent manner, although occasionally U.S. companies have complained of mishandling of certain procedures.

While Panama committed to become a party to the WTO Government Procurement Agreement (GPA) at the time of its WTO accession, its efforts to accede to the GPA have stalled. Although the Panama Canal Authority (PCA) has generally followed transparent and fair bidding processes, the United States has been particularly disappointed by the Government of Panama's failure to include the PCA in its accession offer. The U.S. government is currently addressing the issue of the PCA within the context of bilateral free trade agreement negotiations.

EXPORT SUBSIDIES

Panamanian law allows any company to import raw materials or semi-processed goods at a duty of three percent for domestic consumption or processing, or duty free for export production, except for sensitive agricultural products, such as rice, dairy, pork, and tomato products. Companies not already receiving benefits under the Special Incentives Law of 1986 are allowed a tax deduction of up to 10 percent of their profits from export operations through 2005.

Due to its WTO obligations, Panama revised its export subsidy policies in 1997-98. The government originally had stated its intention to phase out its Tax Credit Certificate (CAT) by the end of 2001, which was given to firms producing certain non-traditional exports. However, during the WTO Ministerial Conference in November 2001, the Government of Panama asked for and received an extension for the use of CATs. The WTO extended this waiver until December 2005, allowing exporters to receive CATs equal to 15 percent of the export's national value added. The certificates are transferable and may be used to pay tax obligations to the government, or they can be sold in secondary markets at a discount. The government has, however, become more strict in defining national value added, in an attempt to reduce the amount of credit claimed by exporters.

In addition, a number of export industries, such as shrimp farming and tourism, are exempt from paying certain types of taxes and import duties. The Government of Panama established this policy to attract foreign investment, especially in economically depressed regions, such as the city of Colon. Companies that profit from these exemptions are not eligible to receive CATs for their exports.

A new domestic subsidy called the Certificate to Foment Industry (CFI), designed to replace the CATs when they end, was signed into law by former President Mireya Moscoso on February 4, 2004. Panamanian authorities have stated that the CFI will be consistent with Panama's WTO obligations.

Other Export-Related Items

- The Tourism Law of 1994 (Law 8) allows a deduction from taxable income of 50 percent of any amount invested by Panamanian citizens in tourism development.

- Law 25 of 1996 provides for the development of export processing zones (EPZ's) as part of an effort to broaden the Panamanian manufacturing sector while promoting investment, particularly in former U.S. military bases. Companies operating in these zones may import inputs duty-free if products assembled in the zones are to be exported. The government also provides other tax incentives to EPZ companies.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Intellectual property policy and practice in Panama is the responsibility of an “Inter-institutional” Committee. This committee consists of representatives from six government agencies and operates under the leadership of the Vice-Minister of Foreign Trade. It coordinates enforcement actions and develops strategies to improve compliance with the law. The creation of specialized prosecutors for intellectual property-related cases has strengthened the protection and enforcement of intellectual property rights (IPR) in Panama. However, given Panama’s role as a transshipment point, industry is concerned Panama will become susceptible to trading in pirated and counterfeit goods.

Copyrights

Though Panama’s 1994 copyright law modernized copyright protection and its 2004 update incorporated a special Copyright Office with anti-piracy enforcement powers, piracy remains a significant problem.

The government of Panama is a signatory to the WIPO Copyright Treaty and the WIPO Performances and Phonographs Treaty, but the Copyright Office has been slow to draft and implement further improvements to the Copyright Law. Nevertheless, the office has proposed to enhance border measures and establish new punishable offenses, such as for Internet-based copyright violations.

Though industry welcomes both the effective police and legal action, which have significantly reduced the rate of VHS piracy, internet piracy is quickly emerging in Panama. Both hard goods sales and films in theatrical release are often downloaded, reproduced on optical discs, and then distributed by street vendors. Despite ongoing investigations to detect laboratory facilities, the legal framework guiding internet use in the country remains incomplete. The United States is working with Panama through the current FTA negotiations to establish a legal regime to combat piracy of audiovisual products over the Internet, including notice and take down provisions and clearly defined ISP liabilities as well as temporary copy protection, protection of technological protection measures, and protection against Electronic Rights Management Information removal/alteration.

SERVICES BARRIERS

In general, Panama maintains an open regulatory environment for services. For some professions, such as insurance brokers, customs brokerage, freight forwarding, architects, engineers, medical doctors, lawyers, and psychologists, Panama requires that individuals hold a Panamanian technical license.

INVESTMENT BARRIERS

Panama maintains an open investment regime and is receptive to foreign investment. Over the years the country has bolstered its reputation as an international trading, banking, maritime, and services center.

However, under the constitution, retail activity is reserved to Panamanians—an issue that the U.S. government is seeking to address within the context of free trade agreement negotiations. On a variety of investment issues, the Panamanian government was not, until recently, very responsive to concerns raised by U.S. investors. For example, a few firms that are closely regulated by, or hold concessions from the Government of Panama, in the past encountered a lack of cooperation from certain officials and abrupt changes related to terms of various concessions or contracts. In 2003, the Government of Panama addressed these problems constructively by re-opening discussions with the U.S. Government under the rubric of the Ad Hoc Investment Commission, which had been used successfully in the past to resolve concerns of U.S. investors. The resolution of a number of these disputes during the past two years helped make possible the November 2003 announcement that both countries agreed to move forward with bilateral negotiations for a free trade agreement.

The U.S.-Panama Bilateral Investment Treaty (BIT) entered into force in 1991 (with additional amendments in 2001). With some exceptions, the BIT ensures that U.S. investors receive fair, equitable and non-discriminatory treatment and that both Parties abide by international law standards such as for expropriation and compensation and free transfers Should bilateral negotiations conclude in a free trade agreement, the agreement will suspend the availability of both investor-state and state-state dispute settlement under the BIT and replace it with investor-state and state-state dispute settlement under the FTA, except with regard to a dispute arising from an investment agreement and for existing investors for a ten-year period.

A 1998 investment law aimed to enhance new investment in Panama by guaranteeing that investors will have no restrictions on capital and dividend repatriation, foreign exchange use, and disposal of production inside a limited number of sectors in the economy. For a period of ten years, investors will not suffer any deterioration of the conditions prevailing at the time the investment was made.

ELECTRONIC COMMERCE

In mid-2001, Panama became the first country in Central America to adopt a law specific to electronic commerce. The law was a collaborative effort between the public and private sectors, resulting from several months of detailed discussions and broad consultations. Panama's electronic commerce law has several important features: it gives legal force to any transaction or contract completed electronically; it creates the National Directorate of Electronic Commerce to oversee the enforcement of the law; and it defines certification organizations and establishes a voluntary registration regime. In addition, in August 2004 partial regulations to the 2001 law were issued to facilitate the registration of certification organizations. The law is expected to have a favorable impact on many sectors of Panama's services dominated economy, particularly the maritime sector.

OTHER BARRIERS

Corruption

The judicial system can pose a problem for investors due to poorly trained personnel, huge case backlogs and a lack of independence from political influence. In addition, allegations of corruption persist, not only in the judicial system, but in the executive and legislative branches of government.

PARAGUAY

TRADE SUMMARY

The U.S. trade surplus with Paraguay was $563 million in 2004, an increase of $133 million from $430 million in 2003. U.S. goods exports in 2004 were $622 million, up 28.6 percent from the previous year. Corresponding U.S. imports from Paraguay were $59 million, up 10.0 percent. Paraguay is currently the 67th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Paraguay in 2003 was $114 million, the same as in 2002.

IMPORT POLICIES

Tariffs

Paraguay's average applied tariff rate was 12.5 percent in 2003. Paraguay is a member of MERCOSUR, a customs union comprising Argentina, Brazil, Paraguay, and Uruguay. Full CET product coverage is scheduled for implementation in 2006. CET tariffs range from zero percent to 35 percent *ad valorem*, with a limited number of country-specific exceptions. Currently, Paraguay maintains 399 exceptions to the CET. A temporary CET surcharge applied to most imports since 1997 was abolished by Paraguay on January 1, 2004.

Customs Procedures

For exports to Paraguay, a Paraguayan consulate in the country of export must certify specific documentation, such as the commercial receipt, certificate of origin, and cargo manifest. If there is no Paraguayan consulate in the country of export, the documents can be certified in the nearest country with a consulate or in the border consulate office in the country from which the exports enter Paraguay (in the case of ground or river shipments). Multiple changes in regulations make it difficult for exporters to ensure they are following the most current regulations, which can delay shipments and lead to unexpected fines.

Customs Valuation

On September 21, 2004, Paraguay complied with its obligation to notify the World Trade Organization (WTO) of its legislation and checklist for implementing the WTO Agreement on Customs Valuation.

GOVERNMENT PROCUREMENT

In the past, U.S. companies have protested Paraguay's non-transparent procurement procedures, citing bid specifications that favor a preferred bidder and the fact that subsidiaries of a single parent company are each permitted to submit separate bids. Other complaints have included the discriminatory use of bid procedures to disqualify a non-preferred bidder, declaring that there were no bids when a non-preferred bidder submitted the best bid, and not requiring preferred bidders to comply with tender requirements. However, the Duarte government has moved aggressively to implement the Law of Public Contracting that came into force in July 2003. Since March 3, 2004, all public contracting in Paraguay with a value over $70 must be done *via* the website of the Director General of Public Contracting, which is www.contratacionesparaguay.gov.py. The Law of Public Contracting applies to the central government as well as to state and local entities. The contracting office screens tenders to avoid preferential specifications in an effort to avoid issuing tenders biased in favor of a particular bidder. All bid documents are made available electronically and, once bids are awarded, the information on the winner and the final price is made publicly available on the website. Complaints are channeled through the Directorate rather than being submitted directly to the contracting entity, and most complaints so far have been adjudicated in favor of bidders. Foreign firms can bid on tenders deemed "international," which accounted for about 60 percent of the total in 2004, and can bid on "national" tenders through a local representative. Paraguay is not a member of the WTO Agreement on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The Duarte Administration has been particularly active and focused in its fight against piracy, counterfeiting and contraband, declaring the fight a national priority. However, serious concerns over the lack of effective border enforcement remain, because Paraguay continues to be a transshipment point for pirated and counterfeit goods to Brazil and other neighboring markets.

In January 1998, the United States Trade Representative (USTR) identified Paraguay as a Priority Foreign Country under the Special 301 provisions of the Trade Act of 1974, and in February 1998, the United States initiated a Section 301 investigation of Paraguay's acts, policies and practices regarding intellectual property. Paraguay is currently subject to Section 306 monitoring of its Memorandum of Understanding (MOU) with the United States on the protection of intellectual property, which allowed the United States to remove Paraguay from its Priority Foreign Country status and to terminate the Section 301 investigation. In the 1998 MOU, the Paraguayan government committed to implement institutional and legal reforms and to strengthen intellectual property rights enforcement and prosecution. In addition, Paraguay agreed to ensure that its government ministries use only authorized software. The two Governments signed a new MOU in March 2004, which focuses on areas that are still of concern.

The Paraguayan government has made a significant effort to implement the MOU and has met regularly with the U.S. Government to review and discuss the progress achieved in addressing IPR-related concerns. The Paraguayan government has submitted legislation to Congress to increase the penalties for IPR infringement, and worked with the private sector to increase enforcement actions. The Paraguayan government has created a special investigative unit dedicated to combating piracy and counterfeiting as well as an IPR statistics center. The investigative unit has coordinated with industry and has supported many significant seizures of infringing goods. Paraguay also signed an agreement with a major television content provider to fight signal piracy. The number of prosecutors dedicated exclusively to IPR cases has been doubled, although from a low base, and Paraguay has received several awards from industry for its improved enforcement efforts. The United States will continue to work closely with Paraguay to address remaining IPR-related concerns, particularly with regard to strengthening border and other enforcement measures to combat piracy and counterfeiting activities.

OTHER BARRIERS

Law 194/93 establishes the legal framework governing relationships between foreign companies and their Paraguayan representatives. Modeled after the Puerto Rico's Dealers Act, this law requires that foreign companies prove just cause in a Paraguayan court to terminate, modify or fail to renew contracts with Paraguayan distributors. Severe penalties and high fines may result if the court determines that the foreign company ended the relationship with its distributor without just cause, which often leads to expensive out-of-court settlements. In several cases, however, the courts have upheld rights of foreign companies to terminate representation agreements after just cause was established, mainly on the basis of lack of sales performance by local representatives. This law may discourage U.S. investment through fear of potential lawsuits.

Privatization

Paraguay has an uneven record on privatization. Political pressures have impeded the process, as the large state-run companies most attractive to foreign buyers (such as telecommunications, water/sewage, and electrical companies) employ thousands of potential voters and are outlets for political patronage. An effort to privatize the telecommunications company failed in 2002, due to intense political pressure and amid allegations of mishandling. In May 2004 several Congress members from the opposition parties attempted to revive legislation that would have allowed privatization to occur. Due to widespread negative public response, however, Congress suspended consideration of the legislation. As part of its Stand-By Arrangement with the International Monetary Fund, the government has committed to undertake independent audits of state-owned firms and to develop business plans for them, with the aim of eventually increasing private sector involvement in the management and ownership of the companies.

PERU

TRADE BARRIERS

The U.S. trade deficit with Peru was $1.6 billion in 2004, an increase of $895 million from $710 million in 2003. U.S. goods exports in 2004 were $2.1 billion, up 23.4 percent from the previous year. Corresponding U.S. imports from Peru were $3.7 billion, up 53.6 percent. Peru is currently the 42nd largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Peru in 2003 was $2.7 billion, down from $2.8 billion in 2002. U.S. FDI in Peru is concentrated largely in the mining sector.

FREE TRADE NEGOTIATIONS

In May 2004, the United States initiated free trade agreement (FTA) negotiations with three Andean nations -- Colombia, Peru and Ecuador. Bolivia is participating as an observer and is expected to become part of the agreement at a later stage. The U.S. Government will seek to address the issues described in this chapter within the context of these negotiations. The four Andean countries collectively represented a market of about $8.5 billion for U.S. exports in 2004, and were home to about $7.2 billion in U.S. foreign direct investment.

IMPORT POLICIES

Tariffs

Peru applies tariffs to virtually all goods exported from the United States, although the Government of Peru has lowered tariff rates in the past few years. Currently, a 12 percent tariff applies to 45 percent of the products imported into Peru; four percent and seven percent tariffs apply to about 23 percent and 15 percent of goods, respectively; and 17 percent and 20 percent tariffs apply to most of the rest. The government maintains a five percent "temporary" tariff surcharge on agricultural goods to protect local production and domestic investment in the sector. The United States is seeking the elimination of Peru's duties on U.S. exports in the FTA negotiations, upon entry into force of the agreement where possible and over time for the most sensitive products.

Certain sensitive agricultural products – e.g., corn, rice, sugar and powdered milk – are subject to a Peru-specific "price band," or variable levy, which fluctuates to ensure that the import prices of such products equal a predetermined minimum import price. This levy is the difference between the minimum import price and an international reference price plus an adjustment for insurance, freight and other factors.

The U.S. Government is seeking through the FTA negotiation to eliminate Peru's barriers to trade in our agricultural products, while providing reasonable adjustment periods and safeguards for producers of import sensitive agricultural products.

Non-Tariff Measures

The Government of Peru has eliminated almost all non-tariff barriers, including subsidies, import licensing requirements, import prohibitions and quantitative restrictions. However, the following imports are banned: used clothing, used shoes, used tires, remanufactured machine parts, cars over five years old and heavy trucks (weighing three tons or more) over eight years old. Used cars and trucks that are granted import permits must pay a 45 percent excise tax – compared to 20 percent for a new car – unless they are refurbished in an industrial center in the south of the country upon entry, in which case they are exempted entirely from the excise tax. Import licenses are required for firearms, munitions and explosives, chemical precursors (since these can be diverted to illegal narcotics production), ammonium nitrate fertilizer, and wild plant and animal species.

SENASA, the Peruvian plant and animal health agency, imposes several significant trade barriers (which include bans, import requirements and sanitary permits) on agricultural products, including poultry, live animals and animal genetic material. Among the affected products are:

--Poultry Products: The Peruvian government lifted its ban on U.S. poultry products in July 2004. Peru began importing small amounts of American poultry in November 2004.

--Beef and beef products: SENASA enacted a ban on U.S. beef products in March 2004, due to BSE.

--Paddy Rice: Peru has a ban on paddy rice imports from the United States. SENASA is currently conducting a Pest Risk Assessment that, if successful, will result in lifting the ban. SENASA has not indicated when it will make a final decision.

GOVERNMENT PROCUREMENT

In 2000, in an effort to support national companies, Peru began adding 15 percent (on its rating scale of 100) to bids by Peruvian firms on government procurement contracts. In January 2002, the government raised the point preference an additional five percent, to a total of 20 percent, until 2005. U.S. pharmaceutical and medical equipment firms have raised concerns about this practice with regard to bidding on Health Ministry purchases. U.S. firms contend that the 20-point margin is excessive, giving unfair advantage to Peruvian competitors that would otherwise lose these bids on cost or technical grounds. In 2001 Peru began distinguishing between national and international bidding processes, reserving certain solicitations for participation by domestic firms only. In November 2004, the Peruvian government eliminated this distinction for the majority of products, applying it only to construction works. Peru is not a signatory to the WTO Agreement on Government Procurement. In the FTA negotiations the U.S. Government is seeking opportunities for U.S. companies to bid on Peruvian government procurement.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Peru is a member of the World Intellectual Property Organization (WIPO). It is also a member of the Paris Convention, Berne Convention, Rome Convention, Geneva Phonograms Convention, Brussels Satellites Convention, Universal Copyright Convention, the WIPO Copyright Treaty (WCT) and the WIPO Performances and Phonograms Treaty (WPPT). Peru remains on the U.S. Trade Representative's Special 301 Watch List. Concerns remain about the adequacy of IPR law enforcement, particularly with respect to the relatively weak penalties imposed on IPR violators by the criminal justice courts. Although the Peruvian government recently increased the minimum penalty for piracy to a four-year sentence, there have yet to be any convictions under the new law.

The United States is currently negotiating IPR provisions under the ongoing Andean FTA negotiations to improve protection and strengthen enforcement of IPR. The U.S. Government is seeking to address specific U.S. industry concerns related to the protection and enforcement of copyrights and related rights, patents, proprietary data for pharmaceutical and agricultural products, trademarks and geographical indications.

Copyrights

Peru's 1996 Copyright Law is generally consistent with the TRIPS Agreement. Peru joined the WCT in July 2001 and the WPPT in February 2002. Although most of the provisions of these two WIPO treaties are included in Peru's 1996 Copyright Law, officials at Indecopi, the IPR administrative agency, have acknowledged the need for additional legislation in order to clarify the rights of artists and producers. The National Association of Music Publishers continues to criticize Indecopi's enforcement, claiming that its members are not receiving the royalties due to them.

Despite Peruvian government efforts to increase enforcement, including increased raids on large-scale distributors and users of pirated material, piracy remains widespread. The International Intellectual Property Alliance estimates that piracy levels in Peru for recorded music was 98 percent in 2003-2004 with damage to U.S. industry estimated at $90 million, while motion picture piracy accounts for 60 percent of the market for a loss of an estimated $5.5 million. Indecopi estimates that software piracy levels have decreased from 60 percent in 2003 to 56 percent in 2004.

Patents and Trademarks

Peru's 1996 Industrial Property Rights Law provides the framework for patent protection. In 1997, based on an agreement reached with the U.S. Government, Peru addressed several inconsistencies with the WTO TRIPS Agreement provisions on patent protection and most-favored nation treatment for patents.

However, the U.S. pharmaceutical and agrochemical industries continue to have concerns about Peru's protection of confidential test data. Peruvian government health authorities approved the commercialization of new drugs which were the bioequivalents of already approved drugs, thereby denying the originator companies the exclusive use of their data. In effect, the government of Peru is allowing the test data of registered drugs from some companies to be used by others seeking approval for their own pirate version of the same product. U.S. companies also are concerned that the Peruvian government does not provide patent protection to second uses, which would allow a company with a patented compound for one use to subsequently patent a second use of that compound. Although Peruvian law provides the means for effective trademark protection, counterfeiting of trademarks and imports of counterfeit merchandise remain widespread.

SERVICES BARRIERS

The U.S. Government is seeking through the FTA negotiations to secure greater access for U.S. providers of cross-border services to the Peruvian market, including in the areas of financial and telecommunications services.

Basic Telecommunications Services

In the WTO negotiations on basic telecommunications services, concluded in March 1997, Peru made commitments on all basic telecommunications services, with full market access and national treatment to be provided as of June 1999. Peru is continuing the process of developing a competitive telecommunications market and lowered its interconnection rates for most types of telephones in 2001. Termination rates for calls to mobile networks, however, remain one of the highest in the world. This issue has become particularly acute as a result of the recent acquisition by Telefonica of the second largest wireless provider in the country, thereby increasing Telefonica's market share in the wireless sector to over 70 percent. Other suppliers claim that unconstrained pricing by the dominant supplier has created significant barriers to competition in the wireless sector. In addition, some concerns remain about the independence and strength of the government regulatory body established to oversee the sector. In particular, U.S. industry has complained about the lack of transparency in the regulatory decision-making process.

INVESTMENT BARRIERS

National treatment for foreign investors is guaranteed under Peru's 1993 constitution. Prior approval is not required for investment by foreign or domestic persons, except in banking and defense-related industries. There are no limitations on the repatriation of capital or profits. Arbitration is available for disputes between foreign investors and the Government of Peru. Several U.S. companies have chosen to pursue claims through arbitration, with mixed results.

Peruvian law restricts majority ownership of broadcast media to Peruvian citizens. Foreigners are also restricted from owning land or investing in natural resources within 50 kilometers of a border, but they can operate within those areas with special authorization. National air and water transportation are restricted to domestic operators. In July 2001, inter-urban land transportation was also reserved for Peruvian carriers.

Under current law, foreign employees may not comprise more than 20 percent of the total number of employees of a local company (whether owned by foreign or Peruvian persons) or more than 30 percent of the total company payroll, although some exemptions apply. Newly established companies, multinational service providers, banks and transportation companies are all granted exemptions. Additionally, foreign companies do not have limitations on the number of foreign management officers they may hire.

Several U.S. firms complain that executive branch ministries, regulatory agencies, the tax agency and the judiciary lack the resources, expertise and impartiality necessary to carry out their respective mandates. Peru's weak judicial branch is a particular problem. Commercial disputes that end up in Peruvian courts are often delayed and can yield results that are not foreseeable based on a review of relevant precedents. The tax agency, with its retroactive reinterpretation of rules and disproportionate fines, has also created additional investment and trade barriers. The Toledo Administration has tried to address institutional weaknesses in the executive branch and has offered plans for judicial reform. The U.S. Government has worked with the Government of Peru both before and in parallel with the FTA negotiations to ensure a fair resolution of U.S. investor disputes, consistent with Peruvian law. Some of those disputes have been resolved while others remain pending.

The U.S. Government is seeking through the FTA negotiations a range of protections with respect to the treatment of U.S. investors, as well as a guaranteed right for those investors to have recourse to international arbitration in the event of disputes with the Peruvian government.

Electronic Commerce

The Peruvian government is moving to put in place legislation that will facilitate electronic commerce. It has already passed laws giving legal status to digital signatures, creating a framework for electronic contracts and making it illegal to tamper with, destroy or interfere with computer systems or data. The U.S. is seeking in the FTA negotiations to include rules prohibiting duties on and discrimination against digital products, such as computer programs, videos, images, and sound recordings, based on where they are made or the nationality of the firms or persons making them.

PHILIPPINES

TRADE SUMMARY

The U.S. trade deficit with the Philippines was $2.1 billion in 2004, the same as in 2003. U.S. goods exports in 2004 were $7.1 billion, down 11.5 percent from the previous year. Corresponding U.S. imports from the Philippines were $9.1 billion, down 9.1 percent. The Philippines is currently the 21st largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to the Philippines were $1.4 billion in 2003 (latest data available), and U.S. imports were $1.4 billion. Sales of services in the Philippines by majority U.S.-owned affiliates were $1.3 billion in 2002 (latest data available), while sales of services in the United States by majority Philippines-owned firms were $13 million.

The stock of U.S. foreign direct investment (FDI) in the Philippines in 2003 was $4.7 billion, up from $4.6 billion in 2002. U.S. FDI in the Philippines is concentrated largely in the manufacturing and finance sectors.

The United States and the Philippines concluded a bilateral Trade and Investment Framework Agreement (TIFA) in 1989. In recent years, the United States and the Philippines have held regular meetings under the TIFA. The United States has used the TIFA to raise and seek resolution of many of the issues raise below. The United States-Philippines TIFA can be seen as a part of the Enterprise for ASEAN Initiative (EAI), which was launched by President Bush in October 2002. The EAI offers the prospect of bilateral Free Trade Agreements between the United States and ASEAN countries that are committed to economic reforms and openness.

IMPORT POLICIES

Tariffs

In January 2003, the Philippine government announced a reversal in tariff policy and indicated that it would undertake a comprehensive review of all tariff lines. The Tariff Commission issued recommendations for increased tariffs in several sectors and a slowdown of its tariff reduction plans in others. While the increased tariffs, which took effect in 2004, remain below WTO bound rates, they represent a reversal of the hard fought reforms of successive previous Philippine administrations during the 1990s.

Previous progress on tariff liberalization took shape through a series of reform programs beginning in 1995. Normal trade relations (NTR) most favored nation (MFN) tariff rates on all goods (except sensitive agricultural products) were to be gradually reduced to the following target rates: 3 percent for raw materials and 10 percent for finished products by January 2003, and a uniform 5 percent tariff rate for all remaining products by January 2004.

Executive Orders 241 and 264, signed by President Arroyo in October and December 2003, respectively, raised tariff rates on more than 1,000 product lines and maintained 2003 rates for an even greater number of product lines. Products affected include industrial goods produced domestically, such as chemical fertilizers, cement, consumer products such as apparel and footwear, and raw materials. The orders raised rates on these products from the previous rates of between 3 percent and 10 percent to between 5 percent and 20 percent. The tariff increases have been described as temporary, and tariff rates may be reviewed in 2005.

The Common Effective Preferential Tariff (CEPT) Agreement for the ASEAN Free Trade Area (AFTA) requires that tariff rates among ASEAN members on a broad range of products be reduced to between zero percent and 5 percent, while quantitative restrictions and other non-tariff barriers are to be eliminated. ASEAN members agreed on a firm timetable leading up to the full realization of AFTA by the end of 2003. President Arroyo signed an executive order on January 9, 2003, which temporarily suspended the AFTA tariff reduction schedule on petrochemical resins and certain plastic products. As permitted under AFTA, Singapore sought and won compensation from the Philippines for failing to lower Philippine petrochemical tariffs. As of December 2004, nearly 98 percent of Philippine tariff lines under the AFTA-CEPT have been reduced to between zero and five percent, with nearly 60 percent of tariff lines reduced to 0 percent.

Automobile Sector Tariffs

On April 17, 2001, the Arroyo Administration issued an order lowering the tariff on automotive vehicle components from 10 percent to 3 percent under the Philippine government's Motor Vehicle Development Program, a program designed to rationalize the auto industry and transform the Philippines into a regional hub for automotive production. To promote local assembly under the program, imports of finished automobiles (completely built-up units) and motorcycles have been subject to the highest duty rate applied to non-agricultural products. In 2004, tariff rates for completely knocked-down passenger cars imported under the Motor Vehicle Development Program decreased to 3 percent, with a one percent rate applied to non-passenger vehicles with knocked-down status.

In late 2004, the Philippine government proposed raising the NTR/MFN tariff rate to 60 percent for finished vehicles with an engine size of over 2.1 liters for gasoline-powered vehicles and over 3.2 liters for diesel-powered vehicles. The Administration characterized the proposed tariff increase the first step in long-term plans under consideration for energy conservation and environmental measures in the automobile sector and as part of a strategy to encourage purchases of smaller automobiles. After consultations with auto importers, the U.S. Government and foreign governments, the Philippines revised the proposed increase to 35 percent. As of

December 2004, no final decision had been reached, but it appeared likely that the 35 percent tariff rate would be applied to the larger engine vehicles in the near future.

The Philippines imposes a 30 percent tariff on motorcycles and a 3 percent tariff on crude oil and most refined petroleum products.

Excise Tax on Automotive Vehicles

In August 2003, the Philippine Congress passed legislation changing the automotive excise tax structure from one based on engine displacement to a system based on vehicle value. The old system generally discouraged imported vehicles with larger engine displacement, including those from the United States. The new law covers most types of imported and locally manufactured vehicles, except for some trucks defined as motor vehicles designed for cargo and buses, which are classified by their tonnage. Vehicles that had been tax-exempt under the 10-seater rule, including Asian utility vehicles (AUVs) are now taxed under the new system.

Under the revised excise tax scheme vehicles are divided into four brackets based on their price: (1) for vehicles with a manufacturer's price of 600,000 pesos and below, the tax is 2 percent; (2) for those priced over 600,000 pesos to 1.1 million pesos, the tax is 12,000 pesos plus 20 percent of the amount in excess of 600,000 pesos; (3) for those priced over 1.1 million pesos to 2.1 million pesos, the tax is 112,000 pesos plus 40 percent of the amount in excess of 1.1 million pesos; and (4) for those over 2.1 million pesos, the tax is 512,000 pesos plus 60 percent of the amount in excess of 2.1 million pesos.

Safeguards

The Safeguard Measures Act, enacted in 2000, authorizes the Secretary of Trade and Industry or the Secretary of Agriculture to raise a tariff or, in the case of an agricultural good, impose a quantitative restriction, to protect a domestic industry from an import surge. The U.S. Government has expressed reservations concerning the Philippine safeguards legislation, noting in particular that the five days afforded to foreign industry to comment on proposed safeguards is not a reasonable period of time as provided for in the WTO Agreement on Safeguards. The U.S. Government has requested that the Philippines lengthen the statutorily mandated period. The Philippine government indicated that it would increase the comment period to 30 days, but this change had not yet been finalized as of December 2004.

In November 2001, the Philippine government put in place a safeguard to protect local cement producers from imports. The Secretary of Trade and Industry imposed the safeguard duty despite the finding of the interagency Tariff Commission's that there was no merit to the cement producers' case. This decision was appealed to the Philippine Supreme Court and was still pending as of December 2004. The safeguard was originally put in place for a period of three years, ending on December 9, 2004. However, the Tariff Commission is currently reviewing a petition from the local cement industry to extend the safeguard.

The Philippine government also has put in place a safeguard measure against ceramic tiles that is due to end in January 2005. The Philippine Department of Trade and Industry is currently reviewing a petition to extend the safeguard. Additional safeguards currently in place are against imported float glass, figured glass and glass mirrors.

In October 2002, the Philippine government implemented a special agricultural safeguard (SSG) on imports of chicken meat and fresh onions. The Philippines subsequently lifted the SSG on onions in December 2002, only to re-impose it in October 2004. In June 2004, in response to rising retail prices of dressed chicken in the country, the Philippine Department of Agriculture allowed the importation of 10,000 MT of chicken between June and August exempt from the SSG.

Agriculture Tariffs and Import Licensing

The Philippines maintains high tariff rates on sensitive agricultural products, including grains, livestock and meat products, sugar, frozen and processed potatoes, onions, coffee, and fresh citrus, including oranges, lemons, and grapefruit.

In 2002, the Philippines issued several executive orders that provided for tariff reductions for most agricultural products through 2004. However, in January 2003, the Philippines reversed this policy by issuing Executive Order 164, which set tariff rates for most agricultural products at their 2002 levels with the exception of pork, poultry, processed meats, corn, coffee and vegetables. Executive Orders 241 and 264, issued in 2003, raised tariff rates on some product lines and maintained 2003 rates on an even greater number of food and agricultural products. Tariffs on some products for which the United States has a substantial market share were affected by the tariff increase.

Among sensitive agricultural products, 15 items (at the four-digit HS level) are subject to a minimum access volume (MAV) or tariff-rate quotas (TRQs). The Philippines' 10-year minimum access commitments under the Uruguay Round expire in June 2005. Final-year TRQ commitments are to be maintained until such time as the products are liberalized or new commitments are negotiated under the Doha Development Agenda. Several products with significant market potential for the United States are subject to TRQs. These include corn, with an in-quota tariff rate of 35 percent and an out-of-quota tariff rate of 50 percent for 2004/2005; poultry meat, with an equalized in-quota and out-of-quota tariff rate of 40 percent on July 1, 2003 that is to be maintained at that level until June 2005; and pork with an in-quota rate of 30 percent and out-of-quota rate of 40 percent, also through June 2005.

The U.S. government continues to closely monitor the operation of the Philippines TRQ system and the allocation and distribution of import licenses, in particular the Philippine government's application of its Veterinary Quarantine Clearance (VQC) certificates for meat and poultry imports.

In response to pressure from domestic meat and poultry producers to limit imports as well as to crack down on illegal importation of meat and poultry into the country, the Philippine Department of Agriculture (DA) maintains a VQC import licensing scheme for imported meat and poultry, although its name connotes an SPS monitoring mechanism. The current meat import regulation (Administrative Order 39) requires a one-time use of a VQC, meaning that each VQC must be surrendered upon arrival of a shipment of a covered product. When the quantity allowed on a VQC is insufficient to cover the amount in a container, the importer must supply an additional VQC to cover the difference. Any remaining tonnage from that second VQC is subsequently forfeited rather than giving the importer a credit for unused tonnage. This practice creates the appearance of discretionary licensing and fosters imprecision in statistical tracking of import volumes. The U.S. government has registered its concern with the Philippine government regarding the VQC process and has requested that its application be made more transparent, flexible and WTO consistent.

The Philippine Fisheries Code permits importation of fresh, chilled, or frozen fish and fish products only when certified as necessary by the Secretary of Agriculture and upon issuance of an import permit by the Department of Agriculture. Among the criteria the Secretary is mandated to consider in determining whether to approve importation is whether there is serious injury or threat of injury to a domestic industry that produces like or directly competitive products. This process appears to be a discretionary application of import licensing.

Excise Tax on Distilled Spirits and Tobacco Products

President Arroyo signed legislation in December 2004 that raised the taxes on alcohol, cigarettes, and tobacco products starting in 2005. The law maintained the preferential treatment the Philippines gives to distilled spirits produced from indigenous raw materials in its excise tax regime, which is a tiered tax structure based on net retail price. This tax regime continues to impede access to the Philippine market for U.S. exports of higher-value distilled spirits and is a primary reason why U.S. exports to this potentially significant market remain quite small.

The new legislation increased the excise tax by 30 percent for distilled spirits produced from indigenous sources, raising the tax from 8.96 pesos to 11.65 pesos on every liter of distilled spirits made from raw materials such as coconut palm, cane, and certain root crops. It also increased the excise tax by 50 percent on distilled spirits made from other materials (which would apply to most imports) from a range of 84 to 336 pesos per 750 ml bottle to a range of 126 to 504 pesos per bottle. The legislation also increased the excise tax on fermented liquor by 20 percent. Wines with an alcohol content of 14 percent or less by volume are assessed an excise tax of 17.47 pesos per liter, while wines with an alcoholic content greater than 14 percent but less than 25 percent alcohol content by volume are charged an excise tax of 34.94 pesos per bottle. Fortified wines (containing greater than 25 percent alcohol content) are taxed as distilled spirits. Depending on the net retail price per bottle, an excise tax ranging from 145.6 pesos to

436.8 pesos per liter is assessed on bottles of sparkling wine and champagne. The legislation increases these rates on alcohol products by 8 percent every two years until 2011.

The Philippines also maintains a four-tiered excise tax system based on retail prices for cigarettes, which will increase by 12 percent and 40 centavos per pack every other year until 2011. Low-priced cigarettes with a retail price below 5 pesos per pack and hand-rolled cigarettes will be assessed a tax of 2 pesos in 2005, rising to 2.72 pesos in 2011. Medium-priced cigarettes with a net retail price between 5 and 6.5 pesos per pack will be assessed a tax of 6.35 pesos in 2005, rising to 7.16 pesos in 2011. High-priced cigarettes with net retail prices between 6.5 and 10 pesos per pack will be charged a tax of 10.35 pesos in 2005, rising to 12 pesos in 2011. Premium cigarettes with net retail prices above 10 pesos per pack will be charged a tax of 25 pesos in 2005, rising to 28.3 pesos in 2011. The legislation assessed an *ad valorem* tax of 10 percent on cigars for those with a net retail price of 500 pesos or lower, and of 15 pesos plus 50 pesos for cigars with a net retail price above 500 pesos.

The Documentary Stamp Tax presents a related national treatment issue with respect to cigarettes. Although the National Internal Revenue Code requires that tax stamps be affixed to all cigarettes sold in the Philippines, this is only effectively enforced on imported cigarettes. Because of lax enforcement, domestically produced cigarettes are often shipped to outlets without the stamps and without paying the connected taxes.

Quantitative Restrictions

The National Food Authority (NFA) administers quantitative restrictions on rice imports. The minimum access volume (quota) for rice is 224,005 metric tons for 2004 and 142,203 metric tons for the first half of 2005. Both in and out of quota tariffs are 50 percent, although this tariff is waived when the NFA contracts these imports. Rice import demand is expected to continue growing in the Philippines due to persistent shortfalls in local production and a high population growth rate (2.4 percent annually). Due to import restrictions, rice is commonly illegally imported into the country from various rice-producing countries in the region.

In 2003, the Philippine Department of Agriculture opened up the importation of rice to the private sector. Prior to this, only the NFA could legally import rice. While the opening to private sector participation is a welcome development, the U.S. Government has raised concerns that the existing plan to transfer import rights to domestic rice farmers ("Farmers as Importers" and "Farmers as Distributors") may result in discriminatory treatment against imports.

Other Import Restrictions

The Philippines maintains other import restrictions. Since April 15, 1999, the National Telecommunications Commission (NTC) has required cellular telephone service providers or authorized equipment dealers to obtain an import permit prior to importation of cellular phone handsets.

Customs Barriers

The Philippine government has made progress during the last several years toward bringing its customs regime into compliance with its WTO obligations, but corruption and other irregularities remain commonplace. The Philippine laws R.A. 8181 (1996) and R.A. 9135 (2001), with supporting regulations, provide the legal context for the Philippines' implementation of the WTO Agreement on Customs Valuation. The Philippines discontinued use of Home Consumption Value and adopted transaction value for the purpose of calculating *ad valorem* rates of duty. Supporting regulations also provided the Bureau of Customs with the authority to create a post-entry audit unit, a risk management unit and a border control unit charged with IPR enforcement.

The 2001 law eliminated private sector involvement in the valuation process. It also clarified that reference values may be used as a risk management tool, but not as a substitute for valuation. The U.S. Government remains concerned, however, about reports of continued private sector involvement in the valuation process, particularly in the activities of the Import Specialist Team, which has the authority to review all green lane entries for possible valuation-related offenses. The Philippine government has made improvements to the valuation system, but periodic procedural irregularities continue to occur, including requests by Customs officials for the payment of unrecorded facilitation fees. The U.S. Government has raised this issue during bilateral trade discussions during the past several years and will continue to closely monitor the situation.

Currently, all importers or their agents must file import declarations with the Bureau of Customs (BOC), which the BOC then processes through its Automated Customs Operating System (ACOS). ACOS uses its selectivity system to classify shipments as low-risk (green lane), moderate-risk (yellow lane) or high-risk (red lane). All shipments channeled through the yellow lane require a documentary review, while red lane shipments require both documentary review and physical inspection at the port. Green lane shipments are not subject to any documentary or inspection requirements. In early 2002, the BOC also announced the addition of a "Super Green Lane" (SGL) facility for importers acknowledged as the lowest risk. The import transactions of Super Green Lane importers are not covered by the selectivity system and thus are exempt from documentary and physical examination. Because of low throughput during the implementation, which was launched in December 2003, BOC, with USAID technical assistance, adjusted the cost to companies of accessing the facility. By the end of 2004, 86 firms were using these facilities.

Despite these improvements, the U.S. Government continues to have concerns about inconsistent application of customs rules and procedures, undue and costly processing delays, and corruption. The United States continuously urges the Philippine government to improve administration of its customs regime. Customs administration could be strengthened by improving classification of entries and providing precise descriptions of imported articles to reduce discretionary authority of customs officials. During bilateral trade discussions in 2003, the Philippines reviewed progress on administrative reforms, including efforts to reduce average clearance time for goods passing through Customs and ongoing internal efforts to eliminate corruption. Reform and modernization within the Bureau of Customs is being supported through technical assistance by USAID and several other donor organizations.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Industrial Goods

Local inspection for compliance with mandatory Philippine national standards is required for 75 products, including cosmetics, medical equipment, lighting fixtures, electrical wires and cables, cement, pneumatic tires, sanitary wares, and household appliances. For goods not subject to such standards, U.S. manufacturers' self-certification of conformity is accepted. Labeling is mandatory for textile fabrics, ready-made garments, household and institutional linens, and garment accessories. Mislabeling, misrepresentation, or misbranding may subject an entire shipment, rather than just the offending goods, to seizure and disposal. The "Generic Act" of 1988 aims to promote the use of generic drugs by requiring that the generic name of a particular pharmaceutical appear above its brand name on all packaging.

Agricultural Goods

The Philippine Department of Agriculture (DA) established plant health regulations in 1995 that allow the import of U.S. apples, grapes, oranges, potatoes, onions, and garlic, provided these products, when necessary, undergo a specified cold treatment to control targeted pests. Importation of Florida grapefruit, oranges, and tangerines into the Philippines is permitted under a March 2000 protocol between the Philippines and the United States. Similarly, under a July 2004 protocol, importation of cherries from the United States is permitted.

In January 2004, the DA issued Memorandum Order No. 33 (MO 33), which provided new requirements for beef and beef products imported from the United States. This was in response to the detection of Bovine Spongiform Encephalopathy (BSE) in a single imported dairy cow in the State of Washington in December 2003. Only beef and beef products derived from cattle 30 months of age or less is allowed entry into the country. Other specified requirements include: only deboned and deglanded muscle cuts of beef from healthy and ambulatory cattle devoid of nerves and any specified risk materials (SRMs) will be allowed entry. Moreover, the production or slaughter date of the cattle must be provided on the packaging label.

GOVERNMENT PROCUREMENT

Although the Philippines is not a signatory to the WTO Government Procurement Agreement (GPA), the Philippine government has taken some steps to reform its procurement process. Nonetheless, in awarding contracts, the Philippine government continues to provide preferential treatment to local suppliers of pharmaceuticals, rice, corn, and iron/steel materials for use in government projects and government-required consulting for infrastructure projects. Contractors for infrastructure projects that require a public utility franchise (*i.e.*, water and power distribution, telecommunications, and transport systems) must be at least 60 percent Filipino-owned.

In January 2003, President Arroyo signed the Government Procurement Reform Act. Although there are some exceptions, the Act generally stipulates equal opportunities for qualified private contractors (whether local or foreign) to bid for the procurement of infrastructure projects, goods, and consulting services, regardless of the funding source. The law calls for public monitoring of the procurement process to promote greater transparency and competition, enhance the flow of information, and lessen discretion among agencies. It also establishes an electronic procurement system to serve as the single portal for all government procurement and requires that all bidders use standardized forms. However, the law allows, in the interest of availability and timeliness, the procuring entity to give preference to the purchase of domestically produced and manufactured goods, supplies and materials. For infrastructure projects, the law provides that, for the next five years, contractors whose head office is located in the province where the project will take place have the right to match the lowest offer made by a non-province based bidder. In addition to these concerns about discriminatory treatment against foreign firms, U.S. firms continue to raise concerns about corruption in government procurement.

In February 2004, President Arroyo issued Executive Order 278, which provides preferential treatment for Filipino consultants in public sector infrastructure projects. The Executive Order stipulates that, as much as possible, the government should fund consultancy services for its infrastructure projects with local funds and using local resources and expertise. When Filipino capability is determined to be insufficient, Filipino consultants may hire or work with foreign consultants, but should be the lead consultants. Where foreign funding is indispensable, foreign consultants must enter into joint ventures with Filipinos. Although concerned, multilateral donor agencies report that their implementation partners have thus far been able to follow donors' internal procurement guidelines despite Executive Order 278. However, because an executive order has the force of law, the specter of problems arising in the future remains.

In 1993, the Philippine government mandated a countertrade requirement for procurements by government agencies and government-owned or controlled corporations that entail the payment of at least $1 million in foreign currency. Implementing regulations set the level of countertrade obligations at a minimum of 50 percent of the import price and set penalties for nonperformance of countertrade obligations. The U.S. government continues to monitor implementation of these laws.

EXPORT SUBSIDIES

Enterprises and exporters engaged in activities under the Philippine government's Investment Priorities Plan may register with the Board of Investments (BOI) for fiscal incentives, including four-to six-year income tax holidays, a tax deduction equivalent to 50 percent of the wages of direct-hire workers, and tax and duty exemptions for the importation of breeding stock and genetic materials. BOI-registered firms that locate in less developed areas may be eligible to claim a tax deduction of up to 100 percent of outlays for infrastructure works and 100 percent of incremental labor expenses. Firms in government-administered export processing zones, free trade zones, and other special industrial estates registered with the Philippine Economic Zone Authority (PEZA) enjoy similar incentives, as well as tax and duty-free imports of capital equipment and raw materials, and exemption from customs inspection. In lieu of national and local taxes, PEZA-registered firms are subject to a 5 percent tax on gross income. Firms that earn at least 50 percent of their income from exports may register with BOI or PEZA for certain tax credits under the Philippines' Export Development Act, including a tax credit on incremental annual export revenue.

Automotive Export Subsidies

To further promote the local assembly and export of vehicles from the Philippines, President Arroyo signed Executive Order 156 in October 2003. The export incentives program allows any auto manufacturer that exports finished vehicles from the Philippines to receive a benefit equivalent to $400 per vehicle. This benefit will be provided in the form of a reduced tariff rate on finished vehicles the manufacturer imports into the Philippines. The reduced tariff rates are: MFN rates of 30 percent and 20 percent will be reduced to 10 percent and the ASEAN Common External Preferential Tariff (CEPT) rate of 5 percent will become 1 percent for imports from the other ASEAN countries. This export incentive will be equivalent to $400 per unit exported for year one to two of the program, $300 for year three, and phased down to $100 by year five.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The U.S. government continues to have serious concerns about intellectual property rights (IPR) protection in the Philippines, despite President Arroyo's commitment to strengthen the IPR regime. In 2004, for the fourth consecutive year, the U.S. government named the Philippines to the Special 301 Priority Watch List. Optical media piracy has significantly increased in recent years, with a noticeable shift to pirate DVD production and burning content onto CD-Rs. The Philippines has become a haven for organized piracy and counterfeiting, as other countries in the region strengthen their enforcement efforts against violators of IPR. Print and broadcast piracy and end-user piracy of business and entertainment software also are serious problems. The Philippines has in recent years put in place new legal regimes and enforcement bodies to tackle rampant IPR piracy, and the United States is closely monitoring these efforts. The United States has encouraged the Philippines to further improve and sustain enforcement efforts and to take steps to enhance judicial capacity.

The Intellectual Property Code

The 1997 Intellectual Property Code provides the legal framework for IPR protection in the Philippines. The 2000 Electronic Commerce Act extends this framework to the Internet. However, the code contains ambiguous provisions relating to the rights of copyright owners over broadcast, rebroadcast, cable retransmission, or satellite retransmission of their works; and burdensome restrictions affecting contracts to license software and other technology. We also remain concerned about the judiciary's lack of authority to order the seizure of pirated material as a provisional measure without notice to the suspected infringer.

The Philippine government took several positive steps in recent years to address legislative deficiencies in its IPR regime. In 2001, the Philippines enacted a new law to protect layout designs (topographies) of integrated circuits. In January 2002, the Philippine Supreme Court adopted rules establishing *ex parte* authority in civil cases of IPR infringement. In June 2002, President Arroyo enacted legislation to comply with its TRIPS Article 27.3 (b) requirements on the protection of the exclusive rights of breeders with respect to their new plant varieties. However, U.S. seed company representatives have expressed concern about the vagueness of key provisions of the law, particularly relating to rules that could affect their operations and the provision exempting local farmers from licensing requirements.

In addition to its commitments under the WTO TRIPS Agreement, the Philippines is a party to the Paris Convention for the Protection of Industrial Property, the Berne Convention for the Protection of Literary and Artistic Works, the Berne Treaty on the International Recognition of the Deposit of Microorganisms, the Patent Cooperation Treaty, and the Rome Convention. The Philippines, as a member of the World Intellectual Property Organization (WIPO), ratified the WIPO Performances and Phonograms Treaty and the Copyright Treaty in March 2002. The treaties took effect in October 2002. However, the Philippine government has not yet enacted necessary amendments to its copyright law that would fully implement the requirements of the WIPO Treaties. The U.S. government continues to urge the Philippines to enact this needed legislation.

President Arroyo signed into law the Optical Media Act (OMA) on February 10, 2004, which is intended to regulate the import, export and production of optical disks, including the tools and materials involved in the replication of optical disks. In addition, the Act created the Optical Media Board (OMB) as a replacement for the Videogram Regulatory Board. On February 1, 2005, implementing regulations for the Optical Media Act were finally approved by the Congressional Oversight Committee. Full implementation of this law and regulations, including prosecution of IPR violators, will be critical to strengthening the Philippines IPR regime. During bilateral trade discussions in 2004 and early 2005, the U.S. government continued to raise concerns regarding insufficient legal protection and enforcement of IPR and encouraged swift action and full funding support for enforcement efforts and judicial capacity building. Furthermore, the U.S. government continues to encourage the closure of malls and other outlets where pirated optical discs are the primary product on offer. The U.S. government also urged the Philippines to adopt laws that would extend further IPR protection to the Internet by accommodating electronic commerce and outlawing online piracy, and take further steps to combat piracy of textbooks and other protected printed materials. The U.S. government continues to provide technical assistance and training to strengthen capacity within Philippine agencies responsible for the protection of intellectual property.

IPR Enforcement

The United States continues to have serious concerns regarding the lack of consistent, effective and sustained IPR enforcement in the Philippines. U.S. industry estimates the annual losses due to copyright piracy in the Philippines in 2004 at $139 million. U.S. distributors report high levels of pirated optical disks of films and musical works, and computer games, business software, and widespread unauthorized transmissions of motion pictures and other programming on cable television systems. Trademark infringement in a variety of product lines is also widespread, with counterfeit or pirated merchandise openly available in both legitimate and illegitimate venues.

Serious problems continue to hamper the effective operation of agencies tasked with IPR enforcement. Many enforcement agencies suffer from a lack of resources while IPR issues remain a relatively low priority. Enforcement efforts such as raids and seizures often have only a temporary effect due to ineffective post-raid enforcement. Lack of effective interagency coordination also has had a negative impact on enforcement efforts. The Intellectual Property Code of the Philippines stipulates that the Intellectual Property Office (IPO) has jurisdiction to resolve disputes concerning alleged infringement and licensing. However, the IPO has been unable to effectively coordinate enforcement activities among the agencies responsible, including the Department of Justice, the National Bureau of Investigation, the OMB, the Bureau of Customs (BOC), and the National Telecommunications Commission. The IPO's administrative complaint mechanisms have also been ineffective.

The Philippine government has taken some administrative steps intended to strengthen enforcement. A customs administrative order in September 2002 strengthened the ability of the BOC to prohibit the importation of pirated products, and created an Intellectual Property Unit within the BOC to oversee IPR violations at ports of entry. The BOC is required to maintain an IPR registry where property holders may record their rights and other information to facilitate enforcement. Nonetheless, U.S. industry continues to cite the absence of effective border enforcement as a significant concern.

In addition, the BOC signed a memorandum of agreement with the Videogram Regulatory Board in June 2003, resulting in the Philippine government conducting more raids on suspected counterfeit products and the seizure and destruction of pirated goods valued in the millions of dollars. Nonetheless, significant quantities of pirated and counterfeit products continue to enter the country.

The Philippines created specialized Intellectual Property Courts in 1995, but in practice those courts were not exclusive to IPR cases and thus lacked technical expertise. These courts remained subject to backlogs and delays. In June 2003, the Supreme Court issued a resolution transferring all IP cases to the newly designated Special Commercial Courts, effectively revoking the previously existing 34 special IPR courts. The Special Commercial Courts handle cases formerly adjudicated by the Securities and Exchange Commission, in addition to cases involving IPR issues. It is unclear whether the judges have sufficient time or adequate technical knowledge of IPR issues to be effective. Moreover, IPR cases are not considered serious crimes and take lower precedence in court proceedings.

In October 2003, a new law increased the compensation of judges, with the long-run objective of recruiting more judges to fill up court vacancies. The Department of Justice has also created a task force on intellectual property piracy, with 28 state prosecutors tasked to handle the preliminary investigation of IPR complaints filed with the task force.

There have been very few successful cases of prosecution and imprisonment. Some companies have invested significant resources with investigations and litigation, but many cases remain unresolved as long as a decade after the initial complaint. The Philippines has failed to establish punitive sanctions sufficient to serve as a deterrent to IPR violators. For example, the nominal damage awarded by the Philippine courts in most IPR cases adds little to the cost of doing business for IPR pirates, with no risk of imprisonment.

SERVICES BARRIERS

Basic Telecommunications

The Philippine Constitution limits foreign ownership of telecommunications firms to 40 percent. During the WTO negotiations on basic telecommunications services, the Philippine government made commitments on most basic telecommunications services and adopted some pro-competitive regulatory principles contained in the WTO Reference Paper. It did not provide market access or national treatment for satellite services and made no commitments regarding resale of leased circuits/closed user groups. As of December 2004, the Philippine government has yet to ratify the Fourth Protocol to the WTO General Agreement on Trade in Services (GATS), embodying its proposed obligations under the WTO Basic Telecommunications Agreement, despite U.S. urging.

In February 2003, the Philippine Long Distance Telephone Company (PLDT) and other major Philippine carriers announced on the same day an identical increase in termination rates for foreign carriers, and some cut off direct service to U.S. companies that refused to pay. The U.S. Federal Communications Commission (FCC) ruled that this action was anti-competitive and ordered U.S. companies to cease payments to the Philippine carriers involved. As of March 2004, all Philippine carriers had restored service and had reached interim agreements with U.S. carriers. As a result, the FCC lifted the stop payment order with respect to all Philippine carriers.

As of December 2004, U.S. carriers continue to negotiate new agreements with Philippine carriers.

Financial Services

The Philippines also has yet to ratify the Fifth Protocol to GATS, embodying its obligations under the WTO Financial Services Agreement.

Insurance

Although current practice permits up to 100 percent foreign ownership in the insurance sector, the Philippines only committed in the GATS to a maximum of 51 percent equity participation and grandfathered existing insurers with more than 51 percent foreign equity. Under current regulations, minimum capitalization requirements increase with the degree of foreign equity. As a general rule, only the state-owned government insurance system may provide coverage for government-funded projects. A 1994 administrative order extended this policy to public and private build-operate-transfer projects. Private insurance firms, both domestic and foreign, regard this as a significant trade barrier. Current regulations require all insurance/professional reinsurance companies operating in the Philippines to cede to the industry-owned National Reinsurance Corporation of the Philippines at least 10 percent of outward reinsurance placements.

Banking

Pursuant to 1994 legislation, 10 foreign banks were permitted to open full service branches in the Philippines or to own up to 60 percent of a new or existing local subsidiary. Foreign branch banks are limited to six branches each. Four foreign-owned banks that had been operating in the Philippines prior to 1948 were each allowed to operate up to six additional branches. The Philippines only committed to foreign ownership at 51 percent in its 1997 WTO financial services offer and included a reciprocity test for authorization to establish a commercial presence. The General Banking Law of 2000 (signed in May 2000 to succeed the 1948 General Banking Act) created a seven-year window during which foreign banks may own up to 100 percent of one locally incorporated commercial or thrift bank (up from the previous 60 percent foreign equity ceiling). Such investments can be made only in existing banks since the Bangko Sentral ng Pilipinas (BSP, the central bank) imposed a moratorium on the issuance of new bank licenses in September 1999 to encourage consolidation in the banking system. Current regulations mandate that majority Filipino-owned domestic banks should, at all times, control at least 70 percent of total banking system assets. Rural banking remains completely closed to foreigners.

Securities and Other Financial Services

Membership in the Philippine Stock Exchange is open to foreign-controlled stock brokerages that are incorporated under Philippine law. Foreign equity in securities underwriting companies is limited to 60 percent. Securities underwriting companies not established under Philippine law may underwrite Philippine issues for foreign markets, but not for the domestic market. Although there are no foreign ownership restrictions governing acquisition of shares of mutual funds, current law restricts membership on a board of directors to Philippine citizens. The Philippines took an MFN exemption on foreign equity participation in securities firms, stating that Philippine regulators would approve applications for foreign equity only if Philippine companies enjoy similar rights in the foreign investor's country of origin.

Advertising

The Philippine Constitution limits foreign ownership of advertising agencies to 30 percent. All executive and managing officers of advertising agencies must be Philippine citizens.

Public Utilities

The Philippine Constitution specifically limits the operation of certain utilities (water and sewage, electricity transmission and distribution, telecommunications, public transport) to firms with at least 60 percent ownership by Philippine citizens. All executive and managing officers of such enterprises must be Philippine citizens.

The June 2001 Electric Power Industry Reform Act provides for the privatization of the transmission and distribution assets of the National Power Corporation. Transmission and distribution require a public utility franchise under the Act, which would be subject to a 40 percent foreign-ownership ceiling (1986 Constitution). Legislation facilitating the privatization of the national transmission grid, known as Transco, continues to languish in the Senate, although the Arroyo administration has taken steps to sell transmission assets without additional legislation. Five small hydroelectric generating stations and one large coal-fired power plant had been sold by the end of December 2004. The privatization and modernization of the sector is considered critical to attracting additional foreign investment.

Practice of Professions

As a general rule, the Philippine Constitution reserves the practice of licensed professions (*e.g.*, law, medicine, nursing, accountancy, engineering, architecture, customs brokerage) to Philippine citizens. Philippine law (R.A. 8182) also requires that preference be given to Philippine citizens in the hiring of consultants and other professionals necessary for the implementation of projects funded by foreign assistance. Legislation signed in February 1998 (R.A. 8555) gives the Philippine President the authority to waive this and other preferences applicable to the procurement of goods and services funded with foreign assistance.

Shipping

The Maritime Industry Authority prohibits foreign-flagged vessels from engaging in the provision of domestic carriage services. The country's bareboat chartering laws stipulate that Philippine-flagged vessels should be manned by a Filipino crew and disallows foreign crew/officers, except as supernumeraries.

Express Delivery Services

Foreign air express couriers and airfreight forwarding firms must either contract with a 100 percent Filipino-owned business to provide local delivery services, or establish a domestic company with a minimum of 60 percent Philippine-owned equity. U.S. companies currently operate hub operations in the Philippines, made possible by partial open skies provisions. In 2003, the U.S. government attempted to negotiate amendments to the bilateral aviation agreement with the Philippine government, seeking enhanced passenger rights and cargo seventh-freedom rights. Seventh-freedom cargo rights would enable U.S. and Philippine operators to carry cargo between two countries without having to pass through their home country. During aviation talks in July 2003, the Philippine delegation claimed that seventh-freedom rights were unconstitutional, but the Philippine government is currently reviewing the constitutionality issue. In December 2003, President Arroyo signed an executive order permitting cargo seventh-freedom rights for the two international airports located within the Clark and Subic economic zones for carriers of any country, provided such rights were extended reciprocally to Philippine carriers. As of December 2004, however, implementing rules and regulations of the Executive Order have not been adopted due to domestic opposition.

INVESTMENT BARRIERS

The 1991 Foreign Investment Act contains two "negative lists" enumerating areas where foreign investment is restricted. The restrictions stem from a constitutional provision that permits the Philippine Congress to reserve for Philippine citizens certain areas of investment. The Executive Branch reviewed the list and released a revised version at the end of December 2004.

List A restricts foreign investment in certain sectors because of constitutional or other constraints. Enterprises engaged in retail trade (with paid-up capital of less than $2.5 million, or less than $250,000 for retailers of luxury goods), mass media, small-scale mining, private security, cock fighting, utilization of marine resources, and manufacture of firecrackers and pyrotechnic devices are reserved for Filipino citizens. Up to 25 percent foreign ownership is allowed for enterprises engaged in employee recruitment and for public works construction and repair (with the exception of build-operate-transfer and foreign-funded or -assisted projects, that is, foreign aid, where there is no upper limit). Foreign ownership of 30 percent is allowed for advertising agencies, while 40 percent foreign participation is allowed in natural resource extraction (although the President may authorize 100 percent foreign ownership), educational institutions, public utilities, commercial deep sea fishing, government procurement contracts, and rice and corn processing (after 30 years of operation, before which time 100 percent foreign participation is allowed). Up to 40 percent foreign ownership of private land is allowed. Full foreign participation is allowed for retail trade enterprises with (1) paid-up capital of $2.5 million or more provided that investments for establishing a store is not less than $830,000, or (2) specializing in high end or luxury products, provided that the paid-up capital per store is not less than $250,000. Enterprises engaged in financing and investment activities, including securities underwriting, are limited to 60 percent foreign ownership.

List B restricts foreign ownership (generally to 40 percent) for reasons of national security, defense, public health, safety, and morals. Sectors covered include explosives, firearms, military hardware, massage clinics, and gambling. This list also seeks to protect local small- and medium-sized firms by restricting foreign ownership to no more than 40 percent in non-export firms capitalized at less than $200,000.

In addition to the restrictions noted in the "A" and "B" lists, the Philippines generally imposes a foreign ownership ceiling of 40 percent on firms seeking incentives with the BOI under the annual investment priorities plan. While there are exceptions to the ceiling, divestment to reach the 40 percent level is required within 30 years of the initial investment, or longer as allowed by the BOI. As a general policy, the Philippine Department of Labor and Employment allows the employment of foreigners, provided there are no qualified Philippine citizens who can fill the position. However, the employer must train Filipino understudies and report on such training periodically. The positions of elective officers of enterprises (i.e., president, general manager, and treasurer) are exempt from the labor market test and understudy requirements.

The Philippine Constitution bans foreigners from owning land in the Philippines. The 1994 Investors' Lease Act allows foreign companies investing in the Philippines to lease land for 50 years, renewable once for another 25 years, for a maximum 75 years.

Trade Related Investment Measures (TRIMS)

The BOI-imposed industry-wide local content requirements under its Motor Vehicle Development Program were eliminated in July 2003. The U.S. government is continuing to closely monitor Philippine implementation of this WTO commitment.

In 1995, pursuant to the WTO TRIMS Agreement, the Philippines notified the WTO of its maintenance of local content and foreign exchange balancing requirements to promote investment. Proper notification allowed the Philippines to maintain such measures for a five-year transitional period, ending January 1, 2000. In October 1999, the Philippines requested a five-year extension for the measures in the motor vehicle sector. After extensive consultations on this issue with the United States, the Philippines agreed in November 2001 that it would discontinue the exchange balancing requirements immediately and remove all local content requirements in the motor vehicle sector by July 1, 2003, following the implementation of a phase-out program begun in January 2002. The final phase out of the local content and foreign exchange requirements was completed by July 1, 2003.

Under a 1987 executive order, the soap and detergent industry is required to use a minimum of 60 percent of raw materials that do not endanger the environment. The order also prohibits imports of laundry soap and detergents containing less than 60 percent of such raw materials. The law is intended to require soap and detergent manufacturers to use coconut-based surface-active agents of Philippine origin. In 1999, the Philippine Department of Justice determined that this executive order conflicts with the Philippines' obligations under the WTO TRIMS Agreement and since then, while not repealed, the order has not been enforced.

The United States continues to monitor other TRIMS requirements. Regulations governing the provision of BOI-administered incentives impose a higher export performance requirement for foreign owned enterprises (70 percent of production should be exported) than for Philippine-owned companies (50 percent). A 1987 executive order requires that pharmaceutical firms purchase semisynthetic antibiotics from a specific local company, unless they can demonstrate that the landed cost of imports is at least 20 percent less than that produced by the local firm. A 1984 measure, which requires mining firms to prioritize the sale of copper concentrates to the then government-controlled Philippine Associated Smelting and Refining Company (PASAR), has yet to be repealed despite PASAR's privatization in 1998. In addition, there appear to be unwritten "trade balancing" requirements for firms applying for approval of ventures under the ASEAN Industrial Cooperation scheme.

TRIMS and Retail Trade

Legislation passed by the Philippine Congress in February 2000 requires that foreign retailers, for 10 years after the bill's enactment, source at least 30 percent (for retail enterprises capitalized at no less than $2.5 million) or 10 percent (for retail enterprises specializing in luxury goods) of their inventory, by value, in the Philippines. In addition, prospective investors in the retail sector face a reciprocity requirement. The Retail Trade Act states that only nationals from, or juridical entities formed or incorporated in countries that allow the entry of Filipino retailers, shall be allowed to engage in retail trade in the Philippines.

Public Utilities

The Philippine government's most important privatization effort, the June 2001 Electric Power Industry Reform Act, provided that the National Power Corporation (NPC) should privatize at least 70 percent of its generating assets located in Luzon and Visayas within three years. As of December 2004, NPC had privatized only 12 percent of its generating assets in these regions. The Philippine government is now aiming to reach this target by the end of 2005. Seventy-five percent of the funds used to acquire NPC assets must be inwardly remitted and registered with the BSP. However, foreign participation may be restricted pursuant to a constitutional provision regarding utilization of certain natural resources (such as water and geothermal resources) and power generation as well as provisions requiring a minimum 60 percent Filipino ownership to obtain water rights for hydropower generation under the implementing rules of the 1976 Water Code of the Philippines.

Licensing of Technology

The Philippine government defines technology transfer arrangements as: 1) contracts involving the transfer of systematic knowledge for the manufacture of a product; 2) the application of a process, or rendering of a service including management contracts; and, 3) the transfer, assignment, or licensing of all forms of intellectual property rights, including computer software (except for software developed for the mass market). The Intellectual Property Office requires that all technology transfer arrangements comply with provisions outlined in R.A. 8293, including the prohibition of the use of certain clauses in such arrangements. The scope of these provisions is extremely broad and serves to obstruct the normal contracting process between unrelated parties or as part of intra-company business.

Mining

The Philippine Supreme Court, in a decision issued on December 2, 2004, reversed its January 2004 ruling that declared key provisions of the Mining Act of 1995 unconstitutional and prohibited majority foreign-owned firms from engaging in mining in the Philippines. The reversal allows the mining sector to remain open to direct foreign investment. The sector's unexploited wealth is approximately $840 billion, or ten times the Philippines' annual GDP and 15 times its total foreign debt. The Philippines has some of the richest deposits of metallic and non-metallic minerals in the world (e.g., copper and gold). Mining output currently represents 1.33 percent of gross domestic product (GDP), or about $500 million per year. There are nine million hectares where mineral deposits may be found, although the government has issued permits for only 1.4 percent of those lands.

ANTICOMPETITIVE PRACTICES

The Philippine Constitution provides the government with authority to regulate or prohibit monopolies, and it also bans combinations of entities in restraint of trade and unfair competition. However, there is no comprehensive competition law to implement this constitutional provision. Instead, there are a number of laws dealing with competition, including the 1930 Revised Penal Code, the 1961 Act to Prohibit Monopolies and Combinations in Restraint of Trade, 1949 Civil Code, the 1980 Corporation Code, the 1991 Price Act, and the 1932 Consumer Act. However, enforcement agencies do not effectively enforce these laws, as they do not have the resources or capability to challenge well-entrenched economic and political interests.

ELECTRONIC COMMERCE

The Electronic Commerce Law, signed June 2000, provides that business transactions entered into through an automated electronic system such as the Internet are functional and legal, equivalent to a written document protected under existing laws on commerce. Business-to-business transactions include domestic and international exchange of information, arrangements and contracts for procurement, payments, supply management, transportation, and facility operations. An Internet service provider (ISP) generally is not criminally liable if the ISP does not directly commit any infringement or other unlawful activities or does not cause another party to commit any unlawful act. The law includes provisions to penalize, among other offenses, hacking or cracking (unauthorized access into or interference in a communications system) and piracy (or the unauthorized reproduction, distribution, importation, use, removal, alteration, and downloading, or broadcasting of copyrighted works including legally protected sound recordings). Electronic transactions are not currently subject to any tax measures. However, a reciprocity clause specifies that all benefits, privileges, and advantages established under the act will be enjoyed only by parties whose country of origin grants the same benefits and privileges or advantages to Philippine citizens.

OTHER BARRIERS

Corruption is pervasive and a longstanding problem in the Philippines. The United States has, during discussions under our bilateral TIFA, conveyed to the Philippines its views on specific cases where corruption appears to be a factor and urged the Philippines to tackle the problem of corruption as a means of improving the country's investment climate. The Philippines' score in Transparency International's annual Corruption Perceptions Index survey has averaged 2.5 to 2.6 (out of a best score of 10) since 2002, down from 3.6 in 1999. The Philippine Revised Penal Code, the Anti-Graft and Corrupt Practices Act, and the Code of Ethical Conduct for public officials are intended to combat suspected corruption and related anticompetitive business practices. The Office of the Ombudsman investigates cases of alleged graft and corruption involving public officials. The Sandiganbayan (anti-graft court) prosecutes and adjudicates cases filed by the Ombudsman. In addition, a Presidential Commission Against Graft and Corruption is tasked with prosecuting corruption cases linked to the former Marcos regime.

Soliciting or accepting and offering or giving a bribe are criminal offenses, punishable with imprisonment of between six and 15 years, a fine and/or disqualification from public office or business dealings with the government. As with many other laws, however, enforcement of anti-corruption laws has been inconsistent. The Philippine government launched an initiative to strengthen public and private governance, including anticorruption efforts, in cooperation with bilateral and multilateral aid donors in May 2000. To date, results of this initiative have been limited.

The government seems to have reinvigorated its anti-corruption drive. The Office of the Ombudsman reported improved conviction rates. In December 2003, the President issued an executive order creating an anti-corruption watchdog - the Revenue Integrity Protection Service (RIPS) - in the Department of Finance that has worked closely with the Ombudsman to help curb corruption in revenue collection agencies. President Arroyo has articulated her desire to strengthen the Office of the Ombudsman to become as efficient as Hong Kong's Independent Commission Against Corruption. Achieving that goal will require strong political will and significantly greater financial and human resources than currently dedicated to the effort.

Both foreign and domestic investors express concern over the propensity of Philippine courts and regulators to stray beyond matters of legal interpretation into policymaking functions and about the lack of transparency in these decision-making processes. In addition, there are many reports that, influenced by bribery, courts improperly issue Temporary Restraining Orders impeding the conduct of legitimate commerce. Investors also have raised concerns that regulators rarely have any background in economics, business, or a competitive economic system. This enables entrenched economic interests to manipulate the legal system and regulatory process - whether by bribery or through exploiting the lack of expertise among regulators - to protect market positions. For example, spectrum allocation and licensing in the telecommunications sector is well guarded by incumbent firms, despite regulations that require transparent distribution of these rights.

QATAR

TRADE SUMMARY

The U.S. trade surplus with Qatar was $67 million in 2004, a decrease of $9 million from $76 million in 2003. U.S. goods exports in 2004 were $455 million, up 12 percent from the previous year. Corresponding U.S. imports from Qatar were $387 million, up 17 percent. Qatar is currently the 76th largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Qatar in 2003 was $3.1 billion, up from $2.4 billion in 2002.

The United States and Qatar signed a Trade and Investment Framework Agreement (TIFA) in March 2004, providing a forum to address U.S. concerns.

IMPORT POLICIES

Tariffs

As a member of the Gulf Cooperation Council (GCC), Qatar applies the GCC common external tariff of five percent for most products, with a limited number of country-specific exceptions. Qatar's exceptions to the common external tariff include duty exemptions for basic food products such as wheat, flour, rice, feed grains, and powdered milk. The tariff on alcoholic beverages and tobacco products is 100 percent. Qatar also has a 20 percent tariff on iron bars and rods, non-alloy hot-rolled steel and 12 millimeter steel bars. Qatar maintains a five percent tariff on all textile imports. Projects funded by the Qatar Industrial Development Bank (QIDB) can be granted a customs duty waiver for the import of machinery, raw materials, and other industrial inputs.

Import Licensing

Qatar requires importers to have a license for most products, and only issues import licenses to Qatari nationals. Only authorized local agents are allowed to import specific goods produced by the foreign firms they represent in the local market. However, this requirement may be waived if the local agent fails to provide the necessary spare parts and backup services for the product. The importation and distribution of alcohol is the exclusive right of the Qatar Distribution Company (QDC). Pork and pork derivatives may not be imported.

Documentation Requirements

In Qatar, a letter of credit is the most common instrument for controlling exports and imports. When a letter of credit is opened, the supplier is required to provide a certificate of origin. The Qatari embassy, consulate, or chamber of commerce should notarize the certificate of origin in the United States. To clear goods from customs zones at ports or land boundaries in Qatar, importers must submit a variety of documents, including a bill of lading, certificate of origin, *pro forma* invoice, and import license.

All imported beef and poultry products require a health certificate from the United States and a halal slaughter certificate issued by an approved Islamic center in the United States. The Qatari embassy, consulate, or chamber of commerce in the United States must legalize all shipping documents.

STANDARDS, TESTING, LABELING AND CERTIFICATION

In October 2002, Qatar established a General Authority for Standards and Specification, though most Qatari standards are derived from standards developed by the Gulf Cooperation Council (GCC). The Ministry of Public Health provides input on standards related to public health issues, and Qatar enforces government-mandated shelf-life standards for about seventy-five food products. Qatar also requires importers to comply with shelf-life standards defined in Gulf Standard 150/1993, Part II, although this standard was never officially endorsed. Food products must arrive at the destination with at least half the shelf life remaining, and shelf-life validity of all foodstuffs should not be less than six months at the time of entry of the products into Qatar. All foodstuffs are examined at government central laboratories before they are distributed to consumers. Qatar has not fully implemented the WTO TBT Agreement.

Like most countries in the Gulf Cooperation Council (GCC), Qatar still imposes a ban on imports of U.S. beef in response to the discovery of bovine encephalpathy spongiform syndrome (BSE) in a single dairy cow in Washington State. In February 2004, Qatar also banned imports of U.S. poultry meat due to the discoveries of low pathogenic avian influenza in a flock of chickens in Delaware and high pathogenic avian influenza in a flock of chickens in Texas. In May 2004, Qatar modified the import ban against U.S. poultry to exclude all fresh poultry from Delaware and Texas.

GOVERNMENT PROCUREMENT

Qatar gives preferential treatment to contractors that include high local content in bids for government tenders. As a rule, bids must be submitted through local Qatari agents, but in practice certain exceptions exist. Qatar gives a 10 percent price preference to local firms and a five percent price preference to GCC firms in all government procurement. Qatar is not a signatory to the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

Qatar does not maintain export subsidies but allows duty-free importation for raw materials, machinery, and production inputs for select government tenders and projects established under the Qatar Industrial Development Bank.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Qatar was removed from the Special 301 Watch List in 2003 in recognition of the passage of the 2002 Copyright Law (Law No. 7/2002) and its improved, sustained enforcement actions against copyright infringement. The new copyright law provides a series of important changes to Qatar's legal framework, addressing many of the deficiencies and moving the country towards TRIPS compliance. The law also requires that an "Office for the Protection of Copyright and Neighboring Rights" be established under the Ministry of Economy and Trade. However, the copyright law does not provide explicitly for national treatment or coverage of unpublished works, does not appear to criminalize end-user piracy, and does not clearly treat computer programs as literary works.

An agreement between the UAE and U.S. pharmaceutical companies provides de facto patent protection for a number of U.S. patent-protected medicines. In 2004, the UAE resolved a number of IPR complaints with U.S. pharmaceutical manufacturers. However, concerns over the lack of effective border enforcement remain because the UAE continues to be a transshipment point for pirated and counterfeit goods to neighboring markets.

In 2003, Qatar authorized government officials responsible for IPR enforcement to independently conduct raids and seize pirated material without Ministry of Interior officials, and the Copyright Office continues to prosecute resellers of unlicensed video and software. These efforts have helped significantly reduce piracy in Qatar over the last several years.

In July 2001, the Emir approved Qatar's accession to the Paris Convention for the Protection of Industrial Property. Qatar is also a party to the Berne Convention for the Protection of Literary and Artistic Works. In September 2003, the government of Qatar and Microsoft signed a three-year software licensing agreement that covers all Qatari government ministries and agencies. Qatar is considering joining the WIPO Copyright and Performances & Phonograms Treaties.

Qatar uses the GCC patent law with derogations as needed to comply with its obligations under the TRIPS Agreement. It also established a joint committee between the Ministry of Economy and Commerce and the Ministry of Public Health to coordinate their efforts and ensure that only patented products or authorized copies of pharmaceutical products are registered for sale.

Qatar provides protection for trademarks registered with the Office of Commercial Registration. In June 2002, Qatar promulgated Law No. 9 for Trademarks and Geographic Indicators. However, the implementing regulations to the new law have yet to be issued so it is unclear if the new law complies with obligations under the TRIPs Agreement.

SERVICES BARRIERS

Insurance

In 2004, Law No. 31/2004 amended the Organization of Foreign Capital Investment Law (Law No. 13/2000) to allow foreign investment in the insurance sector pending approval by decree from the Cabinet of Ministers. Foreign insurance companies wishing to operate in Qatar are subject to the same laws that apply to foreign firms in all other sectors.

Banking

In 2004, Law No. 31/2004 amended the Organization of Foreign Capital Investment Law (Law No. 13/2000) to allow foreign investment in the banking sector pending approval by decree from the Cabinet of Ministers. Qatari regulations for local and foreign bank practices are the same, with new licenses available through the Qatar Central Bank application process. In 2003, the Qatar Central Bank allowed foreign banks to establish representational offices and the existing foreign banks in Qatar to open new branches.

Agent and Distributor Rules

The vast majority of foreign firms operating in Qatar are required to engage local agents. Only firms granted 100 percent foreign-ownership by the government in five sectors – agriculture, industry, tourism, education, and health – are excluded from the local agent requirement. Qatari laws state that only Qatari nationals can act as local agents, distributors, or sponsors. The 2002 Commercial Agents Law grants agents and distributors exclusive rights to import, market, and distribute particular goods and services. The Commercial Agents Law allows individuals other than exclusive agents to import products provided they pay up to five percent commission to the registered agent/distributor. In practice, some Qatari ministries may waive the local agent requirement for foreign companies that have contracts directly with the government of Qatar.

INVESTMENT BARRIERS

Qatar's Organization of Foreign Capital Investment Law (Law No. 13/2000) allows foreign investors to own up to 100 percent of projects in the agriculture, tourism, education, industry, and health sectors, pending approval by decree from the government. In the energy sector, foreign companies may own 100 percent of projects subject to approval from the government. The law also gives foreign investors the right to lease land for up to fifty years, which is renewable (also subject to government approval). The new law annuls provisions of Law No. 25 (1990) that restricted foreign-ownership of limited liability business concerns to a maximum of 49 percent. Foreign equity is limited to 49 percent in other sectors. Law No. 13/2000 does not allow foreign investment in the banking, insurance, and telecommunication sectors. In 2004, Qatar amended the Organization of Foreign Capital Investment Law (Law No. 31/2004) to allow foreign investment in the banking and insurance sectors pending approval by decree from the

Cabinet of Ministers. Qatar also passed a law allowing foreigners to own some residential property in select projects of the Pearl of the Gulf Real Estate Development Project (Law No. 17/2004).

Law No. 13/2000 does not allow foreign investment in the telecommunications sector, but foreign nationals are allowed to buy a limited quantity of stock in Qatar Telecommunications (Q-Tel) Company, which is majority-owned by the government of Qatar and has a fifteen-year license to operate as a monopoly.

ELECTRONIC COMMERCE

Qatar has established national committees to explore the possibilities of enhancing electronic commerce and E-Government. Some government services, including immigration services, driver license renewals, and donations to the Zakat Fund are now available online. Some Qatari banks have recently established online electronic banking facilities.

OTHER BARRIERS

Corporate Tax Policies

Qatar levies corporate income taxes on foreign firms at rates from 5 percent to 35 percent of net profits, including profits from majority-owned Qatari joint ventures exceeding 100,000 Qatari riyals (approximately US$30,000). All Qatari owned firms and joint ventures are exempt from corporate income taxes. Under Law No. 13 of 2002, the Ministry of Finance may grant a tax holiday of up to ten years for new foreign investments in key sectors. Other foreign companies may be granted tax exemptions on a case-by-case basis by Emiri Decree.

ROMANIA

TRADE SUMMARY

The U.S. trade deficit with Romania was $351 million in 2004, a decrease of $13 million from $363 million in 2003. U.S. goods exports in 2004 were $502 million, up 36.8 percent from the previous year. Corresponding U.S. imports from Romania were $852 million, up 16.7 percent. Romania is currently the 72nd largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Romania in 2003 was $403 million, up from $332 million in 2002.

IMPORT POLICIES

Tariffs

Romania's trade policies are shaped primarily by its World Trade Organization (WTO) commitments and by its efforts to join the European Union (EU). Romania has a preferential trade agreement with the EU (the "Europe Agreement"), and free trade agreements with its Central European neighbors (the "CEFTA") and European Free Trade Area (EFTA) countries. Romania provides duty-free access to its market for nearly all products imported from the EU but maintains higher levels for non-EU trading partners, including the United States. The free trade arrangements with the EU and EFTA, and the CEFTA, result in customs duty differentials for many U.S. products, often of as much as 30 percent. U.S. exporters have voiced concerns about these tariff differentials, including exporters of distilled spirits, wheat, animal feed supplements, wine, rubber tires, upholstery, lightning arresters, switching gear for telephone lines, and commercial washers and dryers.

Romania has bound most of its tariff rates at the WTO for both agricultural products (average rate of 109 percent) and non-agricultural products (average rate of 34.4 percent). Lower applied rates are generally used, resulting in average applied rates of 30 percent in the case of agricultural products and 16.2 percent in the case of non-agricultural products. Romania is a party to the WTO Information Technology Agreement and eliminated tariffs on products covered by the agreement effective January 1, 2000. High Most Favored Nation (MFN) rates on distilled spirits (60 percent *ad valorem*, except for bourbon whisky, taxed at 35 percent), wine (60 percent), and textiles (12 percent to 32 percent) provide limited access to the Romanian market for these U.S. products.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Romania has begun to harmonize sanitary and phytosanitary measures with those of the EU. Adoption and implementation of EU measures will have a negative impact on U.S. exports of poultry, beef and biotechnology products to Romania. The U.S. Government has been working closely with Romanian officials to ensure that U.S. products continue to have market access for these key products in the interim period leading up to Romania's accession to the EU.

GOVERNMENT PROCUREMENT

Romania is an observer to the WTO Government Procurement Agreement (GPA), but will become subject to the GPA when it joins the EU. With the exception of the procurement of armaments and public works, Romania's government procurement law covers purchases by central government bodies, the parliament, the presidency, the government and ministries, institutions of higher learning, the judiciary, as well as state-owned enterprises.

State-owned companies with the status of commercial companies have their own internally developed purchasing policies based on commercial principles. Article 5 of Decree OG12/1993 establishes two key conditions for the participation of foreign suppliers: (1) Romanian suppliers are granted similar treatment in the country of origin of the foreign supplier; and (2) a Romanian supplier is either not available or cannot fulfill the conditions of the purchase. The Romanian government's web-based public procurement project, operational as of March 2002, is an important step forward in improving government efficiency and curbing institutional corruption. The electronic procurement system is used for basic standardized products. Romania's tender announcements, bid processing, and offer appraisals are entirely computer based, and the list of ongoing and closed auctions, names of adjudicators, and closing prices are available to the public. The government asserts that the project has reduced costs, increased competition and saved more than $120 million since its inception.

EXPORT SUBSIDIES

In 2004, the Romanian government approved export subsidies for 8,080 HL of wine for any destination except the European Union, valued at roughly $111,500, but this amount was not entirely disbursed.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Romania's criminal enforcement with respect to copyright piracy and trademark counterfeiting remains inadequate. Although Romania's legislation is fairly modern and comprehensive, enforcement remains quite weak. Due to inadequate enforcement against copyright piracy, Romania remained on the Special 301 Watch List in 2004. The rates of copyright piracy in Romania remain high, although the authorities have made gradual, limited improvements. Industry reports that levels of DVD piracy have risen to 80 percent, while levels of videocassette piracy are down to 20 percent and the most blatant retail piracy has been eliminated.

While legislative improvements allow for greater criminal prosecution, very few IPR cases are prosecuted and many prosecutors refuse to recognize IPR crime as a social harm. Despite a number of seizures, infringement is increasing as pirated CDs and DVDs are smuggled into

Romania from Ukraine, China, and Moldova. Moreover, police acknowledge that sources in Romania may be building capacity to start domestic production of pirated CDs. In April 2004, as result of cooperation by the Phonogram Producer Union in Romania with its Bulgarian counterpart, Romanian and Bulgarian customs authorities seized 120,000 Bulgarian made DVDs and 52 prints that were to transit through Romania on their way to Russia. Likewise, the Romanian Organization against Copyright Theft cooperated with Romanian customs and border police in Siret to seize an additional shipment of over 100,000 videotapes from Bulgaria en route to Russia via the Ukraine.

Industry groups are working to train judges and prosecutors in IPR law, and have proposed the idea of specialized IPR courts or magistrates. The appointment of a special IPR prosecutor in 2003 by the Prosecutor General has helped efforts to combat IPR piracy. Specially appointed IPR prosecutors have been designated for all Romanian counties, and specialized judges have been designated to serve on the Bucharest Tribunal. IPR training sessions in 2004 specifically focused on training prosecutors, judges, police and border police officers, and customs officials on IPR piracy.

Another area of focus is the illegal sale of counterfeit decoder devices. The stealing of video signal is hindering cable companies' efforts to upgrade networks and keep subscription rates as low as possible. Currently, Audio-Visual Law 504 of 2002 stipulates fines for the trading of counterfeit decoders. However, the law is not enforced, threatening profits of cable companies. One video provider estimates that for each legitimate subscriber, five others are fraudulently watching transmissions through counterfeit devices.

SERVICES BARRIERS

In accordance with its Association Agreement with the EU, Romania was required to implement the EU Broadcast Directive that provides for European content quotas. However, Romania also included a provision of the Directive which gives the government flexibility in implementing this rule. Specifically, Law 119 of 1999, which amended the Audio-Visual Law 48/1992, provides that television stations must gradually devote, as much as possible and by appropriate means, at least 51 percent of total broadcast time to European productions, minus news and sport shows, games, advertising, and teletext services. The result is that at least 40 percent of total broadcasting must be Romanian. Many Romanian Parliamentarians regard the reformation of Romanian legislation to reflect EU requirements impractical, because Romanian stations that comply with the requirement would dramatically lose market share and revenues.

As of August 2002, foreign lawyers not licensed in the practice of Romanian law can only provide legal advice on foreign or international law. They can, however, provide legal advice on Romanian legislation after passing the Romanian Lawyers Union Exam in Romanian Legislation. A law passed in May 2004 brought more flexibility for EU lawyers, enabling them to practice in Romania after a three-year probationary period as an alternative to taking the exam in Romanian legislation. Foreign lawyers may work in Romania as individuals in law offices associated with Romanian firms or international law firms. Due to the frequent legislative changes in this field, it is likely that these legal provisions will be modified.

Romanian law previously required that doctors and health care professionals be Romanian citizens. A law passed in June 2004 makes it possible for doctors and healthcare professionals from EU member states to practice in Romania, but maintains the restriction for non-EU citizens. This effectively hinders the provision of medical services by foreign medical professionals.

Foreign insurance companies must establish a partnership venture with a Romanian partner to enter the Romanian market. Romania has made limited GATS commitments for cross-border provision of insurance services.

During 2003, Romania phased in many of its GATS telecommunications commitments and adopted the pro-competitive regulatory principles contained in the WTO Reference Paper. Romania still needs to establish a transparent, non-discriminatory licensing system as specified in the WTO Reference Paper. Romania, however, has yet to establish a transparent licensing system as specified in the Reference Paper. The government sold a strategic stake in the telephone company Romtelecom to the Hellenic Telecommunications Organization in 1998. While Romtelecom's monopoly on fixed-line telecommunications services expired on January 1, 2003, rates remain subject to governmental supervision through the National Regulatory Authority for Communications (ANRC). Other telecommunications segments (Internet service providers, mobile telephone service providers, cable communications, etc.) have been liberalized.

INVESTMENT BARRIERS

The U.S.-Romania Bilateral Investment Treaty (BIT) provides guarantees for U.S. investors: both national and MFN treatment; the right to make financial transfers freely and without delay; international law standards for expropriation and compensation; and access to binding international arbitration. In 2003, to address several actual and potential incompatibilities between BIT obligations and EU law, the United States exchanged interpretive notes with the governments of Romania and seven other European countries expected to join the EU over the next few years. The United States and the prospective EU member states also agreed to make several narrow amendments to the texts of the relevant BITs. Both the United States and Romania have ratified the BIT amendments, but the amendments will not enter into force until Romania joins the EU.

A controversial law on securities, Law 525/2002, requires that majority shareholders owning 90 percent of the total stock in a firm buy residual shares. This law is considered to be a compromise to provide very limited minority shareholder protection.

A continued impediment to foreign investment is Romania's inconsistent legal and regulatory system. Tax laws change frequently and are unevenly enforced. Tort cases often require lengthy, expensive procedures, and judges' rulings are often not enforced.

In 2003, to address several actual and potential incompatibilities between BIT obligations and EU law, the United States exchanged interpretive notes with the governments of Romania and seven other European countries that have either recently joined the EU or are expected to join over the next few years. The United States and the prospective EU member states also agreed to make several narrow amendments to the texts of the relevant BITs. Both the United States and Romania have ratified the BIT amendments and the amendments will enter into force until close to the time when Romania joins the EU.

ELECTRONIC COMMERCE

Romania has one of the highest incidences of Internet credit card fraud in Europe, which has discouraged international vendors from making payments electronically to Romania. The most common problems result from the use of stolen credit card numbers for the purchase of goods on the Internet. Romanian hackers have also attacked U.S. companies' servers and stolen proprietary information. To counter the millions of dollars worth of credit card fraud each year, in 2002 the Romanian government passed an electronic commerce law that defines and punishes cyber crime. The law includes criminal sanctions for falsifying cyber-pay instruments, carrying out fraudulent financial transactions, accepting fraudulent financial transactions, or performing unlicensed cyber transactions.

Twenty two banks in Romania have acquired at least one type of authorization from the Ministry of Communications and Information Technology for 30 distance access payment instruments of various types. The Ministry issued 12-month valid licenses in order to monitor how the banks used this instrument.

OTHER BARRIERS

Though more than two-thirds of Romanian GDP is created by private entities, large state-owned enterprises and government-subsidized enterprises are major impediments to free and fair market competition in certain sectors. Preferential debt rescheduling and total or partial cancellation of debts, including taxes, by the Romanian government was continuing at least up to the government change in December 2004. In addition, allegations of non-transparent aid schemes to state companies and the firms of well-connected Romanians remain prevalent.

The most common complaints of American companies operating in Romania are the frequency with which the government changes its laws, unfair public procurement, weak enforcement of existing laws, concerns about judicial competence, lack of court impartiality, and corruption.

RUSSIA

TRADE SUMMARY

The U.S. trade deficit with Russia was $8.9 billion in 2004, an increase of $2.7 billion from $6.2 billion in 2003. U.S. goods exports in 2004 were $3.0 billion, up 20.9 percent from the previous year. Corresponding U.S. imports from Russia were $11.8 billion, up 37.5 percent. Russia is currently the 38th largest export market for U.S. goods.

The flow of U.S. foreign direct investment (FDI) to Russia in 2003 was $1.2 billion, up from $666 million in 2002. U.S. FDI in Russia is concentrated largely in the banking and information sectors.

Russia is in the process of negotiating terms of accession to the World Trade Organization (WTO). By the end of 2004, the Government of Russia had met over 20 times with WTO members in formal Working Party meetings and many more times in informal Working Party sessions, plurilaterals, and bilaterally. Russia tabled its initial goods and services market access offers in February 1998 and October 1999, respectively. Russia has subsequently revised its goods and services offers and is currently actively engaged in negotiations with Working Party members on those offers. In 2004, the Russian Federation concluded bilateral agreements on goods and services market access with the European Union and other WTO members; negotiations continue with a number of other trading partners, including the United States.

IMPORT POLICIES AND PRACTICES

Russia continues to maintain a number of barriers with respect to imports, including tariffs and tariff-rate quotas, discriminatory and prohibitive charges and fees, and discriminatory licensing, registration, and certification regimes. Discussions continue within the context of Russia's WTO accession to eliminate these measures or modify them to be consistent with internationally accepted trade policy practices.

Quotas

In January 2003, the Russian Government announced the imposition of a quota for poultry and tariff-rate quotas for pork and beef. These quotas became effective in April and May 2003, respectively. The United States reached an agreement in principle in September 2003 with the Russian Government for market access parameters on poultry, pork and beef. The agreement has yet to be finalized. However in November 2003 and December 2004, Russia announced quota allocations for U.S. poultry, pork, and beef for 2004 and 2005, respectively, based on historical U.S. export levels as provided for in the agreement.

Customs

The new Customs Code, which is intended to bring Russia's customs regime into compliance with WTO requirements, came into force on January 1, 2004 and, despite some early transitional difficulties, overall assessments have been positive. The new Code simplifies customs procedures and establishes specific procedures for the application and payment of tariffs. Draft legislation on customs valuation is being prepared within the Government of Russia and will take the form of amendments to the Customs Tariff Law. Customs authorities continue to assess duties on the royalty value of imported audiovisual materials, such as TV master tapes and DVD masters, rather than basing these duties on the physical value of the material. Russia has announced that it is considering a pre-shipment inspection program for selected goods, although such a program has not yet been formally introduced.

Since 1995, Russian import tariffs have generally ranged from five percent to 30 percent. Import tariffs have declined in importance as a revenue source in recent years, but they remain significant. Under a major revision of the Russian tariff system that took effect as of January 1, 2001, tariffs were consolidated into major product groups (raw materials, semi-finished goods, foodstuffs and finished products) with tariffs ranging from five percent to 20 percent for nearly all tariff categories. However, many rates are accompanied by alternative minimum rates, making the actual applied rate less transparent. The tariff unification resulted in an overall lowering of tariff rates. In addition, there are limited exceptions to the rate scheme, including higher rates for automobiles (25 percent), and higher tariffs on some used goods. The Russian government proceeded with the tariff unification to help combat customs fraud and improve collections; however, while there have been some improvements in this regard, the overall weakness of Russian customs administration still leads to many abuses.

A value-added tax (VAT) is applied to virtually all imports, and excise taxes are applied to a small selection of goods. As of January 1, 2004, the VAT, which is applied to the price of the imported good plus its tariff, was reduced to 18 percent, and there are ongoing discussions to lower it to 15 percent or 16 percent at some point in the future. Although pharmaceuticals and printed matter were exempt from the VAT, and some food products and items for children (e.g., diapers) were taxed at a lower VAT rate of 10 percent, the Government of Russia took steps to eliminate such special provisions in January 2002.

Several industries complain of excessively high tariffs and discriminatory tariff policies over a range of sectors, including motorcycles, sugar, distilled spirits, wine, fruit, processed food, and forest products. Pharmaceutical importers have complained that new pharmaceuticals imported in the clinical trial stage (prior to registration) were improperly assessed the VAT because they could not produce a certificate of registration. Russian import tariffs on automobiles, aircraft, and aircraft parts present particular hindrances to U.S. exports to Russia. In the case of automobiles, combined tariffs, VAT and engine displacement-weighted excise duties can increase import prices by 70 percent for larger U.S.-made passenger cars and sport utility vehicles. In addition, in 2003 the Russian government passed a law that increased customs duties to 25 percent of the customs value for used cars between three and seven years old. The Russian government has also declared protection of the domestic aircraft industry a priority, and the current import tariff on aircraft stands at 20 percent. When the import tariff is added to the VAT and other customs handling fees, the amount of total taxes paid on the importation of foreign aircraft exceeded 40 percent in 2004.

Non-Tariff Barriers

The Russian government continues tight controls on alcohol production (including wine), including: duplicative and strict licensing requirements, import quotas on all distilled spirits except cognac and brandy, export duties, and increased excise taxes. Many of these controls are intended to increase budget revenues. Import licenses are required for various other goods, including encryption software and related equipment, radioactive materials and waste including uranium, strong poisons and narcotics, medicines and dietary supplements, raw and processed sugar, combat and sporting weapons, self-defense articles, explosives, military and ciphering equipment and precious metals, alloys and stones. Most import licenses are issued by the Russian Ministry of Economic Development and Trade or its regional branches and are controlled by the State Customs Committee. Import licenses for sporting weapons and self-defense articles are issued by the Ministry of Internal Affairs. In some industries, such as pharmaceuticals, alcohol, and encryption software and related equipment, activity licenses are also required. According to U.S. information technology companies, overly broad and non-transparent import licensing requirements on cryptography equipment, combined with unclear product standard requirements, create a barrier to doing business in Russia.

With respect to pharmaceutical products, government decisions regarding which products to place on reimbursement lists for state-provided healthcare are having an adverse impact on U.S. exports to Russia. U.S. industry reports that higher-priced imports, which are often safer and of a higher quality than locally produced pharmaceuticals, are often discouraged from appearing on reimbursement lists and state purchases because the government focuses more on price concerns than on the quality and safety of the products.

Although Russia is expected to form one of the largest global markets for new nuclear plants, nuclear fuel, and enriched uranium over the next decade, U.S. companies' ability to supply the market continue to be hindered because of Russia's lack of nuclear liability coverage, which creates a prohibitive risk to business operations. Because no private company can operate without such liability insurance, the Russian state-owned nuclear energy company, TVEL, occupies an unassailable position in the domestic market. At present, Russia is not a signatory to either the Paris or Vienna Conventions related to nuclear liability.

While U.S. exporters face a variety of trade barriers in Russia, lower-than-expected imports from the United States can also be attributed to aggressive marketing and investment strategies of European companies, particularly in the consumer product, food processing, light manufacturing and machinery sectors, bolstered by geographical proximity. However, strong economic growth and an appreciating ruble have led to increased Russian purchasing power and have allowed U.S. agricultural export levels to rebound.

EXPORT POLICIES AND PRACTICES

The Russian government's industrial policy guidelines emphasize export promotion and import substitution. In practice, there has been limited budgetary funding for such initiatives. The subsidy-like effect of Russia's current domestic gas pricing policy is a key issue due to the potentially adverse impact this policy may have on certain U.S. industries. The price of gas for Russian industrial consumers is artificially low, and, according to numerous reports, prices are well below the full cost of production. The downstream effects of this pricing policy are significant, as gas sells on Russia's domestic market for about $25/tcm, while estimates of cost-recovery levels are at roughly $35-$40/tcm, and gas for export on the world market sells at $100-$120/tcm. Russia is currently considering numerous reform plans for the sector and has been gradually increasing domestic prices. However, the gas sector and Gazprom, Russia's monopoly supplier, play a significant role in Russia's economy. The Russian Government is proceeding slowly and cautiously with reform of the sector. Russia has no direct export subsidies on agricultural products, although it has suggested in WTO accession talks that it would like to reserve the option to use agricultural export subsidies in the future.

Russia maintains export taxes on a variety of products. In May 1999, Russia imposed a 15 percent export tariff on ferrous steel scrap (amounting to not less than 15 euros per metric ton). Additional restrictions preventing steel scrap exports from certain Russian ports were imposed in 2001 and subsequently removed in early 2004. At a time when world demand and prices have been rising the export tax has tended to increase Russian steel scrap supply, providing artificially low scrap costs to Russian steel producers while limiting global supply of a key steel input. Russian export tariffs on copper cathode have also created a market distortion, which is promoting vertical integration within the Russian copper industry. Russia currently maintains a 10 percent export tariff on copper cathode and a 0 percent export duty on copper wire rod. As a result, it is advantageous to export the higher value-added product (copper wire rod). Russian copper wire rod producers can obtain favorable prices on copper cathode, since cathode producers cannot export their product for its fair market value.

STANDARDS, TESTING, LABELING AND CERTIFICATION

U.S. companies report that Russian standards and procedures for certifying that imported products and equipment meet those standards are non-transparent, expensive, time-consuming, and redundant. Russian regulatory bodies seem reluctant to accept foreign testing centers' data or conformity assessment certificates. U.S. firms active in Russia have also complained of the limited opportunity to comment on proposed changes in standards or certification requirements before the changes are implemented. Occasional jurisdictional overlap and disputes between different regulatory bodies compound certification problems. Russia claims that amendments to the Law on Certification of Products and Services, which took effect July 31, 1998, generally meet the requirements of the WTO. The law allows a manufacturer to submit a declaration of conformity as part of the conformity assessment certification procedure for a limited number of products. The government of Russia has established a list of 200 products eligible for this procedure. U.S. industry estimates that approximately 30 percent of the 22,000 Russian standards now conform to international norms.

On July 2, 2003, the Law on Technical Regulations came into force. The law is intended to bring Russia's standards regime into compliance with WTO norms and streamline the adoption of standards and the conformity assessment certification process for imported goods. Under the provisions of this law, many mandatory standards will become voluntary. Implementation of this new law will result in the amendment of approximately 300 separate laws and regulations. At the end of an implementation period, any existing technical regulation which has not been revised in accordance with the new law will become a voluntary standard.

The current Russian product certification regime makes it difficult to introduce foreign-produced products into the Russian market. Manufacturers of telecommunications equipment, construction materials and equipment, and oil and gas equipment have reported serious difficulties in obtaining product approvals. Certification procedures for telecommunications equipment were thrown into confusion on January 1, 2004 when the Law on Communications went into effect, eliminating old certification procedures without replacing them with new ones. The law was a step forward in one sense, since it allowed for manufacturers to self-certify some products. However, no implementing regulations have been released specifying which equipment is eligible for self-certification. The situation is causing serious problems for telecommunications equipment providers who are unable to get new products certified for import, especially for those companies that regularly introduce new products with short life-spans (such as mobile phone manufacturers). Implementing regulations are not expected to be completed until mid-2005.

In December 2002, the Russian Ministry of Health established a mandatory conformity assessment requirement for pharmaceuticals. This certification requirement appears to be duplicative of other certification requirements for pharmaceuticals and could lead to delays in the marketing of medicines. Although the 2002 certification requirement was to be replaced by self-certification through a declaration of conformity in 2004, to date no guidelines have been issued for the self-certification scheme. Companies therefore must continue to comply with the old certification requirements. In addition to pharmaceuticals and telecommunications equipment, manufacturers of alcoholic beverages are also subject to certification requirements imposed by the Federal Agency for Technical Regulation and Metrology and the Ministry of Health.

Russian sanitary and phytosanitary (SPS) measures are often burdensome and at times do not appear to be grounded in science-based concerns regarding food safety. Bioengineered food products are likely to continue to attract regulatory attention from Russian authorities in the coming year, as companies continue to register new products and develop varieties for testing. Russia has taken measures against U.S. poultry and beef exports due to alleged food safety concerns. In August 2002, the United States concluded intensive negotiations with Russia on a new veterinary certificate for U.S. poultry. In December 2003, the Russian government announced a ban on U.S. beef after the detection of one positive case of Bovine Spongiform Encephalopathy (BSE) in the State of Washington. Russian officials, however, have stressed the temporary nature of this measure and have announced that the quota share for U.S. beef will not be reallocated as a result.

GOVERNMENT PROCUREMENT

Russian ministries and government agencies are frequent purchasers of equipment, goods and services for their own needs or for the needs of various domestic organizations or groups (i.e., the military, regional health organizations, or population centers located in remote areas). In April 1997, the Russian government established procedures for public tenders for some government procurement, but this process needs clearer guidelines. A draft law on government procurement was being considered within the Government of Russia in late 2004. The law would eliminate restrictions on the participation of foreign suppliers, ensure transparency of the government procurement mechanism, and reduce opportunities for corruption. However, the draft law also contains a provision that would allow the government to limit procurement of foreign goods, works or services. Domestic suppliers are not currently accorded many official advantages or privileges in competing for government procurement. Nonetheless, the Russian government shows a strong political bias toward supporting domestic industries.

Manufacturers of telecommunications equipment, construction materials and equipment, and oil and gas equipment have reported serious difficulties in obtaining product approvals. The new Law on Telecommunications overrode an amendment to the Federal Law on Communications that encouraged government agencies to purchase Russian-produced equipment.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Significant deficiencies remain in Russia's regime for the protection of intellectual property. Due to these deficiencies, a case remains pending to review Russia's status as a beneficiary country under the U.S. Generalized System of Preferences (GSP) Program. Russia has been on the Special 301 Priority Watch List since 1997.

Intellectual property violations continue to be a serious problem in Russia. According to industry sources, estimated losses to U.S. copyright industries due to copyright piracy (films, videos, sound recordings, books and computer software) continue to exceed $1 billion annually. 2004 saw a continued rise in illegal optical disc production capacity far in excess of Russian demand, with pirated products intended not only for domestic consumption but also for export. The U.S. film industry estimates that over 80 percent of all DVDs on the Russian market are pirated. Piracy of music is estimated at approximately 66 percent of sales, and software piracy at approximately 88 percent.

In 2004 the Russian government took some steps to combat IPR problems. Following reorganization of the Russian government in the spring of 2004, IPR issues were placed under the direction of the Minister of Science and Education Andrey Fursenko, who has stressed the importance of protecting intellectual property in order to stimulate Russian innovation and economic development. The Federal Service for Intellectual Property, Patents and Trademarks (Rospatent) has been given an overall coordinating role between the various Russian government agencies involved in IPR issues.

In July 2004, the Interministerial IPR Commission, which was established in 2002 and was reconstituted under Prime Minister Fradkov, approved an IPR Action Plan that includes a combination of legislative changes, administrative measures and enforcement actions to be undertaken by a variety of federal ministries. While the plan contains a number of welcome actions, its success will rely primarily on the effectiveness of the Russian government's enforcement efforts, which remain the weak link in Russia's IPR regime.

In order to gain accession to the WTO, Russia has passed a number of laws in order to meet obligations under the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement). In 2004, Russia passed amendments to the Law on Copyright and Related Rights to provide protection for pre-existing copyrighted works and sound recordings. In 2002 and 2003, Russia enacted amendments to laws on trademark and appellations of origin, patents, protection of layout designs for integrated circuits, plant varieties, and protection of computer software and databases. Strengthened criminal penalties for IPR infringement went into effect on January 1, 1997, and even stronger penalties were adopted in Article 146 of the Criminal Code in 2003. The Russian government's Licensing Law, adopted in August 2001, included licensing requirements for optical media producers, and several licenses were suspended in the summer of 2004 for failure to meet these requirements. However, U.S. copyright industries believe that the licensing scheme provision is inadequate to control optical media piracy and have pressed the Russian government to adopt a comprehensive regulatory framework dealing with the production and distribution of optical media.

Despite concerted efforts, several other deficiencies remain in Russia’s IPR regime, including: a lack of explicit protection for test data for pharmaceutical products and agricultural chemicals, denial of national treatment for protection of geographical indications, and problems with enforcement.

U.S. and multinational companies also continue to report counterfeiting of patented and trademarked goods as a serious problem, especially for consumer goods, distilled spirits and pharmaceuticals.

While the Russian government has begun to pay more attention to IPR enforcement, this issue remains the weak link in the protection of IPR in Russia. Even where Russian law provides for serious penalties such as the destruction of counterfeit or pirated goods, goods seized during enforcement actions are rarely destroyed and consequently may return to the stream of commerce even if they are found to be illegal. In the vast majority of cases, alleged infringers receive miniscule fines or suspended prison sentences.

Administrative and judicial review bodies are beginning to become active in protecting IPR in Russia, and the number of police and judges with relevant expertise, though still small, is expanding. At the prosecutorial and judicial levels, many officials still do not consider IPR infringement a serious offense when compared to other crimes, although an increasing number of prosecutors are willing to file cases related to copyright piracy. U.S. investors also consider the Russian court system ill-prepared to handle sophisticated patent cases. However, a specialized higher patent chamber has been established at Rospatent, which has brought greater expertise and efficiency to resolution of patent disputes.

SERVICES BARRIERS

Discrimination against foreign providers of non-financial services is, in most cases, not the result of federal law, but can stem from abuse of power, sub-national regulations, and practices that may violate Russian law. For example, a few foreign providers of services have sometimes noted discrimination in obtaining licenses from local authorities. Foreign providers are forced to pay a range of fees that domestic companies allegedly bypass via bribes.

Central Bank regulation 721-U previously required that purchases of foreign currency of greater than $10,000 for a limited number of imported services, mainly in the hospitality and tourism sector (e.g. Russians seeking to buy foreign currency to pay foreign suppliers), must receive advance permission from the Ministry of Finance. While intended to combat capital flight, this measure had the potential to delay financial transactions and impede the participation of foreign firms in this sector. The Law on Currency Monitoring and Regulation, signed by President Putin on December 10, 2003, eliminates the need for advance permission but requires Central Bank notification in most circumstances unless specifically noted in the law. Under the new law, all currency controls are to be lifted by 2007.

Financial Services and Insurance

The federal law on "Banks and Banking Activity of 1996" permits foreign banks to establish subsidiaries in Russia. The law allows the Central Bank to impose a ceiling on the total amount of foreign bank capital calculated as a percentage of the total bank capital in Russia, although the Central Bank has never availed itself of this clause. Russia has been asked to clarify the situation and explicitly remove any limits as part of its WTO accession, and the Central Bank has indicated that it does not want to dissuade foreign banks from operating in Russia. Since 1997, the Central Bank has required new foreign bank subsidiaries to have a minimum of Euro 10 million in capital (the same requirement is applied to domestic banks) and that at least 75 percent of the bank's employees and 50 percent of the bank's management board be of Russian nationality. Heads of foreign banks' Russian offices are required to be proficient in the Russian language. In WTO accession talks, the United States has urged the Russian side to liberalize completely by allowing branches, as well as subsidiaries.

In the insurance sector, since 1999 foreign majority-owned insurance companies have been allowed to operate in Russia subject to a 49 percent equity restriction. (Foreign firms that were active in Russia when this requirement came into effect were grandfathered in and not subject to the foreign cap limit.) In addition, total foreign capital in the Russian insurance sector is limited to 25 percent. However, on January 17, 2004, a law came into effect that effectively exempts EU-based insurance companies from the 49-percent cap (based on a 1994 Russia-EU treaty). This exemption also applies to insurance companies based in the EU that have since been purchased by non-EU foreign companies. The government of Russia has stated that access to the Russian insurance sector will be equalized for all potential foreign participants upon Russian accession to the WTO. However, until then, EU firms will enjoy an advantage over their counterparts from the United States and elsewhere, since they can offer life and mandatory forms of insurance in Russia directly, without the requirement to work through a majority Russian-owned partner. The new law retains the requirement that chief executives and chief accountants of foreign insurers operating in Russia be Russian citizens.

Telecommunications

In the telecommunications sector, the new Law on Communications went into effect on January 1, 2004; however, final implementation regulations corresponding to the Law have not been released. The Law's impact on the business of competitive alternative telecommunications operators (many of which enjoy large foreign investment), could be substantial, since these companies will now fall under tighter government regulation. In particular, new regulations on interconnection (the process by which alternative operators connect their networks to the Russian public switched telephone network) place interconnection contracts and fees under the tight regulatory authority of the Ministry of Communications. Alternative operators fear that interconnection fees will be raised in order to subsidize network upgrades of government-owned and ministry-controlled local and long distance operators. Many in the telecommunications industry were disappointed that the new law did not improve transparency in the licensing process, and have criticized the five- to ten-year license terms, which they argue do not allow them sufficient time to recoup their investment. Russian policy in the telecommunications sector is a subject of debate in negotiations on Russia's WTO accession, and current WTO members have expressed concern that the new Law on Communications may de-liberalize a now relatively open market, particularly through the adoption of new rules and regulations as set forth under the new Law.

In December 2004, the legal situation in the telecommunications sector was no clearer than at the beginning of the year. As noted above, the Law on Communications is a framework law that depends on implementing regulations in order to function properly. Very few of these regulations have been completed, leading to much legal confusion in the sector over such important issues as licensing requirements and procedures, equipment certification, and the nature of the Law's universal services provision. The regulations are not expected to be completed until the middle of 2005.

Significant barriers have been identified in the provision of satellite telecommunications services in Russia. In particular, satellite regulation is not transparent, and the legal requirements and administrative responsibilities associated with the provision of these services appear to be discriminatory. The Russian Federation establishes a preference for the use of Russian satellite communications systems, which puts competing satellite systems at a disadvantage.

Russian entities with over 50 percent foreign ownership are prohibited from sponsoring television or video programs or from establishing television organizations capable of being received in more than 50 percent of Russia's territory or by more than 50 percent of the population. Tax preferences formerly provided to Russian film producers were abolished effective January 1, 2002.

INVESTMENT BARRIERS

Despite the passage of a new law regulating foreign investment in June 1999, Russian foreign investment regulations and notification requirements can be confusing and contradictory. The law on foreign investment provides that a single agency (still undesignated) will register foreign investments and that all branches of foreign firms must be registered. In 2004, the Russian Duma did not actively consider ratifying the Bilateral Investment Treaty (BIT) between the United States and Russia that was signed in 1992 and ratified by the U.S. Senate that same year.

Corruption in commercial and bureaucratic transactions and problems with the implementation of customs regulations also inhibit investment. Trade and investment would benefit, for example, from improved dispute resolution mechanisms, the systematic protection of minority stockholders rights, conversion to international accounting standards, and the adoption and adherence by companies to business codes of conduct. Initiatives to address these shortcomings, either through regulation, administrative reform or government-sponsored voluntary codes of conduct have made little headway in countering endemic corruption. More transparent implementation of customs, taxation, licensing and other administrative regulations is necessary. Anecdotally, transfer-pricing tactics continue to be employed by large Russian holding companies to the detriment of minority shareholders.

National Treatment

The 1999 Investment Law codifies principles of national treatment for foreign investors, including the right to purchase securities, transfer property rights, protect rights in Russian courts, repatriate funds abroad after payment of duties and taxes, and receive compensation for nationalizations or illegal acts of Russian government bodies. However, the law goes on to state that federal law may provide for a number of exceptions, including, where necessary, for "the protection of the constitution, public morals and health, and the rights and lawful interest of other persons and the defense of the state." The potentially large number of exceptions thus gives considerable discretion to the Russian government. The law also provides a "grandfather clause" that stipulates that existing 'priority' foreign investment projects with foreign participation of over 25 percent be protected from unforeseeable changes in the tax regime or new limitations on foreign investment. The law defines 'priority' projects as those with a foreign charter capital of over $4.1 million and with a total investment of over $41 million. However, the lack of corresponding tax and customs regulations means that any protection afforded investors by this clause is only theoretical.

The Land Code that was passed in 2001 allows equal treatment of domestic and foreign entities to buy land and buildings, although purchase of agricultural land by foreigners is still prohibited. Discussion on specific land policy continues, including legislation on transfer of use, but a conclusion has not yet been reached. Foreign entities are restricted from buying land close to federal borders and in areas that the President determines are critical to national security. Current Russian legislation restricts foreign investment in the aerospace industry to less than 25 percent of an enterprise. Foreign investment in the natural gas monopoly, Gazprom, is formally limited to 20 percent, and in the electrical power giant, Unified Energy Systems, to 25 percent. In practice, these limits have been exceeded, and there is discussion of whether to eliminate or raise the limits. Foreign investment in Russian spirits concerns is limited to 49 percent.

In addition to a burdensome certification process, the satellite industry reports that a local presence requirement and discriminatory treatment create barriers to doing business in Russia. Telecommunications companies also report investment restrictions.

Taxes

Effective January 1, 2005, the Unified Social Tax, which is paid by employers and covers pensions, healthcare and social security, dropped from an effective rate of about 30 percent to a top rate of 26 percent on salaries up to 280,000 rubles (about $10,000) a year. A major tax reform law became effective January 1, 2001 and reduced tax-related investment barriers, substantially amending the VAT, excise taxes, personal income tax and unified social tax. It established a flat income tax rate of 13 percent for residents and 30 percent for non-residents. The corporate profit tax has been 24 percent since 2002.

Regions and municipalities have the authority to grant exemptions to the regional portion of profits taxes, with some regions granted specific regional exemptions, particularly the Leningrad region. Regions are not able to grant individual tax exemptions.

The VAT refund system functions poorly. Companies report that VAT refunds due to a Russia-based exporter, which should be provided within three months after a claim is submitted, often do not occur on time, with customs and tax authorities applying a number of burdensome additional requirements for refunds. In addition, input VAT is often not refunded for a number of reasons, forcing exporters to avail themselves of the court system. VAT refunds on exports are also the source of a great deal of fraud, making it that much more difficult for legitimate exporters to obtain their refund.

Duties on the production and export of oil, which are generally quite high, have been adjusted several times over the past few years. In 2003, new legislation restored full discretion to the Russian government in establishing export duties on refined petroleum products. To take advantage of revenues generated by high oil prices and foster diversification in the economy, changes in the tax code in 2004 shifted the burden away from manufacturing and services and towards the energy sector. In 2004, the Government considered bills to establish a legislative mandate for a differentiated tax on oil production and, more broadly, higher taxes in the oil sector, but nothing has been signed into law as of yet.

Energy Sector

A new Law on Natural Resources (also called the Subsoil Law) is expected to be presented to the Duma in spring 2005 with passage most likely slated for the middle of the year. The law deals with the natural resources licensing regime and represents a modest improvement over the current law (as amended). In the current draft, the government has included several of the key provisions that industry had been seeking, including a guarantee that licenses will carry over from the exploration to the development stage, a provision that licenses will be based on civil rather than administrative law, and a limitation on the number of reasons for license revocation. However, the law will likely also include a provision allowing only companies registered in Russia to participate in auctions to win the right to use natural resources. There is also a possibility that the law will contain language reserving the right for the Russian government to allocate certain "strategic" reserves outside of a transparent auction process.

In September 2004, the government announced that Gazprom would merge with state-owned oil company Rosneft, and through a share-swap grant the state a direct, controlling stake in the gas giant. President Putin also indicated that the “ring-fence” -- the cap on foreign share ownership in Gazprom -- would subsequently be eliminated. Removal of the “ring fence” would clearly be a boon for investors (increased ability to trade in Gazprom shares) and Gazprom (improved access to capital), but the long-term significance is that it is the first step in reforming Gazprom. However, it is unclear whether the government has the political will to follow through with reform of this omnipresent giant. In addition to this, Gazprom has been acquiring other assets in related industries (electrical generation and oil) in what appears to be an effort to create a national champion in the energy sector. Several major oil companies are working out the terms for joint exploration and development of large gas fields under Gazprom's control.

In 2003, President Putin signed legislation implementing legal amendments restricting Russia's use of production sharing agreements (PSAs). PSAs are designed for energy projects that require high capital expenditure and a long period before profits or significant tax revenues are generated. These amendments severely limit the number of energy deposits eligible for PSA status and favor companies that bid to develop energy deposits on a non-PSA basis. The PSA amendments include local content requirements or targets for equipment and local labor. Another provision in the existing PSA regime limits the total amount of foreign investment to 30 percent of Russia's "strategic" oil reserves. The precise meaning and significance of this restriction remain unclear.

More than $5 billion has been invested to date in the Sakhalin II consortium, and ExxonMobil has announced that it is proceeding with a $12 billion development plan for Sakhalin I. The $2.6 billion Caspian Pipeline Consortium (CPC) project, inaugurated in 2001, has periodically had to resist bureaucratic pressure to designate it as a "natural monopoly", even though its founding agreements explicitly exempt it from application of the Law on Natural Monopolies. Such a designation could cast doubt on CPC shareholders' discretion regarding transportation fees and access rights for the pipeline. CPC is currently working out the details that will allow expansion of the pipeline's capacity.

Central Bank restrictions on medium-term loans (more than 180 days) of hard currency for the purchase of imported inputs have also presented an obstacle to foreign investment projects in Russia's energy sector. In addition, non-transparent regulations concerning environmental permits and pipeline access remain of concern to potential U.S. investors.

Aviation

Despite an aging civil aviation fleet and use of outmoded avionics and engines, replenishment of the Russian fleet has not proceeded. Current Russian law stipulates preferential treatment (tax holidays, guarantees on investment) for Russian and foreign investors in aviation-related research and manufacturing ventures. However, it limits the share of foreign capital in aviation enterprises to less than 25 percent and requires that board members and senior management staff be Russian citizens. There is speculation that the 25 percent limit could be raised or done away with altogether to make way for further investment. Some observers, however, doubt that recent proposals to raise the limit to 49 percent would be sufficient to attract capital from abroad for Russia's aircraft industry.

In 1996, the United States and Russia concluded a Joint Memorandum of Understanding (MOU) reflecting U.S. concerns about barriers to the Russian civil aircraft market and the application of international trade rules to the Russian aircraft sector. The MOU states that U.S. aircraft manufacturers will be able to participate in the Russian market and share in its growth. The MOU also makes clear that the Russian aircraft industry will become fully integrated into the international economy over time. Russia pledged to eventually undertake the same international trade principles in the aircraft sector as the United States and many others have done, as embodied in the WTO Agreement on Trade in Civil Aircraft. In the interim, the MOU commits Russia to take steps, such as the granting of tariff waivers, to enable Russian airlines to meet their needs for non-Russian aircraft on a non-discriminatory basis.

Despite continued bilateral assurances that the Russian Government would join the Agreement on Trade in Civil Aircraft, Russia has expressed an unwillingness to join the Agreement in the context of WTO accession. Through 2004, discussions continued with the aim of securing a commitment that Russia join the Agreement, including adopting a commitment to eliminate tariffs on aircraft and parts.

The government is also looking to reorganize and revitalize Russia's aircraft industry in the context of a larger restructuring plan for Russia's defense industry. Specifically, the government is considering large-scale consolidation of the aircraft industry through mergers and privatizations. Additionally, to support the leasing of Russian-manufactured aircraft, the Russian Government has injected over $100 million (in the form of share purchases) into two domestic aircraft leasing companies -- Ilyushin Finance Company (IFC) and Finance Leasing Company (FLC). Several Russian airlines operate Western aircraft. Two of the airlines (Aeroflot and Transaero) acquired these aircraft through tariff waiver schemes in the mid-1990s. The other airlines that operate Western aircraft acquired them more recently and paid the import tariffs. While Russian airlines have been vocal about seeking further tariff waivers, the Russian Government has been equally vocal in saying they will not be granted.

Capital Flows

Russia has assumed obligations under Article VIII of the IMF Articles of Agreement to permit free payment of current transactions, but the Central Bank continues to maintain controls on capital flows. A new law on currency controls took effect in 2004, which reduces the maximum amount to which Russia’s surrender requirement for export earnings may be set to 30 percent, and which will completely abolish the requirement by 2007. In November 2004, this surrender requirement was reduced to 10 percent of export earnings, well under the 30 percent limitation imposed on the Central Bank. Investors may repatriate coupon payments on government and corporate bonds and invest in other bonds. Licenses are not required for most transactions transferring money into or out of Russia, but proper notification is required. Russia also maintains an advance import prepayment requirement that serves as a trade barrier.

ELECTRONIC COMMERCE

E-commerce has yet to become a serious market in Russia. Though Internet access in Russia is steadily growing, penetration is only around 15 percent of the population, with roughly half of these users located in the Moscow and St. Petersburg regions. Relatively low usage, combined with a low number of credit card users and onerous tax laws means that e-commerce will grow slowly in the near future. An electronic commerce bill has been under consideration for several years. The bill, while closely following an International Chamber of Commerce model bill, has significant problems, including the fact that it limits electronic transactions to the sale and purchase of moveable goods, services agreements, and shipments. The adoption of the new World Intellectual Property Organization (WIPO) Digital Treaties should help promote the development of electronic commerce in Russia.

Russian law does not currently provide identical legislative protection for both electronic and paper documents. Settlement issues need to be considered in conjunction with applicable currency control provisions. Registered trademarks are not recognized as entailing rights to the equivalent domain names and the property rights which trademarks secure for their registered owners are currently not protected for the purposes of Internet advertising and commerce through web sites. Tax implications from electronic commerce are unclear.

A law on electronic digital signatures came into effect in 2002. The law defines electronic signatures strictly, making public-key technology the sole acceptable digital signature technology. It also requires that hardware and software used in digital signature authentication programs be certified in Russia. This gives the Russian government the right to insist on the decompilation of electronic signature programs, and thus gives the government access to the source code.

OTHER BARRIERS

The U.S. logging industry reports that illegal logging accounts for as much as 20 to 30 percent of Russia's timber harvest. Illegal wood supplies have begun to appear in China, hurting U.S. exports to that market.

SAUDI ARABIA

TRADE SUMMARY

The U.S. trade deficit with Saudi Arabia was $15.7 billion in 2004, an increase of $2.2 billion from $13.5 billion in 2003. U.S. goods exports in 2004 were $5.2 billion, up 14.1 percent from the previous year. Corresponding U.S. imports from Saudi Arabia were $20.9 billion, up 15.8 percent. Saudi Arabia is currently the 25th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Saudi Arabia in 2003 was $4.2 billion, up from 3.8 billion 2002.

Saudi Arabia is in the process of negotiating terms of accession to the World Trade Organization (WTO), providing a forum to address U.S. concerns.

IMPORT POLICIES

Tariffs

As a member of the Gulf Cooperation Council (GCC), Saudi Arabia applies the GCC common external tariff of five percent for most products, with a number of country-specific exceptions. Saudi Arabia's exceptions to the common external tariff include 394 products that may be imported duty-free, including aircraft and most livestock. The Saudi government also applies a 12 percent tariff on 492 products, in some cases to protect local industries. Certain textile imports, including carpets but not apparel, are among the products to which the 12 percent rate applies. A number of Saudi infant industries enjoy 20 percent tariff protection, including those producing sesame extract, furniture, cooking salt, edible offal, rabbit meat, mineral water, and plastic pipes. In addition, long-life milk and nine other agricultural products are subject to a 25 percent tariff. Saudi Arabia imposes a 40 percent tariff on dates. Saudi Arabia also imposes a 100 percent tariff on cigarette and other tobacco imports. (Saudi Arabia's complete tariff schedule is available online at www.saudi-customs.net.)

Import Licensing

In Saudi Arabia, the importation of certain articles is either prohibited or requires special approval from competent authorities. Specifically, the importation of alcohol, firearms, illegal drugs, pork products, and used clothing is prohibited. Imports of agriculture seeds, live animals, fresh and frozen meat, books, periodicals, movies, tapes, religious books and tapes, chemicals and harmful materials, pharmaceutical products, wireless equipment, horses, radio-controlled model airplanes, products containing alcohol, natural asphalt, and archaeological artifacts require special approval.

Documentation Requirements

To export products to Saudi Arabia from the United States, the U.S. Department of State's Authentication Division and the Saudi Embassy or Consulate must authenticate the documentation. The United States-Saudi Arabian Business Council is not required to certify legal documents, but will do so if requested. Some products, most notably agricultural biotechnology products, need a certificate from the country of origin attesting to the product's fitness for human consumption and that it is sold widely in the country of origin. Products that are regulated by the Saudi Arabian Standards Organization (SASO) must have a certificate of conformity issued through Saudi Arabia's International Conformity Certification Program (ICCP) before entering the country. The categories of regulated products include, but are not limited to, playground, amusement and fairground equipment, toys, electrical elements and electronics, automotive, and chemicals.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Saudi Arabia initiated the ICCP in 1995 to monitor and control the quality of certain products imported into the country. The ICCP applied to 76 regulated consumer product lines and is managed by a private firm that inspects and tests shipments bound for Saudi Arabia on behalf of Saudi Arabia Standards Organization (SASO). The United States and many other WTO members have raised concerns about the ICCP in the context of Saudi Arabia's efforts to join the WTO. Among other concerns, the United States and many other exporting countries believe the ICCP needs modifications to be consistent with the WTO Agreement on Technical Barriers to Trade. For example, the ICCP accords favorable treatment to products manufactured in the Gulf Region, is more trade-restrictive than necessary, charges *ad valorem* fees unrelated to cost, and lacks transparency.

The proposal for a GCC Conformity Certification Scheme for Countries Exporting to GCC Member Countries is still under consideration by member countries. Saudi Arabia announced in October 2003 that it would abandon the ICCP in favor of a new, yet to be determined, system. The United States has had a constructive dialogue on this issue to establish alternative regulatory practices that address identified difficulties in the context of Saudi Arabia's WTO accession.

The Saudi Arabian Standards Organization (SASO) imposes shelf-life requirements on food products. In practice, the Saudi government requires imported food products to arrive in port with at least one-half of their shelf-life remaining, calculated from the date of production. Over the past few years, SASO has shortened the shelf-life duration for baby foods, eggs, stuffed cookies, chilled meats, and some snack foods, all products of interest to U.S. exporters. Saudi Arabia requires an animal protein-free certificate for imports of poultry, beef, and lamb and their by-products. In addition, the Saudi Government bans the import of therapeutic medicines used in animal feed. These measures were taken with little to no advance notice, contrary to Saudi statements to follow the provisions of the relevant WTO agreements. The United States is working with the Saudi Government to resolve U.S. concerns.

The Ministry of Commerce and Industry imposed a mandatory labeling requirement for agricultural biotechnology products in late 2000, and a requirement that importers sign a pledge stating that they were aware of the possible health risks of such products. After a period of uncertainty, the Ministry of Commerce announced a positive-labeling-only requirement (i.e., containing ingredients derived from biotechnology), rather than requiring labels for both the presence and absence of such ingredients, and delayed implementation until December 1, 2001. The Ministry also imposed a ban on imports of agricultural biotechnology products manufactured from animal products. In November 2002, the Ministry of Commerce agreed to language that it would accept on an export certificate to accompany all shipments containing agricultural biotechnology products entering Saudi Arabia. The export certificate must be issued by a government entity from the country of origin, preferably at the federal level, although the sub-federal level is acceptable. In February 2003, the Ministry of Agriculture issued new regulations for labeling of biotechnology food. U.S. companies found to be in violation of Saudi Arabia's biotechnology labeling requirements are banned from exporting the product in question into the Kingdom, but may continue to export other products that have been suitably labeled.

GOVERNMENT PROCUREMENT

Saudi Arabia's government contracts on project implementation and procurement are regulated by several royal decrees that strongly favor GCC nationals. However, most defense contracts are negotiated outside these regulations. Under a 1983 decree, contractors must subcontract 30 percent of the value of the contract, including support services, to majority-owned Saudi firms. An exemption is granted in instances where no Saudi company can provide goods and services to fulfill the procurement requirement.

In addition, Article 1(d) of the tender regulations requires that Saudi individuals and establishments be given preference over all other suppliers in government procurement. The same regulations also accord preference to other suppliers as long as Saudi nationals hold at least 51 percent of such suppliers' capital.

Article 1(e) of the tender regulations gives preference to products of Saudi origin that satisfy the requirements of the procurement, even when the product is inferior to that of a foreign counterpart. Saudi Arabia also gives priority in government purchasing programs to GCC products. These items receive up to a 10 percent price preference over non-GCC products in all government procurements in which foreign suppliers participate.

Foreign suppliers involved in government projects are required to establish a training program for Saudi nationals. Some government contracts also require a minimum amount of subcontracting with Saudi companies. In addition, the Saudi Government may favor Saudi-foreign joint venture companies as opposed to foreign firms and will also support companies that use Saudi manufactured goods and services. However, foreign companies providing services to the Saudi Arabian government can do so without a Saudi service agent and can market their services to various other public entities directly. For large military projects, there is frequently an offset requirement.

Foreign contractors working only for the government, if not already registered to do business in Saudi Arabia, are required to obtain temporary registration from the Ministry of Commerce and Industry within 30 days of contract signing. Foreign companies also are allowed to establish a branch office through the new Foreign Investment Regulations. These branch offices are usually approved only for foreign defense contractors and high-technology companies, while for others, a liaison office may be established to supervise work in Saudi Arabia and to facilitate coordination between the Saudi government and company headquarters.

In June 2003, the Saudi Council of Ministers passed a resolution calling for increased transparency in government-budgeted projects and government contracts. The Saudi Council of Chambers of Commerce and Industry has begun publishing the details of government contracts on its website. The contract information to be published includes title, parties, date, financial value, brief description, duration, place of execution, and point of contact information.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Currently on the Special 301 Watch List, Saudi Arabia is currently working to revise its intellectual property laws to bring them into conformity with the WTO TRIPS Agreement as part of its efforts to join the WTO. An updated Trademark Law took effect at the end of 2002, and an updated Copyright Law took effect in March 2004. Both laws allow for increased deterrent penalties for violators, including fines and prison sentences. A new unified law on patents, industrial designs, plant varieties, and integrated circuits is working its way through the legislative process.

Saudi Arabia has made progress on copyright enforcement over the past few years, with a steadily increasing number of raids/seizures and fines imposed. However, U.S. software manufacturers seek greater Saudi government enforcement action against software copiers and end-users of unauthorized software. Another area of concern involves the counterfeiting of U.S. trademarked products. The Saudi government is aware of these problems and is considering options to combat them. U.S. industry has expressed frustration with the lack of transparency in the enforcement system, procedural hurdles to judicial enforcement, and a failure to impose punishment at the higher end of deterrent penalties.

The United States continues to have serious concerns over the lack of protection and enforcement of patents. Although Saudi Arabia has recently taken measures to hire and train more examiners, the approval of patents often takes several years due to extreme delays in the processing of patent applications. The currently inadequate patent application process has resulted in a large backlog of patent applications and prevents U.S. patent holders from obtaining adequate protection. The United States has urged Saudi Arabia to enact the new Patent Law legislation as soon as possible, and to ensure some form of *de facto* patent protection in the near term to address the backlog of pending applications.

SERVICES BARRIERS

Insurance

In the last two years, the Saudi Arabian Government has implemented a series of laws giving structure to what had been an essentially unregulated sector and mandating certain types of insurance coverage within the Kingdom. In June 2002, the Cooperative Health Insurance Council issued the by-laws of a mandatory cooperative health insurance scheme. The scheme will be implemented gradually and will require employers to pay for insurance coverage of foreign workers and dependent family members. In November 2002, third party motor vehicle insurance became mandatory in the Kingdom. In October 2003, the Saudi Arabian Government enacted the Control Law for Co-Operative Insurance Companies. The law requires all insurance companies operating in the Kingdom to be locally registered, publicly owned firms. In keeping with adherence to Islamic principles, insurance companies will need to operate on a co-operative or mutual basis. Firms will need to register with the Saudi Arabian Monetary Agency (SAMA). The law sets capitalization requirements for insurers at SR100 million ($26.7 million).

SAMA began accepting applications for insurance operations in November 2003. Insurance firms operating in the Kingdom may offer any insurance product in both the commercial and personal markets as long as the firm is organized consistent with the co-operative insurance structure.

Banking

Although the Saudi Banking Control Law does not limit foreign participation, for the past twenty years the Saudi Arabian Monetary Agency has capped foreign ownership in commercial banks to 40 percent of any individual bank operation. In the last few years, the Saudi Government has taken steps to increase foreign participation in its banking sector by granting operating licenses to foreign banks. The Bahrain based Gulf International Bank (GIB), Dubai-based Emirates Bank International, and Kuwait Bank currently operate in the Kingdom. In November 2003, the Saudi Government granted an operational license to Deutsche Bank. The Saudi Capital Markets Law came into effect in February 2004. The law provides for the creation of investment banks and brokerages in the Kingdom. Allowed levels of foreign participation in these ventures have not been finalized. As capital markets regulations are finalized, Saudi Arabian investment banking will likely see significant growth.

Shipping

Saudi Arabia gives preferences to national carriers for up to 40 percent of government-related cargoes. Under these rules, the Saudi national shipping company and United Arab Shipping Company receive preferences.

Agent and Distributor Rules

Saudi law requires that domestic distributors receive licenses from the Ministry of Commerce and Industry. Only Saudi citizens can obtain licenses. A recent GCC decision may broaden this to make all GCC citizens eligible. Nationals from the GCC countries are also allowed to engage in trading and retail activities, including real estate. In July 2001, the Saudi Council of Ministers canceled the requirement for foreign companies with government contracts to have a Saudi service agent.

INVESTMENT BARRIERS

In April 2000, Saudi Arabia's Council of Ministers approved a new foreign direct investment code with the goal of facilitating establishment of foreign companies, both joint-ventures and 100 percent foreign owned, in Saudi Arabia. Key provisions allow foreign investors to transfer money freely in and out of the country, allow joint-venture companies to sponsor their foreign investors as well as their foreign employees (all foreigners in Saudi Arabia need a legal sponsor to reside in the country), and permit foreign investors to own real property for company activities. The Saudi Arabian General Investment Authority (SAGIA) was established to manage investments under the new code under the guidance of the Supreme Economic Council. In March 2003, SAGIA opened a Women's Investment Center in addition to its existing Service Centers. In theory, SAGIA must decide to grant or refuse a license within 30 days of receiving an application and supporting documentation from the investor. While SAGIA is intended as a one-stop-shop for foreign investors, some companies still experience delays in subsequent steps, for example, in obtaining a commercial registry or purchasing property. Following SAGIA's recommendations, the Supreme Economic Council released a negative list in February 2001 of sectors in which foreign investment is prohibited. The Council updated the negative list in 2003, further reducing the number of sectors and subsectors prohibited to foreign investors. Foreign investment is currently prohibited in 19 sectors and subsectors. (SAGIA publishes the negative list at www.sagia.gov.sa.) SAGIA reportedly approved about 2000 projects representing more than $14 billion by the end of October 2003, with foreign investors accounting for 85 percent of the total. Figures on actual projects initiated or foreign direct investment inflows are not available. Though statistics for foreign direct investment inflows are imprecise, aggregate SAGIA information indicates that 36 percent of project capital comes from U.S. sources, by far the largest single contributor. In October 2003, SAGIA announced that additional foreign direct investments of nearly $1 trillion will likely be required over the next 20 years (over $100 billion in the energy sector alone).

In October 2003, the Saudi Government passed the Capital Markets Law. The law took effect in February 2004. It allows for the creation of financial intermediaries (stock brokerages and investment banks). The law creates an independent stock market and an independent stock market regulatory body. The law sets SR50 million ($13.3 million) capitalization requirements for brokerages and provides penalties for insider trading and wrongful dissemination of information. The law also allows for the development of long-term investment instruments. Allowed levels of foreign participation in investment banks and brokerages have not been finalized. The new law does not repeal the prohibition on direct foreign participation in the Saudi stock market. Foreigners, however, can continue to purchase shares in bank operated investment funds. Foreign participation in these funds is limited to 10 percent of the total value of the fund.

ELECTRONIC COMMERCE

Saudi Arabia is studying various options to incorporate electronic commerce into government and private industry. A proposed National Information Technology Plan encompasses infrastructure, industry, electronic government, and electronic learning. The Ministry of Commerce and Industry completed a national project in 2001 for safeguarding dealers' rights, establishing a dispute-settlement mechanism, and endorsing digital signatures. In December 2003, the Saudi Government approved an electronic system for the official authentication of documents (similar to notarization) through the Internet. Called the e-attestation service, it will be available to members of the Chambers of Commerce and Industry. As of late 2004, the e-attestation service was undergoing limited testing by Chambers of Commerce and Industry members.

OTHER BARRIERS

Corporate Tax Policies

Saudi Arabia taxes foreign companies, but domestic entities are only required to pay zakat (a charitable donation). Only foreign-owned corporations and the foreign-owned portion of joint ventures are subject to the corporate income tax, which ranges from 20 percent to 30 percent of net profits. Domestic corporate partners are subject to a 2.5 percent tax on assets. A resolution issued by the Council of Ministers in April 2000 also eliminated the 10-year tax holiday previously enjoyed by companies and instead provided loss carry-forward provisions without any time limits. In January 2003, the Shoura (Consultative) Council rejected a proposed income tax on expatriate workers.

SINGAPORE

TRADE SUMMARY

The U.S. trade surplus with Singapore was $4.3 billion in 2004, an increase of $2.9 billion from $1.4 billion in 2003. U.S. goods exports in 2004 were $19.6 billion, up 18.4 percent from the previous year. Corresponding U.S. imports from Singapore were $15.3 billion, up 1.1 percent. Singapore is currently the 11th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Singapore were $6.9 billion in 2003 (latest data available), and U.S. imports were $2.3 billion. Sales of services in Singapore by majority U.S.-owned affiliates were $5.3 billion in 2002 (latest data available), while sales of services in the United States by majority Singapore-owned firms were $1.4 billion.

The stock of U.S. foreign direct investment (FDI) in Singapore in 2003 was $57.6 billion, up from $52.4 billion in 2002. U.S. FDI in Singapore is concentrated largely in the manufacturing, wholesale, and information sectors.

The United States and Singapore signed a free trade agreement (FTA) on May 6, 2003, which entered into force on January 1, 2004.

IMPORT POLICIES

Tariffs

With the exception of four tariff lines covering beer and certain other alcoholic beverages, Singapore imposed no tariffs on imported goods prior to entry into force of the FTA. These four remaining tariffs have been eliminated under the United States-Singapore FTA. For social and/or environmental reasons, however, Singapore levies high excise taxes on distilled spirits and wine, tobacco products, motor vehicles (all of which are imported), and gasoline. During the Uruguay Round of multilateral trade negotiations, Singapore agreed to bind 70.5 percent of its tariff lines. The United States-Singapore FTA binds all Singapore tariffs at zero for imports from the United States meeting the FTA's rules of origin requirements. Singapore does not impose any restrictions or duties on imports or exports of textiles and apparel.

Singapore is a signatory to the WTO Information Technology Agreement (ITA). In addition to the United States-Singapore FTA and Singapore's FTAs with ASEAN, Australia, the European Free Trade Association, Japan, Jordan and New Zealand, Singapore is negotiating FTAs with Bahrain, Canada, Egypt, India, Mexico, Panama, Peru, South Korea, Sri Lanka, and a trilateral agreement with Chile and New Zealand. Singapore is also part of the ASEAN-China FTA.

All imported goods (whether for domestic sale or re-export) are taxable under the Goods and Services Tax (GST), which is levied at five percent as of January 1, 2004, unless the goods are specifically given GST relief by the Director General of Customs. Goods kept in Free Trade Zones are not subject to GST, but are subject to GST if they later are imported into Singapore.

Import Licenses

All imports require an import permit, although for most goods this is largely a statistical tracking requirement. Special import licenses are required for certain goods, including strategic items, hazardous chemicals, films and videos, arms and ammunition, as well as agricultural biotechnology products, food derived from agricultural biotechnology products, prescription drugs, over-the-counter drugs, vitamins with very high dosages of certain nutrients, and cosmetics/skin care products. Due to the United States-Singapore FTA, Singapore now allows the importation of chewing gum with therapeutic value for sale, subject to certain provisions.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Under the Consumer Protection (Safety Requirements) Regulations (2002), 45 categories of electrical products[?], electronics, and gas home appliances and accessories are listed as controlled goods and require a stamp of approval from the Government of Singapore's standards and certification authority (SPRING Singapore). SPRING Singapore recognizes test reports issued by accredited testing laboratories and national certification bodies. To date, SPRING Singapore has registered more than 22,000 models of controlled goods. SPRING Singapore has also developed standards for certain sanitary and building products. Labels are required on imported food, drugs, liquors, paints, and solvents. Repackaged foods must be labeled to show (in English) the appropriate designation of the food content printed in capital letters at least 1/16 inch high; whether the foods are compounded, mixed or blended; the minimum quantity stated in metric net weight or measure, the name and address of the manufacturer or seller; and the country of origin.

GOVERNMENT PROCUREMENT

Government procurement is generally free and open. However, some U.S. firms have expressed concerns that government-owned and government-linked companies (GLCs) may receive preferential treatment in the government procurement process. Singapore’s government denies that it gives any preferences to GLCs or that GLCs give preferences to other GLCs. Singapore has been a party to the WTO Government Procurement Agreement (GPA) since 1997. The United States-Singapore FTA provides additional government procurement access to U.S. firms by expanding the contracts that are subject to FTA disciplines.

EXPORT SUBSIDIES

Singapore's government does not directly subsidize exports, although it offers significant incentives to attract foreign investment, with most incentives directed at export-oriented industries. In addition to tax incentives and reimbursements to exporters for certain costs incurred in trade promotion, the government also offers grants to new service suppliers.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Intellectual property protection has improved since the late 1990s, leading to the removal of Singapore from the Special 301 Watch List in 2001. In line with its United States-Singapore FTA commitments, amendments to the Trademarks Act, the Patents Act, a new Plant Varieties Protection Act, and a new Manufacture of Optical Discs Act came into effect in July 2004. Amended Copyright and Broadcasting Acts came into effect in January 2005. After they are fully implemented, Singapore's new and amended IPR laws should help mitigate ongoing problems related to the availability of pirated optical disks, use of unlicensed software by businesses, the transshipment of pirated and counterfeit material through Singapore, and a burdensome process to get pirated material removed from Internet sites.

In accordance with its FTA commitments, Singapore is in the process of implementing Article 1 to Article 6 of the Joint Recommendation Concerning Provisions on the Protection of Well-Known Marks of 1999 and has signed and ratified the International Convention for the Protection of New Varieties of Plants (1991). After the amended Copyright Act comes into force, Singapore will initiate procedures to sign and ratify the Convention Relating to the Distribution of Program-Carrying Signals Transmitted by Satellite (1974), the WIPO Copyright Treaty (1996), and the WIPO Performances and Phonograms Treaty (1996). Singapore is a signatory to three other international IPR agreements: the Paris Convention, the Patent Cooperation Treaty, and the Budapest Treaty.

Parallel Imports

Under the amended Patents Act, the patent owner will have a right to bring an action to stop an importer of "grey market goods" from importing the patent owner's patented product, if the product has not previously been sold or distributed in Singapore.

Enforcement

Singapore's government contends that it is determined to improve IPR protection. Law enforcement efforts have contributed to a sharp reduction in the production of pirated material and blatant storefront retail piracy. According to the Singapore Police, the value of counterfeit and pirated goods seized in 2003 was $19 million, more than three times that in 2002 ($5.0 million). The Singapore Police, in a coordinated operation with the U.S. Federal Bureau of Investigation (FBI), broke up two Internet piracy syndicates, one with links to an international crime syndicate. Singapore's music piracy rate averages 10 percent to 24 percent, according to IFPI; for movies, the piracy rate is about 15 percent according to the Motion Picture Association. Despite tighter enforcement measures, pirated optical disks continue to be available from vendors in street markets, public housing estates, and at other high pedestrian-volume locations. The Intellectual Property Rights Branch (IPRB) of the Singapore Police is working to address such activities, but targeting highly mobile pirates is a challenge. Software piracy levels in Singapore, while among the lowest in the Asia-Pacific region, are almost double the estimated level in the United States; business software losses were estimated at nearly $90 million in 2003.

Prior to the aforementioned changes in IP laws, Singapore's "self help" policy on IPR enforcement, which treated IPR infringement differently than other theft crimes, had placed an undue and expensive burden on rights holders to initiate raids and prosecute pirates. Under the FTA, Singapore has agreed to implement changes to the "self-help" policy, and committed to continue to assume principal responsibility for enforcement.

Over the past three years, a number of local educational institutions (the majority government-operated) have signed agreements to come into compliance with their legal obligations to pay royalty fees to publishers in exchange for the right to duplicate copyrighted printed works for use in course materials. Under the Singapore IP laws, the penalty for illegal photocopying is a fine of up to S$100,000 or a jail term of up to five years, or both. These agreements appear to have helped in resolving a longstanding problem, at least among these educational institutions. Some commercial copy centers, however, continue to routinely take orders to copy entire textbooks. While some raids have been conducted, their effectiveness is limited.

Transshipment

Although it is a major transshipment and transit point for sea and air cargo, Singapore does not collect information on the contents and destinations of most transshipment and transit trade, which account for 80 percent of the cargo coming through the port. This lack of information makes enforcement against transshipment or transit trade in infringing products extremely difficult. In addition, it is unclear whether Singapore law provides for the seizure of infringing products that are being transshipped or in transit. Pursuant to commitments under the FTA, Singapore passed legislation in November 2003 to provide for information-sharing with customs authorities of its FTA partners, including the United States.

Internet

In accordance with the United States-Singapore FTA, Singapore amended its Copyright Act to provide improved protection for digital works, and outline requirements and procedures for removing infringing material from Internet sites.

SERVICES BARRIERS

Basic Telecommunications

On April 1, 2000, Singapore removed all barriers limiting foreign entry to the telecommunications sector. Any foreign or domestic company can provide facilities-based (fixed line or mobile) or services-based (local, international, and callback) telecommunications services. The former monopoly telecommunications service provider, Singapore Telecommunications (SingTel), which is 62.7 percent government-owned, faces competition in all market segments, including fixed-line, mobile, and paging services, although its main competitors, MobileOne and Starhub are also government-linked companies. However, there are concerns that SingTel charges other operators anticompetitive prices for the use of local leased circuits in the Singapore broadband business market. Under the United States-Singapore FTA, Singapore agreed to ensure that major suppliers of leased circuits services provide U.S. enterprises with leased circuit services at rates that are reasonable. The Infocomm Development Authority (IDA) in December 2003 issued a decision requiring Singtel to reduce its wholesale price for its local leased circuits. Following Singtel's appeal, the Ministry of Information, Communications and the Arts (MICA) in July 2004 upheld IDA's decision (with certain modifications). In October 2004, IDA accepted SingTel's amendments to its Reference Interconnection Offer (RIO) in line with MICA's decision. Concerns remain that Singtel's interconnection rates and requirements are anti-competitive .

Under the United States-Singapore FTA, Singapore also agreed that dominant licensees (e.g. SingTel) must offer cost-based access to submarine cable-landing stations and allow sharing of facilities. IDA issued a decision in September 2004 that telecommunications operators owning international capacity that connects to SingTel's submarine cable landing stations will have greater access to this capacity. IDA accepted SingTel's amendments to its RIO in October 2004.

In November 2004, IDA announced its preliminary decision to grant SingTel's proposal to exempt eight out of ten services that come under its Dominant Licensee obligations. This implied that SingTel would no longer be required to file tariffs on these particular services, and would have more flexibility in packaging and bundling them. IDA has invited public comments prior to issuing a final decision.

Audiovisual and Media Services

The local free-to-air broadcasting, cable and newspaper sectors are effectively closed to foreign firms. Section 47 of the Broadcasting Act restricts foreign equity ownership of companies broadcasting to the Singapore domestic market to less than 49 percent, although the Act also gives the Media Development Authority (MDA), which replaced the Singapore Broadcasting Authority (SBA), authority to waive this requirement. The MDA, which came into operation on January 1, 2003, is a merger of the SBA, Films and Publications Department and the Singapore Film Commission. The government also imposes limits on individual equity stakes in broadcasting companies. Part X of the Broadcasting Act states that no person shall, without prior approval, hold more than five percent of the shares issued by a broadcasting company (the limit was three percent before mid-2002). In practice, all current local radio and television broadcasters are government-owned or government-linked. Between 2000 and September, 2004, Singapore Press Holdings (SPH) and MediaCorp each held newspaper and broadcasting licenses. Prior to 2000, SPH held the principal newspaper license and MediaCorp the only broadcasting license. In September, 2004, citing mounting losses in both companies, SPH and MediaCorp announced that they would merge their television operations under a new company, MediaCorp TV, 80 percent owned by MediaCorp and 20 percent by SPH. In approving the SPH/MediaCorp deal, MDA specified that MediaCorp TV had to outsource at least 285 hours of local content production to independent television production companies. Separately, SPH also absorbed MediaCorp's print media business. The exclusivity given to Singapore Cable Vision as the sole provider of pay television services since 1995 ended on June 30, 2002. However, there were no bidders for a second pay television operating license in a government tender held in mid-2003.

Singapore restricts the use of satellite receiving dishes and has not authorized direct-to-home satellite television services. Under Part VI of the Broadcasting Act, the installation and operation of certain apparatus on which broadcasting services are received, including satellite-receiving dishes, is prohibited except under license from the MDA. The government does not routinely issue licenses for television receive-only satellite receiving systems. Satellite broadcasters that want to operate their own uplink facility must get a special license from MDA. Satellite broadcasters who do not have their own facility are restricted to using one of four available uplink facilities.

The Newspaper and Printing Presses Act restricts equity ownership (local or foreign) to five percent per shareholder (raised from three percent before mid-2002), unless the government approves a larger shareholding, and requires that all the directors of a newspaper company be Singapore citizens. The Act defines "newspaper" broadly as "any publication containing news, intelligence, reports of occurrences, or any remarks, observations or comments...printed in any language and published for sale or free distribution." Newspaper companies must issue two classes of shares, ordinary and management, with the latter only available to citizens of Singapore or Singapore companies that have been approved by the government. Holders of management shares have an effective veto over board decisions.

Any importer, producer, distributor, or exhibitor of newspaper (including newsletters, magazines, and periodicals) and audiovisual material, including every film or television program shown in Singapore, must be licensed by the MDA. Authority to issue permits for the distribution of publications is discretionary and subject to conditions; the government can deny or revoke permits without warning or without giving a reason. Some foreign news publications are "gazetted," *i.e.*, numerically limited by the government. The publications must carry printed approval notices or control stickers. Audiovisual content that is considered obscene, excessively violent, or capable of provoking racial or religious conflict is subject to censorship. Only organizations whose business is to exhibit films in cinemas or whose objective is to promote the appreciation of films are allowed to screen "Restricted (Artistic)" films. This category includes those films considered to have sexual, violent, religious, or racial themes.

Legal Services

Foreign law firms with offices in Singapore face certain restrictions. They are unable to practice Singapore law, cannot employ Singapore lawyers to practice Singapore law, and cannot litigate in local courts. U.S. law firms can only provide legal services in relation to Singapore law through a Joint Law Venture (JLV) or Formal Law Alliance (FLA) with a Singapore law firm, subject to the Guidelines for Registration of Foreign Lawyers in Joint Law Ventures to Practice Singapore Law. These conditions have been relaxed for U.S. law firms, pursuant to commitments made by Singapore under the United States-Singapore FTA. As of November 1, 2003, there is only one U.S. JLV. From June 1, 2004, foreign lawyers are allowed to represent parties in arbitration in Singapore without the need for a Singapore attorney to be present.

With the exception of law degrees from certain Australian/New Zealand and British universities, no foreign university law degrees are recognized for the purpose of admission to practice law in Singapore. Under the United States -Singapore FTA, Singapore will recognize law degrees from four U.S. law schools.

Engineering and Architectural Services

Engineering and architecture firms can be 100 percent foreign-owned. The requirement that the chairman and two-thirds of the firm's board of directors must comprise engineers, architects, or land surveyors registered with local professional bodies has been removed in line with the provisions of the United States-Singapore FTA. Professional engineering work in Singapore must be under the control and management of a director of the corporation who: (1) is a registered owner of at least one share of the corporation if it is an unlimited corporation; (2) is a registered professional engineer ordinarily resident in Singapore; and (3) has a valid practicing certificate. In the case of a partnership, only registered engineers may have a beneficial interest in the capital assets and profits of the firm, and the business of the partnership must be under the control and management of a registered professional engineer who ordinarily resides in Singapore. Similar requirements apply to architectural firms. Singapore limits the schools it recognizes as acceptable for qualifying to sit for the local architect exam; in the case of U.S.

graduates, it accepts the Bachelor of Architecture degree accredited to the U.S. National Architectural Accrediting Board. Applicants must also have a minimum of between 12 months and two years practical experience in Singapore.

Accounting and Tax Services

The major international accounting firms all operate in Singapore. Public accountants and at least one partner of a public accounting firm must reside in Singapore. Only public accountants who are members of the Institute of Certified Public Accountants of Singapore and registered with the Public Accountants Board of Singapore may practice public accountancy in the country. The Board recognizes U.S. accountants registered with the American Institute of Certified Public Accountants.

Banking and Securities

Retail Banking

There are legal distinctions between offshore and domestic banking units, and the type of license held (full, wholesale or offshore).

Prior to 1999, the Monetary Authority of Singapore (MAS) had not issued new licenses for local retail banking for over two decades to either foreign or domestic institutions because it considered Singapore's banking sector to be saturated. In addition to barring any other foreign banks from entering the retail market, existing foreign banks in Singapore were not allowed to open new branches, freely relocate existing branches, or operate off-premise Automated Teller Machines (ATMs). However, foreign banks were permitted to install electronic terminals at their corporate clients' premises, and to provide home banking services through telephone and personal computers. Aside from retail banking, Singapore laws do not distinguish operationally between foreign and domestic banks.

In 1999, Singapore embarked on a five-year banking liberalization program to ease restrictions on foreign banks. Since then, the government has removed the 40 percent ceiling on foreign ownership of local banks and granted "qualifying full bank" (QFB) licenses to six foreign banks. A QFB license allows these banks to operate up to 15 customer service locations (branches or off-premise ATMs), up to ten of which can be branches; to relocate freely existing branches; and to share ATMs among themselves. They also can provide electronic funds transfer, point-of-sale debit services, accept Central Provident Fund (CPF) fixed deposits, and provide Supplementary Retirement Scheme and CPF Investment Scheme accounts. In December 2002, the government removed the 20 percent aggregate foreign shareholding limit on finance companies. Despite liberalization, foreign banks in the domestic retail banking sector still face significant restrictions and are not accorded national treatment. Aside from the limit on the number of foreign QFBs and their customer service locations, the foreign QFBs are not allowed to access the local ATM network. Local retail banks do not face similar constraints. Some foreign charge card issuers also face problems because they are prohibited from allowing their local card holders from accessing their accounts through the local ATM networks. Customers of foreign banks are also unable to access their accounts for cash withdrawals, transfers, or bill payments at ATMs operated by banks other than their own. In June 2004, the Singapore government announced further liberalization measures in the domestic retail banking sector. Effective January 1, 2005, QFBs are permitted to increase their service locations from 15 to a maximum of 25. They are also allowed to negotiate with local banks to let their credit card holders obtain cash advances through the local banks' ATM networks.

Acquisition of 5 percent, 12 percent, and 20 percent or more of the voting shares of a local bank requires approval from the Minister of Finance. Moreover, in spite of lifting the formal ceilings on foreign ownership of local banks and finance companies, officials have indicated that they will not allow a foreign takeover of a local bank or finance company. Officials say they want local banks' share of total resident deposits to remain above 50 percent. Foreign penetration of the banking system in Singapore is comparatively high, with foreign banks holding about 40 percent of non-bank deposits.

The United States-Singapore FTA removes most of these restrictions, improving U.S. market access in retail banking in Singapore. The current ban on new licenses for full service banks will be lifted no later than June 30, 2005, and by January 1, 2007 for "wholesale" banks. Licensed full-service U.S. banks will be able to offer all their services at up to 30 locations by January 1, 2006, and an unlimited number of locations within two years after January 1, 2006. Locally incorporated subsidiaries of U.S. banks can apply for access to local ATM networks after June 30, 2006; for non-locally-incorporated U.S. QFBs, this will commence January 1, 2008.

Restricted and Offshore Banking

In 2001, the MAS announced plans to replace the current licensing regime that distinguishes between on-shore and offshore activities to one that distinguishes between retail and wholesale activities. The restricted and offshore licenses are progressively being replaced by a Wholesale Bank (WB) license, which allows wholesale banks to conduct a wider range of activities than restricted or offshore banks. All WBs will be allowed to accept Singapore dollar fixed deposits above S$250,000, to offer Singapore dollar current accounts, and will not face any limits on the amount of Singapore dollar lending. Over time, the MAS will upgrade all Banks to WB status. The application process will also be open to new foreign bank entrants. License criteria include prudential considerations and the applicants' current scope of activities and future plans in Singapore.

Restrictions on Singapore Dollar Lending

Non-residents can borrow local currency freely if the proceeds are used in Singapore. Non-resident financial entities may also borrow local currency freely for their activities outside

Singapore provided the proceeds are swapped or converted into foreign currency. There are no controls on the borrowing of Singapore dollars by residents.

Securities

In 1999-2000, the government launched a number of initiatives aimed at liberalizing Singapore's capital markets. As of January 2002, all trading restrictions formerly placed on foreign-owned stockbrokers were removed. However, aggregate investment by foreigners may not exceed 70 percent of the paid-up capital of dealers that are members of the Singapore Exchange Limited (SGX). Legislation, which took effect in October 2002, allows for the direct registration of foreign funds, provided the prospectus is from an entity registered as a foreign company in Singapore and the fund is approved by the MAS. (Formerly, mutual funds and unit trusts had to be registered with the Registry of Companies and Businesses, under the Companies Act, before they could be marketed locally. In practice, this meant that foreign mutual funds had to be registered twice, once in the country of origin and again in Singapore.) The United States-Singapore FTA has relaxed certain conditions that foreign asset managers were required to meet in order to offer products under Singapore's Central Provident Fund (CPF) Investment Scheme.

Distribution Services

Most multi-level marketing arrangements, particularly where participants receive financial compensation for the recruitment of additional participants, are prohibited in Singapore. The restrictions apply equally to both local and foreign arrangements. In January 2002, the Ministry of Trade and Industry implemented its Multi-Level Marketing and Pyramid Selling (Excluded Schemes and Arrangements) Order, to clarify which kinds of multi-level marketing arrangements are legal in Singapore. Any Singapore-registered company or citizen/resident is also prohibited from promoting any overseas pyramid selling marketed through the Internet. Insurance businesses licensed under the Insurance Act and its subsidiary legislations, master franchise schemes, and direct selling schemes that meet conditions listed in the Order are exempted from the Act.

INVESTMENT BARRIERS

Singapore has a generally open investment regime, and no overarching screening process for foreign investment. Singapore places no restrictions on reinvestment or repatriation of earnings and capital. However, Singapore maintains limits on foreign investment in broadcasting, the news media, domestic retail banking, property ownership, and in some government-linked companies. Singapore's government has in the past conditioned approval of licenses to foreign financial service providers and telecommunications service providers on their agreement to performance requirements or commitments to transfer certain additional functions to Singapore. The United States-Singapore FTA prohibits certain performance-related restrictions on investors, such as limitations on the number of service locations.

ELECTRONIC COMMERCE

There are no significant barriers hindering the development and use of electronic commerce in Singapore. The United States-Singapore FTA contains state-of-the art provisions on electronic commerce, including national treatment and most favored nation obligations for products delivered electronically, affirmation that services disciplines cover all services delivered electronically, and permanent duty-free status of products delivered electronically.

Singapore considers the Internet to fall within the scope of its restrictions on broadcasting, as outlined in the Broadcasting Act. All Internet Service Providers (ISPs) must channel all incoming and outgoing Internet traffic through Internet Access Service Providers (IASPs) who function as main "gateways" to the Internet. IASPs must block access to one hundred Internet sites that the Singapore government considers obscene, excessively violent, or likely to incite racial or religious conflict. The Singapore government states that the list of sites is updated annually, but the list is not made public, and the process by which sites are placed on the list is not transparent. While other sites may be considered similarly objectionable, no effort is made to block access to sites beyond the one hundred listed sites. ISPs and IASPs are required to be licensed with the MDA. Internet Service Resellers, Internet Content Providers (ICPs), individuals who put up personal web pages, software developers and providers of raw financial information and news wire services do not have to register with the SBA, but ICPs or individuals who provide web pages for political or religious causes must be licensed by the MDA.

OTHER BARRIERS

Competition

Singapore has an extensive network of GLCs, which are active in many sectors of the economy. Some sectors, notably telecommunications, power generation/distribution, and financial services, are subject to sector-specific competition regulations and regulatory bodies. Some observers have raised concerns that GLCs may act in anticompetitive ways, a charge government officials strongly deny. The United States-Singapore FTA contains specific conduct guarantees to ensure that commercial enterprises in which the Singapore government has effective influence will operate on the basis of commercial considerations and will not discriminate in their treatment of U.S. firms. In accordance with its United States-Singapore FTA commitments, Singapore enacted the Competition Act 2004. The Act will be implemented in three phases, beginning with the establishment of a Competition Commission on January 1, 2005, followed by completion of implementing regulations (except for mergers and acquisitions) by approximately January 2006, followed by implementing regulations for mergers and acquisitions by approximately January 2007. There are also obligations in the FTA for greater transparency on government enterprises with substantial revenues or assets.

Transparency

The United States welcomes actions by Singapore to circulate more draft laws and regulations for public comment. It is our expectation that all legislation drafted to implement the United States–Singapore Free Trade Agreement will be made available for public comment in advance of finalization and submission to Singapore's Parliament, keeping with the transparency obligations of the FTA.

SOUTHERN AFRICAN CUSTOMS UNION

TRADE SUMMARY

The U.S. trade deficit with SACU countries was $3.6 billion in 2004, an increase of $1.2 billion from $2.4 billion in 2003. U.S. goods exports in 2004 were $3.3 billion, up 14.9 percent from the previous year. Corresponding U.S. imports from SACU countries were $6.9 billion, up 30.2 percent. The stock of U.S. foreign direct investment (FDI) in SACU in 2003 was $4.0 billion, up from $3.4 billion in 2002.

OVERVIEW

The Southern African Customs Union (SACU) links the trade regimes of Botswana, Lesotho, Namibia, South Africa, and Swaziland. The South African economy dominates SACU, representing approximately 91 percent of SACU's 2003 GDP of $175 billion. There are currently no internal tariff barriers among SACU members. All SACU members except Botswana share a common currency as members of the Common Monetary Area. Imports from outside SACU are subject to a common external tariff. The 2002 SACU Agreement, which became fully operational in 2004, provided for a more democratic structure that reduces reliance on South Africa for administrative decisions. The agreement set up a Council of Ministers (COM) as the supreme decision making body for SACU. The COM is supported by the Commission of Senior Officials (a group of technical experts) and a SACU Secretariat located in Windhoek, Namibia. A SACU Tariff Board reports directly to the COM and formulates and implements tariff policy.

The United States began free trade agreement negotiations with the five SACU countries in June 2003. The ongoing negotiations provide an opportunity to address trade constraints on U.S. exports to SACU countries, including relatively high tariffs and import restrictions on certain U.S. exports; insufficient copyright protection for software, films, and music; and barriers in telecommunications and other key service sectors. SACU countries are also negotiating free trade agreements with Mercosur and the European Free Trade Association (EFTA).

IMPORT POLICIES

Tariffs and Non-Tariff Barriers

Nearly all intra-SACU trade in goods is free of barriers. Imports from the rest of the world face a common external tariff and a common excise tax. Revenue flows into a common consolidated revenue fund controlled by South Africa. Since the WTO's Uruguay Round in 1994, SACU countries, led by South Africa, have reformed and simplified their common tariff structure. Tariff rates have been reduced from a simple average of more than 20 percent to 5.8 percent. Notwithstanding these reforms, importers have complained that the SACU tariff schedule remains complex and can create uncertainty. Tariff rates mostly fall within eight levels ranging from 0 percent to 30 percent, but some are higher, such as for most apparel items. Many of South Africa's specific and composite duties were converted to *ad valorem* rates, with a few exceptions remaining in a limited number of sectors, including textile and apparel products. In the Uruguay Round, South Africa agreed to a twelve-year phase-down of duties on textiles and apparel, but unilaterally moved to expedite its phase-down process. As of September 1, 2002, the following SACU rates, which are also the end rates, apply: apparel - 40 percent; yarns - 15 percent; fabrics - 22 percent; finished goods - 30 percent; and fibers - 7.5 percent. Duty rates on cars, light vehicles, and minibuses are still at the high level of 36 percent, while the rate of duty on original motor parts is 28 percent.

Country-specific information on the five SACU Members follows.

1. SOUTH AFRICA

IMPORT POLICIES

The South African International Trade Administration Commission (ITAC) came into operation in June 2003, replacing the Board on Tariffs and Trade. It has been tasked with establishing an efficient and effective system for the administration of trade. ITAC's responsibilities include:

- Tariff Investigations - The ITAC administers tariff-related programs, including the Motor Industry Development Program (MIDP) and the Duty Credit Certificate System (DCCS). Interested parties are entitled to approach ITAC with specific requests for a review, reduction, or increase in tariff rates;

- Trade Remedies - The ITAC deals with antidumping and countervailing duties and safeguards. The safeguards procedures were introduced in August 27, 2004, but have not yet been applied; and

- Import and Export Control - The ITAC issues import and export permits for certain items designated by the Minister under the authority of the International Trade Administration Act of 2002, which repealed the Import and Export Control Act of 1963.

Import Control

The Minister of Trade and Industry may, by notice in the Government Gazette, prescribe that no goods of a specified class or kind be imported into South Africa, except under the authority of, and in accordance with, the conditions stated in a permit issued by ITAC. The main categories of controlled imports and the objectives of control are as follows:

- Used goods: Import permits are granted only if such goods or substitutes are not manufactured domestically, constituting a *de facto* ban on such goods. These restrictions are designed to protect domestic industries such as clothing, motor vehicles, machinery and plastics, but also restrict imports of low-cost used goods from the United States and Europe;

- Waste, scrap, ashes, and residues (Basel Convention): The objective of import controls of these goods is to protect human health and the environment;

- Other harmful substances: Imports of substances such as ozone depleting chemicals (Montreal Convention) and chemicals used in illegal drug manufacturing (1988 United Nations Convention) are controlled for environmental, health, and social reasons; and

- Goods subject to quality specifications, such as tires: This restriction permits monitoring of manufacturer adherence to specifications that enhance vehicle safety or protect human life.

Tariffs

ITAC continues to receive requests for tariff protection from industries, especially since the South African rand's appreciation curve started in late 2002. The appreciation of the rand resulted in increased competition from imports. U.S. companies have cited tariffs as a barrier to trade in South Africa, along with port delays and congestion, customs valuation above invoice prices, theft of goods, import permits, antidumping measures, IPR crime, an inefficient bureaucracy, and excessive regulation.

Under SACU, products from Botswana, Lesotho, Swaziland, and Namibia enter South Africa duty-free. In a few cases, products from these countries compete directly with U.S. goods that are subject to duties. For example, soda ash from Botswana comes into South Africa at a zero percent duty, whereas soda ash from the United States faces a 5.5 percent duty. South Africa does not produce soda ash, but the duty on imported soda ash was introduced for the benefit of Botswana. Moreover, a legal complaint from Botswana's soda ash producer under South Africa's competition law threatens to block U.S. exports. The South African Competition Commission has pursued the claim as a "per se" offense, without making any judgment on the U.S. soda ash producer's impact on competition or consumers. If the South African Supreme Court does not grant an appeal so that the legal merits of the case can be argued, U.S. soda ash exports would be adversely affected. If the tariffs on U.S. soda ash were eliminated, industry estimates that U.S. exports of soda ash to South Africa could increase from less than $8 million to $25 million, which is closer to its historical level.

Anti-Dumping

Twelve new antidumping petitions were filed in South Africa during 2003 to 2004, the majority against Chinese products. While no new antidumping investigations against imports from the United States were instituted in 2004, antidumping duties on U.S. chicken meat portions, suspension PVC, roller bearings, lysine, and acetaminophenol remain in force. U.S. industry and the U.S. Government have challenged these petitions. In early 2004, ITAC also increased the MFN applied duty on imports of poultry offal, as requested by the domestic industry. In an important step to increase transparency and clarity in the antidumping investigation processes, antidumping regulations were promulgated on November 14, 2003.

Free Trade Agreement with the European Union

In 2000, South Africa and the European Union (EU) began to implement the development co-operation and financial co-operation provisions of their Agreement on Trade, Development and Cooperation, a free trade agreement (FTA). Under the Agreement, South Africa and the EU will establish a free trade area over a transitional period of up to 12 years for South Africa, and up to 10 years for the EU. The FTA provides for the reduction and eventual elimination of duties for approximately 85 percent of the products imported by South Africa from the EU and 95 percent of the products exported by South Africa to the EU. Certain agricultural products were exempted from liberalization under the agreement. South African and EU negotiators announced at the end of 2003 that they would seek to accelerate the process of negotiation towards freer trade in automobiles. Some U.S. sectors exporting to South Africa are concerned that their products will be less competitive because of the preferences given to the EU. For example, there is a 5 percent differential between the duties on EU and U.S. trucks. Another example includes a tariff differential between EU and U.S. bottled and bulk distilled spirits. Overall, U.S. companies are divided on whether they have been disadvantaged by the EU FTA.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Biotechnology

There has been an active debate in South Africa about products produced using agricultural biotechnology. The Genetically Modified Organisms Act ("the GMO Act"), which entered into force in 1999, aims to ensure that all activities involving the use of agricultural biotechnology (including production, import, release and distribution) will be carried out in such a way as to limit possible harmful consequences to the environment. Since 1999, some stores have promoted claims of selling a limited range of biotechnology-free products, while a few consumer groups have urged the Department of Health to introduce compulsory labeling of biotechnology products.

Under the leadership of the Department of Health's Directorate of Food Control, the South African government issued regulations on the labeling of biotechnology products in early 2004.

The regulations mandate the labeling of foods containing agricultural biotechnology only in certain cases, including when allergens or human/animal proteins are present, and when biotechnology food products differ significantly from a non-biotechnology equivalent. The rules also require validation of enhanced-characteristic claims for food containing agricultural biotechnology. The regulations do not address labeling claims that products are biotechnology-free. Biotechnology advocates are concerned about this omission, noting it could lead to many fraudulent claims. Trade organizations seem satisfied with the regulations, which follow internationally recognized, scientific (CODEX) guidelines. South Africa's CODEX representative comes from the Directorate of Food Control.

In November 2004, the government published draft changes to the GMO Act to bring it into compliance with the Cartagena Biosafety Protocol. The government solicited public comments on the draft changes and, as of early 2005, was evaluating those comments.

In June 2001, the South African government published the National Biotechnology Strategy for South Africa, a document that articulated the South African government's intent to stimulate the growth of biotechnology industries. The document states that biotechnology can make an important contribution to national priorities, particularly in the areas of human health, food security and environmental sustainability. Environmental groups continued to exert pressure on the South African government in 2004 to examine the safety of foods derived from agricultural biotechnology.

The government has approved for commercial production agricultural biotechnology soybeans that are tolerant to herbicides, and cotton and yellow and white maize that are resistant to insects. Farmers are enthusiastically adopting the new technology, and are expected to plant up to one million hectares of biotechnology varieties in 2004, up from about 400,000 hectares in 2003. The use of these products is widespread in the food processing industry.

U.S. grain producers have raised concerns about South Africa's treatment of agricultural biotechnology "stacked events." Although the U.S. Government considers products containing a combination of two previously approved genetic modifications (such as for insect resistance and herbicide tolerance) as "conventional" and encourages producers to notify the U.S. government of such stacked events, South Africa -- like the EU -- considers the combined "stacked events" as a new event, and requires a complete, *de novo* review for registration purposes. This requirement creates significant delays in registering products, causing U.S. exporters to lose export opportunities. At present, U.S. yellow corn is not approved for import by the government of South Africa due to delays in registering stacked events and other new events. As a result, if yellow corn were in short supply in South Africa in 2005, importers would have to apply to the government for a special waiver in order to import U.S. yellow corn, with the guarantee that the U.S. yellow corn would be milled near the port to ensure that it cannot be planted. In 2003 and 2004, Biowatch, an environmental lobby group, took legal action against the National Department of Agriculture (NDA) in order to obtain information on how it made decisions on issuing licenses for biotechnology crops. The local courts ruled in favor of the NDA, which protects certain information on a business proprietary basis.

In September 2003, countries of the Southern African Development Community (SADC), including South Africa, developed common guidelines on the regulation of products resulting from biotechnology. The guidelines assert that the region should develop common policy and regulatory systems that are based on either the Cartagena Protocol or the African Model Law on Biosafety. The leaders of SADC member states also agreed to develop national biotechnology policies and strategies and to increase their efforts to establish national biosafety regulatory systems. Member states were also urged to commission studies on the implications of biotechnology for agriculture, the environment, public health and socio-economics.

Agricultural Standards

The South African government requires prospective importers to apply for an import permit for certain controlled products. The import of irradiated meat from any source is still banned by public health officials. U.S. horticultural producers have complained about various South African phytosanitary barriers on the importation of apples, cherries, and pears from the United States. They estimate that, if these barriers were removed, U.S. exports of each of these fruits could increase by $5 million to $25 million in annual sales to South Africa. U.S. producers have also expressed concern about unnecessary SPS requirements for some grains, pork, poultry, and horticultural products.

In order to fulfill South Africa's commitment under the WTO Marrakesh Agreement on market access, the National Department of Agriculture published the rules and procedures regarding the application for market access permits for agricultural products on October 24, 2003. The permits will be issued to importers registered with the South African Revenue Service (SARS) and the Department of Trade and Industry (DTI) for importation of the agricultural products listed in the Table of Import Arrangements. Ten percent of such permits are reserved for "new importers" (those who have not imported over the past 3 years), and 10 percent for small, medium, and micro-enterprise importers.

In response to the Bovine Spongiform Encephalopathy case in Washington State announced on December 23, 2003, South Africa banned all ruminant animals and products originating in the United States. By January 15, 2004, South Africa, in accordance with World Organization for Animal Health (OIE) standards, exempted non-risk products such as hides, skins, wool and mohair from the ban. At the end of 2004, a ban was still in place on ruminant meat products. The South African Department of Agriculture is impressed with USDA's surveillance program but wants to see a full report with data from the surveillance program before considering lifting the ban.

During 2004 South African grain, pork and poultry producers petitioned the government to raise tariffs, with little success except for poultry offal. Farmers' groups will likely continue to pressure the government to increase tariffs on these items or otherwise limit imports of them.

GOVERNMENT PROCUREMENT

Government purchases are by competitive tender for project, supply, and other contracts. The government uses its position as both buyer and lawmaker, however, to promote the economic empowerment of the historically disadvantaged majority population in South Africa through its Black Economic Empowerment (BEE) policy. (See also the Investment section for more on BEE.)

South Africa's Preferential Procurement Policy Framework Act of 2000 and its implementing regulations set a legal framework and formula for evaluating bidders of government contracts by price and the advancement of socio-economic priorities. Revised draft regulations were released in November 2004 to take into consideration the Broad-Based Black Economic Empowerment (BBBEE) Act of 2003. The new regulations give greater preference to bidders of government contracts who more effectively comply with BEE objectives. In addition, the draft regulations raise tender thresholds. Previously, companies bidding on tenders worth up to R500,000 earned 80 percent of their points from their bid price and 20 percent on their commitment to social objectives. Now, the 80-20 point system is applied to tenders valued up to R1 million and firms are evaluated on their compliance with their respective industry BEE scorecards. Similarly, a 90-10-preference point system is applied to tenders valued over R1 million. The National Treasury is expected to approve and gazette the new Preferential Procurement regulations by mid-2005.

South Africa's Industrial Participation (IP) program, introduced in 1996, subjects all government and parastatal purchases or lease contracts (goods, equipment or services) with an imported content equal to or exceeding $10 million (or the rand equivalent thereof) to an IP obligation. This obligation requires the seller/supplier to engage in local commercial or industrial activity equaling or exceeding 30 percent of the imported content of total goods purchased under government tender. The program is intended to benefit South African industry by generating new or additional business.

In August 2004, the Minister of Finance issued the Code of Good Practice for BEE in Public Private Partnerships (PPPs) that had been released as a draft document in December 2003. The Code of Good Practice sets out the targets for BEE to be achieved in PPPs and provides clarity to bidding private parties.

South Africa is not a signatory to the WTO Agreement on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Legal Regime

Property rights, including intellectual property rights, are protected under a variety of laws and regulations. The South African parliament passed two IPR-related laws at the end of 1997 -- the Counterfeit Goods Act and the Intellectual Property Laws Amendment Acts -- in order to enhance IPR protection. The Department of Trade and Industry (DTI) administers these acts. Although South Africa's intellectual property laws and practices are in some ways in conformity with those in developed countries, there are deficiencies in enforcement and in guaranteeing the protections afforded under these laws. The U.S. government has raised with the South African government concerns about shortcomings in South Africa's IPR protection regime. The United States has also provided training on IPR enforcement to South African government and private sector representatives.

The U.S. software industry has cited three principal deficiencies in the 1978 Copyright Act:

- *Lack of criminal penalties for end user piracy.* South African law currently provides that the sale of infringing software is a criminal offence, but there is no criminal penalty for end users;

- *Lack of presumptions relating to copyright subsistence and ownership*. Amending the law to add ownership and subsistence presumptions would reduce the procedural burden on rights holders in proving their cases; and

- *Non-deterrent civil damages.* Amending the law to introduce statutory damages to cover end users and to ensure that monetary damages serve as a deterrent would improve IPR protection. Neither the current provisions on damages nor the application of these provisions are sufficient to serve as a deterrent to future infringement.

Until these changes are made in the law, the enforcement of individual copyright claims will continue to be complicated by the lack of evidentiary presumptions in the law. Amendments have been considered for years, but relatively little has been done in this area.

In 2001, South Africa introduced measures to enhance enforcement of the Counterfeit Goods Act. The South African government appointed more inspectors, designated more warehouses for counterfeit goods, destroyed counterfeit goods, and improved the training of customs, border police, and police officials. In 2004, there were 100 convictions for people arrested with counterfeit DVDs and computer games, compared to 14 in 2003. Cooperation between industry and customs authorities and police also improved. Despite these efforts, monetary losses from trademark counterfeiting and copyright piracy remain high. U.S. industry estimates total U.S. industry losses from copyright piracy in South Africa in 2004 at $128 million, including $91 million in business software applications and $35 million in motion pictures. U.S. industry is also increasingly concerned about illegal commercial photocopying, especially at universities, libraries, and other on-campus venues. Counterfeit medicines are also a growing problem. Although law enforcement authorities often cooperate with the private sector in investigating allegations of trade in pirated or counterfeit goods, there are concerns about laxity in enforcement of IPR laws against imports of infringing goods. Complainants can take both civil and criminal action against offenders. U.S. industry also reports that South Africa is becoming a transshipment point for pirated and counterfeit goods into the rest of Africa.

U.S. firms have complained that South Africa does not adequately protect the safety and efficacy studies (also called "registration data") filed before national authorities for approval of some products. The U.S. firms claim that these data are unfairly "referenced" by competitors in order to register their products.

South Africa is a member of the World Intellectual Property Organization (WIPO) but has yet to ratify the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty. South Africa has acceded to the Stockholm Text of the Paris Convention for the Protection of Intellectual Property.

Software/Audio Visual IPR Issues

Software piracy still occurs frequently in South Africa. The Business Software Alliance estimates that the piracy rate was 37 percent in 2004 and that U.S. industry in South Africa lost an estimated $91 million. Piracy in the video and sound industry also continues to be a concern. U.S. industry estimates that piracy rates for the audiovisual industry rose from 15 percent to 40 percent from 2001 to 2004, caused mainly by the growth in imports of pirated optical disc products. The Motion Picture Association estimates U.S. industry losses from audiovisual piracy of $35 million in 2004.

SERVICES BARRIERS

Telecommunications

South Africa has scheduled WTO commitments on value-added telecommunications and basic telecommunications services and has adopted the WTO reference paper on pro-competitive regulatory principles. The South African government also committed to license a second supplier no later than January 1, 2004, to compete against the current monopoly supplier, Telkom, in long-distance, data, telex, fax, and private leased circuits services. Despite the end of Telkom's exclusivity period in May 2002, Telkom has been able to continue its monopoly because of the government's unsuccessful attempts to license a second network operator (SNO). Telkom is also involved in an on-going multi-million dollar contract dispute with a U.S. telecommunications software company. The lawsuit is currently pending in the South African courts. Although the Minister of Communications conditionally approved a license for the SNO in December 2003, disagreements between the SNO shareholders over operational control and allocation of the remaining equity stake delayed the operation of the SNO. In February 2005, the Minister of Communications awarded the remaining equity stake in the SNO. The Independent Communications Authority of South Africa (ICASA) will issue the license once the stakeholders finalize a shareholders agreement and business plan.

In September 2004, the Minister of Communications announced a sweeping liberalization of the telecommunications sector, which went into effect February 1, 2005. Among other things, the Minister indicated that mobile operators would be allowed to use any fixed lines for the provision of their service, value-added network services (VANS) could be provided by facilities other than those owned by Telkom and the SNO, VANS providers would be allowed to carry voice using any protocol, and private telecommunications network operators could resell their spare capacity. ICASA is developing regulations to take into account the Minister's announcement. The new regulations are expected to resolve past complaints by Internet Service Providers (ISPs) and VANS providers, who have previously cited problems in acquiring new facilities from Telkom.

The Department of Communications (DOC) released a Draft Convergence Bill in December 2003, which industry analysts hoped would simplify the existing legislative framework, empower the regulator, and open the telecommunications industry to greater competition. Following a highly critical public comment period, the DOC undertook to revise the Bill. Many in the industry believed that the bill did not go far enough and created significant ambiguities. A revised bill is expected to be released in 2005.

Despite the progress these developments represent, some problems in the telecommunications sector still exist. For example, South Africa has continued to restrict the resale of telecommunications services. In the past, service providers have complained about ICASA ineffectiveness in asserting its authority over Telkom and have resorted to pursuing remedies in the Pretoria High Court. Telkom also often challenges decisions taken by ICASA, leading to delays in implementing rulings. Some companies continue to raise questions concerning the consistency of provisions in the Amended Telecommunications Act with South Africa's WTO obligations.

Additional concerns have been raised about the South African market for satellite services. In particular, there is a lack of transparency in satellite regulations, limitations on foreign satellite operators to serve the market, and excessively high licensing fees for Mobile Satellite Services.

Other Services

The United States and the Government of South Africa are currently discussing the possibility of negotiating an open skies air transport agreement. Government-to-government technical discussions were held during January 2005, with both sides promising further consultations later in the year. These were the first formal consultations since negotiations in May 2001, when

South African authorities indicated that their government was not ready for open skies, preferring instead incremental liberalization of the existing 1996 air transport agreement. Open skies agreements provide for open route rights, capacity, frequencies, designations, and pricing, as well as opportunities for cooperative marketing arrangements, including code-sharing and airline alliances. South African Airways (SAA), the national airline wholly owned by the transport parastatal Transnet, had previously noted concerns about U.S. airlines exercising "fifth-freedom rights" in Africa (i.e. carrying passengers between countries other than the United States and South Africa), which could impinge on one of SAA's strategic markets.

U.S. financial services providers have expressed ongoing concerns about the implementation of the Black Economic Empowerment (BEE) charter for the financial services sector. In 2003 and 2004, several of these providers participated in the negotiations with government, labor and industry stakeholders that resulted in the drafting of the BEE financial services charter. DTI has released some generic scorecard targets, including a 25 percent equity ownership target. It is unclear whether this may affect the financial services charter, which currently permits foreign financial institutions to substitute equity ownership requirements by financing and investing in BEE transactions. It is uncertain whether there will be pressure to eliminate this foreign alternative to equity ownership or whether it will be allowed as an exception to the overall generic target. (See the investment section for more on BEE.)

INVESTMENT BARRIERS

Uncertain Implementation of the BBBEE Act

In January 2004, President Mbeki signed into law the Broad-Based Black Economic Empowerment BBBEE) Act of 2003, the legislation enacting South Africa's Black Economic Empowerment (BEE) strategy, which is intended to move the historically disadvantaged majority population in South Africa into the mainstream of the national and global economy. U.S. businesses strongly support the goals of BEE, and many have a long history of instituting human resource management, procurement, and enterprise development policies in South Africa that are consistent with BEE objectives. These businesses hope BEE will be implemented in a manner that allows them to continue these policies and to participate fully in South Africa's economic growth. However, as South Africa's BEE strategy has evolved through a series of human resource development, management, procurement, enterprise development (investment in black-owned firms) and equity transfer policies, several key implementation and interpretation questions remain unanswered, creating uncertainty for investors.

The BBBEE Act directs the Minister of Trade and Industry to develop a national strategy for BEE, issue BEE implementing guidelines in the form of Codes of Good Practice, encourage the development of industry-specific charters, and establish a National BEE Advisory Council to review progress in achieving BEE objectives. The Minister released three Codes in December 2004, with seven more due in 2005. The recently released Codes address specific issues pertaining to the BEE Framework, Equity Ownership, and Management and include a new generic scorecard with suggested targets for areas such as equity ownership, management, procurement, and equality in employment. The Codes are intended to harmonize existing and future industry empowerment charters. Sectors that have completed or are close to finalizing empowerment charters for their respective industries include: accounting, agriculture, chemicals, cosmetics, clothing and footwear, construction, engineering services, financial services, forestry, health, information and communications technology (ICT), liquid fuels, liquor, marketing, mining, property, tourism, transport, and wine.

U.S. businesses hope the Codes of Good Practice will establish flexible criteria that allow them to meet BEE objectives through multiple means, and they believe that flexibility will be especially important with respect to equity ownership. Because of their corporate structures, most U.S. businesses cannot transfer equity, and they are concerned that mandatory equity transfer requirements or provisions that would leave open that possibility could – for very practical reasons – put the future of their South African operations in doubt and perhaps deter further investment.

The Minister is expected to establish the National BEE Advisory Council early in 2005. The Minister is also developing a statement on equity ownership for multinationals to be included in the Code of Good Practice on Equity Ownership, which is expected to explain the South African government's equity expectations for U.S companies operating in South Africa. USTR and the U.S. Embassy in Pretoria have been closely monitoring the ongoing development and implementation of South Africa’s BEE policies and have maintained a continuous dialogue with the South African government and U.S. industry on BEE.

ANTICOMPETITIVE PRACTICES

Ownership Patterns

There is an historical legacy of concentrated ownership in some sectors of the South African economy. During the apartheid years, a large portion of the South African population was entirely excluded from ownership of business enterprises. Moreover, government policies from 1961 to 1994 prohibited some successful companies such as South African Breweries, Anglo American (including DeBeers) and SASOL from investing abroad. They therefore expanded their activities locally. As a result, conglomerates with considerable market power developed in the South African marketplace. This situation has been changing, as many of the major players have been expanding internationally and have been listed on foreign stock exchanges. Together with the more effective competition authority and strong sectoral initiatives to enlarge the share of black participation in the economy, South Africa’s business environment is becoming more competitive and more open to new entrants, including U.S. companies. Sectors such as energy, transport and telecommunications have also historically been controlled or dominated by parastatals. These sectors are gradually restructuring and opening up for competition from the private sector. The privatization program of the South African government, although moving slowly, is also starting to bring a change in ownership patterns.

ELECTRONIC COMMERCE

The Electronic Communications and Transactions Law, effective July 31, 2002, governs all companies that conduct electronic commerce in South Africa. The law was designed to facilitate electronic commerce but instead may increase regulatory burdens and introduce uncertainty into the future of electronic commerce in the country. The law requires government accreditation for certain electronic signatures, takes government control of the ".za" domain name, and requires a long list of disclosures for web sites that sell via the Internet.

In December 2003, the State Law Commission released Issue Paper 24: Privacy and Data Protection. The Issue Paper sought feedback for proposals on privacy and data protection legislation and creation of a statutory regulatory agency. Comprehensive legislation may negatively impact the ability of South African and foreign companies to receive and send trans-border flows of personally identifiable data, thereby weakening cross-border e-commerce and services between South Africa and its trading partners. No bill was submitted to the legislature in 2004.

OTHER BARRIERS

Transparency, Corruption and Crime

South African law provides for prosecution of government officials who solicit or accept bribes. Penalties for offering or accepting a bribe may include criminal prosecution, monetary fines, dismissal from government employment, or deportation (for foreign citizens). South Africa has no fewer than ten agencies engaged in anti-corruption activities. Some, like the Public Service Commission, Office of the Public Protector, and Office of the Auditor-General, are constitutionally mandated and address corruption as only part of their responsibilities. Others, like the South African Police Anti-Corruption Unit and the Directorate for Special Operations (more popularly known as "the Scorpions"), are dedicated to combating crime and corruption. High rates of violent crime, however, are a strain on capacity and make it difficult for South African criminal and judicial entities to dedicate adequate resources to anti-corruption efforts.

During the last few years, crime has been a far more serious problem than either corruption or political violence and an impediment to, and a cost of, doing business in South Africa. The South African police forces have not been effective or well accepted in many communities because of their historical role in enforcing minority rule, as well as their lack of training and internal crime and corruption within the forces. The levels of crime, especially violent crime, are a deterrent to attracting U.S. companies to South Africa.

New laws, such as the Promotion of Access to Information Act signed into law in February 2000, have helped to increase transparency in government in the last few years. The Public Finance Management Act, which became effective on April 1, 2000, helped to raise the level of oversight and control over public funds and improved the transparency of government spending, especially with regard to off-budget agencies and parastatals. Notwithstanding these efforts, businesses complain about the lack of certainty and consistency in interpreting and implementing some government policies.

On April 28, 2004, President Mbeki signed "The South African Prevention and Combating of Corrupt Activities Act" (PCCAA) into law. The PCCAA, *inter alia*, makes it more clear which activities are considered graft, bars the payment of bribes by South African citizens and firms to foreign public officials, and obliges public officials to report any corrupt activities. One shortcoming of the Act is its failure to protect whistleblowers against recrimination or defamation claims.

Immigration Laws

For a number of years, U.S. and other foreign companies have complained that South African immigration legislation and the application of the law made it extremely difficult to get work permits for their foreign employees. Previously, South Africa relied on the apartheid-era Aliens Control Act, which did not take into account international developments and the opening up of the South African market. A new immigration law entered into force on May 31, 2002. The legislation establishes yearly quotas for granting work permits to foreigners. Local businesses have criticized the new law for creating uncertainty because the quota system sets limits on the number of skilled people that may enter the country in particular categories. Corporate investors are allowed under a separate dispensation to make blanket applications for the people they need. It is not clear whether these corporate permits fall in or out of the quota system. The Trade and Industry Minister has suggested that the South African government may need to revise the law to acquire critically needed skills in South Africa. Home Affairs officials oppose moving away from quotas because it might mean reverting to the Aliens Control Act, wherein an employer had to establish the clear need for a skill. The Minister of Home Affairs has said that the new law is an enormous improvement over the previous legislation and places South Africa on a par with other countries, especially with respect to investors and intra-company transfer permits.

2. BOTSWANA

IMPORT POLICIES

Import permits are required for goods entering Botswana directly from countries outside of SACU, with the exception of Malawi, and are obtainable from the Department of Trade and Consumer Affairs in the Ministry of Trade and Industry. The import permits are not transferable. Permits are usually granted upon request.

Prohibited imports include habit-forming drugs and objectionable literature (pornographic magazines and videotapes). Importation of certain agricultural products and plants requires approval from the Ministry of Agriculture prior to obtaining the import permit from the

Department of Trade and Consumer Affairs. Imports of fresh pork are banned, but processed pork products may be imported. Poultry imports are permitted only when there is a domestic market deficit. Imports of some vegetables, meat, and dairy products are seasonally banned.

GOVERNMENT PROCUREMENT

To comply with the Public Procurement and Asset Disposal Act of 2002, the Public Procurement and Asset Disposal Board (PPADB) was created in 2003 as an independent parastatal to take over the functions of its predecessor organization, the Central Tender Board. The PPADB is responsible for the award of all government tenders. The tender process is open. Lobbying of the PPADB or its members is strictly prohibited. The Independent Complaints Review Committee of the PPADB, established in November 2004, reviews the Board's decisions subject to challenge by stakeholders (e.g., contractors and procuring entities). Since December 2003, the PPADB has published its decisions concerning awarded tenders, prequalification lists and newly registered contractors.

Government procurement practices do involve some preference schemes and reserve certain tenders for 100 percent citizen-owned companies. The PPADB has stated that it considers these schemes within the context of Botswana's obligations under the WTO, the Southern African Development Community (SADC), and SACU. Botswana is not a signatory to the WTO Agreement on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

In 1998, Botswana became a member of both the Berne and Paris Conventions, the international baseline intellectual property rights agreements. The Botswana Copyright Law, enacted in 2000 but not yet fully implemented, is intended to improve standards of protection for the rights of creators of literary, artistic, dramatic, cinematographic works; computer programs; broadcasting organizations; and sound recordings. The government believes that, once implemented, the law will put in place mechanisms that will help to deter future infringement.

SERVICES BARRIERS

The government is continuing to reorganize and restructure some ministries and departments, to improve the efficiency and effectiveness of services delivery, and it is moving towards privatizing a number of parastatal businesses. One reform requires the Government to establish autonomous authorities or boards, working largely on commercial principles. One such authority is the Public Enterprise Evaluation and Privatization Agency (PEEPA), which was established in 2000 to oversee the implementation of the Privatization Policy. PEEPA will ultimately determine the extent of foreign participation in the privatization process and the mechanics that will be used to promote citizen participation. The government intends to use privatization as a tool to increase foreign direct and portfolio investment in the country.

The Ministry of Finance and Development Planning, to which PEEPA reports, welcomes foreign investment, but has stated, however, that local investors may be given preference in privatization initiatives in some instances.

The telecommunications market was liberalized in 1996 following the adoption of the Telecommunications Policy of 1995 and enactment of the Telecommunications Act (Act No. 15 of 1996), which abolished Botswana Telecommunication Corporation's (BTC) monopoly in some segments of the market and established the independent regulator, the Botswana Telecommunications Authority (BTA). Botswana did not participate in the WTO extended telecommunications and financial services negotiations. The BTA was created to safeguard competition and inter-connection to the public network, yet the state-owned BTC still maintains a monopoly as the sole licensed supplier of fixed-line voice services, including international calls. Market segments liberalized so far are mobile telephones, data communications, payphones, sale of telecommunications equipment, and Internet services. Competition in the cellular phone industry is dominated by two international firms, Mascom (Portuguese) and Orange (French), who compete for the bulk of the local market share. Voice Over Internet Protocol (VOIP) is not allowed (except over private networks); this prevents licensed Internet providers, as well as suppliers of international data transmission through very small aperture terminals (VSATs), from offering voice services in competition with BTC. BTA has almost complete freedom in deciding the number of licenses and associated conditions. BTA rulings need not be made public, and interconnection agreements between parties (copies are provided to the BTA) remain confidential.

BTC must operate any new telecommunications services as subsidiaries or associated entities to allow sufficient accounting separation from its fixed-line operations (BTC Act and 1996 amendments). BOTSNET, a BTC subsidiary, for example, is competing in Internet services with nine other licensed providers.

INVESTMENT BARRIERS

All foreign investors wishing to invest in Botswana are required to register a company in Botswana in accordance with the Companies Act and to comply with other applicable legislation; transfer technology to Botswana, as appropriate; transfer skills to citizens of Botswana by promoting their involvement and participation in positions in the supervisory, middle and senior management levels of companies; and ultimately replace expatriate employees with Botswana citizens within an agreed period, though there are often exceptions to this rule in practice.

The Botswana Export Development and Investment Authority (BEDIA), founded in 1998, is an autonomous organization established to promote investment in Botswana with a special emphasis on export-oriented manufacturing industries. The Authority is designed to serve as the primary government contact point for both domestic and foreign investors. BEDIA maintains a

One Stop Service Center to help investors secure all clearances and approvals as quickly as possible.

In addition, the Government is developing a competition policy, privatization master plan, and foreign direct investment strategy, all of which are scheduled for consideration by Parliament early in 2005. These new initiatives are geared towards attracting foreign investment by clarifying the rules and regulations for participation in the Botswana economy.

ELECTRONIC COMMERCE

Internet usage is on the rise, but nationwide usage remains extremely low. According to the government, five percent of the population uses the Internet. There is a growing number of Internet Service Providers and Internet cafes, but due to the high cost of fixed-line phone charges associated with dial-up service, the cost of accessing the Internet remains prohibitive for the majority of the population.

OTHER BARRIERS

The legal system is sufficient to conduct commercial dealings, and foreign and domestic parties have equal access to, and standing under, the judicial system. Botswana courts will, in general, accept and enforce decisions of a foreign court found to have jurisdiction in a given case. However, a backlog of cases has seriously impeded international companies that have won government procurement contracts, which have subsequently been challenged in court. There is a growing concern that the backlog could deter American companies interested in competing for contracts in Botswana.

3. LESOTHO

IMPORT POLICIES

Lesotho applies a permit system for all imports from non-SACU members. The system is applicable to all consignments imported by individual consumers and investors. Industrialists are accorded preferential treatment through which a "Blanket Permit" is allowed with a validity of 12 months and an additional grace period of 3 months.

Tariff and Non-Tariff Barriers

Lesotho applies the SACU Common External Tariff. Additional charges include clearing fees ranging from M750 to M1,000 (approximately $130 to $175). Lesotho is a member of the WTO, the Southern Africa Development Community (SADC), and the Africa, Caribbean and Pacific-European Union (ACP-EU) Cotonou trade agreement.

Import Licensing

The agricultural sector has witnessed some structural reforms that halted price subsidies and import controls on maize and wheat produce in favor of market-determined prices. The 1967 Agricultural Marketing Act, however, continues to control the importation of bread, legumes, sugar, eggs, meat, dairy products, fruits and vegetables.

With the exception of eggs, sugar and legumes, the import restrictions allow a minimum exemption for consumer purchases outside the country. The Department of Marketing under the Ministry of Trade and Industry, Cooperatives and Marketing monitors the level of production of these commodities and issues import licenses in the event of short supply. However, national production has never met local demand. As a result, import permits are issued as a matter of course. Non-automatic licenses apply to imported used clothing. In practice, however, no licenses for used clothing are issued, with the effect of a *de facto ban* on this product. Liquor imports are prohibited, with the exception of duty-free allowances from countries outside the SACU area.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Lesotho does not have a national standards body. The Standards and Quality Assurance section of the Ministry of Trade and Industry, Cooperatives and Marketing functions as the focal point for standards and quality assurance. No national standards have been developed to date. Industries in Lesotho have traditionally relied on the South African Bureau of Standards for voluntary standards facilities and quality assurance schemes. Local exporters have relied on traditional export markets and have developed their standards according to technical and quality requirements of importing countries or international standards.

Lesotho participates in a regional program on Standardization, Quality, Accreditation and Metrology for the Southern Africa Development Community. The program aims to harmonize standards for adoption by all member states. Efforts are also underway to develop a regional accreditation authority.

GOVERNMENT PROCUREMENT

The Central Tender Board, a body within the Ministry of Finance and Development Planning, is responsible for the procurement of goods and services for all government departments through mainly (though not exclusively) open tender.

The Board employs a stage-by-stage process that entails among other things, soliciting bids for goods and services from local, regional and international suppliers/contractors. Standard practice for the Board is to follow the UNCITRAL model law on Government Procurement. Lesotho is not a signatory to the WTO Agreement on Government Procurement.

Government procurement rules do not give Lesotho nationals preference in bids for goods and services. The Ministry of Trade and Industry encourages joint ventures.

Lesotho is working on a procurement policy that will conform strictly with SACU and WTO regulations except where there is a clause allowing for special preferences. New procurement guidelines are being considered which, among other things, would use the Internet to widen the scope of coverage for solicitation of bids.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Lesotho's Industrial Property Order (1989), Copyright Order (1989) and the Industrial Property Regulations (1989) are the basis for legal protection of intellectual property rights. Patents, valid for 15 years from the date of application, have rarely been issued in Lesotho, but trademark protection is widely sought and granted. Lesotho is a member of WIPO and the African Regional Intellectual Property Organization.

SERVICES BARRIERS

Foreign participation is not restricted in the service sector. The banking and telecommunications sectors are largely controlled by foreign ownership, in particular by South African institutions.

The Trading Enterprises Order of 1996 restricts foreigners from participating in small trading activities that are reserved for nationals only. These include butcheries, barbershops, general cafes and hair salons.

INVESTMENT BARRIERS

Lesotho welcomes foreign investment. Foreign investors have participated in the country's privatization program without discrimination.

ELECTRONIC COMMERCE

Commercial outlets in Lesotho do not offer electronic trading. Some handicraft producers and tourist destinations market their produce on the Internet, although they do not have Internet payment facilities. The Ministry of Communications, Science and Technology is circulating a National Information and Communication Technology policy paper which proposes the introduction of electronic commerce and the formulation of related regulatory mechanisms. The Standard Bank group this year introduced a debit card that enables its customers to make electronic payments in Lesotho and outside the country.

OTHER BARRIERS

Corruption

Business people state that solicitation of bribes in connection with government services does not occur. The government has received international accolades for its prosecution of multinational companies for corruption related to the awarding of contracts for construction of the Lesotho Highlands Development Project. In cases that have been upheld by the Lesotho Court of Appeals, the former Chief Executive of the Lesotho Highlands Development Authority and three multinational corporations have been convicted for fraud and bribery.

The government has established a Directorate on Corruption and Economic Offenses that continues to prosecute cases regarding the LHDA project, as well as others involving embezzlement and bribery.

4. NAMIBIA

IMPORT POLICIES

Namibia is a member of various regional and international economic and trade bodies including the Southern African Development Community (SADC) and the WTO. Namibia uses the Harmonized System of Classification and applies the SACU common external tariff (CET).

The Directorate of International Trade of the Ministry of Trade and Industry (MTI) is responsible for coordinating the country's trade polices and overseeing Namibia's participation in international trade bodies. The Directorate is responsible for managing import/export procedures. Importers must have an import permit from the Ministry of Trade and Industry. Namibia is a party to the WTO Agreement on Import Licensing. A limited number of products are subject to non-automatic import licensing: medicines; chemicals; frozen, chilled, fish and meat; live animals and genetic materials; controlled petroleum products; firearms and explosives; diamonds, gold and other minerals; and seemingly all second-hand goods such as clothing and motor vehicles. In practice, however, the Ministry of Trade and Industry does not issue licenses for imported used clothing, with the effect of a *de facto ban* on this product. Most non-agricultural imports require a permit issued by MTI. With respect to agricultural trade, the Namibian Agronomic Board issues permits for the import, export, and transit of controlled agronomic crops (i.e., wheat and wheat products and corn and corn products). Imports of agronomic crops and derivatives, as well as all plants and plant products, also require the issuance of a phytosanitary certificate by the Ministry of Agriculture, Water and Rural Development. The Namibian Meat Board regulates the import and export of live animals (cattle, sheep, goats and pigs) and derivative meat products. Importers of live animals and meat products must demonstrate compliance with the country's animal health standards by obtaining a veterinary import permit from the Directorate of Veterinary Services.

In January 2005, Namibia introduced a new regulation to ban the importation of used vehicles older than five years from non-SACU countries, as well as left-hand drive vehicles.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Namibia is a party to the Convention on Biological Diversity and a signatory to the subsequent Cartagena Protocol on Biosafety. To meet its international commitments, the government is drafting new legislation – the Biosafety Act – which will regulate the importation, sale and use of products of agricultural biotechnology and will establish new regulatory and administrative structures. It will impose new registration obligations on facilities that use or produce agricultural biotechnology products and will require persons and companies to receive authorization prior to importing such products. It will require biotechnology products to be clearly labeled and identified for purposes of traceability. Pending passage of the Biosafety Act, the government has imposed a moratorium on the importation of agricultural biotechnology products.

GOVERNMENT PROCUREMENT

Most government transactions, including the awarding of contracts and the purchase of supplies, are made through the Tender Board of Namibia. The Board is comprised of representatives from various government ministries and appointed by the Minister of Finance. Government requests for procurement tenders are publicized in the local media. The Tender Board gives preference for goods manufactured and/or assembled in Namibia. Namibia is not a signatory to the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

Since independence in 1990, the government has pursued policies to diversify its economy and to create employment. To achieve that goal, the government has put in place tax and non-tax incentives to attract manufacturers and export-oriented businesses. The Offshore Development Company administers the country's Export Processing Zone (EPZ) regime. Companies granted EPZ status can set up operation anywhere in Namibia. There are no restrictions on the industrial sector so long as the exports are destined for markets outside the SACU region. Benefits of the EPZ regime include no corporate tax, no import duties on the importation of capital equipment or raw materials, and no VAT, stamp or transfer duties. Non-residents operating in an EPZ may hold foreign currency accounts.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Namibia is a member of the World Intellectual Property Organization. The responsibility for IPR protection is divided between two government ministries. The Directorate of Internal Trade of the Ministry of Trade and Industry oversees industrial property and is responsible for the registration of companies, private corporations, patents, trademarks and designs. The Ministry of Information and Broadcasting manages copyrights.

The government is in the process of updating copyright legislation to bring it in line with the TRIPS Agreement and the WIPO Treaties on Performance and Phonograms and Copyrights. A draft bill is scheduled to be tabled in Parliament in 2005. Absent new legislation, Namibia lacks adequate legal and enforcement mechanisms to address the problems associated with piracy and copyright violations.

SERVICES BARRIERS

Services account for nearly 60 percent of Namibia's GDP with government services representing the largest single component. Foreign participation in the services sector is generally unrestricted. Due to historical links between the two economies, South African companies dominate many commercial services in Namibia, particularly in the retail and financial sectors. Other services -- including telecommunications, water, electricity and most major transport services -- are dominated by Namibian parastatals. Many of the 41 recognized parastatals operate as "commercialized" entities, meaning they are profit-seeking and are not maintained on the national budget. However, only a limited number produce annual reports on a regular basis. There is currently little U.S. participation in the Namibian service sector.

Under the Namibia National Re-insurance Act of 1998, insurance companies are required to cede 20 percent of any policy issued or renewed to the state-owned Namibia National Reinsurance Corporation (NamibRe). In 2001, the government and private insurers reached an agreement in which the mandatory cessions clause would not be enforced for five years. The government-industry agreement will be re-evaluated in 2006.

INVESTMENT BARRIERS

Namibia's Foreign Investment Act of 1990 assures equal treatment of domestic and foreign investors and provides non-discriminatory access to all sectors. The government guarantees foreign investors access to foreign currency, repatriation of capital, and dispute settlement through international arbitration. There are few restrictions on the establishment of private businesses or the size of an investment. The Namibian Investment Centre, which was created by the 1990 Act, is responsible for implementing the country's investment promotion policies.

There is no local participation requirement for foreign investments, but the government actively encourages partnerships with historically disadvantaged Namibians. In certain industries, such as the fishing sector, there has been a concerted campaign to "Namibianize" existing investments.

The Namibian Constitution provides for the expropriation of property in the public interest subject to the payment of "just" compensation. As in other Southern African countries emerging from apartheid, land reform is at the forefront of public debate. The government continues to pursue a "willing buyer-willing seller" program rooted in the Namibian Constitution. The process has been criticized recently for the slow pace of acquiring commercial farmland and resettling Namibia's landless. The government considers foreign-owned and non-productive farmland primary targets for expropriation. The government is poised to implement a new land tax (originally scheduled to take effect in April 2002) in an effort to raise money for land acquisition. Absentee landowners will be subject to higher tax rates per hectare than resident farmers.

ELECTRONIC COMMERCE

Electronic commerce is still relatively unknown to Namibian consumers. Only a small percentage of Namibians enjoy access to the Internet. The government is in the early stages of formulating policies to regulate electronic commerce. MTI's Directorate of Internal Trade has included a section on electronic commerce in an updated version of the Companies Act, which is awaiting Parliamentary action.

OTHER BARRIERS

According to recent surveys, there is a growing public perception that official corruption is on the rise. Several presidential commissions have been established in recent years to investigate allegations of kickbacks and irregularities in Namibian parastatals.

Despite the growing perception of corruption, similar studies have shown that Namibians retain confidence in government institutions to address the problem. Anti-corruption bodies include the Prime Minister's Anti-Corruption and Bribery Committee, the Office of Ombudsman and the Office of the Auditor-General. In 2003, an Anti-Corruption Bill was passed that provides for the establishment of an independent Anti-Corruption Commission (it has yet to be set up due to purported budgetary constraints). In November 2003, the National Assembly released the country's first assets register for lawmakers.

5. SWAZILAND

IMPORT POLICIES

Swaziland is a member of the WTO, the Common Market for Eastern and Southern Africa (COMESA), and the Southern Africa Development Community (SADC). As a member of SACU, Swaziland applies the SACU common external tariff (CET). Swaziland has at times exercised its right under the SACU Agreement to protect infant industries such as fertilizer, cement, and beer by applying tariff rates higher than those included in the CET.

There are no restrictions on imports into Swaziland and no prohibited imports. A limited number of products from outside the SACU area require an import permit. Licensing permits issued by the Ministry of Finance are generally easy to obtain and payment is governed by foreign exchange controls.

GOVERNMENT PROCUREMENT

Although the government accords local business a 15 percent preferential rate in tenders for government contracts, there is little transparency and it appears that this preferential treatment for local bidders is not always granted. A large portion of government contracts is filled by firms from South Africa and other southern African countries, but for small-to-medium sized tenders, bidding companies must be registered in Swaziland. The government inspects the premises of all companies prior to awarding the tender.

Swaziland is not a signatory to the WTO Agreement on Government Procurement. The government solicits for bids 7 days to 30 days before the bid is due, depending on the size of the tender. Bid documents are obtained from Government Stores after the bidder pays at the Government revenue office. Bids are returned to the Central Tender Board. Awards are made known to all bidders.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Swaziland has an IPR regime inherited from the colonial era, under which copyrights, patents, and trade markets were more or less protected under various acts promulgated by the colonial authorities. The Ministry of Justice, responsible for these concerns, has been working on improved laws.

Patents are currently protected under a 1936 act that automatically extends patent protection upon proper application to products that have been patented in either South Africa or Great Britain. Updated patent legislation has been approved by the Cabinet, passed by both houses of Parliament, and is now awaiting the King’s approval. Under the new legislation, patents would be issued by the Swazi government with technical assistance from the African Regional Industrial Property Organization. Protection would be extended to pharmaceutical and agricultural chemical products.

Copyright protection is addressed under four statutes, dating from 1912 to 1933. According to the Registrar General for the Ministry of Justice, the acts have never been implemented and copyright protection in Swaziland is limited. The Ministry of Justice is in the process of finalizing a draft, updated Copyright Act, based on the WIPO model act. Swaziland does not have a bilateral copyright arrangement with the United States.

The 1981 Trade Marks Act was revised in 1994. The Office of the Registrar General in the Ministry of Justice and Constitutional Affairs registers trademarks according to the updated act. There are no known, ongoing disputes with regard to copyrights, patents, or trademarks in Swaziland.

SERVICES BARRIERS

Foreign participation in the services sector is generally not restricted, except for the insurance industry. Swaziland Royal Insurance, monopolized in the 1970s, remains the sole insurer in the country.

INVESTMENT BARRIERS

Swaziland does not have an investment code or securities act. As a result, policies affecting foreign investment are established and influenced more through government statements and decrees than through formal legislative or administrative processes. The Swaziland Investment Promotion Authority (SIPA), which was established in 1998, provides services for investors and designs and implements strategies for attracting new investment. There are no formal policies or practices that discriminate against foreign investors. Companies in Swaziland may be 100 percent foreign-owned and foreign investors are free to invest in most sectors. However, as of December 2004, the government maintained monopolies in insurance, telephones, water, and electricity. Nearly all of the largest businesses in Swaziland are owned by foreign investors, either fully or with minority participation by Swazi institutions.

The government encourages foreign direct investment by providing factory shells at cost and offering generous tax allowances to foreign firms. Tax allowances include a low corporate tax of 10 percent, as compared to the standard 30 percent, and a 10-year exemption from withholding tax on dividends. New investors also enjoy duty-free import of machinery and equipment.

To work in Swaziland, all foreign nationals must acquire work and residence permits. These permits have been a source of tension between the expatriate business community and a government otherwise friendly to foreign investment. Employers must apply to the Immigration Office for a work permit and demonstrate that no Swazi is available to fill the relevant vacancy. Residence permits are only good for two years, at which time they must be renewed. Although permits are almost always renewed, expatriate businesspeople often complain that the process is cumbersome and exasperating.

ELECTRONIC COMMERCE

The Kingdom's telecommunications network is fully digital. Optical fiber and local loop systems have been installed and link with key areas. An Internet gateway that links directly with the United States was launched in July 2000. A cellular network started operating in 1998; only one company, MTN Swaziland Ltd, offers this service. The Internet has become an integral part of the communications network in Swaziland. Internet service providers with web hosting services have been established in Manzini and Mbabane.

SRI LANKA

TRADE SUMMARY

The U.S. trade deficit with Sri Lanka was $1.8 billion in 2004, an increase of $148 million from $1.7 billion in 2003. U.S. goods exports in 2004 were $164 million, up 6.0 percent from the previous year. Corresponding U.S. imports from Sri Lanka were $2.0 billion, up 8.2 percent. Sri Lanka is currently the 105th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Sri Lanka in 2003 was $47 million, up from $31 million in 2002.

IMPORT POLICIES

Sri Lanka witnessed a change of government in April 2004, following parliamentary elections. The current government has espoused a shift to a mixed economy from the largely free market policies of the previous government. The government's Economic Policy Framework has backtracked on the previous government's trade liberalization strategy. It specifically calls for protection of small and medium enterprises and agriculture.

The government has created the National Council of Economic Development (NCED). NCED consists of approximately 18 clusters representing both private and public sector officials which examine various sectors of the economy. The Trade and Tariff cluster is charged with designing trade policy.

Sri Lanka's main trade policy instrument has been the import tariff. The tariff structure is subject to frequent changes. The budget for 2005 reduced the number of tariff bands from six to five. Departing from the previous liberalization path, the Government recently imposed a new import tax on selected items by way of a levy (referred to as a "cess" in Sri Lanka) in light of a decline in foreign reserves. The government also hopes this new tax will protect domestic agriculture and industry.

Import tariffs and other import charges: Currently, there are 5 tariff bands of 0 percent, 2.5 percent, 6 percent, 15 percent, and 28 percent. The highest tariff band was increased from 25 percent in 2002 to 27.5 percent in January 2004, and to 28 percent in November 2004. Textiles, pharmaceuticals, and medical equipment are free of duty. Basic raw materials are generally assessed a 2.5 percent duty. Semi-processed raw material tariffs are 6 percent, while intermediate product tariffs are 15 percent. Most finished products are at 28 percent. There are also a number of deviations from the five-band tariff policy. Tobacco and cigarette tariffs range from 75 percent to 250 percent. In addition, there are specific duties on certain items, including footwear, ceramic products, and agricultural products. These specific duties are designed to protect domestic producers. Some items are subject to an *ad valorem* or a specific duty, whichever is higher, and there is intermittent use of exemptions and waivers. Imports for export industries enter duty-free.

Export Development Board (EDB) Levy: In November 2004, the government introduced a new additional tax on a range of imports identified as "non-essential." The EDB levy is applied on C.I.F value, and ranges from 10 percent to 20 percent. Together with import tariffs, the EDB levy will effectively raise charges on most finished good imports to over 48 percent of the import value, with the highest charges on goods subject to specific duties.

There are other charges on imports:

1) a 10 percent import duty surcharge;
2) a 1.5 percent ports and airports development levy (PAL) on imports;
3) Value Added Tax (VAT) of 0 percent, 5 percent, 15 percent and 18 percent;
4) excise fees on some products such as aerated water, liquor, beer, motor vehicles and cigarettes. Excise fees on motor vehicles were increased sharply in 2004;
5) an Export Development Board surcharge on all imports where the customs duty is more than 45 percent;
6) a port handling charges; and
7) a surcharge of 0.25 percent assessed on the import duty (to fund the National Action Plan for Children, to be finalized and implemented in 2005).

Import prices are increased by 5 percent (by adding an imputed profit margin) when calculating the VAT and excise duty.

According to U.S. trade data, the total value of imports affected by the EDB cess will be about $5 million out of a total of about $143 million annual U.S. exports to Sri Lanka. The total effect on U.S. exports could be much higher, because U.S.-sourced products sent via other trading hubs are not captured in the export data used to compile this analysis. The Embassy has received complaints from affected U.S. exporters regarding the new "prohibitive" tariff regime.

Import Licensing

Sri Lanka requires import licenses for over 300 items at the 6-digit level of the Harmonized System (HS) code require import licenses, mostly for health, environment, and national security reasons. Importers must pay a fee equal to 0.1 percent fee of the import price to receive an import license.

Customs Barriers

The Government of Sri Lanka implemented the WTO Customs Valuation Agreement in January 2003 and follows the transaction value method to determine the C.I.F. value. The scheme has operated quite successfully, and major companies have not faced problems. Customs is also in the process of installing an Electronic Data Interchange (EDI) system to support an automated cargo clearing facility. When implemented, this system should improve customs administration and facilitate trade.

STANDARDS TESTING, LABELING AND CERTIFICATION

At present there are 85 items that come under the Sri Lanka Standards Institution (SLSI) mandatory import inspection scheme. These importers have to obtain a clearance certificate from the SLSI to sell their goods. SLSI accepts letters of conformity from foreign laboratories, but retains the discretion to take samples and perform tests.

There is discussion within some sections of the health and environment sectors to introduce a labeling requirement for imports of biotechnology food, but no requirements are in place currently. The Sri Lankan Government considered previously implementing such a requirement in 2000 – 2001.

A new labeling and advertising regulation was published in January 2004. This relates to the information that should appear on a label of any prepackaged food product offered for sale, transported or advertised for sale in Sri Lanka, including imported food. The regulation came into effect on January 19, 2005. Implementation, however, could be delayed further.

Poultry and meat: The ban on imports of U.S. poultry has been lifted subsequent to the USDA notification to the World Animal Health Organization (OIE) that the United States is free of Highly Pathogenic Avian Influenza (HPAI). An unofficial ban on the import of chicken to protect the local industry was revoked in November 2004 following a Government decision to allow poultry imports into the country. The primary beneficiary of the foreign chicken ban was a Singaporean-owned poultry company in Sri Lanka, which dominates the domestic market with an approximately 80 percent market share. Imports of beef from the United States are banned due to fears of bovine spongiform encephalopathy (BSE).

GOVERNMENT PROCUREMENT

Sri Lanka is not a member of the WTO Agreement on Government Procurement. Government procurement of goods and services is mostly done through a public tender process. Some tenders are open only to registered providers. The Government publicly subscribes to principles of international competitive bidding, but charges of corruption and unfair awards continue. There are no professional evaluation experts in Sri Lanka. The Government recently created a National Procurement Agency (NPA) to introduce an improved system of procurement.

EXPORT SUBSIDIES

Exporting companies approved by the BOI, are generally entitled to corporate tax holidays and concessions. Exporters receive institutional support from the Export Development Board in marketing. Imports for exporting industries and BOI approved projects usually are exempted from payment of VAT. For others, the VAT is refunded. The airports and ports' levy on imports for export processing is 0.25 percent of the CIF value.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Local agents of the U.S. and other international companies representing recording, software, movie, and consumer product industries continue to complain that the lack of IPR protection is damaging their business. Piracy levels are very high for sound recordings and software, making it difficult for the legitimate industries to protect their market and realize their potential in Sri Lanka. Sri Lanka is a party to major intellectual property agreements, including the Berne Convention for the Protection of Literary and Artistic Works, the Paris Convention for the Protection of Industrial Property, the Madrid Agreement for the Elimination of False or Deceptive Indication of Source on Goods, the Nairobi Treaty, the Patent Co-operation Treaty, the Universal Copyright Convention and the Convention establishing the World Intellectual Property Organization (WIPO). Sri Lanka's intellectual property law is based on the WIPO model law for developing countries. Sri Lanka and the United States signed a Bilateral Agreement for the Protection of Intellectual Property Rights in 1991, and Sri Lanka is a party to the WTO Trade-Related Intellectual Property Rights (TRIPS) Agreement.

In November 2003, a new intellectual property law came into force. This law was intended to meet both the U.S.-Sri Lanka Bilateral IPR Agreement and TRIPS obligations to a great extent. The law governs copyrights and related rights, industrial designs, patents for inventions, trademarks and service marks, trade names, layout designs of integrated circuits, geographical indications, unfair competition and undisclosed information. All trademarks, designs, industrial designs and patents must be registered with the Director General of Intellectual Property. Infringement of IPR is a punishable offense under the new law, and IPR violations are subject to both criminal and civil jurisdiction. Relief available to owners under the new law includes injunctive relief, seizure and destruction of infringing goods and plates or implements used for the making of infringing copies, and a prohibition of imports and exports. Penalties for the first offense include a prison sentence of 6 months or a fine of up to $5,000. The penalties could double for a second offense. Enforcement, however, against piracy and counterfeiting is a serious problem, as is public awareness of IP protection. Aggrieved parties must seek redress of any IPR violation through the courts, a frustrating and time-consuming process.

The Sri Lankan police uncovered a Malaysian-owned CD/VCD production facility in a Colombo suburb in October 2004. It is alleged to have produced pirated copies of music, movie and software violating rights of several US companies. The police investigation continues. The police have also conducted a few other raids of stores selling pirated movie and music CDs.

The Director of Intellectual Property and international experts have begun IPR legal and enforcement training for customs and police officials. In September 2004, a group of five lawyers and a judge attended an IPR program in the United States under the International Visitor program of the U.S. State Department. An active US Embassy-led IPR working group comprising adversely affected industries is also working closely with the Sri Lankan Government to pursue more aggressive enforcement and enhance public awareness. It will take time before new procedures and court precedents are established under the new law.

In addition, Sri Lanka needs to ratify and conform to the WIPO Performances and Phonograms Treaty (WPPT) and the WIPO Copyright Treaty (WCT). Sri Lanka is completing its accession to the WTO Information Technology Agreement.

SERVICES BARRIERS

Sri Lanka has opened its services sector to foreign investment. Foreign ownership of 100 percent of equity is allowed in a range of service sectors such as banking, insurance, telecommunications, tourism, stock brokerage, the construction of residential buildings and roads, the supply of water, mass transportation, production and distribution of energy, professional services and the establishment of liaison offices or local branches of foreign companies. These services are regulated and subject to approval by various government agencies. The screening mechanism is non-discriminatory and, for the most part, routine.

Banking

Foreign commercial banks are allowed to open branch offices in Sri Lanka, subject to an economic needs test and approval by the Central Bank. Foreign investors are allowed to hold 100 percent equity in local banks. Currently, there are twelve foreign commercial banks operating in Sri Lanka, including one US bank.

Listed below are the main constraints faced in the commercial banking sector:

1) restriction of banking business by government ministries and departments to state-owned banks;
2) restriction on speculative foreign exchange trading by commercial banks; banks are allowed to buy or sell foreign exchange for commercial transactions only;
3) a VAT on profit before tax and salaries;
4) inadmissibility of electronic documents in courts;
5) the absence of laws to protect and facilitate electronic commerce; and
6) absence of anti-money laundering legislation. Draft legislation is being developed.

Insurance

One hundred percent foreign ownership is allowed in insurance. Foreign insurance companies are required to incorporate in Sri Lanka to conduct insurance business. The government has recently privatized the state-owned insurance companies. Resident Sri Lankans are prohibited from obtaining foreign insurance policies except for health and travel. A major insurance company has reported difficulty in penetrating government business due to corruption. Sri Lanka's insurance regulatory body retains powers to introduce minimum and maximum premiums for various insurance products.

Telecommunications

The telecommunications sector is the most dynamic service industry in Sri Lanka. There is one fixed wire line operator, Sri Lanka Telecom (SLT), two wireless local loop operators and four mobile phone operators. Several private operators also provide radio paging, data communication, internet service and satellite link-ups. The government of Sri Lanka sold a 35 percent stake in SLT to NTT of Japan in 1997. The government sold a further 12.5 percent stake of SLT in 2003 to the public. SLT has recently acquired a mobile phone operator. Due to the past monopoly status under government control, SLT continues to own most of the national telephone infrastructure (including main switches) and the only two international cable landing stations, controls access to the international fiber optic cables and continues to dominate the sector affecting the competitiveness of other operators. All other operators are privately owned.

In early 2003, the government liberalized international telecommunications and issued 33 non-facilities based gateway licenses, ending the SLT monopoly over international telephony. Since then, international outgoing call rates have dropped sharply. However, since new licensees are not allowed to establish terrestrial facilities, they are forced to use the infrastructure of existing domestic operator networks (including SLT and Lanka Internet) to terminate or originate international calls.

A key problem facing the telecommunications sector is restricted interconnection. The Regulatory Authority has failed to enforce regulations provided under the Telecommunications Act to establish an efficient and transparent interconnection regime. SLT, the wireless operators and some of the mobile operators have formed an unofficial cartel to control local gateways and restrict interconnection for other operators. This has adversely affected the operations of most of the other operators and new international gateway licensees who are unable to make use of their licenses due to lack of interconnection by the local exchange operators. This situation has resulted in illegal bypass by some operators. Spectrum management is also weak and frequencies are not properly allocated which affect telecommunication operators. The Regulatory Agency, under a new management, has plans to improve the regulatory regime.

Quotas on foreign films

The state-owned National Film Corporation's (NFC) approval is required to import films. There is a quota restriction on imports of English language films, which is currently set at 100 per year. The quota does not effectively restrict access as annual imports are well below the limit. There are controls on the screening of films: except for the 6 top cinemas, all other theaters in Sri Lanka are required to screen at least 60 percent local films. The theaters exempted from the rule are free to screen foreign films without any restrictions. The NFC also charges a tax of $0.31 per ticket from screenings. Part of the fee on tickets for local films is paid by the NFC to local film producers. NFC, which is instituted by an Act of Parliament, has wide powers that can be used to effectively restrict foreign film imports.

Professional Services

There is no formal national policy on professional services. In practice, many foreign doctors, nurses, engineers, architects, and accountants work in Sri Lanka. Most of them are employed by foreign companies. Sri Lanka has not made any WTO commitments on the presence of natural persons, and national treatment is not accorded to foreign nationals working in Sri Lanka. Most foreign nationals do not have statutory recognition in Sri Lanka and cannot sign documents presented to government institutions or regulatory bodies.

The Immigration Department grants resident visas for expatriates and professionals whose services are required for projects or by companies approved by the Board of Investment. The Department also grants visas for expatriates required for projects approved by the government. Non-BOI companies such as banks can also recruit expatriate staff. Sri Lanka also operates a resident guest visa program for foreign investors and professionals who are recommended by the relevant Ministry.

Legal Services

A person can provide legal consultancy services without being licensed to practice law in Sri Lanka. Foreigners are not allowed to practice law (appear in courts) and do not have statutory recognition in Sri Lanka. Sri Lankan citizens with foreign qualifications need to sit for exams conducted by the Sri Lanka law college in order to practice and register in the Supreme Court.

Doctors

The Sri Lanka Medical Council allows qualified foreign doctors and medical specialists to work in Sri Lanka. They have to be sponsored by a medical institution or a non-government organization, and are required to obtain temporary registration from the Sri Lanka Medical Council (SLMC). Many Indian doctors have been issued resident work visas recently to work in an Indian-owned hospital in Sri Lanka.

Engineers and architectural services

Over the years, most foreign funded projects have used foreign consultants and contractors.

INVESTMENT BARRIERS

Sri Lanka welcomes foreign investment. One hundred percent foreign investment is allowed in most manufacturing and services sectors.

Foreign investment is not permitted in the following businesses: non-bank money lending; pawn brokering; retail trade with a capital investment of less than $1 million (with one notable exception: the Board of Investment (BOI) permits retail and wholesale trading by reputable international brand names and franchises with an initial investment of not less than $150,000); coastal fishing; education of students under 14 years of age for local examinations; and the awarding of local university degrees. Investment in additional sectors is restricted and subject to screening and approval on a case-by-case basis, when foreign equity exceeds 40 percent: shipping and travel agencies; freight forwarding; higher education; mass communications; fishing; timber-based industries using local timber; mining and primary processing of non-renewable national resources; growing and primary processing of tea, rubber, coconut, rice, cocoa, sugar and spices; and, finally, the production for export of goods subject to international quota. Foreign investment equity restrictions and government regulations also apply to air transportation, coastal shipping, lotteries, large-scale mechanized gem mining, and "sensitive" industries such as military hardware, dangerous drugs and currency.

The BOI offers a range of incentives to both local and foreign investors. To qualify for BOI incentives, investors need to meet minimum investment and minimum export requirements. In general, the treatment given to foreign investors is non-discriminatory. Even with incentives and BOI facilitation, however, foreign investors can face difficulties operating in Sri Lanka. Problems range from difficulties in clearing equipment and supplies through customs to obtaining land for factories. The BOI encourages investors to locate their factories in BOI-managed industrial processing zones to avoid land allocation problems. Investors locating in industrial zones also get access to relatively better infrastructure facilities such as improved power reliability, telecommunication and water supplies.

Government treatment of foreign investors in the privatization process has been largely nondiscriminatory with foreigners buying a controlling interest in some companies. The privatization process has not always been transparent, however. For instance, in 2003, the government sold part of the retail operations of state-owned Ceylon Petroleum Corporation (CPC) to a foreign entity without a formal tender process. A major U.S. supplier that had earlier acquired a government-owned lubricant plant has complained that the government had reneged on the terms of an exclusivity agreement extending up to mid-2004.

Access to local credit markets by foreign-owned companies incorporated in Sri Lanka was liberalized in 2003 and such firms can now borrow rupee funds without the approval of the Central Bank. Foreign-owned companies, BOI-approved firms and exporters can access dollar denominated loans. Applications for dollar denominated loans from local firms are considered on a case-by-case basis and not encouraged.

Capital Repatriation

Sri Lanka has accepted Article VIII status of the IMF and has liberalized exchange controls on current account transactions. There are no surrender requirements on export receipts, but exporters need to repatriate export proceeds within 120 days to settle export credit facilities. Other export proceeds can be retained abroad. Currently, contracts for forward bookings of foreign exchange are permitted for a maximum period of 360 days for the purposes of payments in trade and 720 days for the repayment of loans. There are also no barriers, legal or otherwise, to the expeditious remitting of corporate profits and dividends for foreign enterprises doing business in Sri Lanka. Remittance of business fees (management fees, royalties and licensing fees) is also freely permitted. Funds for debt service and capital gains of BOI approved companies exempted from exchange control regulations are freely permitted. Other foreign companies remitting funds for debt service and capital gains require Central Bank approval. Prior to Central Bank approval they also need a tax clearance certificate. All stock market investments can be remitted without prior approval of the Central Bank. Investment returns can be remitted in any convertible currency at the legal market rate.

Controls on capital account (investment) transactions usually prohibit foreigners from investing in debt and fixed income securities. One exception has been the Central Bank's local market dollar denominated bond issues in 2001, 2002 and 2004, which were opened to foreign investors. The government has proposed allowing foreign investment in corporate debentures and government bonds. Local companies require Central Bank approval to invest abroad. The process of granting approval for such investments was streamlined in 2002, resulting in an increase in approvals.

OTHER BARRIERS

Delays in litigation are a problem. For example, a U.S. investor with a substantial investment in an export manufacturing company has faced lengthy delays in a court case over a large insurance claim. The company instituted legal action in June 1999 and court proceedings are still on-going, and the company has suffered financial losses as a result. The government has established a commercial court to hear business litigation, but delays are common.

In order to support the domestic software industry, private sector companies using locally produced software will be allowed to depreciate 100 percent of the cost in the first year, according to 2005 budget proposals. The depreciation allowance on foreign software is only 25 percent. The public sector is required to give preference to locally produced software and ensure at least 50 percent local value addition when using foreign software.

The government has recently re-introduced a 100 percent transfer tax on property purchased by foreign nationals and companies. For this purpose, a “foreign company” is defined as an entity with at least 25 percent foreign equity. Apartments above the third floor of condominium buildings, land for the development of large housing schemes, hospitals, and large infrastructure projects are exempted from the tax. Foreigners maintaining $ 150,000 in a bank account in Sri Lanka will be given concessionary treatment. In addition to the tax, the government has plans to prohibit certain geographical areas for purchase by non-citizens. Property transfers to foreigners were exempted from tax in 2002

SWITZERLAND

TRADE SUMMARY

The U.S. trade deficit with Switzerland was $2.4 billion in 2004, an increase of $345 million from $2.0 billion in 2003. U.S. goods exports in 2004 were $9.3 billion, up 7.1 percent from the previous year. Corresponding U.S. imports from Switzerland were $11.6 billion, up 9.0 percent. Switzerland is currently the 18th largest export market for U.S. goods. U.S. exports of private commercial services (i.e., excluding military and government) to Switzerland were $8.0 billion in 2003 (latest data available), and U.S. imports were $8.3 billion. Sales of services in Switzerland by majority U.S.-owned affiliates were $6.8 billion in 2002 (latest data available), while sales of services in the United States by majority Switzerland-owned firms were $33.1 billion. The stock of U.S. foreign direct investment (FDI) in Switzerland in 2003 was $86.4 billion, up from $71.5 billion in 2002. U.S. FDI in Switzerland is concentrated largely in the wholesale, manufacturing, and banking sectors.

IMPORT POLICIES

In recent decades, agriculture has lost its relative importance in the Swiss economy – though not in society or politics – and preservation in its current form has been due largely to governmental intervention and support. Switzerland is leading the so-called "Group of Ten" net food importers, which lobbied hard in the WTO against moves to tighten limits on import duties for so-called sensitive products.

The simple average tariff in Switzerland on imports of agricultural products is 34.3 percent, while the average for manufactured products is 2.3 percent. Due to high tariffs on certain agricultural products, preferential tariff rates for other countries, and negative public perception of agricultural products derived from biotechnology, Switzerland is a relatively difficult market for many U.S. agricultural products to enter. The U.S. share of the agricultural import market is about 3.16 percent.

Imports of nearly all agriculture products, no matter the country of origin, are subject to import duties and variable import quotas. The Swiss agricultural sector remains among the most heavily subsidized in the world. Although Swiss statistics show that 1,500 farms are forced out of business each year, the number of organic farms grew by 3.3 percent between 2003 and 2004, and organic sales increased by 7 percent to $979 million. Many consumers choose organic products – sold under the Swiss label "ioSuisse" – when they buy dairy, meat, bread, eggs, vegetables, and fresh fruits.

Prices received by farmers in Switzerland are more than 100 percent higher than world market prices. The OECD estimates that Switzerland subsidizes more than 70 percent of its agriculture, compared with 35 percent in the European Union. According to the 2007 Agricultural Program recently adopted by the Swiss Parliament, the funds allocated to Swiss agriculture will increase by $47 million, totaling $10.6 billion from 2004 to 2007. However, milk quotas will be abolished starting in May 2009.

Agricultural tariff-rate quotas also present problems for U.S. exporters, since Swiss regulations often allocate quotas to importers that have incentives to purchase domestic products. This practice has increased protection for domestic producers and in some cases, such as potato products, has effectively blocked U.S. imports. Although public resistance to agricultural products derived from biotechnology or the use of growth hormones remains strong, U.S. agricultural exports to Switzerland maintained steady growth in recent years.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Switzerland has taken a case-by-case approach to agricultural products derived from biotechnology since voters rejected a moratorium on biotechnology research and products in 1998. Agricultural biotechnology products need approval for consumer marketing through certification by the Federal Office of Public Health, and the manufacturer of such products must submit detailed information concerning the process for development. The Swiss authorities must review the product for toxicity, resistance to antibiotics, and allergenic characteristics. Agricultural biotechnology products that are substantially equivalent to conventional foods may have an easier path to approval. Swiss certificates for approval of agricultural biotechnology products are valid for five years.

Switzerland has required labeling for foods containing products derived from biotechnology since 1996. In 1999, the federal government modified its regulations to require labeling only if the percentage of ingredients derived from biotechnology reaches one percent. However, this threshold will be lowered to 0.9 percent starting January 1, 2005 to be compatible with EU regulations. A notable exception to the labeling requirement is the use of substances in the production process extracted or refined from substances derived from biotechnology, such as refined soy oil. According to Swiss officials, these ingredients do not require a label because testing cannot show they are derived from bio-engineered commodities. The pharmaceutical industry has been particularly influential in deflecting harmful regulation and maintaining the legal basis for a possible future, more receptive market.

The animal feed industry has succeeded in establishing a small market for products derived from biotechnology. However, the planting of seed crops derived from biotechnology faces difficult environmental approval hurdles. The government has opposed a call for a five-year moratorium on crops derived from biotechnology in Switzerland. Put forward by a coalition of environmental groups, consumers and farmers, the initiative calls for a ban on the farming of crops derived from biotechnology for use in food, and the import of seeds and fodder derived from biotechnology. However, the cabinet believes that the new Swiss law on genetics (Gen-

Lex), which took effect in January 2004, adequately protects humans, animals, and the environment against abuses.

The most significant barriers for agricultural biotechnology products in Switzerland stem from policies by the major food retailers and Swiss farmers not to purchase such products. Swiss groups opposed to these products in the food chain have been very effective in convincing supermarket purchasing executives and Swiss farm groups to boycott such products.

Since January 2000, imports of fresh meat and eggs produced in a manner not permitted in Switzerland must be clearly labeled as such. Methods not allowed in Switzerland include the use of growth hormones, antibiotics, and other substances in the raising of beef and pork, as well as the production of eggs from chickens kept in certain types of cages.

The Swiss Veterinary Agency continues to refuse to list new U.S. facilities as eligible to export beef to Switzerland and, despite repeated requests, has not produced science-based reasons for this position. Swiss inaction has blocked three plants that the United States requested be listed since early 2002. The Swiss government has made clear that the situation is due to its dissatisfaction with current U.S. regulations that block certain Swiss processed beef exports to the United States due to concerns over mad cow disease and foot-and-mouth disease.

GOVERNMENT PROCUREMENT

Switzerland is a signatory of the WTO Government Procurement Agreement (GPA). On the cantonal and local levels, a law passed by Parliament in 1995 provides for nondiscriminatory access to public procurement. The United States and Switzerland agreed in 1996 to expand the scope of public procurement access on a bilateral basis.

According to a July 2002 revised ordinance on public procurement, all private or state-owned companies such as utilities, transportation, communications, defense, and construction that submit tenders for government procurement must make their bids public if the contract exceeds SFr 250,000 ($219,241). Total procurement expenses – both at the federal, cantonal and community level – are valued at approximately $26 billion. Foreign purchases totaled $446 million.

In September 2004, the Swiss government initiated a series of informal consultations to amend the Swiss Federal Law on Public Procurement. This process should ultimately simplify the public tender procedure, and harmonize it across the cantons. Under the GPA, Swiss cantons are allowed to implement the agreement independently from federal intervention, which sometimes leads to disparities across cantons.

In general, quality and technical criteria are as important as price in the evaluation of tenders. Cantons and communes usually prefer local suppliers because they can recover part of their outlays through income taxes. Foreign firms may be required to guarantee technical support and after-sale service if they have no local office or representation.

Notices of Swiss government tenders are published in the Swiss Official Gazette of Commerce (www.shab-online.admin.ch) and on the on-line Swiss Public procurement website www.simap.ch (French, German and Italian versions only). There is no requirement to have a local agent to bid.

SERVICES BARRIERS

Legal Services

Foreign lawyers are not forbidden to work in Switzerland, but there are practical and legal limits to their activities. For example, a foreign lawyer not licensed in Switzerland must follow carefully the complex requirements of several international conventions to obtain testimony or to serve process in civil matters in Switzerland.

Telecommunications

The 1998 Telecommunications Act brought liberalization and privatization to the Swiss telecommunications sector, opening the market to investment and competition from foreign firms. More than fifty Swiss and foreign companies now offer fixed line services. Three different operators, Swisscom, Sunrise (TeleDanmark), and Orange (France Telecom) share the mobile telephone market, and each company also owns third generation mobile telephony licenses (UMTS). Southern Bell Corporation's 9.5 percent stake in Sunrise's parent company represents the only significant U.S. presence in the Swiss telecommunications market. The incumbent state monopoly – Swisscom – has often used the courts to block the Swiss government's efforts to open the market to competition. For example, Swisscom has successfully fought efforts by the Competition Commission and the Communications Commission to unbundle the local loop and provide leased lines at cost-oriented prices. In response, the government is in the process of reforming the telecommunications law and the law implementing ordinances to create the necessary legal authority for the regulator to implement the initiative.

In February 2003, the Swiss Cabinet approved a proposal for a two-pronged telecommunications reform package. A portion was accomplished by amending the Federal Ordinance on Telecommunication Services needing only the approval of the Swiss Cabinet, while the reform of the 1997 Telecom Act will go through Parliament. The regulatory reform took effect on April 1, 2003, and gave the independent regulator the legal authority to order Swisscom to provide leased lines at cost-oriented prices. In November 2003, the regulator had unsuccessfully tried to force Swisscom to drop its interconnection prices by 25 percent to 35 percent and pay back tens of millions of francs to the competition, but a federal court overturned the decision in March 2004.

In February 2004, the Communications Commission ruled in favor of TDC Sunrise seeking an order to force Swisscom to provide it with unbundled access to the local loop. In its decision, the regulator cited the legal provisions embodied in the April 2003 ordinance as sufficient basis to force Swisscom to unbundle its local loop for bit stream access, shared access, and full access. Swisscom immediately appealed the decision. In December 2004, a federal court rebuffed the ruling on the grounds that Swiss laws – as they stand at present – do not give the regulator authority to require Swisscom to open the local loop to competition.

In October 2004, the lower house began work on amending the Telecom Act with language that will give the regulator explicit authority to force Swisscom to unbundle its local loop, effectively fixing the "flaw" cited two months later by the federal court. The reform will not extend to other technologies, such as Mobile and WiFi. The bill also requires that broadband access be offered to Swisscom competitors at cost-oriented prices over a period of six years, after which all operators are expected to afford the broadband investment themselves. The reform is now being addressed in the Lower House's Committee on Telecommunications. According to the Parliament's secretariat, the bill should come to the floor during the 2005 spring session. Implementation of the new law is not expected until the end of 2005 or early in 2006. In October 2004, Swisscom announced that it would lower its interconnection prices by 7 percent. Some observers have suggested that the move was aimed at reducing the Parliament's interference in its interconnection practices.

Audiovisual Services

Switzerland has no limitations on the amount of non-Swiss or non-European origin programming that can be broadcast, but film distributors and cinema companies must maintain, through self-regulatory solutions, an appropriate diversity – not yet defined – in the products offered within a region. The government may levy a nominal development tax on movie theater tickets if the appropriate diversity is not present. The development tax receipts would be used to finance new theaters that would offer greater diversity in the films being shown within a region.

INVESTMENT BARRIERS

Switzerland welcomes foreign investment and accords national treatment. The federal government's approach is to create and maintain general conditions that are favorable both to Swiss and foreign investors. Swiss banking laws encourage the formation of abundant pools of capital from overseas investors. Some cantons have income tax incentive programs to encourage foreign investment.

The major laws governing foreign investment in Switzerland are the Swiss Code of Obligations, the Lex Friedrich/Koller, the Securities Law, and the Cartel Law. There is no screening of foreign investment – except land ownership and national security establishments – nor are there any sectoral or geographical preferences or restrictions. Cantons have been granted extensive decision making powers when allowing foreigners to buy land. Investment areas in which restrictions related to national security apply include hydroelectric and nuclear power, operation of oil pipelines, transportation of explosive materials, operation of airlines, and marine navigation.

ANTICOMPETITIVE PRACTICES

The Swiss economy has long been characterized by a high degree of cartelization, primarily among domestically oriented firms and industries. In June 2003, the Swiss parliament adopted a revised competition bill, which took effect on April 1, 2004. The most significant improvement in the revised law is authority to sanction anticompetitive behavior without prior warning, with a maximum fine of ten percent of a firm’s total combined revenue for the past three years. Whistle blower companies that cooperate with regulators are eligible for a reduced fine. The transition period to adapt to the new law ends on April 1, 2005.

In the automobile sector, the Competition Commission implemented new rules in 2002 that greatly weakened special antitrust exemptions in the automobile industry. The new regulations forbid manufacturers from implementing a higher Swiss price outside Switzerland, a practice that prevented Swiss car buyers from shopping in neighboring countries for better deals. Industry experts predict cautiously that the price spread for both automobiles and parts imported from the EU will be broader, with prices likely to tumble.

ELECTRONIC COMMERCE

The government generally supports the development of electronic commerce with a minimum of regulatory interference. In December 2003, Switzerland adopted legislation that will recognize the validity of electronic signatures starting January 1, 2005. Electronic signatures will then have the same legal value as handwritten ones. People can sign up electronically for health insurance and apartments. However, some official documents, for example wills or property deeds, will still have to be signed by hand. This move puts Switzerland among the first European countries to recognize e-signatures. Swiss provisions are compatible with European law and are aimed at contributing to the development of cyber administration, e-commerce, and the purchase of goods and services on the Internet. Swiss authorities are promoting electronic government services with a goal of providing services more efficiently and making Switzerland more competitive as a business location.

TAIWAN

TRADE SUMMARY

The U.S. trade deficit with Taiwan was $12.9 billion in 2004, a decrease of $1.3 billion from $14.2 billion in 2003. U.S. goods exports in 2004 were $21.7 billion, up 24.6 percent from the previous year. Corresponding U.S. imports from Taiwan were $34.6 billion, up 9.6 percent. Taiwan is currently the 9th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Taiwan were $4.9 billion in 2003 (latest data available), and U.S. imports were $4.9 billion. Sales of services in Taiwan by majority U.S.-owned affiliates were $8.3 billion in 2001 (latest data available), while sales of services in the United States by majority Taiwan-owned firms were $684 million.

The stock of U.S. foreign direct investment (FDI) in Taiwan in 2003 was $11.0 billion, up from $10.2 billion in 2002. U.S. FDI in Taiwan is concentrated largely in the finance, manufacturing, and wholesale sectors.

IMPORT POLICIES

Tariffs

Taiwan promulgated a comprehensive tariff revision schedule on January 1, 2004 in compliance with Taiwan's Free Trade Agreement with Panama, and Taiwan's accession commitments to the WTO. Tariffs on pharmaceuticals, pulp/paper, iron/steel, construction equipment, agricultural equipment, medical equipment, furniture and toys were eliminated starting on January 1, 2004. As a result, the average nominal tariff rate on imported goods in 2004 was approximately 5.7 percent and is expected to fall to 5.5 percent by 2007. However, U.S. industry continues to request that Taiwan lower tariffs on imports of many goods, including large motorcycles, wine, canned soups, cookies (sweet biscuits), savory snack foods, vegetable juices, potato and potato products, table grapes, apples, fresh vegetables, and citrus products.

Upon Taiwan's accession to the WTO in January 2002, Taiwan implemented tariff-rate quotas (TRQs) on small passenger cars, three categories of fish and fish products, and a number of other agricultural products. On January 1, 2004, in accordance with its WTO accession commitments, Taiwan made additional tariff cuts and increased TRQ amounts on these products. Certain items of interest to U.S. exporters, including chicken meat, pork belly, and poultry and pork variety meats, will be fully liberalized in 2005. In May 2004, Taiwan increased the sugar TRQ by 50,000 tons to 255,000 tons to meet Taiwan's domestic market shortage.

Taiwan has notified the WTO that it maintains Special Safeguards (SSGs) for a number of agricultural products covered by TRQ's. SSGs, permitted under Article 5 of the Agreement on Agriculture, allow Taiwan to impose additional duties when import quantities exceed SSG trigger volumes or import prices fall below SSG trigger prices. As Taiwan has not imported many of these products previously, SSG trigger volumes are relatively low. SSGs will also come into play once certain commodity imports are fully liberalized in 2005 and will likely have the greatest effect on U.S. poultry exports. The United States has raised concerns over Taiwan's use of SSGs.

Licensing and Other Restrictions

In order to comply with its WTO commitments, Taiwan eliminated import controls on over 99 percent of 10,912 official import product categories. Currently, 24 product categories require import permits from the Board of Foreign Trade. Imports of 65 categories are restricted, including ammunition and some agricultural products. These items can only be imported under special circumstances, and their importation is effectively banned.

Agricultural and Fish Products: Prior to its WTO accession, Taiwan banned or restricted imports of 42 agricultural and fish items. In January 2002, Taiwan liberalized imports of 18 of these agricultural and fish categories and implemented TRQs on the remaining 24 items. TRQs on a number of products of interest to the United States (chicken meat, pork belly and offal, and poultry offal) will be eliminated on January 1, 2005 when trade is fully liberalized.

Rice: Before Taiwan's WTO accession, imports of rice were banned. During 2002, rice imports were subject to an absolute quota that covered both public- and private-sector imports. In 2003, Taiwan changed its rice import regime to a tariff-rate quota system without consultation with its trade partners. As a result, in January 2003 the United States, as well as Australia and Thailand, formally objected to Taiwan's proposed rice import system at the WTO. Since then, the United States has also raised concerns regarding Taiwan implementation of its rice import system, including cancellation of mark-up price reductions for several private-sector tenders, and the use of a "ceiling price" for public-sector tenders. Despite these difficulties, U.S. suppliers were able to gain a majority of the rice import market in 2002 and 2003. In 2004, Taiwan's implementation of its import commitments improved significantly and U.S. rice suppliers, again, supplied a majority of rice imports to the Taiwan market. Also, during 2004 the United States and Taiwan made substantial progress in resolving outstanding differences. However, as 2004 came to a close, certain rice suppliers to the Taiwan market other than the United States did not agree to proposed modifications to Taiwan's rice import system. As a result, Taiwan will continue its current system for 2005 while, at the same, working toward final resolution of the rice import issue.

Tobacco and Alcohol Products: As a condition of Taiwan's WTO accession, a new tobacco and alcohol management and tax system went into effect on January 1, 2002. In place of the previous tax on imports administered by the former monopoly authority, the Taiwan Tobacco and Wine Monopoly Bureau (TTWMB), Taiwan agreed to impose an excise tax and to eliminate tariffs on imports of most spirits.

Taiwan also liberalized private alcohol production upon its accession to the WTO and private cigarette manufacturing in 2004. TTWMB became a state-owned corporation, Taiwan Tobacco and Liquor Corporation (TTLC), in July 2002. However, primarily due to resistance by organized labor, the privatization of the TTLC has been postponed until 2005.

Wood Products: Taiwan has revised building codes in line with international practices. However, Taiwan has not yet completed a companion fire code. This delay means that while a wood frame structure may be built, approval by fire inspection authorities is contingent on review and comment by a special committee on details, such as design and usage. U.S. wood products companies have raised concerns that this practice is restrictive and does not encourage wood use in construction. The continued use of a special committee rather than finalizing a fire code unnecessarily delays construction of wood structures and raises the cost of using wood materials significantly beyond that of other materials such as concrete and steel.

Automobiles and Motorcycles: Local content requirements in the automobile and motorcycle industries were lifted as part of Taiwan's WTO accession. The importation of motorcycles with engines larger than 150 cc was liberalized in July 2002 as part of Taiwan's WTO commitments. In mid-2003 Taiwan agreed to set emissions standards for motorcycles over 700 cc in line with international standards, a step which the U.S. motorcycle industry supported. The U.S. Government remains concerned with Taiwan's tariffs and other taxes on large motorcycles as well as Taiwan's restrictions on motorcycle access to highways.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

Industrial and Home Appliance Products: Industrial and home appliance products (such as air-conditioning and refrigeration equipment) are subject to safety and electro-magnetic compatibility (EMC) testing requirements before clearing customs. The manufacturers or importers can choose tests on each shipment either based on "batch-by-batch inspection" (BBI) with Type Approval or "registration of product certification" (RPC). All safety testing for end products must be done in Taiwan by Taiwan accredited laboratories. In accordance with the APEC Telecommunications Mutual Recognition Agreement, Taiwan accepts EMC testing by NIST-accredited laboratories in the United States only for information technology equipment. For those products that adhere to the ISO 9000 quality management system, an alternative factory inspection module was introduced. The manufacturers or importers may choose the module most appropriate to them when applying for registration under the RPC scheme.

Sanitary and Phytosanitary Measures: As a member of the WTO, Taiwan must abide by the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (including notification of such measures). In 1998, Taiwan agreed to accept meat and poultry imports from plants approved by the USDA Food Safety Inspection Service. In 1999 and 2000, Taiwan agreed to accept *Codex Alimentarius* or U.S. pesticide residue standards for some chemicals used on imported fruits and vegetables. However, the United States continues to be concerned that some Taiwan plant and animal quarantine measures are not always based on sound science and are more trade restrictive than required.

Beverage Alcohol Products: On December 31, 2001, immediately before its WTO accession, Taiwan implemented new regulations requiring major ingredient labeling for beverage alcohol products. Although these regulations affect international trade, the United States was not informed by Taiwan in advance of their implementation. Bilateral meetings were conducted in 2002 to discuss this requirement and as a result, enforcement of the ingredient labeling requirement was delayed until July 2003. In December 2003, Taiwan's legislature passed the Tobacco and Alcohol Administrative Law (TAAL), which enabled the Ministry of Finance (MOF) to eliminate ingredient labeling requirements for beverage alcohol products. Effective July 1, 2004, alcoholic beverage product labels do not need to include a list of ingredients.

Agricultural Biotechnology Products: Taiwan authorities generally have taken a cautious, but fairly rational approach to trade in agricultural biotechnology products. Risk assessment documentation on agricultural biotechnology corn and soybeans were required to be submitted to the Department of Health (DOH) before April 30, 2002, and mandatory labeling on certain corn and soybean products commenced in 2003. In October 2003, DOH announced its intention to require registration of agricultural biotechnology products other than corn and soybeans in 2004, but offered an opportunity for life science companies to obtain interim approval for those products currently commercialized. Mandatory labeling on all foods with over 5 percent agricultural biotechnology products content is required. No disruptions to trade have resulted from Taiwan's biotechnology regulations. However, with a number of products entering the regulatory approval pipeline and a lack of investment in a strong domestic regulatory infrastructure, delays in approvals have become more frequent.

Labeling of biotechnology food: Taiwan requires warning labels on foods containing biotechnology corn or soybeans. All food products containing 5 percent or more bioengineered soybean or corn ingredients by weight must be labeled as "Genetically Modified (GM)" or "Containing Genetically Modified."

Medical Devices: Registration and approval procedures for medical device imports are complex and time-consuming, and have been the subject of long-standing complaints by U.S. firms. The registration process requires redundant testing, and foreign manufacturers must re-register new products even though they are based on previously approved devices. In addition, regulations are vague on when local clinical trials are required for the review process or whether industry is allowed to provide additional input in response to questions posed by DOH officials reviewing the clinical trial submissions. The adoption of the U.S. Food and Drug Administration's medical device classification system in June 2000 was welcomed by industry. However, Taiwan's implementation of this system in 2004 was faulted by industry for requiring re-registration of previously approved products. This new system also required the registration of previously unregistered low risk medical devices (Class I) which are not typically registered in most advanced markets. U.S. firms have expressed concern that these new registration procedures require significantly more information (including sensitive information on manufacturing processes) than are commonly requested for other markets. Taiwan has identified both the medical device and pharmaceutical sectors as priorities for local development, resulting in Taiwan's agencies often favoring the interests of local companies over foreign firms.

Pharmaceuticals: Taiwan's lengthy pharmaceutical registration process slows market entry for new drugs that have already been approved in advanced economies and also imposes unnecessary costs on drugs that have been approved in Taiwan. In May 2001, the DOH announced a requirement for firms to submit voluminous amounts of proprietary manufacturing data as part of the registration and approval process for both new drugs and those already on the market. The amount of such "validation" data requested by Taiwan far exceeded international norms. In response to concerns raised by the United States and its industry, the DOH had postponed implementation of this requirement. In December 2002, the United States and Taiwan exchanged letters in which Taiwan affirmed its commitment to adhere to international practices as applied in advanced economies, and agreed that firms can demonstrate validation status by providing documentary evidence, including abridged registration applications. In August 2003, DOH and the U.S. industry reached agreement on validation data resolutions. However, in 2004 DOH began assigning risk-based "priority numbers" that will be used to determine which manufacturers are inspected by DOH. U.S. industry is concerned that these risk priority numbers (RPNs) are based on non-transparent criteria and inspections will unfairly target manufacturers that provide abridged data. Despite a mutual understanding that an abbreviated package that includes summary documentation is sufficient evidence to prove plant validation, companies choosing to provide the summary appear to be subject to automatic assignment of a RPN. Assignment of an RPN, industry believes, will result in costly, unnecessary inspections. Discussions between the United States and Taiwan to resolve remaining issues are ongoing.

Pricing and reimbursement policies also have been a long-standing concern for the U.S. government and innovative pharmaceutical producers. Taiwan uses various methods to lower assigned prices on innovative drugs, including "reference pricing" (assigning a lower price when a drug is approved for an additional use) and lowering assigned prices without a transparent process. In addition, Taiwan continues to restrict consumer choice and limit U.S. market access through disproportionate reimbursement of domestically-manufactured generic drugs. To address concerns of foreign pharmaceutical firms, Taiwan announced a revised reimbursement pricing plan in March 2003. In this plan, the DOH and the Bureau of National Health Insurance agreed to find ways to include a "reward for innovation" component in its pricing mechanism for new drugs. However, industry representatives have criticized the new drug pricing mechanism as non-transparent and believe the reimbursement prices will not achieve the stated objective. Discussions between the United States and Taiwan on this issue are ongoing.

Article 49 of Taiwan's National Health Insurance law mandates reimbursement of healthcare providers at actual transaction costs, but apparently this law is not enforced. In practice, locally-based generics producers offer significant and highly questionable discounts to the reimbursement rate. As a result, Taiwan healthcare providers increasingly choose generics over innovative medicines.

In July 2002, Taiwan introduced a "global budget" system in which hospitals receive lump sums from the National Health Insurance system to cover the cost of providing all services. The goal was to increase efficiency and encourage cost-cutting measures, but critics contend that global budgeting primarily encourages hospitals to increase requests for illegal discounts on pharmaceuticals and discourages the use of innovative medicines as budget pressures grow. Once global budgeting was enacted, hospitals immediately began to depend on larger profit margins from medicines, favoring locally-produced generics with large margins over innovative, usually foreign, pharmaceuticals as a means to cover budget shortfalls. The problem was exacerbated in 2004, when budget growth was capped at 4 percent. Research-based pharmaceutical companies estimate that global budgeting and self management of hospitals has cost them more than $100 million in sales. With 2005 budget growth capped at 3.7 percent, U.S. companies selling innovative medicines in Taiwan face an even more restrictive marketing climate.

Blood and Plasma-derived Products: Taiwan's Legislative Yuan in December 2004 passed a law that directs the Taiwan government to monitor and, if necessary, restrict imports of blood, plasma, and plasma-derived products. These include products manufactured in the United States and frequently relied on by patients in Taiwan. The U.S. Government will closely monitor the implementing guidelines for this new law to ensure that Taiwan provides national treatment and fair market access in this sector.

Other issues: Taiwan banned imports of U.S. beef in December 2003 after the detection of one positive case of Bovine Spongiform Encephalopathy (BSE) in the State of Washington. As of the publication of this report, the U.S. Government is taking aggressive action and is working intensively to re-open the market as quickly as possible. Non-ruminant products for feed use, such as tallow, lard, poultry and porcine meal are banned. Limited exceptions are only approved after a very slow case-by-case review or plant clearance process.

GOVERNMENT PROCUREMENT

Taiwan committed to accede to the WTO Agreement on Government Procurement (GPA) as part of its WTO accession. While Taiwan has applied for accession to the GPA, its accession has not yet been completed due to differences regarding nomenclature issues. To prepare for its GPA accession, Taiwan implemented a new Government Procurement Law in mid-1999. This was an important first step toward establishing a transparent and predictable environment for Taiwan's multi-billion dollar market for public procurement projects. In August 2001, Taiwan and the United States signed a Memorandum of Understanding on Government Procurement (MOU). The MOU called for Taiwan to implement certain procedural commitments immediately, while others are to be implemented upon accession to the GPA. Taiwan also agreed to establish new procedures providing for the independent review of complaints that arise during the tendering process, to encourage its procuring entities to make use of mediation procedures, and to cooperate fully when such procedures are invoked. Despite these commitments, Taiwan officials have continued to incorporate provisions in public procurement tenders that appear to be inconsistent with the GPA. Further, the lack of transparency in the government procurement process as well as the review process for complaints remains a serious issue. U.S. participation in Taiwan's government procurement market continues to decline as a result of these practices. The United States has continuing concerns with Taiwan's government procurement environment.

EXPORT SUBSIDIES

The Taiwan government provides incentives to industrial firms in export processing zones and to firms in designated "emerging industries." Some of these programs may have the effect of subsidizing exports. Taiwan has notified the WTO of these programs and, as part of its WTO accession, committed to amend or abolish any subsidy programs inconsistent with WTO rules. Amendments of relevant laws, such as the Statute for Establishment and Management of Economic Processing Zones and the Statute for Establishment of Scientific Industrial Parks, to eliminate improper subsidies went into effect upon Taiwan's WTO accession. The United States continues to monitor Taiwan's compliance with the commitments it undertook as part of its WTO accession, including those obligations associated with the Agreement on Subsidies and Countervailing Measures.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

IPR protection continues to be an important and serious issue in the U.S.-Taiwan trade relationship. In 2004, Taiwan continued to take measures to improve enforcement of IPR, including intensifying raids against manufacturers and retailers, making permanent previously *ad hoc* task forces, and approving additional revisions to the copyright law that increase penalties for infringers. The U.S. International Intellectual Property Alliance estimates that losses due to IPR infringement in Taiwan cost U.S. industry $315 million in 2004. The U.S. Government also continues to be concerned with the prevalence of counterfeit pharmaceuticals in Taiwan despite several large raids against manufacturers and the passage of amendments strengthening the pharmaceutical law. Another area of concern is the lack of adequate protection for the packaging, configuration, and outward appearance of all products – known as trade dress. U.S. industry has also complained about delays in court cases and the Taiwan judiciary's difficulty in handling technical cases. Generally, U.S. IPR holders find that court procedures themselves constitute barriers and penalties for intellectual property violations are inadequate to deter violators.

In April 2004, Taiwan was placed on the U.S. Special 301 Priority Watch List for the fourth year in a row, but was moved to the Watch List after an out-of-cycle review later that year determined that Taiwan had made sufficient progress to warrant a change in status. In addition, soon after the results of the out-of-cycle review were announced in January 2005, Taiwan's legislature approved a bill to prevent unfair commercial use of pharmaceutical test data. However, despite improvements, the United States will continue to monitor Taiwan authorities' development of implementing regulations for the protection of pharmaceutical test data, effective actions against piracy of copyrighted works over the Internet, and continued strengthening of enforcement efforts so that piracy and counterfeiting are effectively reduced. The United States also will follow with interest Taiwan's efforts to monitor exports of copyrighted materials, particularly software, to ensure that these efforts are as effective, or more effective, than Taiwan's Export Monitoring System Enforcement.

To improve Taiwan's ability to protect IPR, the government formulated a three-year (2003-2005) IPR Action plan. Measures included the establishment of the Integrated Enforcement Task Force (IETF) with a force of 220 police officers in January 2003; the opening of three warehouses for storing counterfeiting seizures; the raising of the informant reward to up to approximately $310,000 per counterfeiting seizure; the strengthening of border control inspection for optical media exports; and the increasing of day and night inspection on optical media production facilities, night markets, and retail shops. Counterfeit goods seized by the U.S. Customs Service from shipments of Taiwan origin dropped from $26.5 million in FY2002 to $610,000 in FY2003, and to $60,000 in the first half of FY 2004. The Business Software Alliance (BSA) also announced that the software piracy rate in Taiwan fell from 54 percent in 2002 to 43 percent in 2003, this rate remained unchanged in 2004.

After concerted lobbying by industry and the Taiwan executive branch, the Legislative Yuan in August 2004 passed a number of amendments to its copyright law. These changes were eliminated from consideration or not considered at all when the law was amended in June 2003. New amendments which improved the existing law include (a) technological protection measures; (b) heavier penalties for infringement; and (c) authorization for Taiwan Customs to take *ex officio* action.

Internet piracy and illegal peer-to-peer downloading are becoming serious concerns for IP enforcement in Taiwan. Infringers are using the Internet to market illegal goods and allowing the unauthorized downloading of music, movies, and software from Internet service providers. Efforts to use the legal system to shut down or restrict the activities of such services have met with limited success thus far.

In response to U.S. and industry requests to improve protection of optical media products and curtail the illegal manufacture of such goods, Taiwan passed an optical media law on October 31, 2001. Manufacturers must apply for production licenses and report any changes to the authorities. Violators face a maximum three-year jail sentence and a fine of approximately $86,000. The law was fully implemented in May 2002. The Optical Media Law and IETF's night and day inspections have led to a dramatic decrease in large-scale factory production of counterfeit optical media products.

The U.S. Government remains concerned with the growing incidence of counterfeit pharmaceutical products in the Taiwan market which create consumer health safety issues. The Taiwan government in March 2004 revised the pharmaceutical affairs law to increase penalties for pharmaceutical counterfeiting. Nevertheless, counterfeit products continue to be a threat to public health and Taiwan's DOH enforcement mechanism is not strong.

In January 2005, Taiwan's legislature approved a bill to provide data protection for pharmaceutical products, a TRIPS commitment and an incentive for innovative pharmaceutical manufacturers to introduce new products into the Taiwan market. The United States will monitor Taiwan's development of implementing regulations to ensure that commitments made by Taiwan regarding the period of protection are adequately codified.

Taiwan's judiciary continues to experience difficulties in handling technical cases, and U.S. industry has complained about long delays in court cases. Often conflicting or unclear lines of bureaucratic authority stymie IPR enforcement efforts. The United States continues to assist in remedying the weaknesses of the judicial system by holding seminars on criminal enforcement and encourages Taiwan to set up IP courts with experienced judges.

SERVICES BARRIERS

Financial Services

Taiwan continues to liberalize its financial market beyond its WTO accession commitments. In January 2001, the Securities and Futures Exchange Commission (SFEC) lifted the restriction on employment of foreigners by domestic securities firms. Also in January 2001, the SFEC removed the 50-percent foreign ownership limit on listed companies. In June 2003, the SFEC phased out a minimum two-year period for foreign holders of global depository receipts (GDRs) to exchange GDRs for equity stocks after a GDR is issued. In July 2003, the SFEC lifted the ceiling limit of $3 billion on inward remittances by a qualified foreign institutional investor (QFII). It also abolished the requirement for a QFII to inwardly remit its investment fund within two years after it receives approval. In early October 2003, the Taiwan government voluntarily abolished the QFII system. Foreign portfolio investors are required to complete registration rather than seek advance approval, and in December 2003, the registration could be done through the Internet. In late 2003, Taiwan allowed foreign portfolio investors to trade in the futures and money markets as a part of financial management prior to actual portfolio investment. However, futures, money market funds and bank deposits are subject to a limit of 30 percent of total inward remittances. All offshore foreign portfolio investors may trade in Taiwan's stock market regardless of their size, except for investments in hedge funds and investors from the PRC. However, foreign individual investors are still subject to an investment limit. Onshore foreign individuals and institutional investors are also subject to annual inward/outward limits.

Taiwan continues to work towards fulfilling its May 1997 commitment to liberalize insurance premium rates and policy clauses. It voluntarily opened the reinsurance market. In November

2001, Taiwan permitted life insurance companies to sell investment-linked products. Taiwan began to allow life insurance companies to set their own premium rates in January 2002 if the companies had their own actuaries to determine such rates. Taiwan adopted a three-stage premium rate liberalization program for non-life insurance. Effective January 1, 2002, insurance firms were allowed to set premium rates for large face-value fire insurance policies and fire insurance policies sold to multinational corporations. The target date for total liberalization is January 2008, but the liberalization date for an individual insurance firm can be advanced if it has a good credit reputation and its capital adequacy ratio reaches 300 percent.

Taiwan adopted a transparent approval procedure for insurance policies in January 2001. Prior approval is not required for products whose policy clauses are identical or very similar to existing products of other companies. New products are subject to prior approval. Taiwan's Insurance Bureau adopted a negative list system in January 2005. Under the new system, new products subject to prior approval will be deeply cut, down from 50 percent to 25 to 30 percent for life insurance and to 10 to 20 percent for non-life insurance. The processing time will be cut from 90 days to 75 days for life insurance and 60 days for non-life insurance. Taiwan's Department of Insurance (DOI) has allowed market access for Taiwan's reinsurance market, and the Central Reinsurance Corporation Statute was revoked in June 2004. The Central Reinsurance Corporation, the only reinsurance firm in Taiwan, was privatized in July 2002. In August 2002, the DOI lowered the capital requirement for entering the reinsurance market. In response to the liberalization, the Swiss Reinsurance Co. became the first foreign reinsurance firm to set up a branch in Taiwan in early 2004.

Telecommunications Services

Following the issuance of licenses to three fixed-line telecommunications service providers in 2000, the Directorate General of Telecommunications (DGT) again opened applications for integrated network licenses in September 2004. The capital requirement for integrated network services was reduced to NT$16 billion from NT$40 billion and system capacity requirements were lowered from one million to 400,000 subscribers' lines. However, during the September 2004 open season, there were no bidders for licenses to provide integrated network services. DGT also announced that it would allow licensing of services in March and September each year. According to DGT's plan, local, long-distance and international call businesses will be added to the licensing schedule under less restrictive conditions in March 2005. A new formula based on local population will be used to calculate the capital requirements for each of the new service licenses; for instance, NT$1.2 billion may be required for a local call license in Taipei City and NT$2 billion for long-distance and international service licenses. While an improvement, these requirements do not appear justified by any objective criteria.

Existing fixed-line operators still face serious difficulties in negotiating reasonable interconnection arrangements at technically feasible points in the network of the dominant carrier, Chunghwa Telecom (CHT). Despite its announcement in May 2004 to share the local loop with the three private providers, CHT set two limitations; non-CHT service providers access to CHT's local loop can only be initiated by end users and only voice service in three metropolitan areas is open to non-CHT operators. Taiwan's Premier announced in November 2003 that the government would invest a total of NT$35 billion in the next five years to help local governments resolve "last mile" problems for telecommunications end-users. This plan, part of a number of telecommunications-related investment proposals called "Mobile Taiwan," will also include the construction of a second broadband network around Taiwan to be jointly used by telecommunications service companies. These new investment projects are expected to help break the monopoly of the telecommunications network by government-owned CHT. Taiwan's telecommunications regulatory body, DGT, and the state-owned former monopoly, CHT, are under the purview of the Ministry of Transportation and Communications, creating a potential conflict of interest. DGT lacks the full authority, independence, and resources to effectively resolve telecommunications-related disputes. Two draft laws, Communications and Broadcasting Basic Law and the statute for the organization of the proposed Cabinet-level National Communications and Broadcasting Commission (NCC), have been introduced by the Cabinet. The Basic Law was passed in December 2003 and the reorganizing statute is currently pending in the legislative process. The NCC will be an independent regulatory body that will unify regulatory authority now split between DGT for wired or wireless communications and the Government Information Office for radio and television broadcasting.

Taiwan's telecommunications market is transforming. In June 2003 the DGT announced regulations governing equal access service, allowing Type I subscribers to select the long distance and international network service of other providers. In August 2003 the DGT amended regulations to open Taiwan's mobile virtual network operator (MVNO) market and began licensing in September 2003. The MVNO market opening offers an alternative third-generation (3G) wireless service to local consumers and allows service providers to operate without a 3G license by partnering with existing 3G operators. Cellular carriers KG Telecom and Far EasTone merged in October 2003. The merger has created a mobile service market equally divided between FarEasTone, CHT and Taiwan Cellular. In November 2003 the DGT announced the regulations governing number portability service, enabling subscribers to retain their existing telephone numbers when switching from their original Type I enterprise to another Type I enterprise engaging in the same business. Actual implementation of the number portability service is likely to be postponed from January to December 2005 due to delays in completing a central database.

In November 2004 DGT began to solicit comments for a proposal to facilitate development in the voice over Internet protocol (VoIP) services. DGT plans to adopt a numbering plan and help safeguard the interconnectivity between VoIP providers and fixed-line operators as given by the Telecom Act, but has not finalized decisions regarding the interconnectivity between VoIP providers. A legislative amendment to the Telecom Act would be required for compulsory interconnectivity between VoIP providers. The United States continues to monitor Taiwan's progress in the telecommunications sector.

INVESTMENT BARRIERS

Taiwan continues to relax investment restrictions in a host of areas, but foreign investment remains prohibited in a handful of industries such as agriculture, wireless broadcasting, oil exploration of Taiwan's coastal area, public utilities, and postal services. Foreign investors in the telecommunications sector are subject to a 60 percent ownership limit, with the limit on direct foreign investment raised from 20 percent to 49 percent in 2002. In February 2003, Taiwan lifted its ban on foreign investment in liquor production, although prior approval is required. Similarly, in January 2004, foreign investment restrictions on cigarette production were removed, although prior approval is required. The 50 percent foreign ownership limit on air cargo forwarders and air cargo terminals was eliminated when Taiwan became a WTO member. The limit on foreign ownership of power plants has been removed, while foreign investment in electricity transmission and distribution remains subject to a 50 percent ownership limit and approval by the Executive Yuan. In October 2003, Taiwan set a foreign ownership limit of 49 percent on high-speed railway transportation.

ANTICOMPETITIVE PRACTICES

In the cable TV market, U.S. program providers contend that the island's two dominant multi-system operators (MSOs) frequently collude to inhibit fair competition. Control by the two MSOs of upstream program distribution deterred U.S. program providers from negotiating reasonable program fees. In December 2003, Taiwan's legislature passed a new broadcasting law combining the Radio and Television Broadcasting Law, the Cable Television Broadcasting Law, and the Satellite Television Broadcasting Law. Following passage of the law, Taiwan officials are working to eliminate political interference in the television broadcasting industry by monitoring public releases of state-owned and party-owned stocks.

ELECTRONIC COMMERCE

Taiwan's approach to electronic commerce and related issues is still evolving. A law protecting personal on-line data was approved in 2001. The Electronic Signature Law, passed by the Legislative Yuan in late October 2001, adopts the principles of the United Nations Commission on International Trade Law's Model Law on Electronic Commerce and recognizes the legal validity of electronic contracts, records, and signatures. Still under discussion is a proposal to assess duties for software sold and downloaded over the Internet. If implemented, such a policy would appear to run counter to the Doha Declaration that WTO Members would maintain their current practice of not imposing customs duties on electronic transmissions. Taiwan has refused to join the United States at APEC in advocating for a permanent moratorium on taxation of Internet transactions.

THAILAND

TRADE SUMMARY

The U.S. trade deficit with Thailand was $11.2 billion in 2004, an increase of $1.9 billion from $9.3 billion in 2003. U.S. goods exports in 2004 were $6.4 billion, up 9.0 percent from the previous year. Corresponding U.S. imports from Thailand were $17.6 billion, up 15.8 percent. Thailand is currently the 23rd largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Thailand were $1.1 billion in 2003 (latest data available), and U.S. imports were $739 million. Sales of services in Thailand by majority U.S.-owned affiliates were $2.2 billion in 2002 (latest data available).

The stock of U.S. foreign direct investment (FDI) in Thailand in 2003 was $7.4 billion, down from $7.6 billion in 2002. U.S. FDI in Thailand is concentrated largely in the manufacturing and mining sectors.

FREE TRADE AGREEMENT (FTA) NEGOTIATIONS

The U.S. government began FTA negotiations with Thailand in June 2004, and has so far conducted two rounds of discussions. Having concluded an FTA with Singapore in May 2003, the United States is seeking to advance President Bush's Enterprise for ASEAN Initiative (EAI), an initiative aimed at enhancing U.S. relations with ASEAN countries. The United States has numerous concerns about Thailand's trade and investment regime, which it hopes to address through these FTA negotiations. These include high tariffs and non-tariff barriers on both industrial and agricultural goods; restrictions on access to the services market; deficiencies in Thailand's intellectual property rights and customs regimes; and other issues.

IMPORT POLICIES

Thailand's high tariff structure remains a major impediment to market access in many sectors. The country's average applied MFN tariff rate is 12.74 percent. The highest tariff rates apply to imports competing with locally produced goods, including agricultural products, autos and auto parts, alcoholic beverages, fabrics, paper and paperboard products, restaurant equipment, and some electrical appliances.

In some cases, tariffs on unfinished and intermediate products are higher than on related finished products. In the aftermath of the 1997-98 financial crisis, the Thai government increased duties, surcharges, and excise taxes on a range of "luxury" imports, including wine, passenger cars, and wool carpets. Some tariff increases have corresponded with implementation of trade liberalization measures; for example, tariffs on completely knocked down (CKD) auto kits increased from 20 percent to 33 percent (but reduced to 30 percent in December 2003) when local content requirements were eliminated in the automotive industry in December 1999. Thailand also imposes a 60 percent duty on motorcycles. When import duties, excise taxes, and other surcharges are calculated, the price of a motorcycle in Thailand is close to double its selling price in the United States. Thailand also does not permit the importation of bulk spirits at bottle strength for local bottling, thus limiting the access of imported spirits to the market.

The Thai government is behind in its schedule to implement its WTO and ASEAN Free Trade Area (AFTA) tariff reduction commitments and rationalizing its complicated tariff regime, which currently has 46 rates. Nonetheless, it continues to lower selected import duties in line with WTO and AFTA commitments, and, as of October 2003, had reduced tariffs on 1,108 items, mostly on raw materials and inputs not produced locally. In September 2003, the Thai government announced tariff reductions on 1,391 items and has gradually phased in these cuts throughout 2004. In January 2005, the Thai government announced tariff reductions on industrial petrochemical products for 100 items from the existing average tariff rates of 20-30 percent to 0-5 percent within 3 years. In addition, the Thai government plans to reduce tariffs on raw and semi-raw materials to 0, 1, 5, and 10 percent by 2007. However, a timeline for tariff reductions on 879 finished product items -- mostly agricultural products – has not yet been set.

Taxation

Thailand's tax administration generally is complicated and non-transparent. Excise taxes are high on some items, such as unleaded gasoline, beer, wine, and distilled spirits. When import duties, excise taxes, and other surcharges are calculated, the cumulative tax burden on most imported whiskey is approximately 169 percent. In March 1999, as part of an economic stimulus package, the value-added tax (VAT) was temporarily reduced from 10 percent to 7 percent and the excise tax on fuel oil was reduced from 17.5 percent to 5 percent. The Thai government is scheduled to restore the VAT to 10 percent on October 1, 2005, but it has scheduled and annulled the VAT restoration three times since 2001.

Agriculture and Food Products

High duties on agriculture and food products and arbitrary management of import licenses and application of sanitary and phytosanitary (SPS) measures (see section below on Standards, Testing, Labeling, and Certification) remain the primary impediments to U.S. exports of high-value fresh and processed foods. Under its WTO Uruguay Round agriculture obligations, Thailand committed to reduce its import duties, but agriculture is scheduled to be among the last sectors rationalized under the Thai government's plan.

Duties on imported consumer-ready food products typically range between 30 percent and 50 percent – the highest in the ASEAN region – with some as high as 90 percent (e.g., coffee). Tariffs on meats, fresh fruits (including citrus fruit and table grapes) and vegetables, fresh cheese and pulses (*e.g.*, dry peas, lentils, and chickpeas) are similarly high, even for products for which there is little domestic production. Frozen french fries, for example, are not produced in Thailand, yet face a tariff of 30 percent. When import duties, excise taxes, and other surcharges are calculated, imported wines face a total tax of nearly 400 percent. The excise tax on wine (made of grapes) is 60 percent of value or 100 baht per liter of pure alcohol, whichever is higher. Fermented spirits made from fruits other than grapes, *e.g.*, mangosteen, are subject to an excise tax of 25 percent of value or 70 baht per liter of pure alcohol, whichever is higher.

With the exception of wine and spirits, Thailand no longer applies "specific" duties for most agricultural and food products, and *ad valorem* rates are declining in accordance with Thailand's WTO commitments. Nevertheless, import duties on some agricultural and processed food goods have an average tariff rate of 25.4 percent. Moreover, bound duties on many high-value fresh and processed food products will remain high, from 30 to 40 percent, even after reductions under WTO commitments. Tariffs on apples are at 10 percent, while duties on pears and cherries remain as high as 60 percent. U.S. fruit growers estimate lost sales of up to $25 million annually from the combined effect of Thailand's high tariffs, surcharges, and a customs reference price system that often disregards the declared transaction price of these products (see "Customs Barriers" section below).

Thailand's overall import policy is directed at protecting domestic producers, and the government has implemented non-transparent price controls on some products and maintains significant quantitative restrictions that impede market access. The United States is concerned that access to tariff-rate quotas for agricultural products is often managed in an arbitrary and non-transparent manner. Although Thailand has been relatively open to imports of feed ingredients, including corn, soybeans, and soymeal, in recent years, the Thai government has issued new and burdensome requirements associated with the issuance of import permits for feed ingredients. For example, corn imports enjoy liberalized tariff rates, but the benefit of this tariff reduction has been offset by a Thai government requirement that corn imports arrive between March and June, a seasonal limitation not provided for in Thailand's WTO schedule. This requirement places U.S. suppliers at a disadvantage, and gives most of the market to corn from the southern hemisphere. Corn is also subject to a tariff-rate quota (TRQ); in 2003, in-quota corn imports (54,440 mt) will be subject to a 20 percent tariff rate, while out-of-quota corn imports are subject to a 73.8 percent tariff. There are unlimited import quotas for soybeans, for which the import duty is five percent. However, Thailand requires that importers purchase a certain amount of domestically-produced product before being granted licenses for imported products, a requirement inconsistent with WTO obligations. Importers of skim milk powder report that import quota allocations are often released late, which sometimes causes interruptions in trade flows.

In addition, the Thai government requires import license fees for meat products of approximately $114 per ton on beef and pork, $227 per ton for poultry, and $114 per ton on offal that do not appear to reflect the costs of import administration. SPS standards for certain agricultural products also often appear to be applied arbitrarily and without prior notification. The Thai government began inspections of meat plants in supplier countries in January 2003, but has delayed implementation in some countries, including the United States.

U.S. agricultural exports, including fish and forestry products, to Thailand, which dropped dramatically in the aftermath of the 1997 financial crisis to $440 million in 1998, have recovered and reached $751 million in 2003. According to U.S. industry estimates, potential exports to Thailand could reach as much as $1.2 billion annually if Thailand's tariffs and other trade-distorting measures are substantially reduced or eliminated and the economy recovers to pre-crisis levels.

Automotive Sector

Thailand’s import duties and taxes are among the highest in ASEAN. In response to the financial crisis, the Thai government in October 1997 raised tariffs on Completely Built Up (CBU) passenger cars and sport utility vehicles to 80 percent, up from 42 percent and 68 percent, respectively. Current tariff rates on parts and components range from 10 percent to 30 percent. However, tariffs on CBU pick-up trucks have been reduced from 60 to 40 percent.

Excise taxes in Thailand are based on engine displacement. In July 2004, Thailand revised its excise tax structure and simplified the previous system. Thailand's taxes on passenger vehicles range from 30 percent to 50 percent, while pickup trucks are taxed at a rate of 3 percent.

Customs valuation issues have been particularly acute in the auto sector (see "Customs Barriers" section below).

Textiles

Thailand's tariff rates for U.S. textile exports are high, ranging from 20 percent to 30 percent for most fabrics and 30 percent for most clothing and other made-up textile products. In addition, Thailand applies specific unit duties on more than one-third of all textile tariff lines, which make effective rates even higher. Thailand's current applied tariffs on some clothing products, as published on the APEC Website, are listed as 60 percent or more depending on whether a specific unit duty is applied.

Quantitative Restrictions and Import Licensing

Thailand is still in the process of changing its import licensing procedures to comply with its WTO obligations. Import licenses are required for at least 26 categories of items, including many raw materials, petroleum, industrial materials, textiles, pharmaceuticals, and agricultural items.

Imports of used motorcycles and parts and gaming machines are prohibited. Imports of other products must meet burdensome regulatory requirements, including extra fees and certificate-of-origin requirements. Thailand does not have specific measures of general application relating to non-preferential rules of origin.

Imports of food, pharmaceuticals, certain minerals, arms and ammunition, and art objects require special permits from relevant ministries. Thailand requires that detailed and often proprietary business information about the manufacturing process and composition of food be provided in applications for food product registration.

Customs Barriers

Thailand continued to take steps to improve its customs practices in 2004, building on discussions held under the U.S.-Thai Trade and Investment Framework Agreement (TIFA). While the international business community maintains that some positive customs policy changes are slow in filtering down through the bureaucracy, most acknowledge the progress to date and recognize that the Thai government is committed to improving its customs procedures and facilitating trade.

In 2003, as part of its effort to improve the transparency and efficiency of customs procedures, Thailand implemented a *de minimis* threshold, exempting goods valued at 1,000 baht or less from formal entry procedures and has increased the low-value informal clearance threshold to 40,000 baht (USD 1000) from 20,000 baht (USD 500). Thailand also has taken action to expand customs clearance working hours, to increase the use of electronic and paperless customs procedures, and to create an English-language version of the Customs Department website.

The Thai government needs to make further progress to enhance the transparency and efficiency of its customs regime. In July 2003, Thailand formally notified the WTO of legislation passed in 2000 implementing the WTO Customs Valuation Agreement. Meanwhile, Thailand has drafted, but not yet submitted to Parliament, legislation limiting the discretion of the Customs Director General to arbitrarily increase the customs value of imports (though in practice, the Director General has not made use of that discretion). Some industry representatives continue to report inconsistent application of the WTO transaction valuation methodology and repeated use of arbitrary values.

Industry representatives have also continued to report practices by Thai Customs that raise concerns regarding Thailand’s implementation of its obligations under the WTO Information Technology Agreement, including software products. In addition, as is the case with some Thai agencies, Customs has an incentives program rewarding officials for identifying violators based on a percentage of the recovered revenues. This practice encourages revenue maximization rather than compliance with legal requirements. Although Thailand has taken steps to streamline its customs appeals procedures, some businesses contend that the process is still too lengthy and not yet fully transparent. Corruption in the Customs Department reportedly remains a serious problem.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Thailand's Food and Drug Administration (TFDA) imposes standards, testing, and labeling requirements, and requires certification permits for the importation of all food and pharmaceutical products, as well as certain medical devices. Many U.S. companies consider the cost, duration, and complexity of the permitting processes to be overly burdensome and are concerned about the periodic demands for disclosure of proprietary information. TFDA has streamlined its procedures somewhat, but U.S. companies still report delays of up to a year. All processed foods must be accompanied by a detailed list of ingredients and a manufacturing process description, disclosure of which could potentially jeopardize an applicant's trade secrets. A labeling regime for genetically modified foods, modeled on the Japanese system, was put into effect in May 2003. The TFDA has introduced new regulations on food safety testing, known as Ministerial Decree 11, requiring that many imported food products undergo testing and certification for a number of chemical additives. U.S. food exporters report that these new rules are burdensome and unclear, and no risk assessment substantiating the need for this testing has been provided. Implementation of Decree 11 has been delayed until April 1, 2005, to allow consideration of U.S. and other countries' comments regarding these new rules.

The Thailand Industrial Standards Institute (TISI) is the national standards organization under the Ministry of Industry. TISI is empowered to provide product certifications according to established Thai standards and is an accredited body for ISO and HACCP certifications in Thailand. The Thai government requires the certification of 60 products in ten sectors, including agriculture, construction materials, consumer goods, electrical appliances and accessories, PVC pipe, medical equipment, LPG gas containers, surface coatings, and vehicles.

U.S. private sector representatives have raised concerns about a number of measures proposed or implemented as a result of TISI's actions. These measures include a technical regulation proposed by TISI on radio disturbance limits for personal computers and another technical regulation issued by TISI requiring all uninterruptible power systems to meet certain testing standards. U.S. industry also has reported that lengthy product approval requirements imposed under another technical regulation issued by TISI significantly delay the introduction of new products to the Thai market.

Thailand bars large-displacement motorcycle traffic from its tollways, including large motorcycles that are engineered to be ridden safely at highway speeds. In 2000, Thailand adopted motorcycle emissions regulations that are an amalgamation of standards and tests used elsewhere in the world, resulting in standards that reportedly are among the most stringent in the world. U.S. industry contends that enforcement of these standards has been non-transparent and that even producers utilizing the advanced low-emission technology have difficulty meeting these standards.

GOVERNMENT PROCUREMENT

Thailand is not a signatory to the WTO Agreement on Government Procurement, although in the past, Thai officials have indicated support for a WTO Agreement on Transparency in Government Procurement. A specific set of rules, commonly referred to as the Prime Minister's Procurement Regulations, governs public-sector procurement for ministries and state-owned enterprises. While these regulations require that nondiscriminatory treatment and open competition be accorded to all potential bidders, different state enterprises typically have their own individual procurement policies and practices. Preferential treatment is provided to domestic suppliers (including subsidiaries of U.S. firms registered as Thai companies), which receive an automatic 15-percent price advantage over foreign bidders in initial bid round evaluations.

A "Buy Thai" directive from the Prime Minister's office issued in 2001 has raised additional concerns about the Thai government procurement policies. Reversing a long-standing non-discriminatory government procurement policy, "Buy Thai" impeded market access of foreign suppliers in selected sectors during 2001-02, notably personal computers. While Thailand officially denies that the "Buy Thai" policy discriminates against foreign producers, specific language used in government instructions on some procurement tenders explicitly excludes foreign-made, non-Thai products from the bidding process.

A procuring government agency or state enterprise reserves the right to accept or reject any or all bids at any time and may also modify the technical requirements during the bidding process. The latter provision allows considerable leeway to government agencies and state-owned enterprises in managing tenders, while denying bidders any recourse to challenge procedures. Allegations that changes are made for special considerations frequently surface, including charges of bias on major procurements. Despite the official commitment to transparency in government procurement, U.S. companies and Thai media regularly report allegations of irregularities. Private sector representatives have expressed concern regarding a Thai government decision to no longer include arbitration clauses in concessions and government contracts.

Regulations promulgated in May 2000 formalized a Thai government practice requiring a counter trade transaction on government procurement contracts valued at more than 300 million baht, on a case-by-case basis. A counter-purchase of Thai commodities valued at not less than 50 percent of the value of the principal contract may be required. As part of a counter-trade deal, the Thai government also may specify markets into which commodities may not be sold; these are usually markets where Thai commodities already enjoy significant access. From 1994 through November 2004, 265 counter-trade agreements were signed, resulting in exports valued at 60 billion baht.

EXPORT SUBSIDIES

Thailand maintains programs to support trade in certain manufactured products and processed agricultural products, which may constitute export subsidies. These include various tax benefits, import duty reductions, credit at below-market rates on some government-to-government sales of Thai rice (established on a case-by-case basis), and preferential financing for exporters. The Thai government terminated its packing credit program in compliance with WTO commitments but received an extension of its WTO exemption period for the Industrial Estate Authority of Thailand and the Board of Investment until December 2005. Low interest loans provided under the Export Market Diversification Promotion Program for exporters targeting new markets ended in December 2003.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Widespread commercial IPR counterfeiting and piracy continue at high levels, despite the promise that accompanied the restructuring of IPR enforcement agencies. U.S. copyright industries reported an estimated annual trade loss of more than $166 million in 2003 from IPR infringement in Thailand. An increasing volume of pirated and counterfeited products manufactured in Thailand are exported. Thailand has been on the U.S. Special 301 Watch List since November 1994.

The United States and Thailand held extensive consultations on IPR issues under the TIFA. In June 2003, the United States provided Thailand with a proposed IPR Action Plan. This plan included detailed proposals for action to be taken on enforcement, legislative/regulatory, and judicial issues. Key among these were : (1) revisions to the optical disk legislation then pending before Parliament and expeditious passage of this legislation; (2) a clear improvement in Thailand's IPR enforcement record through sustained, aggressive, and coordinated enforcement efforts; and (3) improvements in the draft Copyright Act amendments under consideration and passage of these amendments. After the FTA negotiations were underway, Thailand enacted optical disk legislation that lacked many key elements, and U.S. officials continue to press Thailand to address these deficiencies. The Copyright Act amendments have not been enacted and lack of sustained, aggressive, and coordinated enforcement remains a substantial problem.

The implementing regulations for the Trade Secrets Act, which was passed in March 2002, have yet to be drafted and implemented. The Thai Food and Drug Administration (FDA) and Department of Agriculture are drafting regulations to implement the Act, and public comments have been solicited. However, the FDA has put drafting efforts on hold to wait for the outcome of the bilateral FTA negotiations.

The latest available draft of the Trade Secrets Act allows a government agency to disclose trade secrets to protect any "public interest" not having a commercial interest, provided the agency takes "regular measures to protect such trade secrets from unfair commercial use." The U.S.

government has raised concerns that this language would provide authorities with overly broad authority that could deny the protection of approval-related data against unfair commercial use.

A further piece of legislation related to the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), the Geographic Indications Act, was passed by the Thai Parliament in September 2003 and went into effect in April 2004.

Private sector representatives have expressed concern about the implementation and enforcement of the Plant Variety Protection Act, noting the wide availability of pirated or counterfeit seeds and other products in Thailand.

Thailand's IPR enforcement efforts have been inconsistent. Although conviction rates are high, corruption and a cultural climate of leniency can complicate prosecution of cases. The frequency of raids compromised by leaks from police sources remains a concern. Pirates, including those associated with transnational crime syndicates, have responded to stepped-up levels of enforcement with intimidation against rights holders' representatives and enforcement authorities. In 2003, the Ministry of Commerce took the lead in promoting interagency cooperation on IPR enforcement issues, concluding two Memorandums of Understanding between enforcement agencies (Thai police and the Thai Customs Department) and rights holders to better coordinate operations. While these agreements prompted improved retail enforcement leading up to and during the October 2003 APEC Leaders Meeting in Bangkok, retail piracy returned soon thereafter. Despite several attempts throughout 2004, including a new MOU signed in June, the Thai government has yet to successfully sustain enforcement actions against retailers, distributors, and manufacturers of pirated and counterfeit goods.

The Thai Parliament passed legislation in the fall of 2003 to fully authorize the establishment of the Department of Special Investigations (DSI). In its work on IPR enforcement, DSI is expected to focus on major infringing production, warehousing and trafficking operations, as well as those activities associated with organized crime. However, DSI is not yet adequately staffed to carry out these responsibilities. In December 2003, the Thai Cabinet approved in principle draft amendments to the Anti-Money Laundering Act, one of which makes IPR crimes a predicate offense. This amendment would allow police and other law enforcement officials to seize and investigate funds and suspected bank accounts. However, in July 2004, the Council of State, which reviews pending legislation, rejected the inclusion of IPR crimes as a predicate offense, citing concerns that IPR violations are "commercial disputes."

The Thai government established a specialized intellectual property court in 1997, which has improved judicial procedures and imposed tougher penalties. Criminal cases generally are disposed of within 6 to 12 months from the time of a raid to the rendering of a conviction. However, Thai officials generally lack sufficient resources to undertake enforcement actions apart from those initiated by rights holders. Effective prosecutions can be labor-intensive for rights holders, who often investigate, participate in raids, and assist in the preparation of documentation for prosecution.

Patents

Amendments to Thailand's patent regime designed to meet TRIPS obligations entered into effect in September 1999. Thailand's patent office, however, lacks sufficient resources to keep up with the volume of applications, and patent examinations can take more than five years. The Department of Intellectual Property is seeking to contract out some parts of patent search for novelty and preparation of application to academic institutions in order to speed up the registration process. The availability of counterfeit pharmaceutical products in Thailand also is a growing concern.

Copyrights

Thailand's copyright law, intended to bring Thailand into conformity with international standards under TRIPS and the Berne Convention, became effective in March 1995. Despite efforts by Thai police at the retail, distribution, and production levels and by corporate end users, piracy remains a serious concern. The copyright law is ambiguous regarding decompilation, and regulations for enforcement procedures leave loopholes that frustrate effective enforcement.

The Thai government is in the process of amending the Copyright Law in order to bring it in line with two 1996 World Intellectual Property Organization (WIPO) treaties, the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty. These treaties, commonly known as the WIPO Internet treaties, entered into force in 2002. The draft amendments to the Copyright Law have been approved by the Cabinet, but further changes are expected to result from the ongoing FTA negotiations.

Cable piracy continues to be a major problem throughout Thailand, as pirate providers expand their reach in the provinces. In December 2003, the Thai government initiated a new policy offering amnesty to operators who agree to cease infringing actions under threat of legal action. This policy is intended as a temporary measure pending the establishment of the National Broadcasting Commission and new regulations for cable operators. Since December 2003, the Thai government, however, has missed several deadlines to initiate enforcement operations.

U.S. copyright industries continue to express serious concerns over the rapid and unchecked growth of optical media piracy in Thailand. In October 2004, the Thai Parliament passed the Optical Disk Manufacturing Control bill, in the drafting stage since 1999. This legislation is designed to enhance the authority and capabilities of the Thai government to act against operators of illicit optical disk factories and to control the production materials and machines of legal producers. U.S. copyright industries are concerned that the Optical Disk legislation is deficient in several respects, including that penalties are not high enough to deter pirates and do not enhance the government's enforcement and oversight powers sufficiently. The

Constitutional Court has been asked to review certain provisions of this new legislation, delaying implementation into 2005.

Book publishers are concerned that the existing copyright law is being interpreted in a manner that is allowing extensive book piracy, especially in the form of illegal photocopying, to go unchecked. According to industry group AAP, annual losses are estimated to be approximately $30 million.

Trademarks

The Thai government amended its trademark law in 1992, increasing penalties for infringement and extending protection to service, certification, and collective marks. The Thai government also streamlined trademark application procedures, addressing issues raised by the U.S. government in the 1998 IPR action plan. Additional amendments designed to bring Thailand's trademark law into compliance with the TRIPS Agreement were enacted in June 2000, broadening the legal definition of a mark. While these developments have created a viable legal framework and have led to some improvements in enforcement, especially for clothing, accessories, and plush toys, trademark infringement remains a serious problem. U.S. companies with an established presence in Thailand and a record of sustained cooperation with Thai law enforcement officials have had some success in defending trademarks, but the process remains time-consuming and costly. Penalties for proven trademark violations are insufficiently high to have a deterrent effect.

SERVICES BARRIERS

Telecommunications Services

Slow-moving bureaucratic reform of the Thai telecommunications legal regime is a significant obstacle to investment in the Thai telecommunications sector. The seven-member National Telecommunications Commission (NTC), the independent industry regulator mandated by the 1997 constitution as responsible for licensing, spectrum management, and supervision of telecommunications operators, was chosen by the Thai Senate in August 2004 after several years of delay. The King of Thailand officially appointed the Commission on October 1, 2004, and its secretariat was formed from the former Post and Telegraph Department (PTD) on November 1, 2004. Controversial issues such as licensing, interconnection, competition, tariff rebalancing, and standards-making still remain unresolved, and licenses for new Internet Service Providers (ISPs) and many value-added services have yet to be issued. Commissioners expect that they will spend their first year setting up the commissions' administrative procedures and prioritizing the NTC agenda.

The Thai government has allowed foreign participation in the telecommunications sector since 1989, but state-owned enterprises continue to control the market. While Thailand committed under the WTO to fully liberalize its telecommunications sector by January 2006, regulatory delays will make this deadline difficult to meet.

In November 2001 Thailand enacted a Telecommunications Business Law that lowered the permitted percentage of foreign ownership in telecommunication companies from 49 percent to 25 percent. However, the Thaksin Administration publicly stated its intention in 2002 to amend the Telecommunications Business Law to return the foreign ownership limit to 49 percent. Legislation has been introduced to the Parliament to achieve this goal, but has not yet been passed.

In 2002, the Thai government established the Ministry of Information and Communication Technology (MICT) to oversee the telecommunications sector. Under the Ministry's purview, among other issues, are corporatization and privatization of the Telephone Organization of Thailand (TOT) and Communications Authority of Thailand (CAT), and implementing an interconnection regime. Concession conversion, once spearheaded by MICT, has been left to CAT and TOT to negotiate with their individual concession holders, with little progress. Although the formation of the ministry should serve to advance telecommunications industries in the future, progress in the near term rests with the newly formed NTC.

In July 2002, TOT, a former state-owned telecommunications monopoly, was finally corporatized (shares still owned by the state were issued) as a precursor to privatization as part of the Telecommunication Development Master Plan and the Corporatization Act 1999. The Cabinet approved the corporatization of the CAT on July 8, 2003 in accordance with the same plan. The CAT was separated and corporatized into two distinct business entities, the CAT Telecom Public Company Limited and the Thailand Post Company Limited. The planned privatization of TOT has been repeatedly delayed due to poor market conditions for the sale of TOT shares, and the privatization of CAT is not expected until after the completion of TOT privatization. Meanwhile, Prime Minister Thaksin has stated a desire for TOT and CAT to merge before privatization. Moreover, further challenges to privatization remain. Concession contracts granted to private telecommunications operators by the former state-owned monopolies for terms of 20 to 30 years will have to be addressed. Resolution of this issue has proven very difficult; at least two previous plans were withdrawn following public opposition.

The 1997 Thai Constitution and the Frequency Management Act of 2000 also required the establishment of an independent regulatory body for the broadcast sector, known as the National Broadcasting Commission (NBC). The NBC will be responsible for regulating radio and television broadcast businesses. The NBC has not yet been formed due to political disagreements over the composition of the commission. Foreign ownership in terrestrial broadcast networks is currently prohibited.

The Thailand Post Company, Ltd. is a state enterprise that has been corporatized. The Postal Committee, which is under the Ministry of Information and Communication Technology, is the regulator of postal services in Thailand. The provisions of the Postal Act B.E. 2477 (1934) cover basic postal (letters and postcards) and personal information. Any enterprises providing express delivery services not related to personal information as provided by the Act (such as parcel post) fall outside the purview of the Postal Committee.

Legal Services

Current Thai law prohibits foreign equity participation in Thai law firms in excess of 49 percent, and foreign nationals are prohibited from practicing law in Thailand. However, under the U.S.-Thailand Treaty of Amity and Economic Relations (AER Treaty), U.S. investments are exempted from the general restriction on foreign equity participation in law firms. U.S. investors may own law firms in Thailand; however, U.S. citizens and other foreign nationals (with the exception of "grandfathered" non-citizens) may not provide legal services. In certain circumstances, foreign attorneys may act in a consultative capacity.

Financial Services

After the 1997-98 financial crisis, the Thai government liberalized foreign firms' access to the financial sector. Significant restrictions remain on foreign participation in the sector, however. While aliens have been allowed to engage in brokerage services since 1997, for example, foreign firms are allowed to own shares greater than 49 percent of Thai securities firms only on a case-by-case basis.

Foreigners are permitted to hold a maximum of 25 percent of the equity in Thai banks. Within the "Financial Sector Master Plan" drafted by the Bank of Thailand and approved by parliament, this percentage may be increased to 49 percent at such time as the Central Bank deems appropriate. The Master Plan requires all Thai deposit-taking institutions to become either a retail or commercial bank with differing Tier I minimum capital requirements. The Bank of Thailand has indicated that no new banking licenses will be issued until "economic conditions" permit greater competition in the Thai banking market.

Foreign banks currently operating in Thailand are disadvantaged in their ability to compete. Most notably, they are limited to one branch, and are not permitted to operate off-site ATM machines, which are considered as branches. Foreign banks must maintain minimum capital funds of 125 million baht ($3.1 million) invested in government or state-enterprise securities or deposited directly with the Bank of Thailand. Expatriate management personnel are limited to six professionals in full branches and to two professionals in Bangkok International Banking Facility operations, although exceptions are often granted.

Charged with helping to restructure the financial sectors' non-performing loans, the government-owned Thai Asset Management Corporation (TAMC) gives priority to Thai nationals when contracting for management, technical, and advisory services. Foreigners may be hired, however, in the absence of qualified Thai nationals.

Construction, Architecture, and Engineering

Foreigners are prohibited from working as engineers or architects, but in practice, they can work as consultants in these fields. Construction firms must also be registered in Thailand (*i.e.*, establish a commercial presence). Under the U.S.-Thailand AER Treaty, American firms may establish companies in Thailand that provide construction, architectural, and engineering services. The Thai government regulates the billing rates of foreign construction, architectural, and engineering firms. Current practice places a ceiling on billing for these services by foreign firms.

Accounting Services

Foreigners cannot be licensed as Certified Public Accountants and therefore cannot practice accounting in Thailand. Foreign accountants may only serve as business consultants.

Express Delivery Services

The 49-percent limit on foreign ownership in land transport (trucking) hampers investment in and growth of express delivery services. Express delivery firms prefer to have the option of control of items throughout the supply of the service, including both air and ground-based operations in order to speed the movement of goods.

Healthcare Services

Thai government policy is highly restrictive in the healthcare services sector (*e.g.*, hospital, dental, physician services), particularly regarding the lack of transparency relating to hospitals and possibility of foreign ownership, administration, and equity shares in treatment facilities. Thailand has offered no medical services commitment in the current General Agreement on Trade in Services (GATS) negotiations.

Retail Services

Thailand does not have specific legislation that deals directly with retail services. However, other laws, such as the 1975 Town Planning Act and the Trade Competition Act of 1999, include provisions relating to retail services. The Town Planning Department has implemented a regulation on zoning to curb the expansion of large stores in congested areas. The Trade Competition Act established a Trade Competition Commission with the authority to place limitations on market share and revenues of firms with substantial control of individual market sectors, to block mergers, and other forms of business combinations, and to levy fines for price fixing and other proscribed activities.

Advertising

Thai law prohibits advertising on pay television. Television is the most popular media for advertising. There are no regulations on foreign participation in advertising.

INVESTMENT BARRIERS

The Alien Business Act lays out the overall framework governing foreign investment and employment in Thailand. Although the Act prohibits foreign investment in most sectors, Thailand makes an exception for U.S. investors pursuant to the AER Treaty. Under the AER Treaty, Thailand may discriminate against U.S. investors only in the following sectors: communications, transportation, fiduciary functions, banking involving depository functions, the exploitation of land or other natural resources, and domestic trade in indigenous agricultural products. Moreover, Thailand's obligation to accord national treatment to U.S. investors in all other sectors does not extend to "the practice of professions, or callings reserved for [Thai] nationals."

The Alien Business Act's prohibitions on foreign investment generally do not affect projects established by Board of Investment promotion privileges or export businesses authorized under the Industrial Estate Authority of Thailand law.

Trade-Related Investment Measures

In 1995, pursuant to the WTO Agreement on Trade-Related Investment Measures (TRIMS), Thailand notified the WTO that it would maintain local-content requirements to promote investment in a variety of sectors, including milk and dairy processing, and the motor vehicle assembly and parts industries. Thailand eliminated the measures in the auto sector by the January 1, 2000, deadline established by the TRIMS Agreement. In 2001, along with several other developing countries, Thailand received an extension for its milk and dairy processing measures. It eliminated those measures at the end of 2003.

ELECTRONIC COMMERCE

The Thai government has placed a high priority on the development of electronic commerce and approved an electronic commerce framework in October 2000. However, an undeveloped legal framework and limited Internet penetration constrain development of electronic commerce. A new Electronic Transactions Act entered into force in April 2002, but is awaiting the Thai Cabinet's issuance and approval of a royal decree required to implement this law. The Thai government plans to pass four additional, related bills. A computer crimes bill was approved by the Cabinet in September 2003 and an electronic funds transfer bill, a data protection bill, and the national information infrastructure bill currently are being drafted.

The large role played by the CAT is an obstacle to development of the Internet and electronic commerce. Its mandatory share ownership (CAT, 32 percent; CAT employees, 3 percent) of all licensed Internet Service Providers (ISP) and its monopoly on international telecommunications services impose high costs on online business. Required divestment of its ISP interests has not been implemented. When constituted, the National Telecommunications Commission, which currently is being formed, (see telecommunications services section above) is expected to develop new market rules.

OTHER BARRIERS

Several government firms are protected from foreign competition in Thailand. In the pharmaceutical sector, the Government Pharmaceutical Organization is not subject to requirements faced by the private sector on registration. In addition, it can produce and market generic formulations of drugs marketed in foreign countries irrespective of safety monitoring program protection. Thai government requirements limiting government hospitals' procurement and dispensing of drugs not on the national list of essential drugs (NLED) significantly constrain the availability of many imported products.

The Thai government retains authority to set price ceilings for 20 goods and services, including medicines, sound recordings, milk, sugar, fuel oil, and chemical fertilizer. Price control review mechanisms are non-transparent. Price control determinations are sometimes based on outdated assumptions, including exchange rates, and go for long periods without review, even upon repeated petition for review by affected parties. Only sugar currently is subject to a retail price ceiling. In practice, the Thai government also uses its control of major suppliers of products and services under state monopoly, such as the petroleum, aviation, and telecom sectors, to influence prices in the local market.

The Thai government has made some efforts to counter official corruption. The Thai Constitution of 1997 contains provisions to combat corruption, including enhancement of the status and powers of the Office of the Counter Corruption Commission (OCCC), which is independent from other branches of government. Persons holding high political office and members of their immediate families now are required to disclose their assets and liabilities before assuming and upon leaving office. Moreover, a new law regulating the bidding process for government contracts both clarifies actionable anti-corruption offenses and increases penalties for violations. Nonetheless, counter-corruption mechanisms continue to be employed unevenly. The lack of transparency in administrative procedures also contributes to perceptions of corruption in Thailand. Prescribed comment periods for new legislation and regulations are sometimes not honored, and implementing regulations can be unclear, causing uncertainty among companies about the interpretation of the provisions.

TURKEY

TRADE SUMMARY

The U.S. trade deficit with Turkey was $1.6 billion in 2004, an increase of $686 million from $888 million in 2003. U.S. goods exports in 2004 were $3.4 billion, up 15.9 percent from the previous year. Corresponding U.S. imports from Turkey were $4.9 billion, up 30.3 percent. Turkey is currently the 32nd largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Turkey in 2003 was $2.0 billion, up from $1.9 billion in 2002. U.S. FDI in Turkey is concentrated largely in the wholesale, manufacturing, and banking sectors.

IMPORT POLICIES

Tariffs and Quantitative Restrictions

As a result of its 1996 customs union with the European Union (EU), Turkey applies the EU's common external customs tariff to third-country (including the United States) non-agricultural imports and imposes no duty on non-agricultural items from EU and European Free Trade Association (EFTA) countries.

Turkey maintains high tariff rates (25 percent average Most-Favored-Nation rate) on many food and agricultural products to protect domestic producers. The Turkish government often increases tariffs on grains during the domestic harvest. High feed prices harm Turkish livestock industries, particularly for beef and poultry. Duties on fresh fruits range from 61 percent to 149 percent. Processed fruits, fruit juices and vegetable tariffs range between 41 and 138 percent. The Turkish government also levies high duties as well as excise taxes and other domestic charges on imported alcoholic beverages that increase wholesale prices by more than 200 percent.

Import Licenses and Other Restrictions

While import licenses generally are not required for industrial products, products which need after-sales service (e.g., photocopiers, ADP equipment, and diesel generators) require licenses, as do distilled spirits. We have concerns about the lack of transparency in Turkey's import licensing system, which can result in costly delays, demurrage charges, and other uncertainties that stifle trade for many agricultural products. For the previous four years, the Ministry of Agriculture and Rural Affairs (MARA), through its quarantine service, has stopped issuing import licenses for rice and corn prior to the harvest. After the harvest these restrictions were lifted. However, in 2004 the Turkish government failed to remove the import restrictions on rice that were levied in late 2003, significantly disrupting rice imports. We are also concerned about the restrictive effects of the licensing system, as well as export and consumer subsidies, on Turkey's imports of U.S. sugar. In concert with its unpredictable licensing system, Turkey has also recently implemented import quota programs for rice and corn. Import quotas, often tied to procurement of domestic crops, tend to fluctuate throughout the marketing year, making it very difficult for commercial traders to plan their import programs.

Turkey is in the process of rewriting its import regulations for agriculture products in order to comply with EU regulations. However, some new regulations do not appear to be fully consistent with those of the EU. For many products, no written standards exist, for example, for red meat and wine imports.

Recent changes in Turkish law call for a liberalization of the spirits and tobacco market over a five-year period, which should improve the competitive environment. The Turkish government has privatized the alcohol operations of TEKEL (a parastatal company) and is in the process of privatizing TEKEL's tobacco operations.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The Turkish government has a poor track record of notifying WTO members of proposed technical regulations and phytosanitary requirements, and implementation appears to be arbitrary. Importers report increasing difficulty in obtaining information on sanitary and phytosanitary certifications. The Turkish government often requires laboratory testing on items not normally subject to testing by trading partners, allegedly without any scientific basis.

The government requires laboratory tests and certification that quality standards are met for the importation of foods, human and veterinary drugs, and medical equipment and appliances intended for use by humans.

U.S. CE-marked products, particularly medical devices, are often detained by Turkish customs authorities for inspection. In some cases, U.S. products apparently have been subject to additional tests, despite their CE marks, while EU CE-marked products gain immediate entry to the Turkish market.

Certification of spare parts for automobiles under the Turkish Decree for Standardization in Foreign Trade remains a problem; even though the decree is no longer formally in place, automakers are still subject to several of its provisions.

Turkey has not yet implemented changes in standards for distilled spirits, which currently limit U.S. exports.

GOVERNMENT PROCUREMENT

Turkey is not a signatory of the WTO Government Procurement Agreement. However, it is an observer to the Committee on Government Procurement. Although its laws require competitive bidding procedures for tenders, U.S. companies sometimes become frustrated over lengthy and often complicated bidding and negotiating processes.

In 2003, Turkey implemented a new public tender law that reformed its government procurement system. The new law established an independent board to oversee public tenders, increased the transparency of its procurement procedures, and lowered the minimum bidding threshold at which foreign companies can participate in state tenders. However, the law provides a price preference of up to 15 percent for domestic bidders, which is not applicable to domestic bidders when they form a joint venture with foreign bidders. In 2003, Turkey expanded the definition of domestic bidder to include corporate entities established under Turkish law, including those established by foreign companies.

Military procurement generally includes an offset requirement in the tender specifications. The offset guidelines were recently modified to encourage foreign direct investment and technology transfer.

EXPORT SUBSIDIES

Turkey employs a number of incentives to promote exports, although programs have been scaled back in recent years to comply with EU directives and WTO commitments. Historically, wheat and sugar have been Turkey's main subsidized commodities. Export subsidies, ranging from 10 to 20 percent of export values, are granted to 16 agricultural or processed agricultural products. In 2004, the Turkish Grain Board (TMO) sold domestic wheat to flour and pasta manufacturers based upon their exports of flour and pasta. This is an implicit subsidy as TMO is selling the manufacturers wheat at world prices, which are well below domestic prices. It is too early to quantify the size of this subsidy. The Turkish Export-Import Bank provides exporters with credits, guarantees, and insurance programs. Certain tax credits also are available to exporters.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Turkey's intellectual property rights regime has improved in recent years, but still presents serious problems. Turkey was elevated from the Special 301 Watch List to the Priority Watch List in 2004, due to concerns about lack of pharmaceuticals data exclusivity protection and continued high levels of piracy and counterfeiting of copyright and trademark materials.

Turkey's 2001 copyright law substantially modernized the legal regime, providing deterrent penalties for copyright infringement. However, it does not prohibit circumvention of technical protection measures, a key feature of the World Intellectual Property Organization (WIPO) "Internet" treaties. In addition, the Turkish courts have failed to render deterrent penalties to pirates as provided in the copyright law but have instead applied the Turkish Cinema Law, which has much lower penalties. Legislation enacted in March 2004 contains several strong anti-piracy provisions, including a ban on street sales of all copyright products and authorization for law enforcement authorities to take action without a complaint by the rights holder. However, the law also reduces potential prison sentences in piracy convictions. U.S. industry estimated losses to piracy in 2004 at $50 million for motion pictures, $15 million for records/music and $23 million for books. There are signs that anti-piracy measures introduced in 2004 may be having a positive impact on industry.

In 1995, new patent, trademark, industrial design, and geographic indicator laws revamped Turkey's foundation for industrial property protection. Turkey also acceded to a number of international conventions, including the Stockholm Act of the Paris Convention, the Patent Cooperation Treaty, and the Strasbourg Agreement. Although the Turkish Patent Institute (TPI) was established in 1994 to support technological progress, protect intellectual property rights and provide public information on intellectual property rights, it is currently understaffed.

In accordance with the 1995 patent law and Turkey's agreement with the EU, patent protection for pharmaceuticals began on January 1, 1999. Turkey has been accepting patent applications since 1996 in compliance with the TRIPS agreement "mailbox" provisions. The patent law does not, however, contain interim protection for pharmaceuticals in the R&D "pipeline".

Parliament amended the Patent Law in June 2004. The new law provides for penalties for infringement of up to 3 years in prison, or 47 billion TL (approximately $32,000) in fines, or both, and closure of the business for up to one year. However, some companies in the pharmaceuticals sector have criticized provisions which delay the initiation of infringement suits until after the patent is approved and published, permit use of a patented invention to generate data needed for the marketing approval of generic pharmaceutical products, and give judges wider discretion over penalties in infringement cases,.

The Health Ministry has accepted applications to register generic copies of products which have a valid patent in Turkey; in the absence of a system for patent linkage, it may become possible for generics manufacturers to register a copy of a brand name drug with a valid Turkish patent, with enormous damage to the interests of the patent owner.

The Government of Turkey introduced limited data exclusivity in a regulation issued by the Health Ministry in January 2005. However, several of the regulation's provisions severely undermine protection for confidential test data. Retroactive application is limited to original products licensed in a Customs Union country after January 1, 2001 for which no generic manufacturers have applied for licenses in Turkey and the term of exclusivity is limited to the duration of the drug patent. Also, the six-year term of data protection starts on the date of licensing in an EU Customs Union country, implying a shorter term of protection because of the length of the marketing approval process in Turkey.

Trademark holders also contend that there is widespread and often sophisticated counterfeiting of their marks in Turkey, especially in apparel, pharmaceuticals, film, cosmetics, detergent and other products.

In 2004, Turkey published its first Plant Variety Protection (PVP) Law. A subsidiary of a major U.S. seed company, however, has been unable to obtain protection for its commercial seed under this new law, reportedly at great cost to the company.

SERVICES BARRIERS

Telecommunications Services

State-owned Turk Telecom currently provides voice telephony and most value-added and basic telecommunications services. In the WTO negotiations on Basic Telecommunications Services, Turkey made commitments to provide market access and national treatment for all services at the end of 2005, and permitted value-added telecommunications services to be licensed to the private sector with a 49 percent limit on foreign equity investment. In the interim, Turkey committed to provide national treatment for mobile, paging and private data networks. In 2000, the Turkish government passed a law unilaterally accelerating the opening of the market for basic telephone services to 2004. A 2001 law provides for liberalization of areas under the Turk Telecom monopoly once the state's share in that company falls below 50 percent; however, the Turkish government has not yet issued implementing regulations. These laws also created an independent regulatory body - the Telecommunications Authority (TK) - and made licensing criteria publicly available. U.S. firms complain that the licensing process still lacks transparency and that revenue sharing with Turk Telecom is required where competition is permitted. Due to a well publicized merger and a government seizure in February, 2004, there are now two private GSM cellular operators in Turkey, with a third (Telsim) currently owned by the Turkish Government.

In November 2004, the Privatization Administration announced the tender for a block sale of 55 percent of Turk Telecom. Law 5189 of 2004 lifted the limit on foreign ownership of Turk Telecom. Turkey has offered to bind this accelerated liberalization in the current WTO services negotiation, and fully adopt the WTO Reference Paper on regulatory principles. While a welcome improvement, Turkey has failed to address either in domestic law or in its revised WTO offer the key outstanding market access barrier, the 49 percent foreign equity restriction for this sector.

Other Services Barriers

There are restrictions on establishment in financial services, the petroleum sector, broadcasting, and maritime transportation (see Investment Barriers section). A 2003 law on work permits for foreigners repealed earlier legislation defining certain professions and services open only to Turkish citizens. This has significantly broadened the range of occupations in which foreigners can be engaged, but there are still restrictions for doctors, attorneys and several other professions.

INVESTMENT BARRIERS

The U.S.-Turkish Bilateral Investment Treaty (BIT) entered into force in May 1990. Turkey has a liberal investment regime, but private investment has often been hindered, regardless of nationality, by excessive bureaucracy; political and macroeconomic uncertainty; weaknesses in the judicial system; high tax rates; a weak framework for corporate governance; and frequent changes in the legal and regulatory environment.

Almost all areas open to investment by the Turkish private sector are fully open to foreign participation, but establishment in the financial and petroleum sectors requires special permission. Foreign equity is limited to 20 percent in broadcasting and 49 percent in maritime transportation and many value-added telecommunications services (such as GSM, satellite and data, though telecommunications legislation has been amended to allow certain company-specific exceptions to these limits). Parliament is considering draft legislation easing restrictions on foreign ownership in the media. Once investors have committed to the Turkish market, they have sometimes found their investments undercut by arbitrary legislative action, such as the imposition of production limits.

The Turkish government accepts binding international arbitration of investment disputes between foreign investors and the state. In 2001 the Parliament approved a law expanding the scope of international arbitration in Turkish contracts. However, at least one American company reports that the judicial system in Turkey has not recognized international arbitration awards. (Turkey has been a party to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards since 1992. It has been a party to the ICSID Convention since 1989.)

The Turkish government passed legislation in February 2001 that aims to introduce a fully liberalized energy market, under which private firms will be able to develop projects with the approval of the Energy Market Regulatory Authority, an independent regulatory body. The state electricity utility has been unbundled into production, transmission, distribution, and trading companies, but little progress has been made in privatizing power generation and distribution. Targeted liberalization of the natural gas sector has also faced delays. The state pipeline company BOTAS will remain dominant, but legislation requires phased transfer of 80 percent of its gas purchase contracts. Privatization of natural gas distribution is proceeding slowly.

As the result of a 1997 court decision, the Turkish Government has blocked full repatriation of investments by oil companies under Article 116 of the 1954 Petroleum Law, which protected foreign investors from the impact of lira depreciation. Affected companies have challenged the 1997 decision and the case is currently in the Turkish court system.

Anticompetitive Practices

As part of its customs union agreement with the EU, Turkey has pledged to adopt EU standards concerning competition and consumer protection. In 1997, a government "Competition Board" commenced operations, putting into force a 1994 competition law. Government monopolies in a number of areas, particularly alcoholic beverages and telecommunications services, have been scaled back in recent years, but currently remain a barrier to certain U.S. products and services. The Turkish government maintains a state monopoly on wine production that restricts the sales of U.S. wine.

Corruption

Corruption is perceived to be a major problem in Turkey by private enterprise and the public at large, particularly in government procurement. The judicial system is also perceived to be susceptible to external influence and to be biased against outsiders to some degree. American companies operating in Turkey have complained about contributions to the community solicited, with varying degrees of pressure, by municipal or local authorities.

Parliament continues to probe corruption allegations involving senior officials in previous governments, particularly in connection with energy projects.

Turkey ratified the OECD antibribery convention, and passed implementing legislation providing that bribes of foreign officials, as well as domestic, are illegal and not tax deductible.

OTHER BARRIERS

Energy: In 2001, the Turkish Government cancelled 46 contracted power projects based on the build-operate-transfer (BOT) and transfer-of-operating-rights models. Turkey's constitutional court ruled in 2002 that the government would have to either honor the contracts or compensate the companies involved. To date, the Turkish government has not commenced negotiations with the companies, one of which has launched an international arbitration case. In 2002, the government requested BOT projects already in operation -- which include U.S.-owned companies -- to apply for new licenses from the new Energy Market Regulatory Authority (EMRA), and has indirectly pressed them unilaterally to lower their prices while the license application process is still underway. Despite lack of action on new licenses, the Turkish government has continued to purchase electricity produced per the existing contracts.

Cola tax: Punitive taxation of cola drinks (raised in 2002 to 47.5 percent under Turkey's "Special Consumption Tax") discourages investment by major U.S. cola producers.

Corporate Governance: Weaknesses in the protection of minority shareholder rights and regulatory oversight have left some American companies at a disadvantage in disputes with Turkish partners.

Automakers: Turkey assesses a Special Consumption Tax of 27 percent to 50 percent on all motor vehicles based on engine size. This tax has a disproportionate effect on U.S. automobiles.

Pharmaceuticals: Besides their intellectual property concerns detailed above, the pharmaceutical industry's sales have been hurt by Government price controls. Research-based industry is also concerned about achieving transparent and equitable treatment in upcoming reforms of the Government's health care and pension system.

UKRAINE

TRADE SUMMARY

The U.S. trade deficit with Ukraine was $452 million in 2004, an increase of $420 million from $32 million in 2003. U.S. goods exports in 2004 were $398 million, up 72.6 percent from the previous year. Corresponding U.S. imports from Ukraine were $850 million, up 223.9 percent. Ukraine is currently the 79th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Ukraine in 2003 was $237 million, up from $198 million in 2002.

IMPORT POLICIES

Ukraine continues to maintain a number of barriers with respect to imports, including fee and certification regimes. Most import tariffs are levied at *ad valorem* rates, ranging from 2 percent to 70 percent and averaging 16.3 percent in 2002. Approximately 16 percent of all tariff line items are subject to either compound, alternative minimum, or specific rates of duty. The value-added tax (VAT), currently 20 percent, and discriminatory excise taxes can also hinder U.S. exports to Ukraine. Import tariffs are particularly high with respect to petroleum products (5-60 EUR/ton) and distilled spirits (7.5 EUR/liter). The import tariff on alcohol is equivalent to an *ad valorem* tariff of 50 percent to 100 percent.

Excise taxes generally range from 5 percent to 100 percent. Excise duty rates are assessed as a percentage of the sum of the declared customs value, customs duties, and fees paid for importing products. Of concern were four categories of imports that were subject to excise taxes in 2004: alcoholic beverages, tobacco, petroleum products, and automobiles. Excise taxes on an array of imported alcoholic beverages range from 2 times to 12 times higher than the duty on domestically manufactured products. The excise duty is 4 times higher on imported unfiltered cigarettes. Excise taxes on imported automobiles range from 0.2 EUR/cc to 3 EUR/cc, while no excise tax is levied on the same product categories if domestically produced. In addition, the excise tax is based on the cubic capacity of the engine, which disproportionately affects automobiles with larger engines.

Import licenses are required for some goods, primarily pesticides, alcohol products, CD production inputs, some industrial chemical products and equipment containing them, official foreign postage stamps, excise marks, officially stamped/headed paper, and checks and securities. The U.S. distilled spirits industry reports particularly burdensome import permit requirements for alcohol products, under which certificates of conformity are issued to importers only after officials of the Ukrainian Government have conducted an exhaustive and costly inspection of the producer’s facilities. In some cases, these practices have led exporters to withdraw their products from the Ukrainian market.

Ukrainian barriers to U.S. agricultural goods are estimated to cost U.S. producers between $10 million to $25 million annually. Talk of increasing tariffs and introducing quotas, possibly limiting imports of U.S. poultry into Ukraine's tax-free Free Economic Zones (FEZs), suggests that U.S. exports may be further hampered.

The two-year ban on U.S. poultry products was lifted in 2003 following the renegotiation of a new veterinary certificate. Shipments of U.S. poultry to Ukraine resumed in the fourth quarter of 2003. Currently, U.S. poultry products are regaining market share. The government of Ukraine continues to limit red meat imports from the United States (valued at approximately $13 million in 2004) due to a ban on hormone additives in feed and restrictive veterinary and packaging requirements. U.S pork exports to Ukraine are hampered by regulations that do not appear to be scientifically justified concerning trichinosis.

Non-tariff barriers such as excessive customs fees, discriminatory licensing procedures, and transparency of regulations and rules continue to affect key exports of U.S. non-agricultural goods, including civil aircraft, information technology, and machinery.

While costs related to business registration have been reduced, Ukraine still requires numerous permits to conduct business and engage in foreign trade. A new law requiring registration of legal entities within three working days of a request for a permit entered into force on July 1, 2004. According to the Cabinet of Ministers’ Committee on Regulatory Policy and Entrepreneurship, additional aspects of the law have complicated business registration procedures and led to a sharp increase in business complaints over registration requirements.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Foreign investors regard Ukraine’s product certification system and licensing procedures as serious obstacles to trade, investment, and ongoing business. The standardization and certification body in Ukraine is the State Committee for Technical Regulation and Consumer Policy (DerzhSpozhyvStandard), the former "DerzhStandard.” As of November 2004, DerzhSpozhyvStandard had a network of 107 accredited product certifying bodies and six accredited certifying bodies for quality management systems, as well as 780 testing laboratories throughout Ukraine. Appropriate resources, such as modern analytical equipment and reactants, are not available in most laboratories. DerzhSpozhynStandard’s system includes 28 state centers for standardization, systematizing weights and measures, certification and 27 territorial departments for consumer protection.

U.S. businesses have complained that the standards and certification requirements affecting the consumer goods industry: (1) lack clarity; (2) include registration requirements that are not feasible for mass trade; (3) lack procedural flexibility; (4) involve complex and lengthy import licensing procedures; (5) impose overly complex and expensive certification requirements; (6) are unevenly enforced; and (7) involve high certification and licensing fees. The process for developing standards has been streamlined over the past few years; however, it remains complex and is subject to frequent changes. While Ukrainian law formally stipulates equal treatment of domestic and foreign companies, U.S. businesses report that they often experience arbitrary application of the law and that discrimination against foreign companies is common. Ukraine authorities do not recognize foreign certificates of conformity with Ukrainian product standards unless recognition is mandated through an international treaty signed by Ukraine.

Numerous certification bodies in Ukraine effectively operate as independent (often monopolistic) entities on a profit-making basis, returning just 20 percent of their fees to the state. DerzhSpozhyvStandard does not properly supervise or enforce pricing rules. Consequently, certification agencies do much of their regulatory work with little or no coordination. Many products require multiple certificates from different agencies, with local, regional and municipal authorities often requesting additional documentation beyond that required by central bodies. According to U.S. telecommunications industry sources, access to the Ukrainian market is impeded by numerous burdensome certification and licensing procedures for equipment. Pharmaceutical and other companies report that they have been required to pay exorbitant additional fees (up to $20,000) to purchase equipment needed to test ingredients that have been used safely for many years.

Ukraine applies a range of sanitary and phytosanitary (SPS) measures, many of which do not appear to be consistent with an international, science-based approach to regulation. The certification and approval process is lengthy, duplicative, and expensive, with politics and corruption often behind arbitrary application of regulations. Beginning in October 2003, the State Department of Veterinary Medicine began detaining large consignments of U.S. salmon, sardines, and roe, citing technical reasons ranging from newly enforced shelf-life regulations to minor certificate errors. In February 2004, a ban on imports of seafood with longer than a 4-month shelf life was announced. For about a year, seafood shipments from the United States worth a total of $2 million were detained for an average of 2 months until being eventually released. No incidents have been reported since October 2004, but the shelf-life restriction still exists and could be enforced at any time.

The government of Ukraine restricts imports of a number of other U.S. agricultural products. Imports of dried-egg products, with a potential value of $1 million, are restricted due to veterinary requirements demanding U.S. certification of the absence of poultry diseases that could not be transmitted via egg powder. In addition, an unofficial ban on biotechnology products may cost American farmers an estimated $2 million in lost sales of corn products, soybeans and meal.

GOVERNMENT PROCUREMENT

Government procurement is conducted under Ukraine's Law on Procurement of Goods, Works and Services Using State Funds, which came into force on February 22, 2000. Under this law, all government procurement of goods and services valued above EUR 40,000 must be conducted via tenders (either open, or open with pre-qualification). Open international tenders must be conducted when procurement is financed by any entity outside Ukraine. Information on government procurement is published in the "State Procurement Bulletin" by the Ministry of the Economy and European Integration. Among the problems still faced by foreign firms (particularly for smaller procurements) are: (1) the absence of public notice of tender rules; (2) the failure to state tender requirements; (3) covert preferences in tender awards; (4) awards made subject to conditions that were not part of the original tender; and (5) the lack of an effective avenue for firms to air grievances over contract awards or an effective means to resolve disputes. Ukraine is not a signatory to the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

The Ukrainian government continues to maintain some industrial policies aimed at import substitution and export promotion, although these practices are decreasing. Some Ukrainian enterprises are not required to pay taxes, receive energy at a concessionary price, clear transactions by offsetting mutual debts, and receive below-cost government inputs.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Ukraine was the only country named a Priority Foreign Country in the 2002, 2003 and 2004 Special 301 reviews conducted by USTR. The United States withdrew Ukraine's benefits under the Generalized System of Preferences (GSP) program in August 2001 and imposed $75 million worth of sanctions on Ukrainian imports on January 23, 2002. These sanctions, which impact a number of Ukrainian products, including metal, footwear, and chemicals, remain in effect based on the repeated failure of the Government of Ukraine to enact and enforce adequate optical disc media licensing legislation in order to fully comply with the June 2000 United States-Ukraine Joint Action Plan to Combat Optical Media Piracy. The Ukrainian Government has drafted amendments to the existing Optical Disc Licensing Law to address the law's inadequacies, but Ukraine's parliament has failed to pass these amendments on several occasions. As a result, Ukraine's law does not have adequate enforcement provisions to prevent unauthorized optical media production and distribution. Ukraine is also a major trans-shipment point and storage location for illegal optical media produced in Russia and elsewhere.

As part of its ongoing efforts to negotiate accession to the WTO, Ukraine has adopted legislation to bring its laws into compliance with the WTO Agreement on Trade- Related Aspects of Intellectual Property Rights (TRIPS). Nevertheless, enforcement remains weak. In addition to optical media piracy, patent and trademark violations are common in Ukraine, and U.S. industries report rampant counterfeiting of pharmaceuticals and consumer products. In addition, the Ukrainian Ministry of Health reportedly does not check the validity of patents when it permits pharmaceutical sales in Ukraine.

In order to increase IPR enforcement, the Ministry of Internal Affairs and the State Customs Service have set up units to deal exclusively with IPR violations. The State Department of Intellectual Property has trained 20 inspectors to enforce Ukraine's CD licensing regime. These under-staffed units cannot, however, adequately deal with the enormous number of IPR infringements. In many cases, the rights holder must actively and continually engage with the Ministry of Internal Affairs or the State Customs Service to obtain enforcement. The judicial system does not provide reliable recourse against IPR infringement, because the number of judges trained in IPR law remains low and enterprises generally lack confidence in the Ukrainian judicial system and therefore do not bring private lawsuits. Legal experts and government officials have called for the formation of a special patent court in Ukraine to adjudicate patent cases, but to date there has been no concrete action towards this end.

SERVICES BARRIERS

Ukraine has few explicit restrictions on services. Foreign professionals are permitted to work in Ukraine, but the lack of transparency and the multiplicity of licensing authorities hinders foreign access to the Ukrainian services market. A local content requirement exists for radio and television broadcasting, although it has not been stringently enforced. Foreign insurance firms and banks are permitted to operate in Ukraine, but they cannot open branches, a prohibition that impedes participation of foreign businesses in Ukraine. Nevertheless, investors can open 100 percent foreign-owned subsidiaries.

INVESTMENT BARRIERS

An underdeveloped banking system, poor communications networks, a difficult and frequently changing tax and regulatory climate, crime and corruption, and a weak legal system create major obstacles to U.S. investment in Ukraine. In 2003, Ukraine passed legislation on tax reform, establishing a flat rate on Personal Income Tax of 13 percent and lowering Enterprise Profit Tax from 27 percent to 25 percent. After the President twice vetoed laws reducing the Value Added Tax (VAT) from 20 percent to 17 percent, Parliament postponed lowering the VAT until 2005. The accumulation of VAT refund arrears has also been a serious problem for foreign and domestic exporters in Ukraine.

Rules governing payment of the VAT discriminate against foreign companies and domestic firms with foreign investment. A decision by the State Customs Service requires those companies to pay VAT (20 percent) upon importation of goods, while Ukrainian tax law allows Ukrainian firms to use promissory notes upon importation of goods for re-export, with notes cancelled when re-export occurs. Because the process for obtaining refund of VAT payments can take from six to eighteen months, this interpretation of the law disadvantages foreign companies.

Combined payroll taxes (mainly for pensions) remain high at an average of 37.5 percent. There are frequent changes in other tax laws and regulations, such as import duties and excise taxes, often with little advance notice, giving companies little time to adjust to new requirements. Improvements are being made in tax filing and collection procedures, although these still differ significantly from those in western countries. The Chairman of the State Tax Administration established an advisory committee on the tax problems of foreign companies, which has been functioning for about two years and has achieved resolution of some difficult issues brought before it by U.S. and other foreign companies.

The United States has a Bilateral Investment Treaty (BIT) with Ukraine, which took effect on November 16, 1996. The BIT guarantees U.S. investors the better of national and MFN treatment, the right to make financial transfers freely and without delay, international legal standards for expropriation and compensation and access to international arbitration.

To attract investment and remove obstacles to trade, Ukraine created eleven Free Economic Zones (FEZs) and nine Priority Development Territories (PDTs), reportedly covering some 10 percent of Ukrainian territory. In August 2002, the Cabinet of Ministers introduced a moratorium on the establishment of FEZs and PDTs until January 1, 2005. There is no single, clear law that regulates the FEZs. Legislative loopholes permit companies to misuse FEZ status, and to avoid taxes and import duties.

Privatization rules generally apply to both foreign and domestic investors, and, in theory, a relatively level playing field exists. In practice, however, the privatization process continues to lack transparency. Clear qualification requirements for investors need to be established, and recognition of procedures and financial information need to be more public, complete, and timely. Each year a list of companies is slated for privatization, but the cash sale of majority shareholdings in several strategic large-scale enterprises has been inconsistent. In the 2004 Presidential election year, the Ukrainian government rushed to privatize large plants including coalmines and steel mills. The privatizations were marked by unclear, non-transparent and changing regulations and by heavy political interference that practically excluded foreign investors from participating in privatization. A particularly egregious case in June 2004 which received wide press coverage was that of Kryvorizhstal, Ukraine's largest steel mill, which was sold to government-backed investors for much less than bids presented by a consortium made up of London-based LNM Corp. and Pittsburgh-based U.S. Steel, as well as other foreign investors.

ELECTRONIC COMMERCE

The Internet and electronic commerce are underdeveloped in Ukraine. In 2003 the Ukrainian parliament adopted three laws regulating the Internet and setting framework regulations for the telecommunications market. Based on one of those laws ("On Telecommunications"), in 2004 the President established the National Council on Communications entrusted with monitoring the telecommunications market. The Council is to begin operating in 2005 with members appointed by the President.

OTHER BARRIERS

As of January 1, 2003, Ukraine imposed an export duty of 30 euros per metric ton on ferrous steel scrap and in the spring of 2004, the government increased by 70 percent railway shipping rates for exported scrap metal, coke and coking coal. This export duty has contributed to a decline in scrap exports from Ukraine, at a time when global demand and prices for steel scrap are rising. The export tax assists Ukrainian steel producers by increasing domestic steel scrap supply, providing them with an advantage in Ukraine and in third markets. The government says it will lower the export duty in the course of its WTO accession, but no specific steps have been taken yet. Moreover, the export duty constricts global supplies of a key steel input, which has the effect of raising prices of steel scrap for otherwise competitive producers elsewhere, including those in the United States. Sunflower seeds have been subject to a similar export duty since June 21, 2001, which benefits local sunflower oil producers. Export duties have also been imposed on live cattle, sheep, hides and skins since 1996. For live calves the duty is 75 percent of custom value (but no less than 1500 EUR/ton of live weight); for live cows it is 55 percent (but no less than 540 EUR/ton of live weight); and for live sheep it is 50 percent (but no less than 390 EUR/ton of live weight). For raw hides of cattle the duty is 30 percent (but no less than 400 EUR/ton of live weight); for sheep hides it is 30 percent (but no less than 1 EUR/hide); and for pig skins the duty is 27 percent (but no less than 170 EUR/ton of live weight).

UNITED ARAB EMIRATES

TRADE SUMMARY

The U.S. trade surplus with the United Arab Emirates was $2.9 billion in 2004, an increase of $542 million from $2.4 billion in 2003. U.S. goods exports in 2004 were $4.1 billion, up 15.8 percent from the previous year. Corresponding U.S. imports from United Arab Emirates were $1.1 billion, up 1.2 percent. United Arab Emirates is currently the 29th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in the United Arab Emirates in 2003 was $1.4 billion, up from $1.3 billion in 2002.

After consultations with Congress, the United States bean Free Trade Agreement (FTA) negotiations with the UAE in March 2005. An important objective of these negotiations is the removal of trade barriers for U.S. goods and services providers. The FTA with the UAE is the next stage in achieving President Bush's vision for a Middle East Free Trade Area by 2013.

IMPORT POLICIES

The United Arab Emirates is a federation of seven emirates (Abu Dhabi, Dubai, Sharjah, Ajman, Umm Al-Qaiwain, Fujairah, and Ras Al-Khaimah). The UAE is part of the Gulf Cooperation Council (GCC), an economic and political policy-coordinating forum for the six member states (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the UAE). The individual emirates founded the UAE in December 1971 after realizing that they were too small and too poor to be viable on their own. Over the last 33 years, the UAE has developed into the third largest economy in the Arab world, with an estimated 2003 GDP of about $80 billion. The UAE has pursued free market, pro free trade policies to diversify its economy away from its dependence on oil. Despite possessing 9 percent to 10 percent of the world's proven oil reserves and the fourth largest proven gas reserves in the world, rapid growth in the non-oil economy reduced oil's share of GDP from 60 percent in 1980 to about 30 percent now.

Tariffs

At its December 2001 Summit, GCC Heads of State adopted an across-the-board common external tariff of five percent for most products. The new tariff regime was implemented in January 2003 as part of the GCC Customs Union agreement. The GCC states also agreed to develop a list of products to which a higher tariff would apply. Currently, the UAE's exceptions to the five percent tariff are a 50 percent tariff on alcohol, a 100 tariff on tobacco, and duty exemptions for 53 food and agricultural items.

Import Licensing

Only firms with an appropriate trade license can engage in importation, and only UAE nationals can obtain such a license (this licensing provision is not applicable to goods imported into free zones). In addition, not all goods require an import license.

Documentation Requirements

Since July 1998, the UAE has required that documentation for all imported products be authenticated by the UAE Embassy in the United States. There is an established fee schedule for this authentication. If validation is not obtained in the United States, customs authorities will apply the fee schedule when the goods arrive in the UAE.

Customs Valuation

The UAE notified the WTO Customs Valuation Committee in October 2004 of its customs valuation scheme.

Textiles

Textile manufacturing represents approximately 10 percent of the UAE's gross domestic product, and Ministry of Economy officials have said that the textile sector is key to UAE efforts to diversify its economy. The UAE has attracted a number of garment manufacturers because of its close proximity to the Indian subcontinent and a lack of corporate and personal income taxes. The majority of garment factories are located in free trade zones, where they operate exempt from UAE commercial law and can be 100 percent owned by foreigners. In 2003, the Dubai Government announced the development of a $60 million textile free zone, called Dubai Textile City that is expected to open in fall 2005. The UAE has proposed eliminating the four percent textile tariff that currently exists between GCC members to further ease restrictions on textile trade.

STANDARDS, TESTING, LABELING AND CERTIFICATION

As part of the GCC Customs Union, member countries are working toward unifying their standards and conformity assessment systems, and have progressed considerably toward the goal of a unified food standard, originally targeted for adoption by 2006. However, each country currently applies either its own standard or a GCC standard, causing confusion among some U.S. businesses.

The UAE opened the Emirates Authority for Standardization and Metrology (ESMA), established under the auspices of the Ministry of Finance and Industry, in October 2002 to manage issues of standardization arising from the GCC Customs Union. The UAE has decided not to implement the GCC International Conformity Certification Program (ICCP). Instead, ESMA launched its own conformity assessment program, the Emirates Conformity Assessment

Scheme (ECAS) on selected products. ECAS applies national or GCC standards to domestically manufactured products, and applies international standards if national or GCC standards do not exist. The UAE asserts that the ECAS is a voluntary program and only applicable to domestically produced goods, but the scope and parameters of ECAS lack clarity and transparency.

Not all UAE national and GCC food standards are consistent with international standards published through the CODEX, OIE and IPPC organizations. In addition, the UAE requires that all consumer-ready food products carry both production and expiration dates and stipulates that at least one-half of a product's shelf life must be valid when a product reaches the port of entry. For red meats and poultry, the product must arrive within four months of production. The UAE maintains import bans on U.S. meat and poultry and cattle products, even though the OIE standard does not support such a ban.

In August, 2004, the UAE cabinet transferred control of the country's Food Safety and Technical Advisory Committee from the General Secretariat of Municipalities to the ESMA.

GOVERNMENT PROCUREMENT

The UAE does not require that a portion of any government tender be subcontracted to local firms, but it grants a 10 percent price preference for local firms in government procurement. The UAE requires that only registered companies be invited to receive government tender documents. To be registered, a company must have at least 51 percent UAE-ownership. However, these rules do not apply to major projects or defense contracts where there is no local company able to provide the goods or services required. Established in 1990, the UAE's offset program requires defense contractors that are awarded contracts valued at more than $10 million to establish joint venture projects that yield profits equivalent to 60 percent of the contract value within a specified period (usually seven years). There are also reports, as well as anecdotal evidence, indicating that defense contractors can sometimes satisfy their offset obligations through an up-front, lump-sum payment directly to the UAE Offsets Group. The projects must be commercially viable joint ventures with local business partners, and are designed to further the UAE objective of diversifying its economy away from oil. To date, more than 40 projects have been launched, including, *inter alia*, a hospital, an imaging and geological information facility, a leasing company, a cooling system manufacturing company, an aquiculture enterprise, Berlitz Abu Dhabi, and a firefighting equipment production facility. Two of the largest offset ventures are an international gas pipeline project (Dolphin) and the Oasis International leasing company -- a British Aerospace offsets venture. The UAE is not a signatory to the WTO Agreement on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

The UAE has made the protection of intellectual property a priority in recent years. The UAE repealed previous copyright, trademark, and patent laws and issued improved legislation in 2002, providing high levels of protection for U.S. intellectual property. In addition, an agreement between the UAE and U.S. pharmaceutical companies provides *de facto* patent protection for a number of U.S. patent-protected medicines, and, in 2004, the UAE resolved a number of IPR complaints with U.S. pharmaceutical manufacturers.

The new copyright law, enacted in July 2002, grants protections to authors of creative works and expands the categories of protected works to include computer programs, software, databases, and other digital works. Efforts to combat computer software piracy in the UAE have been successful. According to 2002 industry estimates, the rate of software piracy in the UAE is the lowest in the Middle East. The UAE is recognized as the regional leader in fighting computer software piracy.

The UAE's new Trademark Law, also issued in July 2002, confirms that the UAE will follow the International Classification System and that one trademark can be registered in a number of classes. The new law provides that the owner of the registration shall enjoy exclusive rights to the use of the trademark as registered and can prevent others from using an identical or similar mark on similar, identical or related products and services if it causes confusion among consumers. However, it remains unclear how the UAE provides protection for geographical indications as required by the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs).

The UAE published the official and final version of the long-awaited Patent Law in November 2002. The Patent Law provides for national treatment for intellectual property owners from other WTO Members, product and process patent protection, and enforcement of intellectual property rights utilizing civil and criminal procedures and remedies. In October 2003, the Ministry of Health issued a circular providing data exclusivity protection in the UAE for pharmaceutical products for up to five years or until a patent is granted or rejected in the UAE, whichever period is shorter.

In 2004, the Ministry of Information issued new regulations allowing for specialized collecting societies as a practical way for sound recording companies to collect royalties on the broadcast and performance of copyrighted material. The UAE is also considering legislation for data protection, privacy, and other IP-related issues. In response to TIFA Council discussions, the UAE has identified points of contact for rights holders to address complaints.

SERVICES BARRIERS

Insurance

In November 2004, the Ministry of Economy and Planning announced that it will open its insurance sector to new foreign insurance companies. About half of the current 47 insurance companies in the UAE are foreign, but the UAE government froze new entries to the market in

1989 due to a perception that the market was saturated. New foreign companies will be required to meet high international rating criteria and to offer new products to the market.

Banking

The UAE has 21 national banks, 26 foreign financial entities, and a total of 457 branches. Following a banking crisis caused by accumulating bad debts after the oil boom in the mid-1980s, the Central Bank stopped giving licenses to new foreign banks. However, in September 2003, the UAE Central Bank announced that it would allow the operation of more banks from other countries on a reciprocal basis. The Central Bank is also considering allowing foreign banks operating in the UAE to set up new branches provided that they undertake to employ UAE nationals. Figures by the Central Bank show national banks enjoy a stronger financial position than foreign banks operating in the UAE, with assets peaking at the end of March 2003 at nearly $68.3 billion compared with foreign banks' assets of around $21.5 billion. The UAE opened the Dubai International Free Zone in 2004, which exempts foreign banks from civil and commercial, though not criminal, law.

Agent and Distributor Rules

The UAE's Commercial Agencies Law requires that foreign principals distribute their products in the UAE through exclusive commercial agents that are either UAE nationals or companies wholly owned by UAE nationals. The foreign principal can appoint one agent for the entire UAE or for a particular emirate or group of emirates. All UAE commercial agents must be registered with the Ministry of Economy and Planning. Once chosen, agents/distributors have exclusive rights, and the law provides that an agent may be terminated only by mutual agreement of the foreign principal and the local agent, notwithstanding the expiration of the term of the agency agreement. Since 1996, the UAE has not recognized new agency agreements in the food sector. Agency agreements in existence prior to this period are still recognized. The UAE is discussing amendments to the Agency Law, although no formal decisions have been made at this time.

INVESTMENT BARRIERS

Except for companies located in one of the free zones, at least 51 percent of a business establishment must be owned by a UAE national. A business engaged in importing and distributing a product must be either a 100 percent UAE owned agency/distributorship or a 51 percent UAE/49 percent foreign limited liability company (LLC). Subsidies for manufacturing firms are only available to those with at least 51 percent local ownership.

The laws and regulations governing foreign investment in the UAE are evolving. There is no national treatment for investors in the UAE. Non-GCC nationals cannot own land, but the emirate of Dubai currently is offering so-called free hold real estate ownership for non-GCC nationals within certain properties. However, the exact legal status of this scheme is still uncertain. 22 out of 53 stocks on the UAE stock market are open to foreign investment. Ministry of Economy and Planning rules allow foreign investors to own up to 49 percent of companies on the stock market; however, company by-laws in many cases prohibit foreign ownership. Claims resolution is a problem as foreign companies tend not to press claims for fear that doing so may jeopardize their business activities in the UAE.

ELECTRONIC COMMERCE

The Emirate of Dubai passed The Law of Electronic Transactions and Commerce No. 2/2002 in 2002, which protects certain electronic records and signatures, and some electronic communications. This law also provides penalties for any person who knowingly creates, publishes, or otherwise makes available false signature or certificate, or provides false statements online for fraudulent or any other unlawful purpose. In March 2003, the International Bar Association hosted a conference in Dubai entitled, Middle East Law and the Internet Age. The conference addressed the legal developments related to new technologies, with a focus on electronic commerce in the Middle East. The Emirate of Dubai has established the Dubai Technology, Electronic Commerce and Media Free Zone (TECOM), which houses both Internet City and Media City, two subdivisions which cater, respectively, to the information technology and media sectors. In April 2004, the UAE announced the opening of the telecommunications sector, revoking Emirates Telecommunications Corporation's (Etisalat) monopoly rights. This decree took affect on January 1, 2005.

UZBEKISTAN

TRADE SUMMARY

The U.S. trade surplus with Uzbekistan was $142 million in 2004, a decrease of $31 million from $173 million in 2003. U.S. goods exports in 2004 were $230 million, down 10.2 percent from the previous year. Corresponding U.S. imports from Uzbekistan were $88 million, up 5.3 percent. Uzbekistan is currently the 94th largest export market for U.S. goods. The stock of U.S. foreign direct investment (FDI) in Uzbekistan in 2003 was $77 million, down from $9l million in 2002.

The U.S.-Uzbekistan Bilateral Trade Agreement, which came into force in 1994, provides for normal trade relations (NTR) between the United States and Uzbekistan and governs other aspects of the bilateral trade relationship. Uzbekistan is currently in the process of negotiating terms of accession to the World Trade Organization (WTO).

IMPORT POLICIES

The Government of Uzbekistan restricts imports in many ways, including high import duties, licensing requirements for importers and wholesale traders, restriction of access of sellers of imported items to retail space, and limited access to hard currency and the local currency (the soum).

Highly discriminatory excise taxes exist to protect locally produced goods. Combined with unofficial payments that must be made to border and customs officials to bring goods over the border, most imported goods are prohibitively expensive for the majority of Uzbeks. According to reports from foreign investors, unofficial duties combined with other tariffs and taxes can cost as much as 100 percent to 150 percent of the amount of the actual value of the product, making the product unaffordable for virtually everyone in the country. For example, imported liquor is reportedly subject to an excise tax of 90 percent versus a rate of 40 percent to 65 percent for domestic liquors. Additionally, by the time they reach the consumer, imported automobiles are subject to duties and taxes totaling approximately 100 percent. Tariffs are officially (not including unofficial duties) 30 percent for most textile products, including carpets and rugs, home furnishings, and essentially all other fabrics and apparel.

Fears of a surge of imports, and thereby a drain on hard currency reserves, caused the Government of Uzbekistan to drastically restrict imports in 2002 by imposing official and unofficial import surcharges. Moreover, the Government of Uzbekistan began requiring retailers to present certificates of origin and customs receipts for imported products upon the request of tax or customs authorities. The Uzbek government often confiscates goods found without such certificates. A new decree enacted in August 2004, but yet to be fully implemented, would impose further import restrictions on traders. In addition to demanding that all individual traders be registered with the local authorities and the Agency for Foreign Economic Relations, the traders will have to prove that they have a commercial bank account and that they imported the goods themselves from the originating country. Surveys of foreign companies consistently conclude that restrictions on access to local currency in order to transact business and pay employees is one of the worst of the many serious obstacles to doing business in Uzbekistan.

Due to the Government of Uzbekistan's acceptance of the International Monetary Fund's Article VIII agreement as of October 15, 2003, dramatic legislative changes took place in the import registration system and the import regime as a whole. One of these new changes states that companies that are not government-owned do not have to register imports. However, the government continues to restrict consumer goods imports in order to prevent hard currency flows and curb the threat of devaluation of the soum (see above). The overall procedure for buying foreign exchange by importers has been substantially streamlined and now includes only three steps, each reportedly taking not more than 2-3 business days each.

Although clearance of import contracts with the state consulting company is no longer needed for customs registration, the regulation requiring the registration has not been abolished. Reportedly, the State Customs Committee is still refusing to register old import contracts for goods from Kazakhstan and Kyrgyzstan dating back to 1999. Secondly, the State Customs Committee still turns down about 5 percent of contracts submitted for registration, purportedly due to mistakes in documents. The companies entitled to convert local currency under import contracts encounter problems with arbitrary requests for documentation by banks. While the required documents are outlined in the instructions issued by the relevant bank, these instructions are often amended without any prior notice. As a result, documents are often rejected on disputable grounds and conversion can be delayed for up to a month, which results in devaluation losses for the importer. Bank dealers have reported cases in which the Central Bank did not approve applications for conversion for some of their clients who needed large sums of hard currency.

In addition to official barriers, the customs clearance process is full of unofficial bureaucratic obstacles leading to significant processing delays of two to three months, even for U.S.-Uzbek joint ventures. Problems include the arbitrary seizure of goods, as well as frequent official and unofficial changes in customs procedures without prior notification. Excessive documentation also makes the Uzbek importing process costly and time consuming. The lack of proper equipment and legislative regulations provides an environment in which the customs official on duty can arbitrarily apply his or her own case-by-case search and seizure procedures. In 2004, the Government of Uzbekistan made an effort to increase regulation transparency at customs border posts, primarily by posting all relevant regulations and decrees where traders can review them.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The system of standardization, accreditation, certification and application of sanitary and phytosanitary (SPS) standards still presents significant barriers to trade. Currently, Uzbekistan applies a mandatory certification requirement to most of its imported and domestically produced products. The National Agency of Standards (Uzstandard) remains in charge of certification, accreditation and state control. The Uzbek Government is in the process of drafting a new law on technical regulation designed to bring Uzbekistan's regime in line with the requirements of the WTO Technical Barriers to Trade (TBT) and SPS Agreements.

The Newly Independent States (NIS) have an agreement on mutual recognition of certificates, which is not being fully honored by Uzbekistan. In August 2004, Uzbekistan's Parliament ratified a decision to join the International Union on Plants Variety Protection, which has been in force since November 11, 2004.

The Government of Uzbekistan accepts U.S. manufacturers' self-certification of conformity with Uzbek foreign product standards and environmental regulations. Effective June 2003, all foreign products must be labeled in Russian and Uzbek. Industry reports that domestic entities, including Uzbek Government enterprises, do not have to meet these mandatory labeling requirements, creating unequal footing for foreign companies.

GOVERNMENT PROCUREMENT

There is no systematic approach to government procurement in Uzbekistan. Instead, procurement decisions are generally made on a decentralized and *ad hoc* basis. Often, the procurement practices of the central government are similar to those of many countries, incorporating tenders, bid documents, bids and a formal contract award. A law enacted in 2002 created more transparency in the procurement process by mandating that all government procurement over $100,000 be completed on a tender basis. However, many tenders are announced with short deadlines and are awarded to companies that provide the most lucrative insider deals. Uzbekistan is in the process of modifying its trade regime to become a member of the WTO, and it is not yet a signatory of the WTO Agreement on Government Procurement.

The most serious barrier to trade with respect to government procurement is in the field of contract obligations. There are numerous cases in which the Uzbek Government is not complying with contract obligations in relation to procuring equipment, equipment pricing and payment guarantees. Further, there are several cases in which a U.S. company provided equipment for a government tender and then was not paid.

EXPORT SUBSIDIES

The Government of Uzbekistan provides agricultural export subsidies in the form of heavily subsidized inputs, such as electricity, water and fertilizer, to farmers who then sell their cotton directly to the Uzbek government. This creates an end product that can be sold more cheaply in the international market. In December 2002, the Government of Uzbekistan issued regulations allowing cotton farmers to sell half of their actual harvest, most often back to the government, at more favorable prices than those allowed in the state order system. It is unclear, however, how well the new regulation is being enforced by the end consumer, which in 90 percent of cases is still the Uzbek Government.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Significant deficiencies remain in Uzbekistan's regime for the protection of intellectual property. Due to these deficiencies, a case remains pending to review Uzbekistan's status as a beneficiary country under the U.S. Generalized System of Preferences (GSP) Program. Uzbekistan has been on the Special 301 Watch List since 2000.

In 1996, the Government of Uzbekistan undertook a comprehensive revision of its copyright law, but copyright protection in Uzbekistan remains significantly below international standards. In its December 2000 session, the Uzbek parliament made minor changes to the Uzbek copyright law and added trademark protections. The 2000 copyright amendments put in place additional protection for national authors and producers of sound recordings; however, these amendments did not extend protection to all works and recordings. In 2005, Uzbekistan joined the Berne Convention for the Protection of Literary and Artistic Works (Berne Convention), but the Uzbek Government declared an exception to Berne Article 18 which requires that signatory countries extend copyright protection to pre-existing works. Further, Uzbek law does not protect U.S. sound recordings, and, although the Government of Uzbekistan has announced its intention to join the Geneva Phonograms Convention, it has not yet applied for membership.

Enforcement of intellectual property remains weak in Uzbekistan. On the streets, in the bazaars and in stores, pirated audio and videotapes and compact disks are sold freely. In fact, it is a challenge to purchase legal recordings in Uzbekistan. Current border enforcement is weak. As a result, illegal recordings freely cross into Uzbekistan for sale. Additional personnel and training courses are needed for more effective border enforcement. The recording industry estimates that trade losses exceeded $31 million in 2004. Uzbekistan does not provide for either civil or criminal *ex parte* search procedures needed for effective anti-piracy enforcement.

SERVICES BARRIERS

For years, the most significant barrier to foreign services firms entering the Uzbek market has been difficulty in currency conversion. However, the Uzbek Government's adoption of currency convertibility in October 2003 eased the process of conversion in 2004. Although the Government of Uzbekistan has created an insurance supervisory board, a system of licensing insurance companies does not yet exist. Insurance firms can currently only operate in Uzbekistan on the basis of a governmental decree.

A ten percent withholding tax imposed on reinsurance premiums amounts to a competitive disadvantage for U.S. reinsurers vis-à-vis other foreign companies, as the United States does not have a double taxation treaty with Uzbekistan. Therefore, U.S. companies would have to add the ten percent charge to their premiums. Uzbek law grants state-owned companies a monopoly over certain forms of mandatory state insurance (i.e. mandatory insurance paid for out of the state budget).

Foreign banks may not operate in Uzbekistan except in a subsidiary status, which makes the banks subject to Uzbek laws and includes the requirement of a charter capitalization fund of $20 million. This is a common requirement in other Commonwealth of Independent States (CIS) countries. For Uzbek firms, the Government of Uzbekistan determines the required size of the charter funds on a case-by-case basis, leading to an unfair business environment.

INVESTMENT BARRIERS

To be considered "an enterprise with foreign investment" under the new laws implemented in 1998, a firm must be at least 30 percent foreign-owned and have initial foreign equity of $150,000. Normally this equity is "hidden" through assets such as equipment or technical expertise. Although reduced from previous levels, these capital requirements are still high enough to exclude foreign investment by small companies. The Government of Uzbekistan has postponed consideration of proposals to ease these requirements further. U.S.-owned companies in Uzbekistan face cumbersome regulations and licensing requirements. Profit repatriation remains extremely difficult for foreign-owned companies due to constant Government interference.

In the past, businesses had to register with numerous government organizations and obtain licenses from separate entities. However, in 2001, the Government of Uzbekistan attempted to introduce legislation to create a 'one stop shop' to make the company registration process easier. These 'one stop shops' are located in local government offices (Hokimiyats) throughout Uzbekistan and have reportedly improved individuals' abilities to form new businesses. However, even with the new regulations, businesses discover local and federal regulatory roadblocks that force them to continue the bureaucratic process at a minimum of 5-10 locations.

Uzbekistan's Tax Code, introduced for the first time in 1998, lacks important provisions that are part of the business environment in most countries. For example, it allows no credit for VAT on capital imports, including plant, machinery and buildings. This puts firms operating in Uzbekistan at a competitive disadvantage compared to those in countries that do allow such credits. (Companies that do receive VAT credits only do so through special Presidential decrees.) In addition, earnings of foreign-owned enterprises are subject to double taxation: their earnings are taxed in Uzbekistan and then taxed again when remitted to the foreign parent. Another significant problem in the Uzbek Tax Code involves the classification of expenses. Many expenses that are normally deductible for the purposes of calculating taxable profits are not deductible under the Uzbek Tax code, thereby increasing the effective tax burden in comparison to other countries. In most countries, expenses such as advertising and business travel are not subject to taxation. However, in Uzbekistan, travel is not deductible and advertising is only deductible based on an archaic formula.

Two factors increase labor costs for foreign firms in Uzbekistan. Corporate income tax rates, although reduced slightly over the last two years, still total 20 percent, and the mandatory contribution for insurance from the pay roll was 36 percent for 2003, a rate significantly higher than other similarly developed countries. While most Uzbek companies do not comply with their tax obligations, foreign investors generally adhere to the law. The Government of Uzbekistan imposed minimum salary requirements in 2001 to obligate foreign firms to pay full taxes on their employees. U.S. companies have complained that Uzbek laws are not interpreted or applied in a consistent manner. On many occasions, local officials have interpreted laws in a manner that is detrimental to individual private investors and the business community at large. Companies are particularly concerned with the consistent and fair application of the Foreign Investment Law, which contains a number of specific protections for foreign investors.

Because of the prohibitive tax code and burdensome regulatory environment when compared to other developed and developing countries, foreign investors in Uzbekistan whose projects would not be economically viable under the existing legislation are required to seek tax and regulatory abatements in the form of Cabinet of Ministers decrees, which must be signed by the President in order to be approved. Such decrees have been a generally effective means through which foreign investors in strategic industries (e.g., mining, oil and gas, and large manufacturing) contract for such investment projects. The process is lengthy and uncertain, however, and lacks the necessary transparency required to attract significant investment over the longer term. Despite the protections that such decrees have on the surface, investors working under Cabinet of Ministers decrees have still faced significant regulatory and bureaucratic impediments. In particular, corporate profit projections that are commonly utilized in many developing countries have very little merit in Uzbekistan, as the investment climate, even for those fortunate companies with a Cabinet of Ministers decree, is constantly in flux.

Persons doing business in Uzbekistan note that if they are engaged in a sector in which either the Government of Uzbekistan or an Uzbek-controlled firm is a competitor, they face increased bureaucratic hurdles and currency conversion problems. Often, competitors are not even allowed in such sectors.

Businesses complain that they lack access under Uzbek law to international arbitration. Moreover, the judiciary in Uzbekistan is not independent. In the event of disputes, courts usually favor firms that are controlled or owned by the state. Trade disputes involving foreign-owned businesses are common and have proven to be nearly impossible to resolve even with high-level intervention from senior U.S. policymakers and legislators.

The regulatory framework for joint ventures in Uzbekistan is extremely prohibitive to profitable trade. Many international corporations complain that the Government of Uzbekistan demands more financial reports than are necessary for the corporations' shareholders – a significant indication of the heavy-handed control the Uzbek Government places on foreign companies doing business in Uzbekistan.

ELECTRONIC COMMERCE

The electronic commerce industry is generally underdeveloped in Uzbekistan, due to a non-market based economy and under-developed technology in the sector. In 1999, the Uzbek Government issued a decree ordering all Internet Service Providers (ISPs) to be re-registered with the state-owned monopoly UzPAK and to obtain new ISP licenses, forcing all ISPs to provide services only through UzPAK lines. However, in October 2002, the Uzbek Government rescinded its decision as a part of larger market reforms and removed UzPAK's monopoly powers. The Uzbek Government reversed this decision first unofficially beginning in March 2003 and then officially in November 2004, giving UzPAK monopoly powers once again. The Uzbek Government granted exclusive control of all international telecommunication networks to Uzbektelekom, the largest national telecom operator. This means that now all providers of voice and data transmission services, including Internet and IP-telephony, receive access to long-distance/international channels only through Uzbektelekom's switchboards.

OTHER BARRIERS

American investors unanimously complain that they do not control their corporate bank accounts in Uzbekistan. The main problem involves restrictions on businesses' access to, and use of, cash in their accounts. Every routine banking operation requires official permission. As a result, businesses expend an enormous amount of senior staff time on simple transactions. A March 24, 2000 decree improved this situation by allowing many farms, restaurants, cafes and other small and medium enterprises with foreign investment ($150,000 or more in foreign capital) to access their own funds in commercial bank accounts, so long as those funds were received and deposited within the previous ninety days.

Most other businesses may hold cash for only a small number of permitted purposes, such as paying salaries and travel expenses. All other money must be held in the bank. Cash receipts must be deposited on the day in which they are received. Even small purchases, such as office supplies, must be paid for via bank transfer. Use of petty cash is not allowed. Uzbek companies handle this problem with salary withdrawals for non-existent staff. Western accounting practices prevent American companies from using these deceptive practices, and instead, companies are required to wait for as long as a week or more for a wire transfer to arrive before purchases of any kind can be made.

Local and international entrepreneurs face payoff-seeking officials due to pervasive corruption, exacerbated by low salaries for officials and an opaque, cumbersome, and internally contradictory legal regime that makes it difficult for business owners to comply with Uzbek regulations. It is reported that local, regional, and national officials, police officers, as well as tax, customs, fire, health, safety, and labor inspectors are all susceptible to bribery and other corrupt practices.

VENEZUELA

TRADE SUMMARY

The U.S. trade deficit with Venezuela was $20.2 billion in 2004, an increase of $5.9 billion from $14.3 billion in 2003. U.S. goods exports in 2004 were $4.8 billion, up 69 percent from the previous year. Corresponding U.S. imports from Venezuela were $25.0 billion, up 45.7 percent. Venezuela is currently the 26th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Venezuela were $2.2 billion in 2003 (latest data available), and U.S. imports were $419 million. Sales of services in Venezuela by majority U.S.-owned affiliates were $4.7 billion in 2001 (latest data available), while sales of services in the United States by majority Venezuela-owned firms were $308 million in 2001.

The stock of U.S. foreign direct investment (FDI) in Venezuela in 2003 was $10.9 billion, up from $10.3 billion in 2002. U.S. FDI in Venezuela is concentrated largely in the manufacturing, mining, and utilities sectors.

IMPORT POLICIES

Tariffs

Venezuela is part of the Andean Community. Venezuela has been using the tariffs established under the Andean Community's price band system since 1995 for certain agricultural products, including feed grains, oilseeds, oilseed products, sugar, rice, wheat, milk, pork and poultry. Yellow corn was added to the price band system in 1996, and processed poultry was added in 2001. *Ad valorem* rates for these products are adjusted according to the relationship between commodity market reference prices and established floor and ceiling prices. When the reference price for a particular commodity falls below the established floor price, the compensatory tariff for that commodity and related products is adjusted upward. Conversely, when the reference price exceeds the established ceiling, the compensatory tariff is eliminated. Floor and ceiling prices are set once a year based on average prices during the past five years. Venezuela publishes these prices each April.

In addition to the traditionally high import tariffs of the Andean Community’s price band system, Venezuela also protects its agricultural producers through a non-legislated system of guaranteed minimum prices and the restrictive use of import licenses and permits. Under its WTO commitments, Venezuela is entitled to maintain tariff rate quotas (TRQ) for up to 62 Harmonized System code headings, but its administration of the TRQs has been arbitrary and nontransparent, and has negatively affected trade in basic agricultural commodities as well as processed products. The Venezuelan Government has denied import licenses for both in-quota and over-quota quantities, even though importers are willing to pay the over-quota tariff for additional quantities of products.

U.S. agricultural exporters indicate that the Venezuelan government also routinely fails to open the TRQs in a timely manner -- in some cases there have been delays of up to four months -- with the immediate consequence of disrupting trade in basic commodities. Further, for some products eligible for TRQs, the Venezuelan government has not taken the necessary steps to publish regulations establishing the TRQ mechanism, and for other products, such as pork, the government has refused to activate the quota at all. For many years, the government and domestic producers have agreed -- behind closed doors -- to minimum prices for major crops such as corn, sorghum and rice. The government generally prohibits imports until the entire local crop has been purchased at the set price, resulting in an effective import ban.

Venezuela also has restricted the issuance of import licenses for sorghum, soybean meal, yellow grease, pork, poultry, oilseeds and some dairy products. For the first time in several years, in 2004 the government published information on import licenses through the Ministry of Agriculture.

Under the Andean Community's Common Automotive Policy, assembled passenger vehicles constitute an exception to the 20 percent maximum tariff and are subject to 35 percent import duties.

Non-Tariff Measures

In response to the rapid decline in the value of the national currency, the Bolivar, following a two-month general strike that brought oil production to a near standstill, the Central Bank of Venezuela halted trade in Bolivars on January 22, 2003. President Chavez announced the creation of an Exchange Administration Board (CADIVI) on February 5, 2003 to regulate the purchase and sale of foreign currency. During much of 2003, CADIVI was unable to process requests for authorization of foreign exchange in an efficient and timely manner and only supplied \$3.6 billion or approximately two months worth of transactions. There has been significant improvement over time. The supply of foreign currency reached a level of approximately \$15 billion in 2004, or 55 percent of approved authorizations. The Ministry of Light Industry (formerly the Ministry of Production and Commerce) maintains a list of imports that are eligible to receive foreign currency approval. This list has grown significantly since the introduction of the exchange controls and now includes services and the repatriation of capital. Although the number of currency certificate approvals has increased steeply, the exchange controls have put a significant constraint on imports, which account for 68.5 percent of requests, followed by private foreign debt with 12.5 percent and foreign investments with 8.6 percent. Exchange control authorities have repeatedly said that the exchange control system will be eased but will remain in place permanently.

Importers of agricultural products have received the majority of dollars under the CADIVI system, since most basic food products are on the import list. Even so, problems with coordinating the timing of access to dollars, approval of import permits and licenses, and contracting the shipments have led to numerous delays and cancelled shipments. Trade in higher value products, such as apples, pears, grapes, nectarines and other fruits and nuts, has been dramatically reduced, as they are not included among the list of high priority products for which foreign exchange is available.

Venezuela also requires that importers obtain sanitary and phytosanitary (SPS) permits from the Agriculture Ministry for most agricultural imports. U.S. industry has raised concerns about the use of SPS permits to unreasonably restrict agricultural and food imports as well as the consistency of Venezuela's SPS practices with WTO requirements. These practices have particularly affected trade in pork, poultry, beef, apples, grapes, pears, nuts, onions and potatoes. Industry representatives have reported that Venezuela also restricts the sale of nutritional supplements or natural products to pharmacies, limiting direct sales efforts.

Although the Venezuelan government has not published requirements on absorption agreements, it has been common practice for years to require the purchase of domestic production before issuing import licenses or permits. Imports of yellow corn are dependent upon the purchase of local sorghum and/or white corn. Soybean imports are dependent upon the purchase of "locally produced" soybean meal, and permits for grape and black bean imports have been tied to the purchase of local product. The use of such absorption requirements is extremely subjective, since Venezuela lacks a good statistical system to track levels of domestic crop production.

In 2002, the United States Trade Representative initiated formal WTO consultations with Venezuela on its agricultural import license procedures for a wide-range of products. Canada, the EU, Chile, Argentina, and New Zealand participated in the first round of consultations. Official consultations were held in November 2002 in Geneva. A subsequent exchange of letters on the SPS permit system was conducted in 2003. During the most recent meeting of the WTO Committee on Agriculture in November 2004, the United States again raised questions about permit and licensing procedures. At that time, Venezuela argued that these questions should be discussed under the WTO Sanitary and Phytosanitary Committee.

Venezuela prohibits the importation of used cars, used buses, used trucks, used tires and used clothing. No other quantitative import restrictions exist for industrial products. Some products such as cigarette paper, bank notes, weapons of war and certain explosives can only be imported by government agencies (tax authorities calculate the cigarette tax on the volume of cigarette paper imported by the manufacturers). The government can delegate authority to import on its behalf, and can place orders for such products with the local sales agents of the foreign manufacturers.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Some Venezuelan importers of U.S. products have alleged that Venezuela applies product standards more strictly to imports than to domestic products. The certification process is expensive. The Venezuelan Commission for Industrial Standards normally requires certification from independent laboratories located in Venezuela but at times will accept a certificate from independent laboratories elsewhere.

In 2003 the Government of Venezuela passed Decree 2444, which requires importers of goods to Venezuela to obtain pre-shipment inspections of all imports. Four companies are certified to conduct these inspections: Bivac Venezuela (Veritas Group), SGS Trade Assurance Services, COTECNA, and Intertek Foreign Trade Standards.

Venezuela’s labeling regulations, which became effective in 2002, establish the register of domestic manufacturers and importers of clothing and footwear and minimum labeling requirements for all clothing and footwear products marketed in Venezuela. Imported products require customized labels that include detailed information about the importer of the goods.

GOVERNMENT PROCUREMENT

Venezuela’s government procurement law covers purchases by government entities, national universities and autonomous state and municipal institutions. The law requires a contracting agency to prepare a budget estimate for a given purchase based on reference prices maintained by the Ministry of Production and Commerce. This estimate is to be used in the bidding process. The law forbids discrimination against tenders based on whether they are national or international. However, the law also states that the President can mandate temporary changes in the bidding process "under exceptional circumstances" or in accordance with "economic development plans" to promote national development, or to offset adverse conditions for national tenders. These measures can include margins of domestic price preference; reservation of contracts for nationals; requirements for domestic content, technology transfer and/or the use of human resources; and other incentives to purchase from companies domiciled in Venezuela. For example, government decree 1892 establishes a 5 percent preference for bids from companies with over 20 percent local content. In addition, half of that 20 percent of content must be from small to medium- sized domestic enterprises.

In an effort to move away from proprietary software products, the Government of Venezuela in 2004 introduced a law mandating the use of open-source software in government and public institutions. This is expected to reduce the demand for U.S. software products somewhat, though much software currently in use is unlicensed or pirated.

In the international arena, Venezuela has reinstituted state controlled purchases of basic food products for its new internal distribution system, Mercal, a network of state-owned stores aimed at low-income Venezuelans. The state-trading entity, CASA, has purchased, to date, sugar, rice, wheat flour, black beans, milk powder, edible oil, margarines, poultry and eggs from a variety of countries. The private sector has complained that CASA has an unfair advantage in that its access to dollars is assured, as is its access to import licenses and permits. Furthermore, CASA, as a government entity, imports products without tariffs and customs duties.

Venezuela is not a signatory to the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

Exporters of selected agricultural products -- coffee, cocoa, some fruits and certain seafood products -- are eligible to receive a tax credit equal to 10 percent of the export's value.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Venezuela is a member of the World Intellectual Property Organization (WIPO). It is also a signatory to the Berne Convention for the Protection of Literary and Artistic Works, the Geneva Phonograms Convention, the Universal Copyright Convention, and the Paris Convention for the Protection of Industrial Property. Venezuela implements its obligations under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) through Andean Community Decision 486.

The Venezuelan Industrial Property Office (SAPI) leaves much room for improvement, and its actions and occasional publicly stated antagonism towards IPR often draw criticism from IPR advocates and rights holders. Protection of IPR is also hindered by the lack of adequate resources for the Venezuelan copyright and trademark enforcement police (COMANPI) and for the special IPR prosecutor's office. Venezuela’s tax agency SENIAT is promoting several measures to fight piracy in an effort to reduce tax evasion, including a new anti-piracy law and the introduction of a tax on street vendors. According to industry representatives, SENIAT seems to be a promising enforcement entity due to its technical and financial capabilities.

Unfortunately, pirated software, music and movies remain readily available throughout the country, and levels of piracy are increasing. In the 2004 Annual Review, Venezuela remained on USTR's Special 301 "Watch List."

Patents and Trademarks

Venezuela provides the legal framework for patent and trademark protection through Andean Community Decision 486 and the 1955 National Industrial Property Law. Andean Community Decision 486 takes major steps towards bringing Venezuela into WTO TRIPS compliance. However, without corresponding local laws, Venezuela is not completely TRIPS compliant. Andean Community Decision 345 covers patent protection for plant varieties.

U.S. companies remain concerned about the impact of the Andean Tribunal’s 2002 interpretation of Articles 14 and 21 of Decision 486, which do not allow for the patenting of “second-use” products. Under pressure from the Andean Community and in line with some changes in leadership at SAPI, Venezuela has revoked previously issued patents. Very few patents were awarded in 2004. Since 2002, Venezuela's food and drug regulatory agency (INH) began approving the commercialization of new drugs which were the bioequivalents of already patented drugs, thereby denying the patent-holding companies protection of their test data. In effect, the government now allows the test data of patented drugs or those for which patents have been requested, most of which required lengthy and expensive development, to be used by others seeking approval for their own unlicensed versions of the same products.

Copyrights

Andean Pact Decision 351 and Venezuela's 1993 Copyright Law provide the legal framework for the protection of copyrights. The 1993 Copyright Law is modern and comprehensive and extends copyright protection to all creative works, including computer software. A National Copyright Office was established in 1995 and given responsibility for registering copyrights, as well as for controlling, overseeing and ensuring compliance with the rights of authors and other copyright holders. Industry experts are concerned about a proposed new copyright law which would require the mandatory registry of works in order to receive protection, reduce protection terms, hamper distribution agreements and increase royalties.

The Venezuelan copyright and trademark enforcement branch of the police (COMANPI) continues to provide copyright enforcement support with a small staff of permanent investigators. A lack of personnel, coupled with a very limited budget and inadequate storage facilities for seized goods, has forced COMANPI to work with the National Guard and private industry to improve enforcement of copyrighted material. COMANPI can only act based on a complaint by a copyright holder; it cannot carry out an arrest or seizure on its own initiative, which leads to weaker enforcement.

SERVICES BARRIERS

Venezuela maintains restrictions on a number of service sectors. Venezuela requires that certain professions be licensed in Venezuela (e.g., engineers, architects, economists, business consultants, accountants, lawyers, doctors, veterinarians and journalists). Foreign nationals wishing to practice these professions in Venezuela must have their credentials validated by a Venezuelan university, provided that a reciprocity agreement exists with their country of origin. Some (particularly government-related) accounting and auditing functions require Venezuelan citizenship, and only Venezuelan citizens may act as accountants for companies with publicly traded stock greater than 25 percent. A foreign lawyer cannot provide legal advice on foreign or international law without being licensed in the practice of Venezuelan law.

Foreigners are required to establish a commercial presence for the provision of engineering services. Foreign consulting engineers must work through local firms or employ Venezuelan engineers. There is a law governing public service tenders, which gives preferential treatment to Venezuelan firms for projects financed with public funds. Foreign participation is restricted to a maximum of 19.9 percent in professional firms.

Venezuela limits foreign equity participation (except from other Andean Community countries) to 20 percent in enterprises engaged in television broadcasting, radio broadcasting and Spanish language newspapers.

The government enforces a "one-for-one" policy that requires foreign musical performers giving concerts in Venezuela to share stage time with national entertainers. There is also an annual quota regarding the distribution and exhibition of Venezuelan films. At least half of the television programming must be dedicated to national programs, and at least half of FM radio broadcasting must be dedicated to Venezuelan music.

Finally, in any enterprise with more than 10 workers, foreign employees are restricted to 10 percent of the work force, and Venezuelan law limits foreign employee salaries to 20 percent of the payroll.

Financial Services

By signing the 1997 WTO Financial Services Agreement, Venezuela made certain commitments to provide market access for banking, securities, life and non-life insurance, reinsurance and brokerage activities. Venezuela did not make commitments on pensions, or on maritime, aviation and transportation insurance, and it reserved the right to apply an economic needs test as part of the licensing process.

Rules governing civil aviation, maritime activities and transportation insurance were issued in 2001 in a package of 49 laws passed under enabling powers granted to President Chavez in 2000. Many of the laws still need implementing regulations. The impact of the legislation is, therefore, still unclear.

INVESTMENT BARRIERS

The government continues to control key sectors of the economy, including oil, petrochemicals and much of the mining and aluminum industries. Venezuela began an ambitious program of privatization under the Caldera administration, but under President Chavez further privatization has been halted.

Foreign investment continues to be restricted in the petroleum sector. The exploration, production, refinement, transportation, storage and foreign and domestic sale of hydrocarbons are reserved to the state. However, private companies may engage in hydrocarbons-related activities through operating contracts or through equity joint ventures with the state-owned oil company Petroleos de Venezuela, S.A. (PDVSA). The Venezuelan constitution reserves ownership of PDVSA to the Venezuelan government. Sales to foreign investors of interests in subsidiaries and affiliates of PDVSA are permitted. In the early 1990s, the Venezuelan government partially opened the sector to private investment in order to promote new petrochemical joint ventures and to bring inactive oil fields back into production. Almost 60 foreign companies, representing 14 different countries, participated in this process. PDVSA and foreign oil companies signed 33 operating contracts for marginal fields after three rounds of bidding.

The Hydrocarbons Law of 2001 has raised concerns in the industry as it mandates a minimum 50 percent national participation in future projects and increases most royalties paid to the government from 16.67 percent to 30 percent. No projects have been negotiated yet under this law. The Gaseous Hydrocarbons Law offers more liberal terms, and the Venezuelan government has sought foreign investment to develop offshore natural gas deposits near the Orinoco delta. In October 2004, the Venezuelan government eliminated a royalty holiday granted to joint venture projects relating to the development of Venezuela's extra heavy crude oil reserves. These joint-venture projects, known as "the strategic associations," were created during the partial opening of the sector and received 35-year contracts that were endorsed by the National Congress.

The government passed legislation in 1998 aimed at introducing domestic and foreign competition into the domestic gasoline market. The law allows foreign and non-governmental Venezuelan investors to own and operate service stations, although the government retains the right to set product prices. The government has not raised gasoline prices in several years, and currency devaluations and a high inflation rate have eliminated service station profit margins.

Hydroelectric power generation in Venezuela is reserved to the state, although private sector participation is permitted in transmission and distribution. In early 2000, the U.S. power generating company, AES Corporation, successfully took control, by means of a stock swap, of Electricidad de Caracas (EDC), the company that provides power to the Caracas metropolitan area.

A range of other natural resources -- including iron ore, coal, bauxite, gold, nickel and diamonds -- is gradually being opened to greater private investment by means of strategic alliances. In 1996, Corporacion Venezolana de Guayana (CVG), a state-owned umbrella corporation with mining interests, announced its first joint venture with a foreign company to develop the Las Cristinas gold mine. President Chavez personally announced the beginning of operations in May 1999. Low gold prices, however, forced CVG and its partners to suspend the project. In 2001, CVG revoked the concession on grounds of the concessionaire's alleged inability to comply with the contract by not developing the reserves as stipulated, and the concession has been granted to another firm. In April 1999, the Venezuelan government updated the 1945 Mining Law in order to encourage greater private sector participation in mineral extraction. However, in 2003, in line with a policy to centralize mining rights under the Ministry of Energy and Mines, the government ratified a 1996 decree requiring CVG to turn over to the Ministry the original files on concessions granted by CVG. In a separate matter, in September 2003 the Ministry acted unilaterally to terminate some concession areas of a private diamond mining company in southern Venezuela, alleging failure to comply with the terms of the concession. As of the end of 2004 this matter remained unresolved.

In early 2005, President Chavez reorganized the ministries that govern the energy and mining sectors as well as those governing commerce and industry. One result of this restructuring was to increase control over basic industries at the ministerial level and to strengthen the state owned CVG, which in addition to mining controls steel and aluminum production and electricity generation. Under a new board of directors, named in February 2005, CVG has announced a review of all existing contracts between CVG companies and third parties.

VIETNAM

TRADE SUMMARY

The U.S. trade deficit with Vietnam was $4.1 billion in 2004, an increase of $882 million from $3.3 billion in 2003. U.S. goods exports in 2004 were $1.2 billion, down 12.2 percent from the previous year. Corresponding U.S. imports from Vietnam were $5.3 billion, up 15.8 percent. Vietnam is currently the 57th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Vietnam were $3.3 billion in 2003 (latest data available), and U.S. imports were $1.7 billion. Sales of services in Vietnam by majority U.S.-owned affiliates were $1.1 billion in 2002 (latest data available), while sales of services in the United States by majority Vietnam-owned firms were $325 million.

The stock of U.S. foreign direct investment (FDI) in Vietnam in 2003 was $3.7 billion, up from $2.8 billion in 2002. U.S. FDI in Vietnam is concentrated largely in the manufacturing, utilities, and banking sectors.

IMPORT POLICIES

Tariffs

On September 1, 2003, Vietnam implemented the ASEAN Harmonized Tariff Nomenclature (AHTN), which is based upon the international Harmonized Tariff System of 2002. The new system consists of 10,689 lines (4200 more than the old one), of which 5,300 lines are at four and six digits and 5,400 lines are at eight digits. There are now fifteen tariff rate bands (down from twenty) and the simple average tariff rate increased from 16.8 percent to 18.2 percent. The tariff bands are applied within the tariff categories described below. In implementing the new tariff system, the government of Vietnam raised tariff rates on 195 items and reduced them on 106. Protection on 72 items, except for welding steel tubes, was converted from price differential surcharges to tariffs. Tariff rates on petrol and oils (heading 2709 and 2710) are not specified in the new schedule.

Currently, there are three categories of tariff rates: normal trade relations (NTR) / most favored nation (MFN) rates that apply to about 75 percent of total imports from about eighty countries that have bilateral trade agreements with Vietnam, including the United States; Common Effective Preferential Tariff (CEPT) rates that apply to imports from ASEAN countries; and general tariff rates (50 percent higher than NTR/MFN) that apply to all other countries. Under the terms of the U.S.-Vietnam Bilateral Trade Agreement (BTA), Vietnam is obligated to significantly reduce tariffs by an average of about one-third to one-half on a broad range of U.S. imports (approximately 244 lines) over a period of three years beginning on December 10, 2001. A Ministry of Finance Decision, effective December 10, 2004, reduced the MFN tariff rates on more than 1100 tariff lines, including the lines covered by the BTA. These tariff reductions apply to imported goods having certificates of origin from the United States as well as imports from other countries that have an MFN agreement with Vietnam.

The National Assembly retains authority over setting tariff bands for each product and the government is free to adjust applied tariffs within the bands. There is no tariff schedule published online, and it is often difficult to determine when and by how much tariffs have changed.

Non-tariff barriers

Non-tariff barriers (NTBs) were introduced in Vietnam when the country shifted from a centrally-controlled economy toward more market-oriented trade in the late 1980s to early 1990s, and they quickly became a key component of Vietnam's trade policy. In the past few years, Vietnam has made significant progress in reducing the use of NTBs and, under the terms of the BTA, Vietnam agreed to eliminate all non-tariff barriers, including import and export restrictions, quotas, licensing requirements, and controls for all product and service categories over a period of three to seven years, depending on the product.

Import prohibitions: Vietnam currently prohibits the commercial importation of the following products: arms and ammunition, explosive materials (not including industrial explosives), military technical equipment and facilities, narcotics, toxic chemicals, "depraved and reactionary" cultural products, firecrackers, some children's toys, cigarettes, second-hand consumer goods, right-hand drive motor vehicles, used spare parts for vehicles, used internal combustion engines of less than 30 horsepower, asbestos materials under the amphibole group, various encryption devices, and encryption software. Vietnam prohibits importation and registration of motorcycles with engine capacity exceeding 175 cubic centimeters for traffic safety purposes. Importation of such motorcycles is allowed only for special purposes such as for the armed forces, security personnel, or for competitive sports.

Quantitative restrictions and non-automatic licensing: Vietnam has been phasing out the use of quantitative restrictions on imports. An April 2001 Decision of the Prime Minister phased-out quantitative restrictions on imports with the exception of sugar (which will remain until 2005). A September 2003 government decision established conditions for importing and re-exporting petroleum. This trading is subject to annual licensing and price regulation. Quantitative limitations on exports in most sectors have been eliminated, with the exception of textiles, garments, and a list of sensitive items.

In May 2003, the Prime Minister issued a decision to implement tariff-rate quotas (TRQs) on certain agricultural products that were not previously under quotas. A May 2003 government decision applied the TRQs to seven items starting in January 2004: cotton, raw tobacco, salt, milk, condensed milk, corn, and chicken eggs. A Ministry of Trade Circular issued in December 2003 provided details on management of these TRQs, established the in-quota volumes for tobacco and salt and set the quota volumes for cotton, milk, condensed milk, corn and eggs equal to demand. In practice, only salt and raw tobacco exporters are currently restricted by quotas. The Ministry of Trade has primary responsibility for establishing quota volumes and allocation of quotas, while the Ministry of Finance determines the in- and out-of quota tariff rates.

Currently all state companies are required to apply for annual quota allocations in order to import foreign pharmaceutical products.

Special authority regulation: Previously, importers required approval from the relevant ministry(ies) to import many goods. This system was changed in 2001. Now, seven ministries and agencies are responsible for overseeing a system of minimum quality/performance standards for animal and plant protection, health safety, local network compatibility (in the case of telecommunications), money security, and cultural sensitivity. Goods that meet the minimum standards can be imported upon demand and in unlimited quantity and value.

Foreign Exchange system: As of April 2003, Vietnam eliminated the foreign exchange surrender requirement. Previously, in 1998, the State Bank of Vietnam (SBV) issued a foreign exchange surrender requirement for all exporters, including foreign invested enterprises. The requirement was initially set at 80 percent of foreign exchange balances, but was subsequently reduced to 30 percent as of May 2002.

May 2000 amendments to the Law on Foreign Direct Investment (FDI) allowed FDI enterprises to purchase foreign currency at authorized banks to finance current and capital transactions and other permitted transactions. Controls on current account transactions have been liberalized. A 1998 Decree allowed both residents and non-residents to open and maintain foreign exchange accounts with authorized banks in Vietnam. A 2001 Circular permitted foreign investors to transfer abroad profits and other legal income upon presentation of relevant documents to the authorized banks. A 2003 decree contains the government of Vietnam's guarantee to assist in the balancing of foreign currency for foreign invested enterprises and foreign business cooperation parties that invest in the construction of infrastructure and certain other important projects in the event that banks permitted to trade foreign currency are unable to fully satisfy their foreign currency demand.

Customs: Under the terms of the BTA, Vietnam was obligated by December 2003 to apply transaction value for U.S. imports and to ensure that no administrative fee or charge imposed by customs authorities in connection with importing or exporting any good exceeds the actual cost of the service provided by Customs. In June 2002, the government issued Decree 60 establishing rules for customs valuation based on transaction value, in accordance with WTO principles. Subsequently the Ministry of Finance issued Circular 118 (December 2003) implementing the provisions of Decree 60 and Circular 87 (August 2004) abolishing the use of all minimum import prices. Vietnam also committed to apply transaction value to imports from ASEAN countries as well as 56 other countries on the basis of reciprocity. These changes have significantly improved customs valuation in Vietnam over the last year. However, application of Customs Valuation

Agreement principles is not entirely uniform and importers complain about the low level of automation of Vietnam's customs system. The government plans to amend the Customs Law of 2000 by May 2005 in order to address remaining problems and facilitate implementation of a $70 million World Bank loan-supported customs modernization project in Vietnam.

Trading rights: The government of Vietnam currently maintains different regulations on trading rights for domestic and foreign-invested enterprises. Domestic Vietnam-owned enterprises are entitled to import in accordance with the business line(s) prescribed in their business registration certificates. They are not required to apply for an import license, except for goods for which the Ministry of Trade (MOT) requires a non-automatic import license. Foreign-invested enterprises are not permitted to import goods freely in Vietnam. Foreign-invested enterprises are allowed only to import goods used as inputs in the manufacturing process, as well as machinery equipment, transportation means and materials used in the construction and installation of their project in accordance with their investment license.

Under the terms of the BTA, beginning in December 2004, enterprises with capital directly invested by U.S. nationals and companies in production and manufacturing will be able to engage in trading activities in most products and will be able to enter into joint ventures with Vietnamese partners to engage in trading activities in all products, as long as the U.S. partner holds no more than a 49 percent share in the venture. Under the BTA, beginning in December 2008, U.S. companies will be able to establish wholly-owned trading companies in Vietnam. The right to trade in certain goods is subject to a phase-in period.

Taxes: In December 2002, the government issued a strategy for the auto sector with a primary goal of significantly increasing the local content in domestically produced vehicles. At the same time, the Ministry of Finance issued a decision to raise the import duty rates for automobiles produced from kits (CKDs). A joint campaign waged by affected foreign auto companies and their representative Embassies resulted in postponement of the change. However, in May 2003, the National Assembly passed a Ministry of Finance proposal to impose a 10 percent VAT on all cars and increase the special consumption tax (SCT) on cars manufactured from CKDs starting in 2004 and going up to 80 percent on some models by 2007. The SCT was increased from 5 to 24 percent in January 2004 and from 24 to 41 percent in January 2005. Under a Ministry of Finance 2004-2010 roadmap for the harmonization of tariff rates applied to CKDs and completely built units (CBUs), MFN tariff rates applied to CKDs will rise 5 to 10 percent per year until 2008. The changes to the tax and tariff policy were made years after foreign auto manufacturers had committed significant resources to Vietnam. They have driven down sales and are endangering the profitability of foreign automakers in Vietnam.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Sanitary and Phytosanitary Measures

Vietnam is currently working on the establishment of an SPS regime based on international standards, guidelines and recommendations. Its existing regime is based on CODEX and FAO/WHO standards, the standards of regional or developed countries, or national standards. Vietnam has an inter-ministerial Working Group that coordinates SPS activities and the Ministry of Agriculture and Rural Development (MARD) currently serves as a general enquiry point for information on sanitary and phytosanitary requirements. Specific responsibility for sanitary and phytosanitary controls, plant and animal quarantine, health quarantine and fisheries inspection is further assigned to other Ministries and agencies.

In December 2003, the government banned imports of U.S. beef because of a fear of BSE (Bovine Spongiform Encephalopathy), a degenerative neurological disease affecting the central nervous system in cattle. On October 5, the Ministry of Agriculture and Rural Development issued a notice that it would allow imports of U.S.-origin boneless beef, with the conditions that the beef not originate from the state of Washington and only be consumed in hotels and restaurants. After much discussion, MARD lifted the restriction on Washington State. Boneless beef from the United States is now permitted entry into Vietnam. In early January 2005, the first shipment of U.S. boneless beef arrived in Vietnam since the December 2003 ban.

Standards and Technical Barriers to Trade

The main ministry involved in standardization and quality requirements is the Ministry of Science and Technology (MOST). The Directorate for Standards and Quality (STAMEQ) under the MOST is generally responsible for advising the government on issues related to standards, measurements, and quality. There are currently three levels of standards: national standards, sectoral standards, and company standards. The system is complicated and not always transparent. Some items are subject to voluntary application, while other items are subject to regulation by the line ministries. Exporters and importers must obtain a permit from the line ministries or a receipt showing an inspection is in process for the controlled items to be allowed through customs.

On March 25, 2003 Vietnam's TBT enquiry and notification point was formally established in the offices of STAMEQ. However, this enquiry point will not be fully functional until the end of 2005 or upon Vietnam's accession to the WTO.

Pharmaceutical companies face significant barriers to trade. The Ministry of Health now prohibits the registration or re-registration for import of 11 pharmaceutical products (reduced from 23) that are produced domestically. In addition, pharmaceutical companies complain that the registration process for pharmaceuticals lacks transparency. Guidelines and regulations are unclear and/or are not applied in a consistent manner. The Ministry of Health issues product visas with validity periods as short as one year.

The government requires that all pharmaceutical raw materials be imported into Vietnam within six months of the date of manufacture. Additionally, foreign manufacturers of vaccines are required to conduct clinical trials in Vietnam before being permitted to register their vaccines for sale.

GOVERNMENT PROCUREMENT

Government procurement practices can be characterized as a multi-layered decision-making process, which often lacks transparency and efficiency. Although the Ministry of Finance allocates funds, various departments within the ministry or agency involved determine government procurement needs. Competition for government procurements may take any of several forms: sole source direct negotiation, limited tender, open tender, appointed tender, or special purchase. Currently, ministries and agencies have different rules on minimum values for the purchase of material or equipment, which must be subject to competitive bidding. High-value or important contracts such as infrastructure (except World Bank, Asian Development Bank, UNDP, or bilateral official development assistance projects) require bid evaluation and selection and are awarded by the Prime Minister's office or any other competent body. No consolidated or regular official listing of government tenders exists; however, some solicitations are announced in the both Vietnamese and English language newspapers.

EXPORT SUBSIDIES

Export credit is very limited in Vietnam. The Export Promotion Fund managed by the Ministry of Finance, provides subsidies in the form of interest rate support (full or partial refund of interest incurred on ordinary bank loans), direct financial support (to first-time exporters, for exports to new markets, or for goods subject to major price fluctuations) and export rewards and bonuses. Since 1998, the average annual export reward provided to eligible enterprises has ranged from $2,900 to $4,710. Provision of export bonuses, originally targeted for exports of agricultural products, was expanded in 2002 to include non-agricultural products such as handicrafts, rattan and bamboo ware, plastic products and mechanical products. Since 2001, the Export Promotion Fund has also provided support to enterprises for expenditures on trade promotion activities.

Since September 2001, the Development Assistance Fund has administered an export credit program that has provided short-term loan guarantees, medium and long-term investment loans, post-investment interest rate support and investment credit guarantees to domestic enterprises.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Vietnam is a member of WIPO and is a signatory to the Paris Convention for the Protection of Industrial Property. It has acceded to the Patent Cooperation Treaty and the Madrid Agreement. On October 26 2004, Vietnam joined the Berne Convention on Protection for Literary and Artistic Works. Vietnam is also obliged, under the terms of the 1997 U.S.-Vietnam Bilateral Copyright Agreement, to provide U.S. copyrights protection on a national treatment basis in accordance with the terms of the Berne Convention. Under the terms of the BTA, Vietnam was obligated by December 2003 to make its system for protecting IPR, including enforcement, consistent with the WTO TRIPS agreement. Considerable progress has been made over the past few years in establishing the legal framework for IPR protection. New legislation in 2004 included more detailed regulations on plant varieties and administrative sanctions against counterfeiting. However, the legal reform process is not yet complete. The government has instructed the Ministry of Science and Technology (MOST) and the Ministry of Culture and Information (MOCI) to draft a separate law on intellectual property rights. The GVN plans to submit the law to the National Assembly for approval in 2005.

Enforcement of IPR protection remains extremely weak. The BTA requires the government of Vietnam to provide expeditious remedies to prevent and deter infringement of IP rights, including particular judicial and administrative procedures, prompt and effective provisional measures secured by sufficient evidence, and criminal procedures and penalties for willful trademark counterfeiting or infringement of copyrights or neighboring rights on a commercial scale.

Patent and Trademarks

Trademark registration in Vietnam is relatively straightforward, although infringement is widespread and enforcement of administrative orders and court decisions finding IPR infringement remains problematic. Vietnam's laws offer some protection for foreign patent holders, but there are infringements. The National Office of Intellectual Property (NOIP), under the Ministry of Science and Technology, administers Vietnam's patent and trademark registration systems. NOIP has made significant progress in recent years to build adequate capacity to record and adjudicate patent and trademark claims, and is working with a number of foreign patent and trademark agencies to enhance its systems. Obtaining expeditious adjudication and administrative enforcement of patent and trademark violations remains difficult. Victims of infringement have encountered difficulties implementing NOIP enforcement decisions.

Pharmaceutical companies are concerned that Vietnam still lacks the legal provisions necessary to protect test data from unfair commercial use when it requires the submission of such data as a condition of approving the marketing of pharmaceutical products.

Copyrights

The Vietnam Office of Literary and Artistic Copyright is under the control and supervision of the Ministry of Culture and Information. Significant progress has been made in putting in place the legal framework required to protect copyrights, including those belonging to foreigners, but enforcement is almost non-existent. This is particularly true for certain categories of products, such as PC software, music and video CDs, VCDs, and DVDs. Industry estimates of piracy rates for software, music, and videos run as high as 92 percent. Local police authorities often are slow to act on administrative orders fining infringement and enforcing court decisions. After Vietnam joined the Berne Convention, the Ministry of Culture and Information made an effort to tighten copyright regulations on foreign musical and theatrical works. All event organizers must now obtain permission in writing from the copyright holders before performing their works.

SERVICES BARRIERS

Under the terms of the BTA, Vietnam agreed for the first time to liberalize a broad array of service sectors, including telecommunications, accounting, banking, and distribution services, and to apply MFN treatment to U.S. services suppliers in all sectors and for all modes of supply (with itemized exceptions). The BTA also incorporated the GATS (except Articles 3 and 4), Annex on Movement of Natural Persons, Annex on Telecommunications (except Articles 6 and 7), and the Telecommunications Reference Paper. Vietnam's commitments to liberalize market access on services are phased in over specified time periods depending on the sector. The commitments by sector are as follows:

Accounting, Auditing, and Bookkeeping Services: For the first three years under the BTA, licenses were granted on a case-by-case basis. The company must employ at least five persons with licenses to be a CPA in Vietnam who have practiced in Vietnam for more than one year. For the first two years under the BTA, firms with U.S. equity were only allowed to supply services to foreign-invested enterprises and foreign-funded projects in Vietnam. Two new decrees in 2004 revised the regulations for the accounting and auditing sectors. Government Decree 105 allows auditing firms to be established in the form of partnerships, private enterprises or foreign-invested enterprises. Decree 105 allows foreign-invested auditing firms to set up branches in Vietnam. Government Decree 129 allows accounting firms to be established in the form of limited liability companies, partnerships or private enterprises. Branching is not permitted.

Taxation Services: For the first five years under the BTA, licenses will be granted on a case-by-case basis, and firms with U.S. equity will only be allowed to supply services to foreign-invested enterprises and foreign-funded projects in Vietnam. Branching is not permitted.

Architectural, Engineering, and Computer Services: For a period of two years from the date of establishment and operation, U.S.-owned companies may only provide services with foreign-invested enterprises in Vietnam. U.S. companies have to be legally registered in the United States. Branching is not permitted.

U.S. companies and companies with U.S. directly-invested capital are not permitted to carry out topographic, construction, geological, meteorological, and environmental investigations; or technical investigations for designing rural-urban construction plans, unless otherwise authorized by the government of Vietnam.

Legal Services: Under the terms of the BTA, 100 percent equity ownership in companies, joint ventures, and branches are permitted. U.S. lawyers may not appear before Vietnam's courts. However, U.S. firms may advise on Vietnam's law if they hire persons with Vietnamese law degrees who satisfy the requirements applied to like Vietnamese practitioners. Branches of law firms may receive a five-year renewable license. In July 2003, the government promulgated Decree 87 significantly reforming the regulatory framework for the operations of foreign law practices and foreign law firms. The decree substantially broadened the scope of practice of foreign law firms in Vietnam. Foreign law practices are permitted to provide advice on foreign and international law in the areas of business, investment and commerce, which had been prohibited previously. By virtue of these reforms, foreign law firms may now offer a full range of legal services and employ Vietnamese lawyers.

Advertising Services and Market Research: Vietnam has not agreed to provide market access for advertising services for wines and cigarettes or for the cross-border supply of market research services. U.S. companies in these sectors may initially only establish a commercial presence through joint ventures or business cooperation contracts with Vietnamese partners. U.S. investment is limited to 49 percent of the legal capital for the first five years under the BTA, 51 percent for years six and seven, and is unlimited after that. Vietnam has not agreed to ensure national treatment for the cross-border supply of market research services.

Management Consulting: U.S. companies may only establish a commercial presence through joint ventures or business cooperation contracts. After the BTA has been in effect for five years, enterprises with 100 percent U.S. ownership will be permitted.

Telecommunication Services: Initially, the provision of basic telecommunications services, value-added telecommunications services, and voice telephone services are only permitted through business cooperation contracts with Vietnamese gateway operators. According to the terms of the BTA, U.S. value-added telecommunications service providers may establish joint ventures with Vietnamese partners with up to 50 percent equity ownership. These joint ventures may not, however, construct their own long-distance and international circuits. However, Vietnam's law does not yet provide specifically for joint ventures in the telecom sector, and the government has not issued any regulations or other documents specifically authorizing joint ventures with U.S. companies or clarifying the procedures for such partnerships in the telecom sector. Four years after entry-into-force of the BTA, U.S. basic telecommunications service suppliers can establish joint ventures with Vietnamese partners with up to 49 percent U.S. equity ownership. These joint ventures may not, however, construct their own long-distance and international circuits. Six years after entry-into-force of the Agreement, U.S. voice telephone service providers may establish joint ventures with Vietnamese partners with up to 49 percent U.S. equity ownership.

Audiovisual Services: Vietnam has not agreed to provide market access or national treatment for cross-border supply or consumption abroad of audiovisual services. U.S. service suppliers may establish a commercial presence only through a business cooperation contract or joint venture with a Vietnamese partner. For the first five years after entry-into-force of the BTA, U.S. ownership may not exceed 49 percent. After five years, U.S. ownership may not exceed 51 percent. The government strictly limits the importation of foreign films, videos, television and books. Numerous licensing, pricing and remittance restrictions exist. IPR protection for audio-visual products is ineffective, censorship is restrictive and rules are often applied in an ad-hoc manner.

Construction and Related Engineering Services: Vietnam has not agreed to provide market access or national treatment for the cross-border supply of construction and related engineering services. Branches are not permitted. For the first three years after their establishment and operation, 100 percent U.S.-owned enterprises could only provide services to foreign-invested enterprises in Vietnam. U.S. companies must be legally registered for operation in the United States.

Distribution Services: Vietnam does not provide market access or national treatment for the cross-border supply of distribution services. Three years after entry-into-force of the BTA, U.S. service providers may establish joint ventures with Vietnamese partners with up to 49 percent U.S. equity. After six years, U.S. ownership in joint ventures will be unlimited. After seven years, companies with 100 percent equity will be allowed. One retail outlet per firm may be established upon entry-into-force of the BTA, while additional outlets will be considered on a case-by-case basis. For some agricultural and industrial products, market access in this sector is subject to additional limitations, which will be phased out over a period of three to five years. There are a limited number of products for which Vietnam did not commit to allow distribution services.

Educational Services: Vietnam will not provide market access or national treatment for the cross-border supply of educational services. For the first seven years after entry-into-force of the BTA, U.S. companies may only establish a commercial presence through a joint venture. After that, schools with 100 percent U.S.-invested capital may be established. Foreign teachers employed by educational units with U.S.-invested capital must have five years teaching experience and be recognized by the Ministry of Education.

Insurance Services: Vietnam has agreed to allow market access for the cross-border supply of insurance services to enterprises with foreign invested capital or foreigners working in Vietnam; reinvestment services; insurance services in international transportation; insurance brokering and reinsurance brokering services; and advisory, claim settlement, and risk assessment services. Starting in 2005, U.S. companies can establish joint ventures with Vietnamese partners with up to 50 percent U.S. equity participation. After five years, 100 percent U.S.-invested companies may be established.

While the government has allowed foreign investment in both "life" and "non-life" insurance markets, access has been extremely limited for U.S. service providers (only one U.S. "life" insurer has been issued a 100 percent foreign-owned license to operate). Some joint ventures with Vietnamese companies have been allowed to convert to 100 percent foreign ownership, but the terms have been arbitrary and subject to the "ad hoc" approval of the government.

Companies with U.S.-invested capital cannot provide insurance for motor vehicle third party liability, insurance in construction and installation, insurance for oil and gas projects, or insurance for projects and construction of high danger to public security and environment. Vietnam agreed to eliminate this limitation for joint ventures as of December 2004. After six years, this limitation is eliminated for companies with 100 percent U.S. capital.

For the first 5 years after entry-into-force of the BTA, any company with U.S. capital must reinsure part of the accepted liabilities (currently at a minimum rate of twenty percent) through the Reinsurance Company of Vietnam.

Banking: Vietnam has not agreed to provide market access or national treatment for the cross-border provision of banking services, except for financial information services and advisory, intermediation, and other auxiliary services. U.S. banks may establish branches, joint ventures with Vietnamese banks, wholly owned U.S. financial leasing companies or joint venture financial leasing companies with Vietnamese partners. However, foreign branches cannot be opened in both Hanoi and Ho Chi Minh City (with full branch status) and operate as single legal entity.

Until 2005, the only legal form apart from banks and leasing companies in which U.S. companies could provide financial services was through joint ventures with Vietnamese banks. During the first nine years of the BTA, U.S. equity in joint venture banks must be between 30 percent and 49 percent. After nine years, 100 percent equity participation in subsidiary banks will be allowed. The government recently amended the Law on Credit Institutions, laying the groundwork for the establishment of 100 percent foreign-owned banks ahead of Vietnam's BTA obligations. A Decree on Foreign Banks (currently in draft) and an implementing circular need to be promulgated before this change will come into effect. It is expected that these regulations will be completed late in 2005.

The right of U.S. banks to accept Vietnamese currency deposits on the same basis as domestic banks is phased in over eight years for business clientele and ten years for retail depositors. After this, U.S. bank branches will be entitled to full national treatment. Vietnam is fulfilling this commitment by gradually allowing U.S. banks to increase the amount of deposits in Vietnamese Dong (i.e. the local currency) relative to the branch's legal paid-in capital with the ratio presently at 400 percent for legal persons and 350 percent for natural persons. (Prior to entry-into-force of the BTA, this ratio was 25 percent.) In addition, financial institutions with U.S. equity cannot issue credit cards on a national treatment basis until eight years after entry-into-force of the BTA. U.S. banks are now allowed to place automatic teller machines outside their office on a national treatment basis.

Vietnam reserved the right to limit, on a national treatment basis, equity investment by U.S. banks in privatized Vietnamese state-owned banks.

U.S. bank branches, subsidiaries, or U.S.-Vietnam joint ventures must obtain a license to establish a commercial presence in Vietnam. A U.S. parent bank must provide minimum capital of $15 million to establish a branch. Establishing a U.S.-Vietnam joint venture bank or a U.S. bank subsidiary requires minimum capital of $10 million. Authorized capital levels for state-owned commercial banks, joint-stock commercial banks, investment banks and joint venture banks are set at more advantageous levels.

Until 2005, financial institutions with 100 percent U.S. equity ownership may not take an initial mortgage interest in land use rights. Starting in 2005, these institutions will be allowed to take an initial mortgage interest in land-use rights held by foreign-invested enterprises, and may use mortgages or land-use rights for the purpose of liquidation in case of default.

Establishing a wholly owned subsidiary of a U.S. financial leasing company or a joint venture leasing company requires three consecutive profitable years, and $5 million in legal capital.

Vietnam was not obligated, until December 2004, to provide national treatment with respect to access to central bank rediscounting, swap, and forward facilities. However, in 2003, the State Bank of Vietnam allowed one U.S. bank with branches in Vietnam (and some local banks) to provide swap service on a pilot basis. In May 2004, the State Bank of Vietnam issued Decision 648 allowing commercial banks to provide forward and swap facilities to their clients.

Licenses for foreign banks currently are limited in validity to only 20 to 30 years and extensions (if any) are subject to the approval of the State Bank of Vietnam.

Non-banking Financial Services: The BTA allows 100 percent U.S. equity in financial leasing and in other leasing after 3 years. Government Decree 79 issued in 2002 permits the establishment and operation of finance companies in Vietnam, including joint venture and wholly foreign-owned finance companies.

Securities-Related Services: Vietnam has not agreed to provide market access or national treatment for the cross-border supply of securities-related services. Non-bank U.S. securities service suppliers may only establish a commercial presence in Vietnam in the form of a representative office. In 2003 the government issued Decree 144 on Securities and Securities Trading, allowing foreign investment in securities investment funds and fund management companies. Government Decision 146 issued in July 2003 limited foreign capital contribution in joint venture security companies or joint venture fund management companies to 49 percent.

Health-Related Services: U.S. operators may provide services through the establishment of 100 percent U.S.-owned operations, joint ventures with Vietnamese partners or through business cooperation contracts. The minimum investment capital is $20 million for a hospital, $2 million for a polyclinic, and $1 million for a specialty unit.

Tourism and Travel-Related Services: U.S. companies may establish a commercial presence to provide hotel and restaurant services, provided that this is done in conjunction with investment for the construction of a hotel. The commercial presence may take the form of a business cooperation contract, a joint venture with Vietnamese partners, or a company with 100 percent U.S. equity investment.

There are limitations with respect to travel agencies and tour operators. U.S. companies supplying these services may establish a commercial presence only through a joint venture with Vietnamese partners and can initially only contribute 49 percent of the capital. Starting in January 2005, 51 percent participation is allowed, and all limitations will be abolished after five years. Tourist guides in joint ventures must be Vietnamese citizens. Service supplying companies with U.S.-invested capital may only supply inbound service.

INVESTMENT BARRIERS

At present, the government of Vietnam maintains an extensive investment licensing process, which is characterized by stringent and time-consuming requirements that are frequently used to protect domestic interests, limit competition, and allocate foreign investment rights among various countries. Foreign businesses are permitted to remit profits, share revenues from joint ventures, incomes from services and technology transfers, legally owned capital, and properties in hard currency. Foreigners are also allowed to remit royalties and fees paid for the supply of technologies and services, principal and interest on loans obtained for business operations, and investment capital and other money and assets under their legitimate ownership.

The BTA provides a broad range of benefits to U.S. investors in Vietnam that should significantly enhance the investment environment for U.S. firms. Vietnamese investment obligations under the BTA include: providing national and most-favored-nation treatment, except where explicit exceptions have been made; ensuring compensation for expropriation consistent with international standards; and guaranteeing access to third-party investor-state dispute settlement. In practice, however, recognition and enforcement of foreign arbitral awards in Vietnam currently remains unpredictable.

In addition, Vietnam is obligated under the BTA to gradually discontinue application of any Trade-Related Investment Measures (TRIMS) or performance requirements inconsistent with the WTO TRIMS Agreement.

Under the BTA, Vietnam retained the right to require that an investment project export at least eighty percent of its production for seven years in the following sectors: cement; paint; toiletry tiles and ceramics; PVC and other plastics; footwear; clothing; construction steel; detergent powder; tires and inner tubes for cars and motorbikes; NPK fertilizer; alcoholic products; tobacco; and paper. In December 2001 (three days prior to entry-into-force of the BTA), Ministry of Planning and Investment Decision 718 revised the list of products subject to an export requirement. However, many of the products identified in Decision 718 are not in the list agreed upon in the BTA. According to Decision 718, Vietnam currently has an eighty percent export requirement for: motorcycles; minibuses and trucks (less than 10 ton); some irrigating pumps; medium voltage, low voltage and normal electric transmission cables; cargo ships, audio-visual products; aluminum profiles products; construction glass; NPK fertilizer; PVC; bicycles and bicycle parts; transformers under 35 KV; and diesel motors under 15 CV.

Vietnam is also obligated to refrain from imposing requirements to transfer technology as a condition for the establishment, expansion, acquisition, management, conduct, or operation of an investment. Vietnam currently imposes a number of performance requirements with respect to the establishment of an investment and/or the receipt of a benefit or incentive. Vietnam retains restrictions on foreign shareholding in Vietnamese companies, although the ratio has been raised from twenty to thirty percent. In March 2003, the government issued Decree 27 amending the Law on Foreign Investment, removing trade balancing requirements and foreign exchange controls. In April 2003, the government issued a decision to reduce the foreign exchange surrender requirement to zero percent.

Decree 27 also now allows foreign investors to recruit Vietnamese workers directly, without having to go through labor recruitment agencies. However, in September 2003, Government Decree 105, drafted by the Ministry of Labor, Invalids and Social Affairs, established a regulation limiting all enterprises operating in Vietnam to employing foreign nationals at the lesser of: (1) a maximum rate of 3 percent of their total work force; or (2) 50 persons. Despite repeated complaints from the foreign business community, the government appears unwilling to lift the cap. Proposed amendments to the Decree may provide exemptions for certain sectors and types of employment and eliminate the 50-person limit.

In the BTA, Vietnam committed to gradually shift from an investment licensing regime to an investment registration regime for most sectors. According to Decree 27, the following types of investment are no longer subject to investment licensing: investment projects that export eighty percent of products; investments in “encouraged” or “specially encouraged” projects located in industrial zones (with some exceptions); and investment in the manufacturing sector with a value of up to $5 million in investment capital.

According to Government Decree 45 (from 1998) the royalty rate for technology transfer cannot exceed 5 percent of the “net selling price” of the products produced with the technology. Decree 45 also narrowly defines the “net sales price” to which the royalty is applied, resulting in very small royalties.

ELECTRONIC COMMERCE

To date, electronic commerce has not made much progress in Vietnam. Obstacles to its development include: the low number of Internet subscribers in-country, obtrusive firewalls, limited bandwidth and other problems with the Internet infrastructure, limitations of the financial system (including the low number of credit cards in use), and regulatory barriers. However, recent developments to facilitate the growth of electronic commerce in Vietnam include legal acceptance of e-signatures and implementation of the electronic inter-bank transaction system. The number of online transactions has been increasing. The National Assembly Committee for Science, Technology and Environment will be drafting an e-transaction law, which will include electronic commerce issues. The Committee expects to submit the draft to the National Assembly for approval in late 2005.

The government of Vietnam continues to attempt to keep close control of all websites established in Vietnam. In October 2002, the government of Vietnam passed a new regulation on the establishment and modification of websites. The regulation requires domestic and foreign agencies, organizations, and enterprises to obtain a license from the Ministry of Culture and Information before establishing new websites. The Ministry then has 30 days to make a decision on granting the license. The regulation also requires diplomatic and other foreign entities to obtain written approval from the Ministry of Foreign Affairs (MFA) before requesting a license from MOCI. Vietnam may also require organizations to request permission from MOCI before making changes to the content of their existing websites based on licensing requirements in the regulation.

OTHER BARRIERS

U.S., other foreign, and domestic firms have identified corruption in Vietnam in all phases of business operations as an obstacle to their business activities. Vietnam scored a 2.6 out of a possible high score of 10 points on Transparency International's Corruption Perception Index. In large part due to a lack of transparency, accountability, and media freedom, widespread official corruption and inefficient bureaucracy remain serious problems that even the Communist Party of Vietnam and the government of Vietnam admit they must address on an urgent basis. Competition among government agencies for control over business and investments has created confusing overlapping jurisdictions and bureaucratic procedures and approvals, which in turn create opportunities for corruption. Low pay for government officials and woefully inadequate systems for holding officials accountable for their actions compound the problems.

Implementation of the government of Vietnam's public administration reform program, developed with the assistance of the World Bank, as well as Vietnam's obligations under the transparency provisions of the BTA promise some improvement in the situation in the medium to long term, but it appears unlikely there will be much improvement in the near term.

Vietnam maintains a policy of bias in favor of domestic-market oriented industries, particularly those dominated by state-owned enterprises. Although all registered firms, regardless of ownership, can engage legally in foreign trade, barriers exist that discourage trading by non-state enterprises. Monopolies in production result in monopolies in trading, as in the case of coal. The tariff structure also favors domestic industries, particularly those dominated by state-owned enterprises. Most lower tariffs are on items predominantly used by those enterprises as inputs.

In April 2003, the United States and Vietnam concluded a textile trade agreement. The textile agreement assists U.S. domestic manufacturers by including Vietnam within the global textile quota regime and helps our importers by providing certainty and avoiding the unpredictability of frequent, random, unilateral limits. This agreement also contains a labor provision. Both parties reaffirm their commitments as members of the ILO and also indicate their support for implementing codes of corporate social responsibility as one way of improving working conditions in the textile sector. The agreement also calls for a review of progress on the goal of improving working conditions in the textile sector through consultations between the U.S. Department of Labor and Vietnam’s Ministry of Labor, Invalids, and Social Affairs.